

**IMPROVING CONSUMER PROTECTION IN THE
PREPAID CALLING CARD MARKET**

HEARING

BEFORE THE

**COMMITTEE ON COMMERCE,
SCIENCE, AND TRANSPORTATION**

UNITED STATES SENATE

ONE HUNDRED TENTH CONGRESS

SECOND SESSION

SEPTEMBER 10, 2008

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ONE HUNDRED TENTH CONGRESS

SECOND SESSION

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IMPROVING CONSUMER PROTECTION IN THE PREPAID CALLING CARD MARKET

WEDNESDAY, SEPTEMBER 10, 2008

U.S. SENATE,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
Washington, DC.

The Committee met, pursuant to notice, at 10 a.m., in room SR-253, Russell Senate Office Building, Hon. Bill Nelson, presiding.

OPENING STATEMENT OF HON. BILL NELSON, U.S. SENATOR FROM FLORIDA

Senator NELSON. Good morning. The meeting will come to order.

And as a nod to our distinguished Senator from Texas who has another important appointment, I want to yield to her to please make an opening statement.

STATEMENT OF HON. KAY BAILEY HUTCHISON, U.S. SENATOR FROM TEXAS

Senator HUTCHISON. Mr. Chairman, thank you so much.

I really appreciate your letting me go first, and I just want to make a brief statement.

First of all, I will cosponsor your bill. I think it is very important that we have the ability to establish a standard and it is kind of a clear, easy bar to clear that whatever is on a card should be on a card. And we have had trouble in my home State of Texas and the Attorney General has even filed a lawsuit against a company that was found not to have produced the correct number of minutes for what was promised. And I think it particularly preys on people who perhaps do not speak English or elderly people, people who use these cards in good faith.

So I think we need to take action, and I really appreciate the leadership that you are showing. And I will look forward to reading the testimony from the Chairman and look forward to working through this so that there is a standard that Americans or anyone buying a card can rely on.

Thank you very much. And thank you, Mr. Chairman.

Senator NELSON. And I want to thank the Senator from Texas for her leadership also with regard to our Space Subcommittee. We have a real challenge, as she well knows, in trying to get little old NASA back on track. And now with insurgent and resurgent Russia, how can we continue to rely on the Russians to get to the International Space Station, which is a national laboratory thanks to the Senator from Texas, for a 5- or 6- or 7-year period?

And this is one of the most mismanaged programs that we have ever seen. It has put us in this terrible circumstance of having built and paid \$100 billion for a national lab that is an International Space Station, and come 2011, we may not even be able to get to it. The Russians would have total control of it, and who knows, they might decide to form a joint partnership with the Chinese and take advantage of our \$100 billion.

Senator HUTCHISON. Mr. Chairman, I think we need to take a very strong action because the possibilities I think have been clarified even in the last 2 months that Russia may not be a reliable partner for us to use. And I think we should step up the efforts to get the Crew Return Vehicle moved up. And then I think we need to extend our shuttle missions to finish out the Space Station so that it can do the most good for us in energy research, as well as the other research that's being done there. I think that it will take a very bold action, and I think we should start that effort right now.

Senator NELSON. Well, I am going to need the Senator from Texas' help because we want to put all of this in the NASA reauthorization bill, but we are having difficulty with a certain Senator from South Carolina. And I need the Senator's help.

Senator HUTCHISON. I was not aware that we had a problem in South Carolina, but I am certainly willing to discuss that.

So that this wonderful conversation we are having is relevant, we all want to have calling cards that can take us to Mars.

[Laughter.]

Senator NELSON. And I thank the Senator.

Well, let us come back down to Earth. We have got all kinds of skullduggery going on here that we need to attack. It has to do with prepaid calling cards which are used by millions of folks and they buy these cards to stay in touch with their loved ones. It is a simple, little card. They buy these and they can call their loved ones around the country, around the world. It is particularly helpful to military members, seniors, immigrants, and low income Americans. With limited financial resources, these things become a lifeline to their family and their friends.

But what we have seen is a number of unscrupulous providers that are now operating in the market. And basically what it is is deception.

Now, most of the calling cards are from large, well-known companies offering these prepaid cards at good rates and conditions that are fair and reasonable. That is most of it. But as is the case in many things, we have people that are taking advantage of the system, and so that is now spilling over into the good companies that are fair and reasonable and their reputation is on the line.

Unlike a legitimate prepaid calling card, the fly-by-night operators increasingly are not interested in the welfare of the Americans buying the calling cards trying to connect with their loved ones. Instead, what they are doing is scamming consumers. And what they end up doing is imposing junk fees, exorbitant rates, selling cards that expire shortly and, in some cases, start expiring right when the consumer starts using the card.

Now, I want to give you two examples. Here is one. It is two bucks. It is marketed to people as if you can use this for \$2 worth

of calling. But you see that little red circle up there? That is what is on this card. Now, I could get a magnifying glass and I might be able to read this. I can tell you with my eyes, even with my magnifiers, it is hard for me to read this.



Senator NELSON. And would you flip it over to the next chart? Let us give you an example of some of the things that are in that small type. Now, this is blown up and bolded and underlined so that you all can see it. This, obviously, is not in that small little writing there. “Rates and fees vary and are subject to change without prior notice. Advertised minutes and rates are based on a single, non-pay phone call from the contiguous United States.”

GO - Terms & Conditions

By using this card, you agree to the following: **Rates and fees vary and are subject to change without prior notice.** Rates are higher for international cellular termination. Domestic rates apply only to calls within the contiguous United States. **Advertised minutes and rates are based on a single non-payphone call from the contiguous United States.** Application of surcharges and fees will have the effect of reducing total minutes available if not used on a single call. **Succeeding calls are billed at a higher rate.** \$2 and \$3 cards are subject to a higher per minute rate. **Calls are billed in three-minute increments.** A post call service fee of 40% and a hang up fee of \$0.99 will apply **per call.** All calls made from a payphone are subject to a \$0.99 charge. . .

Congressman, just have a seat there at the table and we will get to you in a second.

“Succeeding calls are billed at a higher rate. Calls are billed in 3-minute increments.” So if the calling person calls and they get an answering machine and they take all of 30 seconds, it is still billed at 3 minutes. “A post-call service fee of 40 percent and a hang-up fee of 99 cents apply per call.” Now, that’s just that one.

Flip it over to the next one. Is this on the same card? This is on the Africa Card or the Go Card? This is on this one. This is the Go Card.

“A semi-monthly charge of up to 89 cents applies to 24 hours of first use. Card expires 180 days after the date of first use. Standard off-peak hours are from 2 a.m. to 4 a.m.—

GO - Terms & Conditions (Cont'd)

You may incur additional local and regional charges from your telephone service provider. **A semi**

monthly charge of up to \$0.89 applies within 24 hours of first use. Calls to

directory assistance incur a \$1.50 charge (max. duration 3 min.). **Card expires 180**

days after the date of first used. Standard off-peak hours are from 2:00am to

4:00am ET weekdays, excluding holidays. Off-peak hours vary by destination, and

are subject to change without prior notice. For latest rates and fees including peak and off peak

hours, please contact our customer service number. Network services are provided by Geo Telecom.

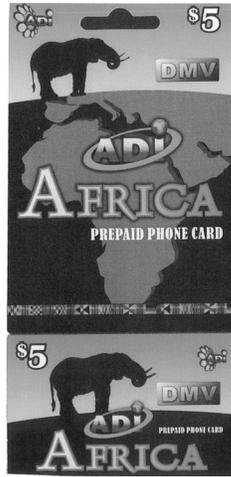
[Laughter.]

Senator NELSON.—“weekdays, excluding holidays.”

Can you flip it to the next one?

Now, this is a card that is aimed at immigrants so that they can call their loved ones in Africa. Look down at the bottom. Can you lift it up there? Down at the bottom, it is so small on this blowup I cannot read it, much less can I read it on that. And that’s the card.

Africa Card – Front & Back



Senator NELSON. And what that says is: “Call time is deducted in 1- to 3-minute increments. Service fees of up to 25 percent apply. A disconnect fee up to 98 cents may apply. A weekly maintenance fee of 69 cents may apply.” This is for a \$5 card. “Card expires 3 months from first use or 2 years from purchase.”

Africa - Terms & Conditions

Minutes announced are based on using the entire card on a single call. **Call time is deducted in 1 to 3 minutes increments.** No connections fees apply. **Service fees of up to 25% apply. A disconnect fee up to \$0.98 may apply. A weekly maintenance fee of \$0.69 may apply.** Calls originating from a payphone will incur a \$0.99 surcharge. Directory assistance calls will incur a \$0.85 surcharge. Rates and fees are subject to change without notice. Total per call charge is rounded to the nearest whole cent. **Card expires 3 months from first use or 2 years from purchase.** Cards have no cash redemption value. Services provided by Elite Telecom.

Senator NELSON. You got any more up there?

OK. You see the problem.

So I hope we can hear some testimony on this subject and try to expose it. You might think that the language might tell you how much it costs to make a domestic or international call, but it does not. And instead, we have a bunch of statements telling you how the card will not work and listing numerous add-on fees and caveats, all of which we have just gone over and which you cannot read on the card. If you can read the King's English, you better have a microscope. Otherwise, you are not going to be able to understand what you have just bought for \$2 or \$5.

So the bottom line is if you use that card twice, you lose it. You lose the value of the card. And you may lose it just by using it once with all those add-ons.

So with that as an intro, I want to call on the Honorable Eliot Engel, Congressman from New York, who wants to make a statement. And Congressman, we understand that—was it Delta or the US Air Shuttle that was late?

Representative ENGEL. It was Delta.

Senator NELSON. OK. Duly noted in the record.

Representative ENGEL. The truth is US Air probably would have been even later, but that is OK.

[Laughter.]

Senator NELSON. Give us a quick statement. We have pretty well laid it out. Senator Hutchison was here and I have laid it out. We want your endorsement and your observation on this.

**STATEMENT OF HON. ELIOT L. ENGEL,
U.S. REPRESENTATIVE FROM NEW YORK**

Representative ENGEL. Well, thank you, Senator.

As you have been stating, legislation of this kind should be a no-brainer. I mean, it is just crying out for attention, and it is something that everybody can agree on.

And I want to thank you and the Ranking Member Hutchison for holding today's hearing and for the invitation to speak. I know, Senator, you have done lots of work on this issue.

I must comment that you have certainly come a long ways since we were House colleagues together, and I am always happy to see my good friends in the House move on to the Senate and do really great work. And that is especially true of the work that you have done. I am always pleased to have your cooperation and your friendship.

I am here to discuss my legislation, the Calling Card Consumer Protection Act, and the reasons that I introduced this bill. I think that you have made it very clear as to why we have introduced bills like this and why it is needed.

Obviously, calling cards are an invaluable resource for people who do not have long distance telephone service in their home or those who make frequent overseas calls. Common users of these cards are students, members of the armed forces, and those whose family lives outside of the country. They are also popular among people who either choose not to subscribe to long distance telephone service or who simply cannot afford it. They are a necessary tool for keeping in touch with friends or family members. Calling cards that provide the services that the companies advertise can

save consumers a great deal of money when they call home. But, unfortunately, as you have pointed out, Senator, and we are seeing over and over again, many companies fail to keep their advertised terms or hide them.

About 2 years ago, I started hearing from a number of constituents regarding their prepaid calling cards. They were contacting me because their calling cards were not providing the number of minutes that were advertised. In fact, many were not even close to delivering the promised number of minutes. Furthermore, when my constituents attempted to contact the calling card company, they found it difficult or impossible to reach a customer service line.

I investigated this myself by purchasing a calling card. I found the same problem that my constituents were having. This is when I decided to introduce my legislation with Congressman Mike Ferguson of New Jersey to ban these practices.

In independent tests, as well as those conducted by States Attorneys General—and I know Florida has done a lot in this regard—calling cards were shown to provide far fewer minutes than they advertised. One study by The Hispanic Institute found that on average the caller only received about 60 percent of the minutes guaranteed by the card. In a \$4 billion a year industry, obviously this deception is costing consumers and honest companies hundreds of millions of dollars every year, and of course, these companies prey on minority communities, communities that do not speak English well. This is especially prevalent in those communities.

Companies have also instituted a variety of hidden fees. For example, some cards deduct minutes even if the call is not connected or if you get a busy signal. Other cards cut off the call after a few minutes so the consumer must redial and again be subjected to the connection charge. And the connection charge is obviously on top of the regular charge, and so people find that it might take 5 minutes or 10 minutes away just for a connection. Some cards round up the number of minutes used in 4-minute increments. Others advertise no connection fees in big letters on a sign, but instead charge you a hang-up fee. These fees take considerable money out of consumers' pockets every time they pick up the phone.

Obviously, calling card fraud harms segments of the population who are among the most vulnerable to being victimized by unscrupulous companies only seeking to make a quick profit. These unscrupulous companies are known to target poor, minority, and immigrant populations, and they do not stop there. Even our soldiers in Iraq have been preyed upon by deceptive practices of calling card companies.

In a recent article in *BusinessWeek* magazine, the author detailed one example of a company that marketed towards Spanish-speaking consumers, but the fine print that detailed all the various fees they would charge the user was in English. The company's answer to this? We are in America, they said. They had the temerity to claim that even when they put Spanish language advertisements in markets with Spanish-speaking consumers, they can hide all their fees in English.

My legislation, like yours, Senator Nelson, would put a stop to a number of deceptive practices employed by these companies. It would require an advertisement or packaging to include clear dis-

closure of all terms, conditions, and fees in the language in which the calling card is advertised. In addition, it would ensure that the Federal Trade Commission has the jurisdiction to pursue enforcement of these rules against companies who are not abiding by them.

Calling cards can be extremely useful for consumers, and I do not want to see honest companies punished and there are, obviously, a lot of honest companies. But the honest companies are also being harmed by these dishonest companies. There is a large enough market for a company to live up to its promises and to turn an honest profit. If consumers know that the card they purchase will provide the full amount of calling time that is advertised, this will benefit both consumers and the marketplace.

So I, in conclusion, would strongly encourage the Members of this Committee to support S. 2998, Senator Nelson's legislation to protect consumers from calling card fraud. With only a few weeks remaining in the 110th Congress, our constituents should not have to wait for Congress to reconvene in 2009 for action on this important legislation.

Once again, Senator, thank you for holding this hearing today and allowing me to testify.

[The prepared statement of Representative Engel follows:]

PREPARED STATEMENT OF HON. ELIOT L. ENGEL,
U.S. REPRESENTATIVE FROM NEW YORK

Chairman Inouye, Ranking Member Hutchison:

I want to thank you for holding today's hearing and for the invitation to speak on this important topic. I especially want to thank Senator Bill Nelson for his work on this issue. I have collaborated with Senator Nelson in the past, and I am always pleased to have his cooperation and his friendship.

I am here to discuss my legislation, the Calling Card Consumer Protection Act, and the reasons that I introduced the bill.

Calling cards are an invaluable resource for people who don't have long distance telephone service in their home or those who make frequent overseas calls. Common users are students, members of the Armed Forces, and those whose family lives outside of the country. They are also popular among people who either choose not to subscribe to long distance telephone service, or who cannot afford it. They are a necessary tool for keeping in touch with friends or family members. Calling cards that provide the services that the companies advertise can save consumers a great deal of money when they call home.

Unfortunately, as we are seeing over and over again, many companies fail to keep their advertised terms.

About 2 years ago, I began hearing from a number of constituents regarding their prepaid calling cards. They were contacting me because their calling cards failed to provide the number of minutes that were advertised. In fact, many were not even close to delivering the promised number of minutes. Furthermore, when my constituents attempted to contact the calling card company, they found it difficult or impossible to reach a customer service line.

I investigated this myself by purchasing a calling card. I found the same problems that my constituents were having. This is when I decided to introduce my legislation, with Congressman Mike Ferguson, to ban these practices.

In independent tests, as well as those conducted by states' Attorneys General, calling cards were shown to provide far fewer minutes than were advertised. One study by The Hispanic Institute found that on average, the caller only received an average of 60 percent of the minutes guaranteed by the card. In a \$4 billion a year industry, this deception is costing consumers and honest companies hundreds of millions of dollars every year.

Companies have also instituted a variety of hidden fees. For example, some cards deduct minutes even if the call is not connected. Other cards cut off the call after a few minutes so the consumer must redial and again be subjected to the connection charge. Some cards round up the number of minutes used in 4 minute increments.

Others advertise “no connection fees,” in big letters on a sign, but instead charge you a hang-up fee. These fees take considerable money out of consumers’ pockets every time they pick up the phone.

Calling card fraud harms segments of the population who are among the most vulnerable to being victimized by unscrupulous companies only seeking to make a quick profit. These unscrupulous companies are known to target poor, minority, and immigrant populations. And they don’t stop there. Even our soldiers in Iraq have been preyed upon by deceptive practices of calling card companies.

In a recent article in *BusinessWeek* magazine, the author detailed one example of a company that marketed toward Spanish-speaking consumers. But the fine print that detailed all the various fees they would charge the user was in English. The company’s answer to this? “We’re in America,” they said. They had the temerity to claim that even when they put Spanish language advertisements in markets with Spanish-speaking consumers, they can hide all their fees in English.

My legislation, like Senator Nelson’s, would put a stop to a number of deceptive practices employed by these companies. It would require an advertisement or packaging to include clear disclosure of all terms, conditions, and fees in the language in which the calling card is advertised. In addition, it would ensure that the Federal Trade Commission has the jurisdiction to pursue enforcement of these rules against companies who are not abiding by them.

Calling cards are a useful product for consumers, and I do not want to see honest companies punished. There is absolutely no reason why a company can’t deliver what is promised, and still turn an honest profit. If consumers know that the card they purchase will provide the full amount of calling time that is advertised, this will benefit both consumers and the marketplace.

I would strongly encourage the Members of this Committee to support S. 2998, Senator Nelson’s legislation to protect consumers from calling card fraud. With only a few weeks remaining in the 110th Congress, our constituents shouldn’t have to wait for Congress to reconvene in 2009 for action on this important legislation.

Once again, thank you for holding this hearing today, and allowing me to testify.

Senator NELSON. Thank you, Congressman. Thank you.

You are welcome to stay. You can leave—whatever is your pleasure. We are very grateful to you for having come over here and also for having introduced this legislation in the House.

Representative ENGEL. Thank you very much.

Senator NELSON. So thank you and good luck to you in the House.

We are pleased to have William Kovacic, the Chairman of the Federal Trade Commission. What I am going to do to truncate this hearing is we are going to take your written testimony and enter it into the record.

[The prepared statement of Mr. Kovacic follows:]

PREPARED STATEMENT OF HON. WILLIAM E. KOVACIC, CHAIRMAN,
FEDERAL TRADE COMMISSION

I. Introduction

Chairman Inouye, Ranking Member Hutchison, Members of the Committee on Commerce, Science, and Transportation, I am William Kovacic, Chairman of the Federal Trade Commission (“Commission” or “FTC”).¹ Thank you for giving the Commission this opportunity to testify before the Committee about consumer protection issues associated with the sale of prepaid calling cards.

The Commission appreciates the Committee’s decision to hold a hearing to shed light on deceptive practices in the calling card industry. Over the last decade, the prepaid calling card industry has grown into a multi-billion dollar a year industry. Prepaid calling cards can provide consumers with a convenient and inexpensive way to call friends and family at home and abroad. Unfortunately, however, purchasers of prepaid calling cards often do not receive the number of calling minutes advertised for the cards they purchase and are charged undisclosed or inadequately-dis-

¹The written statement presents the views of the Federal Trade Commission. Oral statements and responses to questions reflect the views of the speaker and do not necessarily reflect the views of the Commission or any other Commissioner.

closed fees and surcharges that reduce the value of the prepaid calling cards they purchased.

As the Nation's consumer protection agency, the FTC is committed to protecting consumers from deceptive marketing of prepaid calling cards. The FTC recently brought two cases alleging that distributors of prepaid calling cards had been deceptively marketing such cards. The Commission also has other active prepaid calling card investigations.

This statement provides the Committee with background information about the prepaid calling card industry and describes the FTC's recent law enforcement actions against distributors of prepaid calling cards. It also discusses the FTC's consumer education and outreach efforts. Additionally, it offers comments on S. 2998, the "Prepaid Calling Card Consumer Protection Act of 2008," introduced by Senators Bill Nelson, Olympia Snowe, John Kerry, and Mel Martinez. Finally, the Commission reiterates its support for the provision of the FTC reauthorization bill that would amend the FTC Act to repeal the exemption for common carriers subject to the Communications Act. Repealing the exemption for telecommunications carriers would ensure that the Commission can bring law enforcement actions against all participants in the prepaid calling card industry that are engaging in deceptive and unfair practices, including those companies that provide the underlying telecommunications services for these cards.

II. Background

Calling card providers market their cards for a variety of uses. Some cards are marketed primarily for use by consumers making calls within the United States. Such cards usually offer consumers the ability to make domestic long distance calls for pennies per minute. Other cards are marketed to U.S. consumers who want to call the United States when they are traveling or working in other countries. Indeed, many such cards are marketed to members of the United States armed forces serving around the world. In addition, a substantial number of prepaid calling cards are sold to recent immigrants to the United States who depend on calling cards to stay in touch with family and friends abroad.² Such calling cards, which typically retail for between \$2 to \$10 each, are generally sold in small retail outlets, including grocery and convenience stores, gasoline stations, and newsstands.

To advertise prepaid calling cards directed to consumers making international calls from the U.S., companies distribute eye-catching posters that are displayed on the walls and windows of the stores where such cards are sold. One hallmark of such posters is bold claims, made in large, colorful type, about the number of calling minutes the advertised cards provide for calls to particular countries. In stark contrast to the claims about available calling minutes that dominate the posters, the bottom of the posters generally contains small print disclaimers about a wide variety of fees and surcharges that reduce the value of the cards. The disclaimers are frequently in type so small as to be nearly illegible and in language so vague as to be effectively incomprehensible.³

Consumers typically use their prepaid calling cards as follows: the consumer dials an "access number" printed on the back of the card. A recorded message then prompts the consumer to enter the card's authorization code or Personal Identification Number ("PIN"), which is printed on the card. Next, the consumer usually hears an announcement of the monetary value of the card. The consumer then en-

²See Susan Sachs, *Immigrants See Path to Riches in Phone Cards*, N.Y. TIMES, Aug. 11, 2002, available at <http://query.nytimes.com/gst/fullpage.html?res=9800E7D6123AF932A2575BC0A9649C8B63&sec=&spon=&pagewanted=2>; *Talk Isn't So Cheap on a Phone Card*, BUSINESS WEEK, July 23, 2007, available at http://www.businessweek.com/magazine/content/07_30/b4043079.htm; Mark E. Budnitz, Martina Rojo and Julia Marlowe, *Deceptive Claims for Prepaid Telephone Cards and the Need for Regulation*, 19 LOYOLA CONSUMER L. REV. 1 (2006).

³For example, in *FTC v. Alternatel, Inc., G.F.G. Enterprises LLC, also d/b/a Mystic Prepaid, Voice Prepaid, Inc., Voice Distributors, Inc., Telecom Express, Inc., Lucas Friedlaender, Moses Greenfield, Nickolas Gulakos, and Frank Wendorff*, 08-21433-CIV-Jordan/McAliley (S.D. Fla.), the FTC has alleged in its complaint that: "in numerous instances defendants' posters contain vague disclosures about fees in tiny font on the bottom of the poster, stating in relevant part:

by using this card you agree to the following: Prompted minutes are before applicable charges and fees, application of surcharges and fees have an effect of reducing total minutes on cards. One or all of the following may apply: (1) A weekly maintenance fee ranging between \$.49 and \$.79. (2) A hang-up fee between \$.05 and \$1 depending upon length and destination of the call. (3) A destination surcharge of between 0 percent and 100 percent.—minutes and/or seconds are rounded to multiple minute increments.—International calls made to cellular phones are billed at higher rates.—Toll free access numbers are subject to an additional fee of up to 4 cents per minute.—Prices are subject to change without notice.—This card has no cash value.—Card expires 3 months after first use or 12 months after activation."

ters the phone number he or she is trying to reach and hears an automated “voice prompt” announcing the number of minutes of time ostensibly available on the card.

As discussed in more detail below, the FTC, our state law enforcement colleagues, and third parties who have tested a wide variety of prepaid calling cards have found that prepaid calling cards offered by a number of industry participants routinely fail to deliver the minutes promised in their advertising and voice prompts. As alleged in two cases recently brought by the FTC, our testing showed that the defendants’ prepaid calling cards delivered about half the number of promised minutes.

III. Law Enforcement Actions

The FTC works closely with the offices of State Attorneys General and other state agencies. In the fall of 2007, the FTC established a joint Federal-state task force concerning deceptive marketing practices in the prepaid calling card industry. The task force members include representatives from the offices of more than 35 State Attorneys General and other state and local agencies, and the Federal Communications Commission (“FCC”). Working cooperatively allows us to share information and facilitate law enforcement activity in the prepaid calling card area.⁴

Currently, the Commission is litigating two actions in Federal district court, alleging that the defendants deceptively marketed their prepaid calling cards. In addition, as discussed below, the Attorneys General for the states of Florida and Texas recently have taken action against prepaid calling card companies for their allegedly deceptive practices.

A. FTC Enforcement Actions

Under Section 5 of the FTC Act, the FTC has authority to bring cases against companies and individuals for engaging in deceptive or unfair acts or practices in or affecting commerce.⁵ Since the 1990s, the FTC has used this power to bring enforcement actions against entities for deceptively selling prepaid calling cards. The Commission brought its first two prepaid calling card cases against companies that the FTC alleged were deceptively marketing prepaid calling cards by, among other things, misrepresenting the per-minute rates consumers would be charged when using the cards and by failing to clearly and conspicuously disclose connection and maintenance fees associated with the cards.⁶ Since then, the FTC has brought several cases alleging that telemarketers deceptively marketed calling cards to consumers and charged consumers without their authorization.⁷

This spring, the FTC filed two cases against major distributors of prepaid calling cards. On March 25, 2008, the FTC sued Clifton Telecard Alliance, a national distributor of prepaid calling cards based in New Jersey, and the company’s principal.⁸ The FTC alleged that the defendants, which market their cards chiefly to recent immigrants, engaged in deceptive marketing practices by: (1) misrepresenting the number of calling minutes provided by their cards; (2) failing to adequately disclose fees and charges associated with their cards; and (3) failing to adequately disclose that the value of their cards may be reduced even when a call does not connect. In support of its case, the FTC tested 46 of Clifton Telecard Alliance’s calling cards purchased at various retail outlets.⁹ In the FTC’s tests of these cards, none deliv-

⁴ Representatives from the following Offices of Attorneys General are members of the task force: Alabama, Arizona, Arkansas, California, Colorado, Connecticut, District of Columbia, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Maryland, Maine, Massachusetts, Minnesota, Missouri, Montana, New Mexico, Nevada, New Hampshire, New Jersey, New York, North Carolina, North Dakota, Ohio, Oregon, Pennsylvania, Rhode Island, South Dakota, Tennessee, Texas, Virginia, Washington, Wisconsin. In addition, the New York State Consumer Protection Board and the New York City Department of Consumer Affairs have participated in the task force.

⁵ 15 U.S.C. § 45(a)(2).

⁶ *FTC v. PT-1 Comm’ns, Inc.*, 99-CIV-1432 (S.D.N.Y.) (Stip. Final Order filed Feb. 25, 1999) (order requiring monetary relief and barring defendants from misrepresenting the value of its prepaid calling cards and from failing to clearly and prominently disclose fees and charges); *FTC v. Trans-Asian Comm’ns, Inc.*, 97-CIV-5764 (S.D.N.Y.) (Stip. Final Order filed Mar. 17, 1998) (order requiring \$1 million performance bond before defendants can advertise or sell prepaid calling cards and barring future material misrepresentations about prepaid calling cards).

⁷ *FTC v. 9131-4740 Quebec, Inc.*, CV-02242 (N.D. Ohio) (Compl. filed July 25, 2007) (pending); *FTC v. T2U, Inc.*, 101-CV-811 (N.D. Ohio) (Stip. Final Order filed Sept. 13, 2001); *FTC v. Enhanced Billing Servs., Inc.*, 101-CV-1060 (D.D.C.) (Stip. Final Order filed Aug. 1, 2001).

⁸ *FTC v. Clifton Telecard Alliance One LLC, d/b/a Clifton Telecard Alliance and CTA, Inc., and Mustafa Qattous*, 2:08-cv-01480-PGS-ES (D.N.J.).

⁹ The FTC has been able to test prepaid calling cards thanks in part to the invaluable assistance of El Salvador’s Defensoria del Consumidor, Colombia’s Superintendencia de Industria y Comercio, the Egypt Consumer Protection Authority, Mexico’s Procuraduría Federal del Consumidor (PROFECO), Panama’s Autoridad de Protección al Consumidor y Defensa de la

ered the number of calling minutes advertised in posters displayed at the point of sale. Three of the 46 cards failed to work at all, and, on average, the remaining 43 cards delivered only 43 percent of the advertised calling minutes. On April 2, 2008, the Federal district court in New Jersey granted the FTC's motion for a temporary restraining order.

On May 19, 2008, the FTC filed a similar action, *FTC v. Alternatel*, against several companies alleged to act as a common enterprise in distributing prepaid calling cards out of Florida, Massachusetts, and New Jersey. In the *Alternatel* case, the Commission alleged that the defendants violated Section 5 of the FTC Act by misrepresenting the number of calling minutes their cards provide and failing to adequately disclose fees and charges associated with their cards. As in the *Clifton Telecard Alliance* case, the FTC conducted extensive testing of the *Alternatel* defendants' prepaid cards and found that the actual number of minutes provided by the cards fell far short of the defendants' advertising claims. In tests of 87 of the defendants' cards, the cards delivered on average only 50.4 percent of the minutes advertised on posters at the point of sale.¹⁰ On May 23, 2008, the Federal district court for the Southern District of Florida entered a temporary restraining order in the *Alternatel* matter.

In both the *Clifton* and *Alternatel* actions, the defendants have moved to dismiss the FTC's case on the grounds that the underlying telecommunications carriers are necessary parties that the FTC cannot join because of the exemption in the FTC Act for common carriers subject to the Communications Act. The FTC has opposed defendants' motions, and is confident that it will win on the merits. As final relief in both cases, the FTC seeks a permanent injunction and consumer redress and/or disgorgement of ill-gotten gains.

B. State Law Enforcement Actions

Two states recently brought law enforcement actions against a number of prepaid calling card companies. Over the last few months, the Florida Attorney General has announced that he has entered into Assurances of Voluntary Compliance ("AVC") with eleven prepaid calling card companies doing business in Florida.¹¹ These settlements are the culmination of a broad investigation into the prepaid calling card industry launched by the Florida Attorney General in July of 2007. Notably, while the FTC has brought its lawsuits solely against distributors of prepaid calling cards, the Florida Attorney General entered into AVCs with eleven companies that include both distributors and telecommunications service providers for prepaid calling cards.

On May 23, 2008, the Texas Attorney General filed a lawsuit against Next-G Communication, Inc., a telecommunications service provider that produces, sells and distributes prepaid calling cards.¹² The Texas lawsuit alleges that Next-G Commu-

Competencia, and Peru's Instituto Nacional de Defensa de la Competencia y de la Protección de la Propiedad Intelectual (INDECOPI). In this area, as in so many others, international cooperation has proved to be vital to the Commission's law enforcement actions.

¹⁰The results of the FTC testing of the defendants' cards in the *Clifton Telecard Alliance* and the *Alternatel* cases are consistent with the testing results of The Hispanic Institute, a nonprofit organization that has issued a report on its testing of a wide variety of prepaid calling cards. The Hispanic Institute reports that, on average, the cards it tested delivered only 60 percent of the minutes promised in voice prompts. See <http://www.thehispanicinstitute.net/research/callingcard/qa> (visited June 18, 2008). They are also consistent with testing results that have been offered in private litigation. See *IDT Telecom, Inc. v. CVT Prepaid Solutions, Inc., et al.*, Civil Action No. 07-1076 (D.N.J.) (Pls. Mem. In Supp. of Their Order to Show Cause Why a Prelim. Inj. Should Not Issue, at 6-10; Ex. 1 to Suppl. Aff. of Gabi Schechter, dated Mar. 26, 2007) (alleging the defendants' calling cards delivered on average only 60 percent of prompted minutes); *IDT Telecom, Inc. v. Voice Distributors, Inc., d/b/a Voice Prepaid, et al.*, Civil Action No. 07-2465 (Mass. Sup. Ct., Middlesex Cty.) (Compl. ¶16) (alleging that the defendants' calling cards delivered on average only 65 percent of prompted minutes); *IDT Telecom, Inc. v. Diamond Phone Card, Inc., et al.*, Index No. 3682-08 (N.Y. Sup. Ct., Kings Cty.) (Compl. ¶15) (alleging that the defendants' calling cards delivered on average only 59 percent of prompted minutes).

¹¹See *McCollum Announces Prepaid Calling Card Settlements, Industry-Wide Reform* (June 11, 2008) available at <http://myfloridalegal.com/newsrel.nsf/newsreleases/79C6666DB24608D785257465004EC901> (visited on August 27, 2008) (announcing settlements with IDT America, Inc.; Union Telecom Alliance; Total Call International, Inc.; Blackstone Calling Card, Inc.; CVT Prepaid Solutions, Inc.; Dollar Phone Enterprise, Inc.; STi Prepaid, LLC; Alternatel, Inc.; and Cristel Telecommunications, LLC); *Prepaid Calling Company Reaches Settlement with Attorney General* (July 2, 2008) available at <http://myfloridalegal.com/newsrel.nsf/newsreleases/1439BD5308D470588525747A006423B8> (visited on August 27, 2008) (announcing a settlement with Touch-Tel Partners USA, LLC); *Attorney General Reaches Settlement with 11th Prepaid Calling Card Company* (August 21, 2008) available at <http://myfloridalegal.com/newsrel.nsf/newsreleases/C410C546EB409C93852574AC006C9499> (visited on August 27, 2008) (announcing settlement with Cinco Telecom Corp. d/b/a Orbitel).

¹²*State of Texas v. Next-G Commnc'n, Inc., Taj Khwaja*, 2008CI08149 (Bexar County, TX) (Pet. filed May 23, 2008).

nication has marketed and sold prepaid calling cards throughout Texas that fail to deliver the number of minutes it advertises to customers and that the defendant has failed to disclose fees and charges associated with its calling cards. The Texas Attorney General alleges that Next-G's prepaid calling cards consistently delivered only 40 percent of the minutes claimed on the Next-G's advertising posters and confirmed by Next-G's voice prompt given at the beginning of each call.¹³

The FTC applauds the actions of the Florida and Texas Attorneys General and is grateful for the participation of all of our law enforcement partners in the joint Federal-State calling card task force.

IV. Consumer Education and Media Outreach

In addition to bringing enforcement cases, the Commission has made consumer education and outreach a high priority. The FTC recently updated its consumer education brochure on calling cards, which is available in both English and Spanish on the Commission's website.¹⁴ The Commission also has done extensive outreach about prepaid calling cards to media outlets that cater to non-English and English speaking consumers. The FTC wants to make sure consumers know that it is unlawful to advertise calling cards that misrepresent the number of minutes that the calling cards provide or to fail to clearly and conspicuously disclose the fees and charges that reduce the value of the calling cards. The FTC also wants consumers to know that they can and should complain to the FTC if they do not get what they pay for.

V. The Proposed Legislation

As described above, the FTC Act's prohibitions on deceptive and unfair practices provide the Commission with a powerful tool to bring enforcement actions against the distributors of prepaid calling cards. Senate Bill 2998, the proposed "Prepaid Calling Card Consumer Protection Act," is directed at the conduct of prepaid calling card service providers (carriers) as well as distributors, and therefore would implicitly give the FTC jurisdiction over common carriers engaged in the deceptive practices prohibited by the proposed legislation. Consumers would benefit greatly from legislation giving the FTC jurisdiction over such practices by telecommunications carriers. The legislation also would authorize the FTC to seek civil penalties for violations of the Act or of the rules issued by the FTC pursuant to the Act, thus adding an important remedy to those already available to the Commission.

Generally, S. 2998 requires the FTC to promulgate a rule requiring that, among other things, prepaid calling card providers and distributors provide clear and conspicuous disclosures of the number of minutes provided by the calling cards, the amount and frequency of all fees assessed for use of the calling cards, and the expiration date of the cards. The bill also prohibits prepaid calling card providers and distributors from selling or distributing calling cards that do not provide the advertised number of calling minutes or from assessing inadequately disclosed fees. The bill further provides for the FTC to bring suit alleging violations of the Prepaid Calling Card Consumer Protection Act as if they were violations of an FTC rule, thus enabling the agency to seek civil penalties for violation of the Act and the FTC's rule promulgated pursuant to the Act.

The FTC supports the goals of S. 2998, and appreciates the implied extension of jurisdiction—which will ensure a level playing field by allowing the Commission to act to hold violators responsible for deceptive trade practices whether they are providing the telecommunications services or distributing the prepaid calling cards—and the proposed authority to seek civil penalties. Two aspects of the bill raise concerns, however. First, the bill creates a knowledge standard for holding prepaid calling card distributors liable if they violate the Act by distributing calling cards that provide fewer minutes or a higher per minute rate than advertised, or announced on the voice prompt given when a consumer places a call.¹⁵ Incorporating a knowledge standard into the law could create an additional—and potentially very challenging—evidentiary burden on the FTC when seeking injunctive relief in a civil case.¹⁶ Second, the bill explicitly exempts from its coverage prepaid wireless phone

¹³ See *Attorney General Abbott Takes Legal Action Against Prepaid Calling Card Company* (May 23, 2008) available at <http://www.oag.state.tx.us/oagNews/release.php?id=2479> (visited on August 27, 2008).

¹⁴ See *Buying Time: The Facts About Pre-Paid Phone Cards* (2008) available at <http://www.ftc.gov/bcp/edu/pubs/consumer/products/pro04.pdf> (visited on August 27, 2008).

¹⁵ The bill does not have a parallel knowledge requirement for prepaid calling card service providers.

¹⁶ Indeed, under general consumer protection principles and traditional jurisprudence under Section 5 of the FTC Act, 15 U.S.C. §45, the Commission need not show knowledge or intent in order to stop an entity from engaging in unfair or deceptive practices. Notably, however, Sec-

services where the consumer has established a relationship with the wireless carrier by purchasing a wireless service handset package. The Commission is concerned that the bill's exception for prepaid services based on the purchase of a handset and wireless calling services would provide a powerful incentive for the worst actors in the prepaid calling card industry to migrate their business practices to prepaid wireless handsets and refill cards, and thereby avoid the mandates of the proposed law.¹⁷

To enable the Commission to address problems with deceptive conduct involving prepaid calling cards more effectively, the Committee might also consider giving the Commission authority to bring actions seeking civil penalties in its own right against prepaid calling card providers and distributors rather than through the Department of Justice. Giving the FTC authority to bring its own civil penalties cases in this area would help ensure that the Commission does not have to forego quick relief in order to seek civil penalties.

The Commission recognizes that the agency and the Committee share the same goal: stopping unscrupulous calling card companies from defrauding vulnerable consumers. The Commission looks forward to working with the Committee regarding the language of the legislation as the Committee moves forward.

VI. The Common Carrier Exemption

On several occasions, the Commission has testified in favor of the repeal of the common carrier exemption.¹⁸ The Commission continues to endorse its repeal, and thanks the Committee for its continued support for this measure. The FTC Act exempts common carriers subject to the Communications Act from its prohibitions on unfair and deceptive acts or practices and unfair methods of competition. This exemption originated in an era when telecommunications services were provided by highly-regulated monopolies. The Commission believes that the exemption is now outdated. In the current marketplace, firms are expected to compete in providing telecommunications services. Congress and the FCC have dismantled much of the economic regulatory apparatus formerly applicable to the industry. Removing the exemption from the FTC Act would not alter the jurisdiction of the FCC, but would give the FTC the authority to protect consumers against unfair and deceptive practices by common carriers in the same way that it can protect against unfair and deceptive practices by non-common carriers involved in the provision of similar services.

Prepaid calling cards are a case in point. In contrast to the State Attorneys General, who are able to bring enforcement actions to stop both telecommunications providers and distributors offering prepaid calling cards from engaging in unfair and deceptive practices, the FTC has targeted only the deceptive practices of prepaid calling card distributors, because of the FTC Act common carrier exemption. Fur-

tion 5(m)(1) of the FTC Act includes a knowledge standard for instances where the FTC is seeking civil penalties for violations of an FTC Rule, as opposed to equitable relief, such as an injunction. 15 U.S.C. § 45(m)(1) ("The Commission may commence a civil action to recover a civil penalty in a district court of the United States against any person, partnership, or corporation which violates any rule under this chapter respecting unfair or deceptive acts or practices . . . with actual knowledge or knowledge fairly implied on the basis of objective circumstances."). Eliminating the knowledge threshold from the bill would not change the Commission's elevated burden for obtaining monetary relief in civil penalty cases.

¹⁷Some participants in the prepaid calling card industry are beginning to offer prepaid wireless services. As the cost of providing cellular phones and calling minutes continues to decrease, the incentive to move consumers to prepaid wireless accounts from more traditional prepaid calling cards has increased.

¹⁸See *Prepared Statement of the Federal Trade Commission*, Before the Subcommittee on Interstate Commerce, Trade, and Tourism Committee on Commerce, Science, and Transportation, U.S. Senate (April 8, 2008), available at <http://www.ftc.gov/os/testimony/P034101reauth.pdf>; *Prepared Statement of the Federal Trade Commission*, Before the Subcommittee on Interstate Commerce, Trade, and Tourism Committee on Commerce, Science, and Transportation U.S. Senate (Sept. 12, 2007), available at <http://www.ftc.gov/os/testimony/070912reauthorizationtestimony.pdf>; *Prepared Statement of the Federal Trade Commission On FTC Jurisdiction Over Broadband Internet Access Services*, Before the Committee on the Judiciary, U.S. Senate (Jun. 14, 2006), available at <http://www.ftc.gov/opa/2006/06/broadband.shtm>; *The Reauthorization of the Federal Trade Commission: Positioning the Commission for the Twenty-First Century: Hearing Before the Subcomm. on Commerce, Trade and Consumer Protection of the H. Comm. on Energy and Commerce*, 108th Cong. (2003) ("FTC 2003 Reauthorization Hearing") (statement of the FTC), available at <http://www.ftc.gov/os/2003/06/030611reauthhr.htm>; see also FTC 2003 Reauthorization Hearing (statement of Thomas B. Leary, FTC Commissioner), available at <http://www.ftc.gov/os/2003/06/030611learyhr.htm>; *FTC Reauthorization Hearing: Before the Subcomm. on Consumer Affairs, Foreign Commerce, and Tourism of the S. Comm. on Commerce, Science, and Transportation*, 107th Cong. (2002) (statement of Sheila F. Anthony, FTC Commissioner), available at <http://www.ftc.gov/os/2002/07/sfareauthtest.htm>.

thermore, even when the Commission has identified and brought enforcement actions against non-common carriers, the common carrier exemption can impose additional litigation costs on the FTC. For example, as noted above, in both the *Clifton Telecard Alliance* and *Alternatel* cases, which the FTC has brought against distributors of prepaid calling cards, the defendants have moved to dismiss the FTC's cases on the grounds that the FTC has not sued and cannot sue the underlying carriers, which defendants allege to be necessary parties. While the Commission is confident that it will prevail in its opposition to these motions, the burden of having to respond to such motions is not insubstantial.

The American public will benefit greatly from S. 2998's grant to the FTC of jurisdiction over common carriers in the prepaid calling card arena. The FTC respectfully continues to recommend that, rather than take a piecemeal approach to providing the FTC with jurisdiction in this important area of commerce, Congress repeal altogether the FTC Act exemption for common carriers subject to the Communications Act. The FTC has extensive expertise with such areas as advertising, marketing, billing, and collection, areas in which significant problems have emerged in the telecommunications industry.¹⁹ In addition, the FTC has powerful procedural and remedial tools that could be used effectively to address developing problems in the telecommunications industry if the FTC were authorized to reach them.

VII. Conclusion

The Commission will continue its aggressive law enforcement and consumer outreach and education programs in the prepaid calling card arena. The Commission thanks this Committee for focusing attention on this important issue and for the opportunity to discuss its law enforcement program.

Senator NELSON. I am going to start asking questions of you, Mr. Chairman, and if you would then feel free to expand as much as you want with regard to your answers.

STATEMENT OF HON. WILLIAM E. KOVACIC, CHAIRMAN, FEDERAL TRADE COMMUNICATION

Mr. KOVACIC. Great.

Senator NELSON. I understand that the FTC has taken some actions to rein in some of these bad actors and the costs of entering this business are fairly low, and it seems like a lot of these bad actors may be able to get around the injunctions against them and consent decrees by reincorporating and moving on to safer regions or other states.

So as these bad actors are trying to avoid the arm of the law, what do you need to do at the FTC to address this problem? Give us your thoughts as to whether we need to get the criminal justice system involved in going after these bad actors.

Mr. KOVACIC. Let me begin by thanking you, Mr. Chairman, Ranking Member Hutchison, for the privilege of speaking about this enormously high priority area of concern.

I would say there are three things that we should focus on in considering the phenomenon that you mentioned.

One is to continue our existing efforts to strengthen our compliance program. Over the past couple of years, we have devoted a lot of resources to increasing our ability to follow what happens to our existing orders and to identify instances in which people subject to

¹⁹For example, the FTC has brought numerous cases involving the cramming of unauthorized charges onto consumers phone bills. See, e.g., *FTC v. Verity Int'l Ltd.*, 335 F. Supp. 2d 479 (S.D.N.Y. 2004), *aff'd in part, rev'd in part*, 443 F.3d 48 (2d Cir. 2006), *cert. denied*, 127 S. Ct. 1868 (2007); *FTC v. Audiotex Connection, Inc.*, C-97 0726 (DRH) (E.D.N.Y. 1997); *FTC v. Int'l Telemedia Assocs., Inc.*, 1-98-CV-1925 (N.D. Ga., 1998); *FTC v. Sheinkin*, 2-00-363618 (D.S.C., 2000); *FTC v. Mercury Marketing of Delaware, Inc.*, 00-CV-3281 (E.D. Pa. 2000); *FTC v. Epixtar Corp.*, 03-CV-8511 (DAB) (S.D.N.Y. 2003); *FTC v. Nationwide Connections, Inc.*, 06-80180-CIV-Ryskamp/Vitunack (S.D. Fla. 2006); *FTC v. Websource Media, LLC*, Civ. No. H-06-1980 (S.D. Tex. 2006).

our orders have violated them, and to make a point of going after recidivists both with our own resources and in cooperation with other enforcement agencies. I think we have converted what used to be a system of manual retrieval to an electronic database that lets us follow these folks along.

Second, where there are recidivists who violate existing orders, I think you put your finger on a key consideration. Increasingly, we seek to engage the efforts of Federal and State officials who have the capacity to enforce infringements of that type as crimes. And it is our view that where the kind of misconduct that you and the Congressman have been describing is repeated, the only truly credible sanction is to take their freedom away because in many instances they dissipate assets. They hide them effectively so that the sanction that counts is the sanction that involves imprisonment. So greater cooperation through what we call our Criminal Liaison Unit, which is now roughly at its fifth anniversary, but expanded efforts of those types, and with your encouragement and cooperation, we will make that a focal point of what we do.

Senator NELSON. Now, does that unit work with the U.S. Attorney?

Mr. KOVACIC. Yes, sir.

Senator NELSON. And then the U.S. Attorney prosecutes the case.

Mr. KOVACIC. Precisely. The partnership that is developed is with the U.S. Attorney's Office with the Department of Justice, and with our state government counterparts. We assist in preparing the cases and they deliver them through their own efforts and through our cooperation. And I would be happy to share for the record later with you and your staff the extraordinary success that this cooperation has had in putting serious offenders in prison.

Senator NELSON. Do you want to do that in testimony or submit it in writing?

Mr. KOVACIC. If I could submit that in writing to you, I would be delighted to do it. But your encouragement to continue on that path is very important.

[The information referred to follows:]

But there are a couple of ideas the Senate may want to consider including in its legislation. First, you can specify that the FTC can freely share and coordinate enforcement activities and complaint information with authorized State officials in affected States; for instance, State Attorneys General, State Commissions, and certain categories of statutorily authorized consumer advocates. At a minimum, complaint information could be shared with suitable advanced disclosures to the complainant specified. (Meaning the FTC should notify complainants—up front—orally or on the website—that information about their complaint may be shared with State authorities to facilitate resolution). Second, you can require that the FTC maintain the task force initiative. In his testimony, FTC Chairman Kovacic stated the task force was formed at his behest and is not statutory required. Should Chairman Kovacic step down from his post there is no guarantee that a successor would continue this collaborative effort. Memorializing Chairman Kovacic's task force innovative in law would provide consumers with higher level of protection from fraud and abuse.

Mr. KOVACIC. The third element I think is to improve our cooperation with our state and local government counterparts. Last year, with a number of people quite happily in this room whose efforts you will hear about later today, we formed a joint Federal-State task force. What we have come to understand is that in the archipelago of public institutions that work in this area, only if we

link the islands together and work effectively will we be able to track and identify offenders no matter where they go within the United States. And increasingly, they exploit gaps in cross-border enforcement so that the cooperative effort has to involve not simply our partners at the state and local level.

And as you have already heard today, our state counterparts have done wonderful things using their own authority. Someone you know quite well, Attorney General Bill McCollum in Florida, has done a fantastic job as well.

But to deepen the integration of our efforts with our state counterparts because the sum of our efforts will be much greater if those are improved, and by having local authorities and state authorities work with us, sharing the resources we have, both access to information about infringements, access to information about existing orders, sharing information, we greatly increase the likelihood that individuals will not evade the force of the law simply by moving from one place to another.

Those would be three key priorities for us.

Senator NELSON. Tell us about standardized disclosure requirements. Would they help the Commission's enforcement efforts?

Mr. KOVACIC. I think the disclosure requirements that are spelled out in S. 2998 are an excellent foundation for providing standardized disclosures. I think those key ingredients adopted into law will be enormously useful. They address precisely the kinds of concerns that you identified in reviewing the card examples that we have seen today, that assist in overcoming the misleading representations or nonrepresentations that Congressman Engel just mentioned a moment ago. And I think S. 2998—simply adopting that menu of considerations into law—would be a great step toward providing greater assurance about what is actually associated with each of these transactions.

Senator NELSON. What can the FTC do to collect more accurate information regarding the consumer complaints?

Mr. KOVACIC. We have got, I think, the framework of a superb system in place now. It is our Sentinel database through which a large number of government and nongovernment organizations now, again, owing to efforts that had been encouraged with enormous effectiveness by this committee, by this chamber, and by the House—to build Sentinel, which is an electronic database, we obtain information directly through complaints that come into our Complaint Center and through our state and local government enforcement counterparts. So we have not only an excellent repository now that collects information from a variety of streams—literally dozens of partners participate in this—but owing to resources, again, that Congress has generously provided us, we now have mechanisms for identifying almost in real-time patterns of misconduct.

An important supplement to that is to increase our consumer education efforts, that is, to alert consumers about where to go. And this is where the point about economic disadvantage and vulnerability is terribly important. We realize that an increasing focus of our work has to be to reach populations that are not likely to go to public authorities, immigrant populations that are the victims of misconduct, minority individuals in poor communities who may

have simply despaired at the prospect that public authorities of all types will assist them in matters of need.

We are increasing our efforts through our Hispanic language initiative now, which is about 5 years old, where we are retooling many of our brochures that deal with prepaid calling cards to ensure Spanish language speakers inform us and exercise precautions on their own. To inform us, we are also developing efforts that we are pursuing now to work with a host of different organizations to reach populations that might not otherwise alert us to patterns of misconduct. So to expand these consumer education efforts, but in particular, to reach populations that for a variety of reasons, economic disadvantage, social disadvantage, historical disadvantage of all types, may simply not have confidence that public institutions at all levels of our government are willing to help out because if we can detect the misconduct, we now have the apparatus in place to identify problems quickly, to build the cooperative framework with our state and local counterparts and our counterparts at the Federal level to do something about it promptly.

Senator NELSON. And are you doing an outreach to our military population?

Mr. KOVACIC. We are indeed. Under our Sentinel program, we have a cooperative program with the Department of Defense. One of our main partners is the Department of Defense. And a number of our projects involving not simply prepaid calling cards but other areas of concern involving consumer protection, financial practices, and others have our military service people as important focal points. And again, these are relationships that we can deepen and strengthen over time, but I am happy to report to you that the basic infrastructure to do that work is in place and is working now, but it can be enhanced.

Senator NELSON. Describe how you have a mechanism as part of the task force for sharing the complaint information with State and local governments.

Mr. KOVACIC. Through the Sentinel system, our law enforcement counterparts are able to share and access information in those databases. That is a condition of participating. And these are secure systems, and the eligible participants, to obtain that information, are law enforcement authorities, public authorities with law enforcement responsibilities. They have access to this information.

But it is, I think, again something you pointed to before. It is not simply the access to the raw information. It is building the personal relationships and the institutional networks that ensure that we share information about better practices and techniques about what is taking place, patterns we are observing, as well as enforcement techniques that put us in a better position to apprehend wrongdoers and sanction them.

Senator NELSON. Now, some of these charges that they list are payments to the Federal Universal Service Fund and the pay phone owner compensation. How do you go about determining whether these calling card companies have remitted the money to these government entities or in the case of pay phone compensation, to the pay phone owners?

Mr. KOVACIC. Senator, that is an ingredient of the problem that we have not focused on. Typically the payments to the Universal

Service Fund and the fulfillment of obligations have tended to be the province of our telecommunications regulators at the state and Federal level. That is a level of expertise, a specific concern we have not focused on. But we do work actively with our state and local counterparts involving telecommunications oversight on the other dimensions of the problem.

Senator NELSON. And that would be in the case of Government as well where it might be the Federal Universal Service Fund?

Mr. KOVACIC. We tend not to focus on fulfillment of those obligations, but we do work actively with the Federal Communications Commission in sharing information, what we learn about the operation of the sector itself.

Senator NELSON. It seems like that is important because that is another case of fraud about which a prosecutor needs to know.

Mr. KOVACIC. No question.

Senator NELSON. What percentage of the total calling card market would you say constitutes these bad actors?

Mr. KOVACIC. Very hard to determine, Senator, and I do not know that we have attempted a precise calculation. It is about a \$4 billion-plus a year sector. And as you and your colleagues and Congressman Engel have mentioned today, the vast bulk of activity in that sector is performed by legitimate enterprises.

Our concern is that whatever the actual percentage of commerce accounted for by illegitimate enterprises is, it has the capacity to taint the entire sector. That is, if individuals repeatedly have bad experiences, it becomes very difficult for the legitimate enterprise to step forward and say you can trust me. "My representations are honest. I am not going to cheat you." So the real hazard here, again, whatever the precise calculation is—and for the record, we would be glad to take our best stab at giving you our own estimate. Whatever it is, it has a unique capacity to taint the entire field, and that is the menace that we have to deal with.

Senator NELSON. Are you getting cooperation from the good actors?

Mr. KOVACIC. Indeed, we are, sir. Yes. It is the good actors who help identify the nature of the problem. They have made suggestions about what to do about it. And I think for the very reason that you and Senator Hutchison mentioned originally, their own investments, their own good name is at stake. And if consumers believe that this is a bad commercial neighborhood, they will stay out completely and the others will suffer. They are helping us.

Senator NELSON. A minute ago, you mentioned the activity of the states going after these bad actors. And I would like you to comment on what occurs if a state goes after them, the state gets them in a scenario that applies just to that state. So the bad actors move to another state. So the FTC is going to have to coordinate the activities of those state lawsuits when they raise the violation of section 5 of the FTC Act. Tell us about that.

Mr. KOVACIC. I think what we will certainly have to do is, first, to have a network that ensures that all of us are aware of the activity of each institution so that we have a sense of what the individual pieces of enforcement look like, but also a sense of how to develop a collective strategy about the timing and the prosecution of matters.

One thing that increasingly has become part of our portfolio is what we call sweeps, where we work in cooperation with our State counterparts and sometimes our international counterparts where on a single day we will announce the prosecution or completion of literally dozens of matters involving a related practice. And these sweeps have become an extremely valuable tool to ensure that we get broad coverage and from the point of view of raising consciousness, the fact of bringing lots of them at once tends to generate lots of attention which ensures that the consequence of prosecution is greater deterrence.

Senator NELSON. Do you want to comment on the controversial issue in the Committee on common carrier exemption?

Mr. KOVACIC. I would like to thank the Committee, to thank Senator Dorgan, to thank you, Mr. Chairman, for the possibilities in S. 2998 to permit us to operate much more extensively in instances in which a potential wrongdoer is a communications service provider that is a common carrier.

As you know, there are other public institutions that have the capacity in some ways to do what we do, Federal and State. The reason we are keen on eliminating and attenuating these restrictions is that there are many instances in which we are dealing with firms that are not, we believe, common carriers, but they raise defenses that implicate the common carrier exemption. In the two matters that you are aware of, our two cases brought in the spring, *Clifton Telecard* and *Alternatel*, we are having to spend precious resources to defeat—and we believe we will—arguments that communications firms are necessary parties and must be brought into the lawsuit.

In other instances, we see clear evidence of misconduct by firms that are unmistakably communication services providers. We cannot address those directly. We have to hand those off. And that handoff can be a source of fumbles, and it is not always clear that someone else will inevitably take the ball and run with it.

We think that given the changes in the sector today, that if we have the capacity to deal universally across the country with not only the distributors of these cards whom we are dealing with in the *Clifton* and *Alternatel* cases, but also with telecommunication services providers, we have the ability to create a much more effective source of protection.

And it is not to denigrate the work that other public institutions have done in any way. We are simply proud of the experience we built. If I can go back to the Delta or US Airways Shuttle example before, we have flown these routes in advertising and misleading conduct lots of times. And if it is a dark, rainy night on the northern approach coming down the Potomac, which we have done many times into National Airport, which has sort of a short runway, and you think about who you want in the cockpit, you want someone there with a little bit of gray in the temples who has done it a lot, who says this is the 2,500th landing I have made at National on a dark, rainy night.

We have flown this route lots of times, and we think we are pretty good pilots when it comes to dealing with deceitful and misleading behavior so that there are other good pilots out there, but

we think we can fly this route very well if we are given authority to fly over this part of the commercial space.

Senator NELSON. So the bottom line is you support the legislation and you think it would be a step in the right direction.

Mr. KOVACIC. No question, Senator. We have some specific suggestions which we are happy to share with your staff and to continue to discuss with you about areas in which we think the legislation can be improved. There are some technical adjustments we would suggest. But we think the legislation is unmistakably a step ahead and a crucial element that you and the Committee appreciate quite well. Our regulatory frameworks need upgrades over time, and your colleagues, your counterparts in the House, understand this quite well, as Representative Engel just mentioned. And we see the adoption of this type of legislation as being the equivalent of getting the upgrades we need to make sure that the enforcement operating system works well over time.

Senator NELSON. Well, thank you, Mr. Chairman. And without objection, part of the record will be the written material that you wanted to insert in the record.

Mr. KOVACIC. Thank you.

Senator NELSON. And I thank you, and let me call up the second panel.

Mr. KOVACIC. Thank you very much for the chance to be here today.

Senator NELSON. Thank you.

We are happy to have Sally Greenberg, Gus West, Patricia Acampora, and Rosemary O'Brien. Sally Greenberg is the Executive Director of the National Consumers League. Gus West is the President of The Hispanic Institute. Patricia Acampora is Commissioner of the New York State Public Service Commission. Rosemary O'Brien is the Director of Marketing of Military Marketing.

As stated in the previous panel, your written testimony will be included as part of the record.

Senator NELSON. Mr. West and Ms. Greenberg, both of you have followed this issue for some period of time, and it seems that in the past couple of years, there has been a dramatic spike in the number of complaints against the bad actors in the industry. Can you tell us what factor is responsible for this increase in complaints? Is it the low cost of entry into this lucrative market? Is it the failure of regulators? What is your opinion? Ms. Greenberg?

**STATEMENT OF SALLY GREENBERG, EXECUTIVE DIRECTOR,
NATIONAL CONSUMERS LEAGUE**

Ms. GREENBERG. I do believe that the low cost of entry is a contributing factor. It is really easy to get in and out. It is easy to get out from under the lens of law enforcement. I have in my written statement a quote that I could not resist adding from one episode of *The Sopranos* where Tony Soprano is talking about how he and his cronies are in the business of prepaid calling cards and somebody else is left holding the bag. Very easy to get in, very easy to take people's money and run.

One of the things that we are recommending in our testimony is that there be some bond that entrants to the market who are selling prepaid calling cards put up so that if law enforcement finds

that the cards are not providing the minutes that are promised, that we have a place to go to look for and compensate consumers who have been ripped off or defrauded as a result of these cards. So I think that low barrier to entry is a real problem then. I think we could tackle that.

[The prepared statement of Ms. Greenberg follows:]

PREPARED STATEMENT OF SALLY GREENBERG, EXECUTIVE DIRECTOR,
NATIONAL CONSUMERS LEAGUE

Introduction

Good morning, Mr. Chairman. My name is Sally Greenberg and I am Executive Director of the National Consumers League. I appreciate this opportunity to appear before the Senate Committee on Commerce, Science, and Transportation to discuss the need for greater consumer protections in the purchase and use of prepaid calling cards. This largely unregulated consumer product is a “Wild West” of sellers and merchants who too often prey upon the most vulnerable consumers by promising minutes they don’t deliver and loading up on hidden or undisclosed charges and fees. In an industry like this, with low barriers to entry and a totally unregulated market, you can be sure there will be unscrupulous operators who will take the money and run.

The National Consumers League, whose founding in 1899 makes us the oldest consumer organization in the United States, has a longstanding interest in protecting consumers from fraudulent practices and is the only consumer group that operates a national fraud center. (The NCL’s Fraud Center is described at www.fraud.org).

I want to commend you, Senator Nelson, for your leadership in offering S. 2998, the Prepaid Calling Card Consumer Protection Act of 2008. Consumers rely on you, an outspoken defender of consumer rights and protections, to look out for their interests. In my testimony, I will address some of the facts and figures describing the magnitude of the prepaid calling card industry and the large amounts of money involved. I’ll discuss the fraud and deceptive practices associated with that industry and actions taken at the state and Federal levels in response to fraud I’ll discuss why NCL supports your bill, S. 2998, and I’ll make some policy recommendations. Our written testimony also includes a timeline detailing the growth of the industry and the rise in fraud associated with that growth.

Let’s start with the industry. It is illustrative that the shady practices of the prepaid calling industry were featured prominently on the HBO series, *The Sopranos*. In Episode 26, Tony is discussing the mob’s work with prepaid cards. I’ve deleted the obscenities:

TONY SOPRANO. “So, telecommunications once again fails to disappoint. What’s this thing? Telephone calling cards. You find a front man who can get a line of credit, you buy a couple of million units of calling time from a carrier. You become ‘acme telephone card company’. ‘Acme’. You’re now in the business of selling prepaid calling cards. Immigrants especially, no offense. They’re always calling back home to whoever (deleted). And it’s expensive, right? You sell thousands of these cards to the (deleted), cards at a cut rate. But you bought the bulk time on credit, remember? The carrier gets stiffed. He cuts off the service to the card holders, but you already sold all your cards. That’s (deleted) beautiful! (Laughing) it’s a good one.”

Of course, no one should conclude that the whole prepaid calling card industry is controlled by organized crime: we have no such evidence, but this vignette from *The Sopranos* demonstrates how easy it is to get into the industry, rip off consumers, and disappear with no accountability whatsoever. That must change.

Prepaid Calling Card Facts

- Prepaid cards are a \$4 billion a year industry, responsible for 11 billion calls in 2004.¹
- The industry is estimated to reach \$6.4 billion in revenue in 2008.²
- Examples of fraudulent practices used by the prepaid companies include “hang-up fees,” periodic maintenance fees, destination surcharges, and high billing increments.⁵
- Companies that try to “play by the rules” are often punished by a loss of market share due to fraudulent carriers.⁶

- Only 11 states, including California, Connecticut, Florida, and Illinois, currently have laws pertaining to calling card fraud, specifically. Most turn to generic consumer protection statutes, but enforcement has been extremely light.⁷
- Hispanic consumers may be losing up to \$1 million per day because of fraudulent phone cards.⁴
- The average calling card delivers only 60 percent of the minutes promised, according to The Hispanic Institute, a non-profit research group.³
- The FTC's survey of prepaid calling cards confirms The Hispanic Institute's findings. For instance, one calling card tested by the FTC claimed to offer 360 minutes to Panama, but only delivered 23 minutes of calling time. The FTC said that in 87 tests of the prepaid cards, the cards delivered an average of only 50 percent of the advertised minutes.⁸
- The cost-per-minute rates for prepaid phone cards can be up to 87 percent higher than expected. An expected call rate of 15 cents per minute, for example, may end up costing 28 cents per minute.⁹

Customer service representatives for prepaid calling cards are often unavailable or not knowledgeable regarding the prepaid phone cards their employers are selling. A 2005 University of Georgia study found that in a third of the calls to prepaid calling card customer service lines, callers couldn't reach a representative. When they did make contact, the representative often was unable to answer basic questions about fees or rounding up of minutes.¹⁰

Why We Need To Protect Users of Prepaid Calling Cards

The rapid growth of the prepaid calling card industry combined with, until recently, a lax enforcement of consumer protection statutes at the state and Federal levels, has enabled consumer fraud to flourish. Like so many other scams, the most frequent victims of the fraud and deception are the most vulnerable consumers: immigrants and the working poor; and those lower income Americans who often cannot afford or obtain regular phone service. These consumers rely on calling cards to stay in touch with friends and loved ones in the U.S. and abroad. Sadly, we believe that military families are also likely victims of the prepaid card scams and rip-offs.

Yes, the cards provide these users with an alternative means of calling home, but many use false and deceptive practices in the process, and impose unconscionable terms. Fraud is fraud—if an automobile is sold with the promise of a sun roof and chrome wheels, it better have a sunroof and chrome wheels—if a phone card promises 500 minutes to call El Salvador, it should deliver those 500 minutes.

Some state attorneys general—notably in your state of Florida, Senator Nelson—have done a commendable job in prosecuting fraudulent prepaid card companies. The Federal Trade Commission has also conducted investigations and brought important cases against individual prepaid phone card providers. Unfortunately, these scattered efforts are insufficient. We need basic Federal protections to stem the tide of the many deceptive practices in this industry.

NCL believes that FTC regulations, as called for S. 2998, would help to level the playing field for all phone card providers. Such regulations include requirements that prepaid phone card providers and distributors disclose the terms and conditions of the cards, and list the per minute rates, preferred international destination rates, and any fees or surcharges, in their advertising.

We need a national floor of minimum requirements stating what industry practices won't be permitted. We applaud S. 2998's provisions preserving the rights of states to go forward with their own civil cases—as Florida did. The Federal Government should set minimum standards and permit states to go forward with provisions that don't conflict with the Federal law. That's a pro-consumer position and acknowledges the important role states have played in enacting and enforcing consumer protections.

NCL believes that both your bill, Senator Nelson, S. 2998, and Congressman Elliot Engel's bill, H.R. 3402, would go far in addressing the false promises and deception associated with these cards. Anecdotal evidence suggests that the simple threat of regulation has already increased pressure on the prepaid calling card industry to reform its marketing practices.¹² We've also seen evidence through the IDT settlement in Florida that if one company is forced to disclose accurately how many minutes a card will provide and what the surcharges and fees will be, they will lose market share to the other firms who are shading the truth. Therefore, we need to create a level playing field where all participants are required to provide accurate information.

Beyond Disclosure: What More Can We Do To Protect Consumers

While NCL supports your efforts, Senator Nelson, to require full disclosure of terms and conditions on these prepaid calling cards, we find that the terms themselves, when they are disclosed, are too often unconscionable.

For example, the text in fine print on the back of my \$5.00 "Africa Sky" card states the following:

All of the following fees will reduce the number of available minutes and the value of the card. Use of a toll free number from a pay phone will incur a \$.99 per call fee. Per minute rate will be \$.02 higher for calls placed using toll free access numbers. Call time for multiple calls is calculated by rounding the last minute up to the closest multiple of 3 and then adding 1 minute except that if your call lasts less than 1 minute you will be charged only for a minute. If available minutes are not all used up on the first call the following fees will apply: (1) the multiple call rate will be 40 percent higher and will apply to all calls (see poster for details); (2) a fee per call of \$.59 will apply to each call; and (3) and after midnight after the first call a fee of \$.69 will be deducted and then weekly thereafter. Card Expires Three Months After First Use . . . Rates and Fees are Introductory and are subject to change anytime. . . .

The same or similar text is found on most of the cards. So, though we have the terms disclosed, albeit in fine print, we have a company that is rapidly subtracting money from the user's original purchase. A 40 percent higher rate is imposed after the first call; a fee of 59 cents per call will apply to each one after the first call; and after midnight of the first call, the fee is 69 cents, which will be deducted weekly thereafter. This is from an original \$5.00 card. No wonder users find that two or 3 weeks—or sooner—after first use, the card has no credit remaining. Notice the card also contains this catch-all phrase "*Rates and Fees are Introductory and are subject to change anytime . . .*" leaving the card distributors the option of changing the rules whenever they wish.

Worse still is the "Majestic DMV" Card I purchased for \$2.00:

(1) A \$.99 fee applies on the 1st day of use and every 5 days thereafter; (2) Calls made through tollfree access numbers are subject to a fee of up to 4 cents a minute; (3) payphone surcharge of \$.99; (4) A destination surcharge of between 20–60 percent of the total call; and/or (5) a fee of \$.10–\$.99 for connected calls, \$.15/minute maximum domestic call rate (before applicable charges and fees); minutes and/or seconds are billed at a minimum of 1 minute and up to 5 minute increments, plus any applicable fees. Card expires 3 months after first use or 12 months after activation.

As a consumer advocate, I've often found it useful to look at consumer protection measures in other countries. I lived in Australia 2 years ago and used prepaid cards for calls to the United States. My experience was uniformly positive—the Australian prepaid cards tended to deliver the minutes they promised, and they were good for multiple uses. *Choice Magazine*, Australia's counterpart to our *Consumer Reports*, tested these international calling cards and found that indeed, many delivered good value and low rates without connection fees or added charges. When I arrived back in the United States and began buying cards here, I found that their value tended to disappear after the first call. When I read the fine print, I understood why.

I also consulted the document *Consumer Protection in the European Union—Ten Basic Principles*—and note that the Fifth Principle is relevant to our discussion of prepaid calling cards:

Contracts Should Be Fair To Consumers

Have you ever signed a contract without reading all the small print? What if the small print says the deposit you just paid is non-refundable—even if the company fails to deliver its side of the bargain? What if it says you cannot cancel the contract unless you pay the company an extortionate amount in compensation? EU law says these types of unfair contract terms are prohibited. Irrespective of which EU country you sign such a contract in, EU law protects you from these sorts of abuses.

We could apply the EU's notion of contract fairness to this issue. NCL supports S. 2998's disclosure requirements and hopes that they will satisfactorily address the problem of consumers paying good money for a prepaid calling card that fails to deliver the service. An open marketplace where all prepaid calling card companies are providing accurate information may do the trick; the market has a way of working very effectively when consumers have accurate information upon which to compare rates.

NCL would like to suggest, however, that after passage of your bill, the FTC closely monitor the industry and in a year's time, report on whether disclosure is addressing the problem adequately.

Diogenes called the market "a place set apart where men can deceive each other." We must impose some limits on that paradigm. If after a year we still see failure to accurately disclose rates and unconscionable terms when the rates are disclosed, we would urge this Committee to consider stronger regulation of this industry.

NCL Policy Recommendations Related to Disclosure and S. 2998

The National Consumers League strongly supports S. 2998 and its provisions to give enforcement authority to the Federal Trade Commission under the "unfair or deceptive act or practice," clauses of the Federal Trade Commission Act. While prepaid calling cards generally offer savings on international long distance calling versus traditional "Dial 1," 10-10 dial-around and wireless long distance calling,¹³ these savings are no excuse for fraud or deception.

We also support FTC's call to appoint a monitor to oversee the prepaid calling card business,¹⁴ and a requirement that the FTC report back to Congress on a periodic basis regarding the status of its efforts to enforce the terms of the proposed legislation.

As a general proposition, we applaud the requirements included in the Florida Attorney General's June 2008 settlement with prepaid card companies, such as:

- Ceasing all deceptive advertising.
- Providing 100 percent of the minutes advertised.
- Not using hidden fees or misleading minute calculations to increase their profits at consumers' expense.
- Printing disclosures for a given card in any language used to advertise that card.
- Printing the exact number of minutes available and the card's expiration date (if applicable) on the card.
- Prohibiting naming of card surcharges to resemble taxes.
- Requiring one-minute increment billing.

While S. 2998 requires that the disclosure text on the calling card itself, packaging, or other promotional material (including online) be in same language used to advertise the card, we would recommend expanding Sec. 3.(b)(4) of the bill to require that prepaid phone card providers provide toll-free customer service lines staffed by customer service representatives able to converse in the languages that the cards are advertised in.

Further Recommended Action If Disclosure Requirements Are Not Sufficient

If after 1 year, the FTC reports back to Congress with evidence indicating that greater disclosure is not reducing the consumer abuses in the industry, we recommend that further action be considered by this Committee, with the Federal Trade Commission given the authority to enforce these provisions:

- Require all market entrants to be licensed and post a bond before marketing cards to consumers. That bond would go into a fund to compensate consumers who are victims of fraud. Those companies that market prepaid calling cards should also be required to provide a name, address and place of incorporation. Right now, the barriers to entry are so low and the penalties for not making good on the value of the cards are so minimal that it's simply open season on consumers. We believe requiring a bond will act to keep many bad actors out of the industry.
- Require all market entrants to have a 24 hour, 7 days a week toll free number that has a live person on the other end who must be knowledgeable about the use of the card.
- Require that fees and surcharges imposed be related to actual costs. Congress has imposed rules on other industries that were charging consumers outrageous fees—the moving van industry, payday lenders, and funeral homes, to name a few. If, in a year's time, this Committee finds that disclosure is not easing the deception and rip-offs that plague this industry, the Committee should consider imposing stronger regulations on prepaid calling card companies and the many fees and surcharges they impose on consumers.
- Require that all cards have an expiration date and that this date be no shorter than 1 year after activation. If a seller fails to make a disclosure on expiration, the card should be valid indefinitely.

- Require sellers to list the minimum charge per call and the balance in minutes and dollars remaining on the card.
- Require sellers to inform consumers, via a website or toll-free phone number, of any proposed changes in terms and conditions, with consumers given the chance to reject these changes and receive a refund on the card with no fee imposed for requesting such a refund within an appropriate grace period of no less than 30 days after posting of the proposed change. Prepaid calling card providers should also be required to prominently list a mailing address to which customers can direct refund requests and/or a website with a refund form that the consumer can access easily.
- Require uniform terms in all prepaid calling card contracts so that consumers can comparison shop. Companies should not be allowed to confuse consumers by using a variety of terms for charges such as “administrative fee” or “service fee.”
- The amounts involved in prepaid phone card transactions are too small for any one individual to bring a case to court. The only meaningful way to allow consumers to hold prepaid card sellers accountable is through use of the class action process. Consumers need to be guaranteed a private right of action and the ability to band together as a class to bring cases against dishonest prepaid phone card providers.

Conclusion

We strongly support S. 2998 and commend this Committee for holding the hearing today. By requiring much better disclosure on prepaid calling cards, this bill will help to mitigate the deception and fraud associated with these cards. We also support further monitoring of the industry by the FTC, which will in turn report to the Members of this Committee.

NCL also urges Congress to find a way to require that prepaid calling card companies go beyond simple disclosure of their onerous rates. The most vulnerable consumers—military families, immigrants, low-income families—rely on these cards and spend their hard-earned money only to see the value of the cards disappear quickly after first use. NCL believes we can do better by consumers. We support the disclosure required under this bill and hope that it works. If we need to take stronger action, this bill’s requirements will represent an excellent first step.

Thank you, Mr. Chairman, for giving the National Consumers League this opportunity to comment on your bill. We commend you for your pro-consumer record and look forward to working with you and your staff to see this bill enacted into law.

Issue Timeline

We have provided a timeline of enforcement actions and legal settlements pertaining to prepaid calling cards below.

1986	Prepaid calling cards introduced to the North American market. ¹⁵
1996	U.S. prepaid card sales reach \$1.1 billion. ¹⁶
April 2001	New York Attorney General Eliot Spitzer announces settlement with five companies accused of deceptively marketing prepaid telephone cards throughout upstate New York. This settlement was part of Spitzer’s ongoing efforts to combat illegal marketing practices of prepaid phone card companies dating back to 1999. ¹⁷
2006	Newark, NJ-based IDT Corp., the largest prepaid calling card company in the U.S. reports \$2.2 billion in total sales. ¹⁸
2007	U.S. prepaid market reaches \$4 billion in revenue.
January 2007	IDT Corp. settles Federal class action suit brought on behalf of hundreds of phone card customers alleging fraudulent and deceptive advertising practices. ¹⁹
March 2007	IDT files lawsuit against 9 competitors, alleging that they provide 40 percent less time than advertised. Epana Networks, Dollar Phone, and Locus Telecommunications quickly reach settlement with IDT, agreeing to cease any misleading marketing practices. Six other companies named in the suit, including CVT Prepaid Solutions Inc. issue an open letter to the industry, claiming that IDT’s suit is “nothing but an underhanded ploy to regain lost market share by intimidation.” ²⁰

July 2007	Florida Attorney General Bill McCollum announces investigation of 10 prepaid calling card companies for fraudulent or deceptive advertising. ²¹
August 2007	Representative Eliot Engel (D-NY) introduces H.R. 3402 "Calling Card Consumer Protection Act." ²²
March 2008	FTC asks U.S. District Court for the District of New Jersey to halt allegedly illegal marketing practices of prepaid card companies CTA Inc., Clifton Telecard Alliance One LLC, and Mustafa Qattous. ²³
May 8, 2008	Senator Bill Nelson (D-FL) introduces S. 2998 "Prepaid Calling Card Consumer Protection Act of 2008." ²⁴
May 23, 2008	Texas Attorney General Greg Abbott announces filing of legal enforcement action against prepaid calling card company Next-G Communications, Inc. over allegedly deceptive marketing practices employed by the company. ²⁵

Endnotes

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²¹Hatcher, Monica. "McCollum probes calling card deceptions," *The Miami Herald*. July 24, 2007.

²²U.S. House. 110th Congress, 1st session. H.R. 3402, Calling Card Consumer Protection Act. Online. *Thomas.gov*. Available at <http://www.thomas.gov/cgi-bin/bdquery/z?d110:HR03402:@@L&summ2=m&> [Retrieved on July 25, 2008].

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Senator NELSON. Mr. West?

STATEMENT OF GUS K. WEST, PRESIDENT AND CHAIRMAN OF THE BOARD, THE HISPANIC INSTITUTE

Mr. WEST. Mr. Chairman, I do not know that we necessarily at The Hispanic Institute would want to make it harder to do business. We sort of believe that the problem really lies in the enforce-

ment. It seems that these fraudulent practices are illegal at the Federal, State, and local level already, and it just needs to be enforced. Feedback that we have gotten from a few of the companies is that they were not going to change their practice until the enforcement was stepped up, until they were forced to deliver what they are promising.

[The prepared statement of Mr. West follows:]

PREPARED STATEMENT OF GUS K. WEST, PRESIDENT AND CHAIRMAN OF THE BOARD,
THE HISPANIC INSTITUTE

Mr. Chairman and distinguished Senators of the Commerce Committee, my name is Gus West, President and Board Chair of The Hispanic Institute, a Washington D.C. based non-profit. Thank you for inviting us here today to give testimony regarding international prepaid calling cards. These calling cards are an economical way to make international phone calls. In the United States, Latinos purchase and use these cards more frequently than any other group. The cards are used primarily to talk with family, friends, and relations.

These cards are sold in neighborhood stores/tiendas/bodegas. We all have seen posters in the windows of these stores, advertising the cost of a certain number of minutes to a particular country. The cards are normally in boxes behind the cashier and the customer is able to select the card they wish to purchase. On the back of each card is an 800-number and a PIN number assigned to the card. One calls the 800-number, enters the PIN number, the international phone number desired, and then receives a message telling the caller how many minutes he has for a phone call.

We have tested hundreds of these cards and have found that on average these cards deliver about half the minutes promised. In an effort to have the most objective analysis we hired a private firm, Washington-based Network Analytics, to conduct testing of international prepaid calling cards sold in the Florida, New York and the Washington D.C. markets. I have a copy of our study here today and it is posted on our website at www.thehispanicinstitute.net. The conclusions of the independent study mirror the results of the internal testing that we conducted at The Hispanic Institute.

I have been using these cards myself, and been cheated out of minutes. In my current role as Chairman of The Hispanic Institute, I have often been asked by reporters if we could put them in contact with other victims of this fraud. I ask them to go to anyone of these neighborhood stores where these cards are sold, and ask anyone you see buying these cards, if they have been cheated out of call minutes. You will find that 100 percent of the people who use these cards will tell you that they have been cheated out of minutes.

The most popular cards, the ones that are purchased most often, are the \$2 and \$5 cards. While losing money on a \$2 or \$5 card may seem minimal to some, it can be significant to a low wage earning family. For reasons such as language, income, and lack of familiarity with regulations the users of these cards have had little recourse to address this fraud by a billion dollar industry.

This is false advertising and it is illegal under existing Federal, state, and local laws. Moreover, we believe that other industries intentionally prey on Hispanics when advertising in Spanish as the majority of advertising for prepaid calling cards is done.

THI has been highlighting this issue for well over a year now. While several State Attorneys General, State Legislatures, and the Federal Trade Commission have begun to take action against calling card fraud we have not seen any measurable improvement in this situation. We look forward to the day when consumers in the United States can be protected against this kind of fraud. Thank you.

Hispanic Institute

CALLING CARD VERIFICATION TEST PLAN

Provided by: Network Analytics Corporation

Objective

The purpose of this testing is to determine if calls to certain destinations using commercially available prepaid calling cards are providing the amount of minutes specified by the card providers.

Methodology

Call generators will be used to place the calls via the calling card and complete the call to the destination call generators. Every attempt will be made to use all the available time in a single call. If this is not successful, most commonly due to quality of the line and drops, additional calls will be made to the same destination until all the remaining balance in the cards is used. Each call is recorded by the units in order to interpret the amount of minutes announced by the calling card platform.

Units

The testing will be performed using Call Generators (CallWave) in the U.S. (Washington, D.C. and New York lines) and terminating to Call Generators (CallWave) with Mexico and Guatemala numbers.

Cards

The following calling cards will be used:

Florida (\$5)—Telmex Compañero, STI Florida, Touch-Tel Hondureña, Touch-Tel Guatemalteca, Touch-Tel Salvadoreña, Dollar Phone Coffee Time, Dollar Phone Rey, MPTA Florida Idol, MPTA Nine, PCI Pilot, PCI Prima and TST Si Pues.

New York (\$2)—Diamond Bingo, Diamond Arenque, SDI I Love NY, Lycatel Success, Lycatel Call Me, STI World, RTG Martini, RTG Cocktail and IDT Play Ball.

Washington, D.C. (\$2)—IDT Boss

Toll Free (\$5)—GEO Florida

Two cards of each are provided in order to attempt to test to each destination with each card.

Test Deployment

The following are the numbers for the lines used:

Washington Originated calls: (202) 609-9875 and (202) 244-1066

New York Originated calls: (917) 779-8197

Mexico Termination: +525585256265

Guatemala Termination: +50222630419

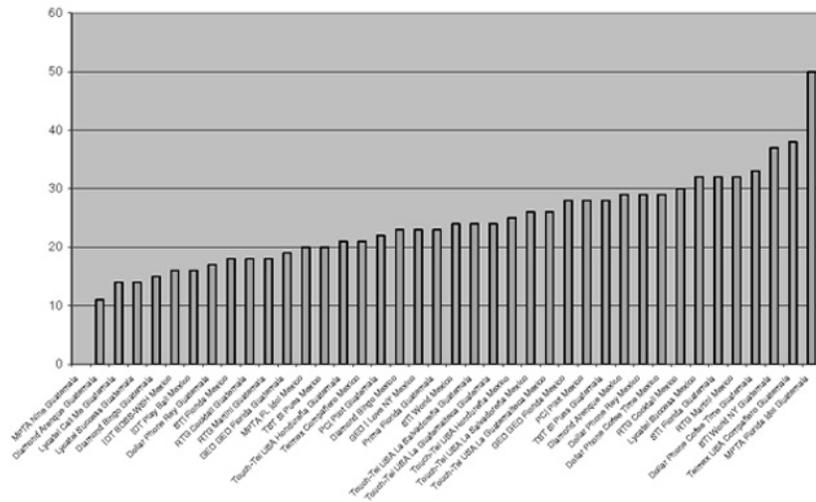
Test Scope

The testing will provide the following data for each call:

Seq. Number	Disconnect Reason
Date	Call Duration Recording (Sec)
Time	Call Duration Trace
Card Vendor	Call Duration Destination carrier CDR (Sec)
Card Name	Call Duration Minutes
Card Denomination	PAMS Score LQ
Card Code	PAMS Score LE
Originating Number Area Code (City)	Per call Extra Charge (Using Next Call's announced balance)
Originating Number	Next Call Announced Balance
Access Number Dialed	Card indicated connection fee
Destination Country	Card indicated Rounding Increments
Destination Number	Card indicated maintenance fee
Destination Cell or Landline	Toll-Free use surcharge
From Number shown at destination	Calculated p/min charge based on 1st call announcements
Announced Balance \$	CCR
Announced Balance (minutes)	AVE PDD
Rate Per Minute	AVE Extra Charge
Minutes Not Provided (If call used all balance)	AVE PAMS LQ
Recording file name	AVE PAMS LE
End of Dial Time	Total Minutes provided
Call Progress detection time	Completed Calls
Post Dial Delay	Actual p/minute rate experienced
Call Disposition	Total Minutes announced
Call Answer Time	Percentage provided vs. announced
Call End Time	Minutes Not Provided (If call used all balance)
Warning Provided	Percentage provided vs. announced (last call)

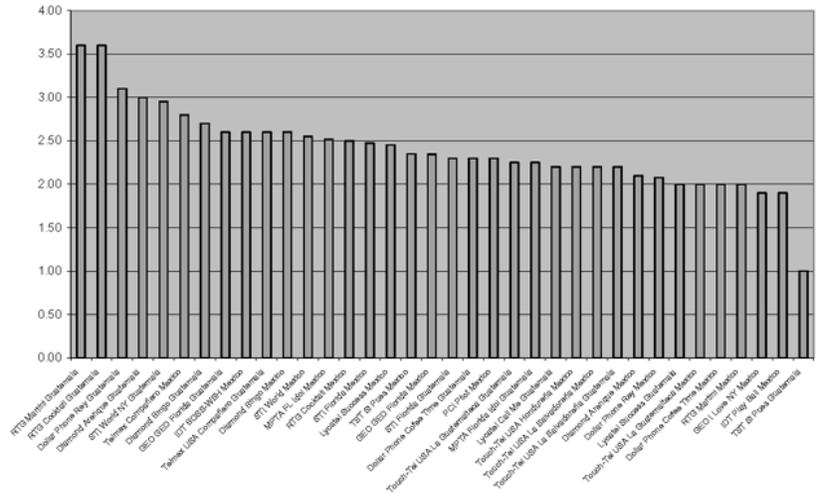
The following chart provides information about the Average Post Dial Delay provided by each of the cards, sorted by lowest (better) to highest (worst).

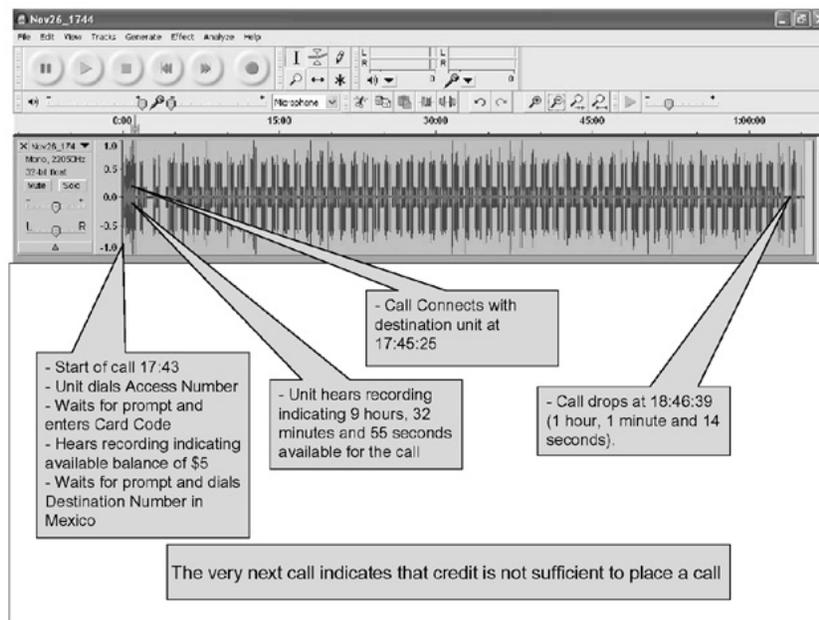
Post Dial Delay (PDD Seconds)



The following chart provides information about the Average Listening Quality provided by each of the cards, sorted by highest (better) to lowest (worst).

PAMS Listening Quality





Senator NELSON. Ms. O'Brien, you were nodding your head.

**STATEMENT OF ROSEMARY G. O'BRIEN, PRESIDENT,
MILITARY MARKETING LLC**

Ms. O'BRIEN. Yes, sir. I agree with Mr. West that enforcement is key here. You already have lots of legislation and rulemaking around this. What is critically important is that the bad actors are brought to a competent body to account for their actions. Generally speaking, I think the vast majority of the prepaid industry is considerably reputable and makes full disclosure. But I think that there are populations that are disproportionately affected by the bad actors. And we know where to find them. Let us find them and do what we need to do. Enforcement is key.

[The prepared statement of Ms. O'Brien follows:]

PREPARED STATEMENT OF ROSEMARY G. O'BRIEN, PRESIDENT,
MILITARY MARKETING LLC

Thank you for your invitation to speak to the Committee about the military and the prepaid card industry. My name is Rosemary Grace O'Brien. I have a Military Marketing practice located in New York City.

I would like to briefly summarize my background which qualifies me to speak with you today. My professional career is deeply rooted in telecommunications. It began back in 1981 with work performed for NY Telephone. It continued uninterrupted with major and on-going assignments from NYNEX, Southern New England Telephone, Southwestern Bell, and a handful of telecom start-ups made possible by divestiture in 1984. Eventually in 1997 I joined AT&T for a period of 7.5 years. That experience is most relevant to your agenda today.

My work at AT&T was as General Manager of their worldwide Military business. To be clear, not mission critical communications, rather my team and I had the responsibility of providing *Personal* Telecommunications Services—in-room phone service in barracks, dedicated public payphones on military installations in 18 coun-

tries, on larger U.S. Navy and Coast Guard ships, and in Forward-Deployed locations, such as Bosnia and Kuwait, and eventually Iraq and Afghanistan.

My job was to make sure Soldiers, Sailors, Airmen, Marines, and Coastguardsmen were aware of the special plans and programs AT&T built just for the military, how they could access them, and the best methods to pay for them. My mission was to be sure that servicemembers always had a way to call home, to reach family and friends no matter where they lived or served our country. At its peak, the business comprised 11 “platforms” with prepaid cards representing just one of them. AT&T secured the right and obligation to provide these services through contracts it won in several competitive bidding processes conducted by the Military Exchanges. It spent millions of dollars of capital building out infrastructure, and millions more educating the military community through informative advertising, in-person briefings, and other methods to build awareness of all products and services.

You probably already know that servicemembers are intense communicators. They spend more on communications than the average American. Much more . . . The ability to talk to loved ones is a critically important quality of life issue, to their sense of well-being and the peace of mind of their families. Let’s face it, military life can be lonely, and dangerous. Separations from family and friends are especially difficult. So while it is still possible to write letters, and today, to send and receive e-mails, there is just no substitute for the human voice. Communications is essential and that fact will never change. That’s the key reason why prepaid cards are so essential in the military.

The second reason, is equally as important, but completely practical. First, think back if you can, to when there were no prepaid cards or cell phones, how did you pay for a call when you were away from your home or office? Either you deposited change into the payphone, or if you were lucky enough to have home phone service, you could get a special calling card—a subscriber card—that allowed you to charge payphone calls to your home phone bill. If you were desperate or didn’t care what it cost, you paid with a credit card.

Well cash is impractical for long distance calls, especially from foreign countries. Credit cards are not an affordable option. Subscriber calling cards are helpful, but they come with some limitations.

First, you need to have a home phone to get one. Soldiers who live in tents, in barracks, on ships, or overseas, do not necessarily have a U.S. home phone.

Second, the cost of aggregating the call data related to your card, so the carrier can render and collect a bill, needs to be built into the cost of each call.

Third, a calling card does not have a mechanism that allows the user to understand how much he is spending, or has already spent this month.

Prepaid cards became popular in the military, and remain so today, because prepaid cards effectively address all of these issues. Anyone can buy a prepaid card. Prepaid cards makes calls cheaper than calling cards. And prepaid cards enable the service member to budget himself.

In the military, service members mostly buy cards at their military exchanges. Troops have a fairly sophisticated understanding of how to use the card so that they get the most from it. For example, generally speaking, when a card is used to call back to the United States from a foreign country, multiple units, or minutes are deducted for each minute of talk time. No surprise, international calls are more expensive. Multiple minutes is a way to recover the true cost of the call. Troops know this. Servicemembers recognize that, whenever possible, they should use the Defense Secure Network when calling the U.S. from a foreign country, because this enables them to get a “free ride” back to the U.S., where a domestic operator helps them place a call and their minutes are deducted one for one, as if the call originated in the U.S.

The Military Exchanges recognized the need for prepaid cards and have done an excellent job of procuring cards for service members. That’s why the cards that the Exchanges sell have the lowest rates from the countries that military people call from the most—Iraq, Afghanistan, Germany, Italy, Japan, etc. And their high value cards offer a better rate to servicemembers than the big box retailers who dwarf them in size. I believe the cost of a payphone call from Iraq to the U.S. is about 16 cents per minute. I cannot make a call from one side of Manhattan to the other for that little money, using a card I bought at Sam’s Club or Wal-Mart, or another big box retailer.

Every retailer, when he buys the prepaid cards that will be sold in his store, considers his customer base; and as prepaid cards are typically custom-built, he builds his prepaid cards to satisfy his audience. And he sets the retail price for the cards he sells. That is sometimes where the trouble comes in. If a card that is built to be optimal (lowest) for calls from the U.S. to Mexico, is used to make a call from the U.S. to Korea, chances are good the call to Korea will be unexpectedly expen-

sive. Or when a patriotic-minded American goes to his favorite big box retailer, buys a card made by a reputable carrier, and sends it to his grandson in Iraq, it is important to know that card, made by a reputable company will never offer as good a deal as the card that the Military Exchange sells to that soldier. And that soldier may complain to his wife about how little talk time he received from grandpa's card compared to his Exchange card. And his wife, frustrated at her circumstances and missing her husband and the father of her children, may write you a letter complaining about how that reputable carrier is ripping off soldiers. But it is just not true . . . because it is likely that the card that grandpa sent was never meant for international inbound calls. But that does not stop them from writing their Congressman, or their local newspaper, or tv consumer advocate. I handled many of these complaints in my tenure with AT&T. Those kinds of stories should not ordinarily be a cause for overreaction on your part.

However, I do encourage you to look closely and carefully so you can distinguish *the needs* of the reputable carriers who do an excellent job of making full disclosure, from the bottom feeders in the prepaid industry who have the ability to give the product or its maker a bad reputation. They prey on ignorance and inexperience, by deliberately tricking out their cards with inordinately short expiration dates, or come-on rates for one country with very high rates for *all others*, or very low-advertised rates that come with high, one-time surcharges. Their goal is to produce a product that allows them to enjoy very large, gross profits. I, for one, would support your carefully constructed plans to reign in prepaid chicanery, but would complain strongly about any Band-Aid attempts that do not fully consider the underlying elements of the prepaid business.

Thank you.

Senator NELSON. Ms. Acampora, the joint Federal-State slamming enforcement regime is often mentioned as a good example of a Federal-State partnership. Do you think that the model of Federal rules within the joint Federal-State enforcement regime works in this prepaid calling card scam?

**STATEMENT OF HON. PATRICIA L. ACAMPORA,
COMMISSIONER, PUBLIC SERVICE COMMISSION, STATE OF
NEW YORK; MEMBER, COMMITTEE ON CONSUMER AFFAIRS,
NATIONAL ASSOCIATION OF REGULATORY UTILITY
COMMISSIONERS**

Ms. ACAMPORA. I think that, yes, it will work, and your legislation we believe is very well put together—we added some thoughts in our testimony that I have given to the Committee on this—but your bill allows your constituents to continue to use and exploit existing State enforcement mechanisms. As we know, State Government is a little bit more convenient to relate to rather than the Federal Government because of geography and also time changes between Washington and the various states. As you know, California usually has a problem with a lot of complaint litigation because of the time differences.

It also helps, I believe, in times where the economy is so stretched. It enables the Federal Government and the State government to leverage scarce resources and join together to be able to do that.

And of course, it is always nice to leave our State “cops” on the beat which can only maximize the odds that the bad actors will be punished and will be caught expeditiously. And I think that in the future, with your bill, the bad actors will face more enforcement—because of this state cooperation, and your constituents will get their grievances addressed quite quickly.

And I think that the FCC has and continues to coordinate well with our national association of regulators which is called NARUC,

and the members of NARUC on these issues. And the FCC—I'm talking about slamming enforcement—helped coordinate and it works with NARUC. It has conference calls.

And I think in speaking to the Chairman from the FTC, that the FTC has set up a similar task force on these issues as was set up with slamming with the states at the FCC. This will work quite well. And we really do look forward to working with the FTC as presently right now, there is more of a coordination with the Attorneys General, and I think it would help and assist if NARUC was also reached out to and could participate as a member of that task force.

Senator NELSON. Is that organization something that could help us on State registration requirements and bonding requirements?

Ms. ACAMPORA. Well, we certainly would have—we have the staff and we have the ability to work with you to let you see what the various states have on the books. Right now, we have a few states that do have legislation. California has laws. New York certainly does, and some other states still do not. So I think it would be important that NARUC provide you with a lot of information that would make your job a little bit easier.

PREPARED STATEMENT OF HON. PATRICIA L. ACAMPORA, COMMISSIONER, PUBLIC SERVICE COMMISSION, STATE OF NEW YORK; MEMBER, COMMITTEE ON CONSUMER AFFAIRS, NATIONAL ASSOCIATION OF REGULATORY UTILITY COMMISSIONERS

Introduction

Chairman Inouye, Vice Chair Hutchison and Members of the Committee, I appreciate the opportunity to testify today on consumer protection in the prepaid calling card market. This is an important piece of legislation for your constituents. I thank you for calling this hearing and commend Senator Nelson, the sponsors of the bill, and the Members of this Committee for your leadership on this important consumer issue.

My name is Patricia Acampora. I am a Commissioner of the New York State Public Service Commission and a member of the National Association of Regulatory Utility Commissioners' (NARUC) Committee on Consumer Affairs. NARUC represents the State utility commissioners in each of your states and the U.S. territories that have oversight responsibilities over *all* the critical utility infrastructures—telecommunications, energy, and water. NARUC has not yet established a specific position on national standards for prepaid calling card services, but we do have well-established positions on specific issues raised by the Prepaid Calling Card Consumer Protection Act of 2008 (S. 2998).

As early as July 31, 2002, the NARUC Board of Directors adopted a resolution indicating that "consumers of all telecommunications services" should "receive clear and complete information regarding rates, terms and conditions for services." In July, NARUC's Committee on Consumer Affairs convened a panel on prepaid cards at our Summer Meetings in Portland, Oregon, which I moderated. The panel, which focused on existing State initiatives, was widely attended. You can expect that NARUC and its members will continue to be active on these issues. Shortly before that panel discussion, NARUC did an expedited informal survey finding that 18 of 30 responding NARUC member commissions handle complaints about calling card services. State oversight and interest in this industry segment comes at multiple levels.

Several entities are involved in providing these services. Telephone companies are responsible for the telephone lines that carry calls. Resellers buy telephone minutes from the telephone companies and "resell" them to end-users. Issuers set the card rates and provide toll-free customer service and access numbers. Finally, there are the distributors and retailers. Companies that fall into one or more of the first three categories frequently require certification from many of NARUC's member commissions. But even where a State commission lacks authority, they frequently attempt to resolve complaints informally or cooperate with other State agencies, *e.g.*, the State Attorneys General, on enforcement efforts.

Fraud and Abuse in the Prepaid Calling Card Market

Many Americans rely on prepaid calling cards to complete intrastate, interstate, and international calls. Analysts believe the main victims of abuse in this market are minorities, immigrants, the elderly, low-income consumers, members of our Armed Services, and others either not inclined or not able to adopt other communications options. It is widely acknowledged that fraud and abuse in this market is more prevalent than complaint data indicates.

My colleagues on the NARUC Consumer Affairs Committee report several issues with calling card providers, including: (1) the provider is either not required to seek Commission registration or certification or they have chosen to ignore that requirement; (2) the calling time provided is substantially lower than advertised; (3) the provider engages in misleading and false advertising by overstating achievable calling time or understating unit cost/rate; (4) the advertised rates expire after short “promotional period”; (5) the provider charges substantial undisclosed surcharges and fees; and (6) the card expires within a short period following the completion of the initial call.

Prepaid calling cards present the usual enforcement challenges for State authorities. As mentioned earlier, frequently providers are headquartered in another jurisdiction and fail to register or seek certification from a State commission (in states that require such certification) or even register an agent for service of process under so-called State long-arm statutes. Moreover, most often, even in states where certification is required, the most easily located entity in the marketing chain—the retail store—is not subject to State Commission oversight.

New York’s Public Service law provides consumer protections which have allowed my Commission to help assist customers with calling card complaints. Some of those complaints are related to completion fees that deplete the card faster than the consumer could have realized. Another common complaint we receive is from consumers who have a defective card that does not allow him or her to complete any calls, and want reimbursement from the card provider, or who are trying to contact the service provider for general customer service issues. Consumers also frequently complain of call completion fees they did not discover until using the card. Both New York’s law and S. 2998 require some information to be printed on the calling card, information on the rates and fees. This is a logical step; if this information is more readily available, it can stem the tide of customer dissatisfactions caused by inadequate disclosures. But there is a problem. Some disclosures now are often printed on the packaging material—material which is discarded almost immediately by the consumer.

Although NARUC has no specific position on this problem, I do have some suggestions. In lieu of printing information related to rates and fees on the card packaging, I would like to suggest two options. Under the first, the service provider is required to include all rates and fees on a piece of card stock included with the calling card when sold. This card would be the same size as the calling card and would have the phrase “**CONSUMER: DO NOT DISCARD**” printed on both sides in 14pt, boldface type. Another option, less useful to those without Internet access and is referenced in Section 3(a) of the bill, is to require the service provider to print a web address on the calling card which the consumer could access to confirm the rates and terms preprinted on the typically discarded packaging. Even if a consumer does not have access to the Internet or is not Internet savvy, the consumer could provide the consumer complaint call center with the website which would aid the investigation and resolution of a complaint by relevant authorities.

State Enforcement of Federal Rules Proposed in S. 2998

The Prepaid Calling Card Consumer Protection Act of 2008 protects consumers by requiring the accurate and reasonable disclosure of the terms and conditions of prepaid telephone calling cards and services. As previously stated, NARUC has not formally taken a position on what Federal standards should be, but we have urged—albeit in other contexts—that consumers should receive meaningful disclosures about such services, and that states must be able to enforce any Federal standards using existing procedures and penalties.

There are many circumstances that explain why a consumer may not report a complaint. They may not know who to call or where to file a complaint. The value of the card may not justify the hassle of trying to get a refund or assistance. Also language skills and cultural barriers, particularly for recent immigrants, can make it difficult for some consumers to file complaints. There needs to be a proactive outreach effort to ensure consumers know that there are rules that protect them and how to seek assistance.

Many NARUC member commissions actively address calling card abuses. Several States, including Texas, California, and my home State of New York have laws specifying required disclosures, including notice requirements at the point of sale,

verbal disclosures at the beginning of calls, and a required warning 1 minute before a card is depleted. As in most consumer service matters, a small number of bad actors create the bulk of the consumer complaints. What troubles me is the negative impact those bad actors can have on the industry which is also comprised of many service providers that deliver quality service at reasonable prices. The reputable providers make up the heart of the industry and should embrace the rules proposed in S. 2998.

The fraud and inadequate disclosure problems which are the focus of this bill cannot be handled by market forces. The partnership established in Sections Six and Eight of S. 2998 recognizes that, under State procedures, consumer concerns can be addressed promptly, often through informal processes. Also, Section Eight effectively incorporates NARUC's general positions that (a) Federal rules should be "[a] floor, not a ceiling," as ". . . blanket preemption on consumer affairs will restrict consumer redress in the future," and (b) that ". . . consumers should *not* have to wait for Federal rulemaking every time a new issue arises."

S. 2998 recognizes that, even in those instances when minimum Federal consumer protection standards are appropriate, states must be allowed to enforce those standards and to adopt more specific standards where needed. This bill also provides states with flexibility in the method of enforcement. Section Six of the bill empowers a *State AG, PUC or other authorized State consumer protection agency* to bring civil action against a carrier that violates its provisions. This is wholly appropriate.

States vary on their method of enforcement. In some states consumer complaints may go to the Attorney General, in others complaints go to the PUC or another agency. The Federal Government should not dictate the agency or procedure for State enforcement. Such Federal dictates would require states to waste taxpayer dollars to shift resources to different agencies. In addition, such a change could only cause consumer confusion by changing the current contact State agency.

From an enforcement standpoint S. 2998 is a clear win for consumers because it not only establishes clear national standards, but it also couples those standards with coextensive Federal and State enforcement. NARUC does suggest one minor addition to Section 6(c)(5) to make clear that states can use existing administrative penalties as well as procedures to "enforce the provisions of the law of such state."¹ With this very minor change, the bill clearly ensures multiple "cops on the beat" protecting consumers from bad actors.

Conclusion

NARUC supports the jurisdictional balance struck in The Prepaid Calling Card Consumer Protection Act of 2008. As drafted, the bill provides consumers with increased national disclosure requirements and ensures strong enforcement of national standards by allowing states to enforce those standards. It also efficiently preserves existing State options for consumer relief.

Thanks again for the opportunity to testify. I look forward to your questions.

APPENDIX A

STATEMENT BY CHAIRMAN BARRY SMITHERMAN

PUBLIC UTILITY COMMISSION OF TEXAS

July 30, 2008

Executive Summary

On May 23, 2008, the Texas Attorney General filed the state's first enforcement action against a prepaid calling card company, Next-G Communications, Inc. The investigation which led to the enforcement action was done in conjunction with the Public Utility Commission of Texas, and determined that Next-G's calling cards consistently delivered only 40 percent of the minutes on international calls claimed in the advertising for the cards.

The results of the investigation show that Next-G inadequately disclosed the fees and charges associated with each call, reducing the number of minutes available for calling. The Texas Attorney General filed the enforcement action under the Texas Deceptive Trade Practices-Consumer Protection Act.

History

Beginning in 2004, staff from the Consumer Protection Division of the Public Utility Commission of Texas investigated whether calling card companies were following the advertising and disclosure requirements under the Public Utility Commission

¹ Specifically, Section 6(c)(5) should be revised to read: "to establish or utilize existing administrative procedures *or penalties* to enforce the provisions of the law of such state."

Substantive Rule 26.34. The initial investigation revealed that calling card companies were not following the Commission rule related to accurate disclosure of rates and charges on the card or at the point of sale. The Commission rule also requires that enforcement actions for fraudulent, unfair, misleading, deceptive, or anti-competitive business practices will be coordinated with the Texas Attorney General in order to ensure consistent treatment of specific alleged violations. Customer Protection notified the Texas AG's Office of the issues relating to the accurate disclosure of information to customers, and during the summer and fall of 2007, worked with the Texas Attorney General's Office to test the calling cards from Next-G Communications to determine the number of minutes that the cards provided.

During the investigation on the Next-G calling cards, Customer Protection staff made calls to numbers in Honduras and El Salvador using \$5 and \$10 calling cards purchased in San Antonio, which are typical of the calling cards purchased at convenience and grocery stores. Consumer Protection Staff made several different types of calls using different calling cards: "straight line" calls to the target phone numbers, where a call is made until it is terminated by the provider, five-minute calls, and 10-minute calls. When calls were made using the calling cards, a voice prompt is given at the beginning of each call stating the number of minutes available for each call. The minutes stated in the voice prompt were compared to that actual number of minutes received or to the minutes stated in a subsequent call using the same card.

The results of the investigation showed that callers often received less than half of the minutes advertised. For example, when calls were made to Honduras using the \$5 calling cards, the voice prompt indicated that there was 35 minutes of calling time. Callers received only 12 minutes for these calls. With calls to El Salvador using the \$5 cards, the first five-minute call would use up 18 minutes of calling time, and the first 10-minute call would use 25 minutes of calling time, as indicated by comparing the minutes stated on the voice prompt in subsequent calls.

Based on the results of the investigation, the Texas Attorney General filed a lawsuit asserting that Next-G engaged in false, deceptive and misleading acts and practices, specifically, not providing the minutes offered in the advertisements or voice prompt at the beginning of phone calls, and using advertising with vague, misleading, and confusing disclosures about fees and charges. The Attorney General requested that the defendant disgorge all money fraudulently taken from individuals and businesses, and requested a temporary and permanent injunction against Next-G selling cards that do not give all the minutes advertised or indicated in the voice prompt. The lawsuit is currently proceeding in State District Court in San Antonio.

Conclusion

Based on the investigation of the Next-G calling cards, it is obvious that some calling card companies mislead and confuse customers by including vague disclosures on charges and rates that dramatically alter the number of minutes available to a customer. Customers that use calling cards, especially for international calls, are generally immigrant or low income individuals attempting to contact families or friends. Calling card companies should be required to accurately disclose the fees and charges, rather than use incomplete and misleading language. By putting these precise terms up front, customers will be aware of what they are paying for, and can make better decisions in choosing their telecommunications needs.



California Public Utilities Commission
Headquarters Office: 505 Van Ness Avenue, San Francisco, CA 94102

Prepaid Phonecard Issues in California

by
Robert Haga
Chief of Staff to Commissioner Chong

Overview

- CPUC's Jurisdiction on Prepaid Phonecard Providers
- Consumer Complaints and Issues
- California Business and Professions Code
- CPUC's Enforcement Actions
- Pending Legislative Changes

Prepaid Phonecard Providers are Required to Register with CPUC

- Section 885(a) of the California Public Utilities Code requires any entity offering the services of telephone prepaid debit cards to register with the Commission unless that entity is already certificated by the Commission to provide telephone service.
- A wireline telephone carrier that has been certificated by the Commission to provide telephone service in California does not have to register separately as a telephone prepaid calling card provider.

3

Exceptions to Registration Requirements

- So long as these entities do not purchase and provide access to bulk time at a per minute cost, and/or have access to a switch so as to control rates in offering and administering prepaid calling card services:
 - Under Section 885 (b) (1) retailers who only provide a marketing venue for telephone prepaid debit cards do not have to register with the Commission.
 - Under Section 885 (b) (2) entities who are merely the printer of the cards for the prepaid service providers do not need to register with the Commission.
- Under Section 885 (c), telephone prepaid debit cards offered in a promotional manner shall not subject the provider to the registration requirement, unless the cards are issued in conjunction with the sale of telephone related goods or services.

4

Unlicensed Prepaid Phonecard Providers Subject to Fines

- Under Section 886 of the California Public Utilities Code entities that are required to register, but have failed to do so, and entities denied registration but that continue to offer telephone prepaid debit cards shall be subject to fines or other sanctions that may be ordered by the Commission.

5

Consumer Complaints and Issues

- Commission receives approximately 50 calls per year regarding prepaid phonecards
- Common issues include:
 - Service provider not registered with the Commission
 - Actual calling time provided substantially (by as much as 50% to 75%) lower than advertised
 - Misleading and false advertising by overstating achievable calling time or understating unit cost/rate
 - Advertised rates expire after short "promotional period"
 - Charging of substantial undisclosed surcharges and fees that quickly used up the balances in the prepaid phonecard
 - No live operator answering the toll-free customer service number
 - Customer service not provided in the language cards were advertised

6

Ca. Business and Professions Code

- **Section 17200** prohibits unfair competition including any unlawful, unfair or fraudulent business practice and unfair, deceptive, untrue or misleading advertising.
- **Section 17500** prohibits untrue or misleading advertising. Any violation of the provisions of this section is a misdemeanor punishable by imprisonment in the county jail not exceeding six months, or by a fine not exceeding two thousand five hundred dollars (\$2,500), or by both.
- **Section 17538.9** regulates the advertising and sale of prepaid calling cards and services.

7

Ca. Business and Professions Code

- **Section 17538.9** requires:
 - Any advertisement of the price, rate, or unit value in connection with the sale of prepaid calling cards or services to include any geographic limitation and disclosure of any additional surcharges or fees
 - Information to be legibly printed on a prepaid calling card, such as name of the company, toll-free customer service and network access number, authorization code expiration date, etc.
 - A company that sells prepaid calling cards and services shall make disclosures on the card and packaging, and the retail vendor shall make disclosures at the point of sale, regarding fees, minimum per-call charge, surcharges, and policies on recharge, refund and expiration
 - A company to maintain a toll-free customer service telephone number: with a live operator 24 hours a day, seven days a week; with sufficient capacity and staffing; and, provided in the language used in the advertising of the card
 - A company to provide a refund within 60 days to any purchaser of a card or services if the network services associated with the card or services fail to operate in a commercially reasonable manner.

8

Enforcement Actions

- The Commission's Consumer Protection and Safety Division (CPSD) enforces prepaid phonecard registration requirement through Cease and Desist directives. The Commission also sends enforcement letters to carriers doing business with unlicensed entities.
- Commission staff investigates consumer complaints, conducts testing of prepaid phonecards' disclosures, and has initiated a series of compliance measures that could ultimately escalate into a Commission Order Institution Investigation resulting in fines and penalties.
- CPUC also works jointly with the Ca. Attorney General (AG) in suing prepaid phonecard providers who mislead consumers and falsely advertise the available minutes in the phonecards they sell.

9

Pending Legislative Changes

- Assembly Bill 2885, sponsored by Assembly Member De La Torre would authorize the Commission to enforce the standards and requirements in Business and Professions Code 17538.9.
 - This would enable the Commission to undertake prosecutions of certain violators independent of the Attorney General and enable us to target violations by small prepaid calling card providers that do not warrant high priority attention by the Ca. Attorney General.
- Status of the Bill: Passed by the Assembly; currently in Senate Appropriations Committee

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Pending Legislative Changes

- Assembly Bill 2136, sponsored by Assembly Member Mendoza, seeks to amend Section 17538.9 of the Business and Professions Code. AB 2136 would:
 - Require an advertisement of the price, rate, or unit value in connection with the sale of prepaid calling cards or services to clearly and conspicuously disclose any geographic limitation and all ancillary charges and conditions.
 - Require that, upon a rate increase at the time of recharge, the customer be informed of that increase prior to the customer agreeing to pay for the recharge.
 - Require that disclosures, which are to be printed legibly on a card or packaging, be readable without having to open the packaging, and require that information to be current.
 - Prohibit a person from offering or selling any prepaid calling card or prepaid calling services that do not contain the information required to be disclosed on the card or packaging, and would require a distributor that sells directly to a retail vendor to provide the vendor with the current information required to be displayed by the vendor.
 - Require a company that sells prepaid calling cards and services to provide a voice prompt at the beginning of each call that states the number of minutes that are available for that call.
 - Require a refund based on the failure of network services associated with prepaid calling cards or services to be made within 30 days.
- Status of the Bill: Passed by the Assembly; currently in Senate Appropriations Committee

11

Contact Information

- Consumer Complaints: **1-800-649-7570**
- Consumer Info.: www.calphoneinfo.com
- CPUC: www.cpuc.ca.gov
- **Telco Fraud Unit: Chris Poschl**
- **Robert Haga: 415-703-3700**

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Senator NELSON. Senator Pryor?

**STATEMENT OF HON. MARK PRYOR,
U.S. SENATOR FROM ARKANSAS**

Senator PRYOR. Thank you, Mr. Chairman, and thank you for doing this.

If I may, I would like to direct my first question to Ms. Greenberg, and that is, out there in the marketplace, out in the field right now, if someone has a problem with a calling card, what do they do right now?

Ms. GREENBERG. Well, as has been mentioned, there are State regulators. I think I would probably call my state. I would tell consumers, as we do, to call their state Attorney General's Office or whoever runs their consumer protection division in the State. I would recommend they report a loss of minutes and money spent on these cards to the FTC as well. We know the FTC has been involved. And people do call us about the cards and complain.

I myself use the cards because I have friends. You know, I lived abroad for a period of time and I have friends who are abroad. And what I noticed is, when I lived abroad, the calling cards there actually deliver the minutes that are promised. Here the series of cards you buy at the five-and-dime typically are shockingly quick to subtract your minutes.

So I think that there are places that you can call.

I think there are very good possibilities for enforcement. I do think that the low barriers to entry do militate for a kind of bonding system that we need to have and some State legislation calls for that kind of thing.

Senator PRYOR. If someone does complain, say, for example, to their state Attorney General, or whoever does their consumer work—I think in Florida it is actually the Department of Agriculture—what remedy is available? Does he get his money back, or what does he get usually?

Ms. GREENBERG. Well, I think the satisfaction comes in complaining because the likelihood that you are going to get your money back on a \$2 card from state regulators at this point really has not proven very fruitful.

There are also class action lawsuits brought by attorneys. That is one way to try to distribute some money. But the money is going to be pretty negligible. So consumers are really left holding the bag.

Senator PRYOR. Have there been class action lawsuits on these cards?

Ms. GREENBERG. Yes. My understanding is there have been a couple of class action lawsuits on prepaid calling cards.

Senator PRYOR. Commissioner Acampora?

Ms. ACAMPORA. Yes.

Senator PRYOR. How many complaints do you all receive in New York? Do you track those? I mean, how is that working there?

Ms. ACAMPORA. Well, the complaints that do come in to our office we can track. We have an Office Of Consumer Services. But in the State of New York, they could be calling the Attorney General's Office on their own also. They could be calling the Consumer Protection Board. If they are in New York City, they could be using the consumer services in New York City. So it would be kind of hard to track all the various entities that consumers could use.

However, when you are dealing with a population that are immigrants and some do not speak English, I think most of the time people do not complain. They just suck it up and they lose the cost of the card. So it would be hard to estimate how many do not even call.

Senator PRYOR. Right. I am sure that is the case. Given the dollar amounts involved here, I think a lot of people probably simply do not call.

And let me ask all the panelists, if I may, your thoughts on whether you believe the Federal Trade Commission is doing enough and if you think Congressional action is necessary. Do you want to go ahead, Ms. Greenberg?

Ms. GREENBERG. Yes. We are certainly supportive of your bill, Senator Nelson, and Congressman Engel's bill as well. I think disclosure is critical, and it will be certainly helpful in at least, I think, diminishing somewhat the bad actors.

You know, I would go a few steps further in terms of—I have already talked about I think a bond should be put up. I also think there is an unconscionability factor here in the rates because, as we saw with your fantastic posters here, there is disclosure. It may be fine print, but there is disclosure. It is not always honest in terms of what you get. But *Black's Law Dictionary* defines unconscionability as, "unconscionability is generally regarded to include an absence of meaningful choice on the part of one of the parties to a contract, together with contract terms which are unreasonably favorable to the other party." Boy, is this an example of that.

So I guess I would push for something a little stronger. I have talked about that in my written testimony.

And also, you know, the ability to compare rates. That is a critical tool that consumers use. But these card sellers, the vendors, come in and out of the market. It is very hard. You know, you can go 1 week to your local store and buy one of these, and then the next week, this card is not there anymore. So we do not know who is behind these cards. I do not have a good feeling about the reputation of many of these companies. But I think we really have to get tough with them and start to learn who they are and allow consumers to compare rates between cards so then they can pick and choose and use the marketplace to make their choices.

Senator PRYOR. Mr. West, do you feel like we need legislation?

Mr. WEST. Yes, sir. We at The Hispanic Institute probably believe that the FTC has not done enough, and we do need legislation, sir.

Senator PRYOR. Commissioner?

Ms. ACAMPORA. Yes, I definitely think so. Your legislation is great. In fact, it has made us in New York look at what we already have, and I think we need to strengthen that.

But the legislation is—definitely you need the legislation. As a former legislator, I can tell you that.

Senator PRYOR. Ms. O'Brien?

Ms. O'BRIEN. Yes, sir. With regard to the portion of the market that I will call the bottom-feeding portion of the market, I think that you do need legislation. I would suggest strongly to you that you make clear who has the responsibilities for enforcement. Do

not put a little piece over here and a little piece over there because I think ultimately that will water everything down.

My own experience, particularly in military, is that frequently, to sort of harken back to your previous question a little bit, when people had an issue and they called the customer service line, the company was always very good about trying to resolve it. And frequently we found that a lot of their complaints were, frankly, pure misunderstanding on their part, with regard to how the system worked or what they were actually getting. They were very quick to jump the gun and believe that there was an issue with our company ripping off service members; but that was clearly not the case, once we were able to explain it to them. If there was at any point an irreconcilable beef, and they felt uncomfortable about it, we would either refund their money or give them an additional card if that satisfied them.

I think those kinds of issues are always going to be around. I do not think that legislation should in some way, shape, or form hinder the companies that are doing a good job, but for the bottom feeders, yes, I think legislation is necessary. But again, clear oversight as to who is responsible for enforcement.

Senator PRYOR. Thank you.

Mr. Chairman, thank you again for holding the hearing but also for your work on this issue because there really is some bad activity going on out there that we need to address. Thank you for your leadership on this issue.

Senator NELSON. Thank you.

Senator Thune?

**STATEMENT OF HON. JOHN THUNE,
U.S. SENATOR FROM SOUTH DAKOTA**

Senator THUNE. Thank you, Mr. Chairman, and I too want to thank you for holding the hearing today. And I appreciate all the witnesses making time to come up and testify. Although I missed the earlier panel, I know that Representative Engel in the House has a bill, has a great interest in this issue.

Calling cards are particularly important, I think, for recent immigrants and low income consumers who may not have access to other telecommunication services and, at the same time, may not have a lot of knowledge of the consumer protection laws, our language in some cases, how to register complaints against providers when those laws are violated. And because of this, I believe that violations of consumer protection laws in the prepaid calling card market are particularly egregious, and I am pleased to see that the FTC has recently undertaken actions to enforce those laws.

And I look forward to supporting proposals that ensure that consumers have the opportunity to acquire the necessary, relevant information when purchasing prepaid calling cards.

And I want to thank the witnesses for their testimony and their effort to protect our Nation's consumers.

And I want to just follow up and maybe drill down a little bit from what Senator Pryor asked with regard to legislation.

First off, I guess I am interested in whether you have seen any improvements in the prepaid calling card market after the FTC's recent actions.

Mr. WEST. We have done testing over the last couple months and we really have not seen any improvement in what is being promised and what is being delivered at this point. So we have no evidence of any improvement even though there is stuff going on with Attorneys General around the country, State legislatures, and this legislation being introduced. We have no scientific data to support that.

Senator THUNE. You talked about perhaps Congress acting in this regard. Is that a preferred approach to having states enact some sort of legislative framework and accountability at that level as opposed to having Federal legislation and oversight and a framework for addressing this? I mean, you said many of the states are acting—

Mr. WEST. Well, like what has happened in Florida where they have settled with some companies, the problem is they have only settled with 10 companies there. There are many other companies doing business there. And then that legislation and those efforts are restricted to Florida only. So you have the other 49 states still going about their business. So I think that while we welcome what is happening in the individual states, it would be a piecemeal effort.

Senator THUNE. How many states have taken steps in the form of a legislative solution?

Mr. WEST. Somebody here on the panel may have more information on it than I do.

We know that New Jersey has taken action in the legislature. We think the Attorney General Brown in California, Attorney General Cuomo are looking at this now. I know the District of Columbia is looking at legislation now. So we have been in contact with the Attorney General in Illinois also. So there is a lot of activity. We have recently been contacted by the City of San Francisco. So now it seems like some cities are getting involved also.

Ms. GREENBERG. If I can jump in. I think our preference from a consumer standpoint, consumer advocacy standpoint, is to have the Federal legislation require some sort of baseline disclosure, as S. 2998 does, and then allow the states to focus on companies that may actually be located there.

One other suggestion I had is that perhaps the industry needs to set some voluntary standards, which members of the industry can agree to. We talk about bottom feeders and we could maybe cast away some of the worst actors and get the industry to—

Senator THUNE. Is there any of that kind of self-policing going on today? I mean, does the industry have any sort of baseline voluntary requirements—

Ms. GREENBERG. I have not seen any evidence of that, but maybe others on the panel know.

Mr. WEST. I think, Senator, there was one company that ran into some trouble, and now they are trying to get everybody else onboard to deliver what they are promising. But I do not think that they did it out of altruistic reasons or anything like that. So I do not see it happening.

Ms. ACAMPORA. Senator, to your question about how many states are active. NARUC undertook a quick survey of its members on this issue; and of 30 respondents, the PUCs in 18 states had rules

and handled consumer complaints regarding prepaid calling cards. Eighteen states have legislation.

Senator THUNE. OK. And do the states who have enacted legislation—are they similar in terms of—is everybody taking a different approach to this? Is there any agreement, I guess, on kind of what a formula would be to—

Ms. ACAMPORA. I think that is really why the Federal legislation would be very helpful, and just going through the legislation, as I said previously, what we have set up in New York definitely could be strengthened by some of the ideas and some of the mechanics set forth in this legislation.

Senator THUNE. Is it the consensus pretty much of everybody on the panel that we do need some sort of Federal legislative action on this? Is that fair to say?

Ms. ACAMPORA. I think so.

Ms. GREENBERG. From our perspective, yes. Like a baseline, a set of sort of minimum standards for disclosure and other issues the bill addresses I think would be very helpful.

Ms. O'BRIEN. If I may, I would also like to add I think some consumer education would be extremely helpful to many people. If we make them smarter, they will not make the mistake of buying a bottom feeder's card is what it comes down to. And I am sure there has been a lot of that, but speaking for someone who had responsibility for the military for 8 years, we spent millions of dollars educating military consumers.

And to your question regarding self-policing, we had a standard within the company not to produce any form of card for the military consumer that could in any way, shape, or form be conceived or construed as deceptive. But nonetheless, when the Iraq War broke out, I had literally thousands of complaints that were borne out of, frankly, just plain ignorance of how prepaid cards work, why the rates are different from card to card, why a card purchased at the U.S. Post Office was different than a card purchased at Sam's Club or Wal-Mart or anywhere else.

So while enforcement is important, I think that we just cannot dismiss this as a bowl of Jello that is easily understood. It takes a little understanding. And for that reason, I would strongly recommend consumer education wherever we can.

Ms. ACAMPORA. Could I just piggyback on that? We recommended in our testimony that the packaging be changed because most people take the packaging, rip it up. I am not an expert on how you manufacture, but maybe providers could double the size of the card but allow it to be folded in half which would make it a little bit thicker. But currently holding onto that packaging is really key because that is what gives a lot of the information we in N.Y. need for enforcement to investigate. And certainly if they were buying it also through a website, there needs to be information on that website too, which would be helpful.

Senator THUNE. Very good. Thank you, Mr. Chairman.

Thank you all.

Senator NELSON. I want to go back to something that one of you said about the distribution of the cards through merchants. What do we do there? And as distribution technology changes and then eventually you are going to have virtual cards available on the

Internet, it is going to make enforcement harder. Ms. O'Brien, what do you think about all this?

Ms. O'BRIEN. You have virtual cards now. AT&T makes a virtual card available, prepaid cards available, to the military community through the military exchanges. You need only go to their website and plunk down your form of payment, whatever that might be, a credit card, military STAR card, and as a result, you will get e-mailed back to you the virtual PIN number that you need to make a call, along with all the terms and conditions that apply to that particular card.

Yes, it will complicate enforcement, to be sure. Again, I would come back to the notion of education as being something to help overcome some of the issues.

Senator NELSON. Does anybody else want to comment on that?

Ms. ACAMPORA. Thank you. I think again that you should include in the e-mail the terms and conditions to the customers if they purchased it online. But I think your bill does strike a very good balance, and you have specified disclosures for online services. And giving the FTC rulemaking authority with sufficient flexibility to address some new attempts to bypass some of those protections—I think you have to kind of work on that.

Senator NELSON. As we were talking and we had those examples up here of fine print and information that you really cannot read, we need to provide more information for the consumer to beware. But what is the practical way to obtain this?

Now, the language barrier is clearly a problem that we have already unveiled here. But rates and conditions are not printed on the card packaging. So some of you have suggested in your testimony either attaching a rate card to the calling card or listing a website address or a toll-free number. Talk about this.

Ms. O'BRIEN. Sir, I could tell you that AT&T cards frequently had, depending on the nature of the card and the size of the card and how it was going to be sold, and in order to make full disclosure, a separate leaflet inserted that had virtually all the terms and conditions on it. And I can tell you if you walked onto any military base, after service members bought those cards, what you would see are those leaflets all over the bottom of the phone booths. People just would not read them. And so that was when we really determined that we needed to educate people as to how to use them and how to be smart consumers when buying them.

I don't know how you get around that need for education issue with the vast majority of Americans. Still today grandpa buys a card for his grandson in Iraq, and it does not go the way he expected. And he bought it from the U.S. Post Office when he picked up his stamps, and he is angry about it. It is an issue. It is an issue honestly I am not quite sure you could address.

More information, of course, is always better, but it has to be information that is willing to be consumed. It cannot just be a 5-pound pile of something; it needs to be better than mice type that people are just going to throw on the floor.

Mr. WEST. Senator?

Senator NELSON. Mr. West?

Mr. WEST. One of the things when you buy one of these—we were talking earlier about the class action suit, and the thing is

you throw the card away. So there is no way of really reclaiming the money that you have lost. And I think that the Internet activity will—you know, if there are virtual cards and so forth, it will be easier to track your loss of money and compensate people who have been fraudulently dealt with.

But one of the issues is that these companies will—you know, if a consumer is educated, he will spend 3 months using a card and getting all the minutes that they want. And what the company will do is suddenly pull the rug out from under them and in the fourth month try to recoup a lot of the profits—you know, increase that profit margin. So if he thought he was buying a good card for 2 months, in the third, fourth month, he is not buying a good card.

Senator NELSON. Ms. Greenberg, in your testimony you say that the FTC ought to appoint a monitor to oversee the industry. How should that work?

Ms. GREENBERG. What we suggested is let us look at how well disclosure works. Your bill sets out some very good and strong requirements for disclosure. Give it a year. Let us have the FTC oversee how the industry is, if it is improving.

You know, I am concerned about the cards that you go in and get at the—I get them at the gas station. This is a \$6 billion industry. These cards do not deliver what they say they are going to deliver. The fine print tells you that you are being ripped off. You read it. You read it out loud. It is a \$2 card and 99 cents comes off the card each time you make a call. You do not have any money on this card. So we have really got to get a handle on how we are going to rein in what I think is really a colossal rip-off for so many consumers.

So what we are recommending is that the FTC come back, take a look and see how the disclosure has worked. I think disclosure will have a positive impact. Whether it will rein in sort of a level of fraud and scamming that is going on, particularly of folks who do not speak English, who have relatives overseas, who are not going to take any action, not going to take any corrective action—they are generally not going to be part of a class action lawsuit. They are probably not going to report this to the FTC. These are the people that I am most concerned about protecting, and I think the FTC could come back in, take a look at where we are in a year, and see whether these practices have been reined in.

Senator NELSON. A couple years ago when I got involved in preventing the fleecing of military members on payday loans with exorbitant interest that was being charged to service members—and we were able to pass that legislation—I heard all the way up to the Chairman of the Joint Chiefs of Staff about how military members were being hurt.

Now, I have not heard that commentary, which does not mean that it is not there. And I am curious, Ms. O'Brien. Do you think the Pentagon is aware of this particular fleecing that is going on of the military community?

Ms. O'BRIEN. Yes, sir. I think that they are. I think the order of magnitude of the problem in the military specifically may not be as large as you might think it is. Generally speaking, most cards that military people buy and use personally are purchased at their exchanges. The exchanges do a very good job of educating their

own consumers about the cards that they buy, why they are better than the cards they would buy on the outside, and in point of fact, why in the countries where military people use cards the most, they are the best cards you can get, bar none.

I would also add to that, though, that cards that come as gifts, of course, there will be some complaints about those cards because frequently those cards were never designed to be used in the military.

Third, I would add that the military is a very tight fraternity, and so 1st Sergeants are very, very scrupulous about making sure that their charges know exactly how to use cards, exactly what retailers to stay away from, exactly where they should be doing their purchasing of cards. But that is not to say that family members of military people are not affected by this problem because clearly they are. But generally speaking, the military itself—

Senator NELSON. You gave the example of a grandpa who wants to buy a card for his grandson who is deployed to Iraq or Afghanistan.

Ms. O'BRIEN. Yes. That was based on an actual experience where a veteran himself, a retired marine, had bought a card at his local post office for a grandson who was in Iraq, and he assumed that a card purchased at the post office would be a good card for that purpose. Of course, he was retired many years out of the service, not familiar with the current state-of-the-art. And actually in his time, he was lucky if there were pay phones, much less cards. So even though he himself was former military, he did not have the level of education that most military people have today. And for that reason, he purchased a card that was not well suited for a call back to the United States from Iraq.

Senator NELSON. Does anybody on the staff want to ask any more questions?

OK. Well, this has been most enlightening. Thank you. We are going to proceed with this legislation. Thank you.

And the meeting is adjourned.

[Whereupon, at 11:19 a.m., the hearing was adjourned.]

A P P E N D I X

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DECEPTIVE CLAIMS FOR PREPAID TELEPHONE CARDS AND THE NEED FOR REGULATION

Mark E. Budnitz*, Martina Rojo[†], Julia Marlowe[‡]

I. Introduction

The United States prepaid phone card industry is a multi-billion dollar industry. In 2002, prepaid long distance cards alone generated \$3.6 billion and the industry is estimated to grow significantly.¹ Growth in the market for prepaid phone cards is expected to continue, in part because sales are linked to the increasing use of cellular phones.² Already the bulk of convenience stores' general merchandise sales are for prepaid phone cards.³ In fact, one industry source reports that phone cards are the highest profit center in Walgreens stores after prescriptions.⁴

The cards are often promoted to niche markets consisting of college students, immigrants and certain businesses.⁵ According to Barry Catmar, Vice President of Operations for Digitac, "the large number of immigrants who call friends and relatives abroad is a perfect market for phone cards."⁶ The increase in the immigrant population in the United States, especially Latino consumers, has led to the marketing of some cards specifically to the Spanish-speaking consumer.⁷ As a result, the market for prepaid telephone cards is segmented and some groups of consumers are particularly vulnerable.⁸ There is evidence that consumers in the United States who use cards to call Spanish-speaking countries face much higher prices than expected due to hidden fees and confusing, contradictory and inaccurate information.⁹

In most states, there is little or no regulation of prepaid telephone cards. Thus most states do not require phone card companies to disclose essential information and substantive rights that ensure consumers receive satisfactory service. Consequently, information provided on the cards and by customer service representatives is often misleading or unavailable.¹⁰

Consumers have few rights, and even where consumers do have rights that are violated, it is often difficult for them to obtain a remedy. Additionally, because each card has a small monetary value, litigation is not always a viable option, especially if contracts include arbitration clauses and prohibit class actions.¹¹ For example, low-income consumers are likely to purchase cards that sell for less than \$10, rendering the apparent cost of using prepaid phone cards insignificant. Because of their low income, however, the cumulative cost may be significant.¹² Furthermore, many immigrants have no alternative if they need the cards in order to communicate by phone with their families in another country.

Given these conditions, the Federal and the state governments should consider passing legislation to regulate phone cards. On the Federal level, both the Federal Trade Commission (FTC) and the Federal Communications Commission (FCC) have done little to address the problems other than minimal enforcement of current inadequate regulations. The FTC has addressed few instances of deceptive advertising,¹³ and the FCC currently enforces the limited area of federally required fees on prepaid phone cards.¹⁴ On the state level, consumer protection varies greatly. Legislation is warranted unless (1) the market works and consumers acting reasonably are able to make efficient choices and protect themselves, (2) the loss to consumers is small and there are few reported consumer problems, and (3) market conditions are such that the industry can be counted upon to engage in effective self-regulation.

This article explores the need for legislation by reviewing a combination of approaches, including an economic analysis of the market for prepaid phone cards, findings from an empirical study of Hispanic phone card usage in calling Spanish-speaking countries, and the current law on this issue. The results of this investigation demonstrate a need for national regulation. We recommend that Congress enact a statute which mandates a minimum standard of protection and authorizes the FTC to issue regulations. Such a Federal statute would also contain disclosures, substantive protections, and consumer remedies. Additionally, states should be per-

mitted to enact requirements that provide more protection as long as they are not inconsistent with the Federal law. If Congress decides not to pass a Federal statute, state legislatures can easily adopt the features of our Model Prepaid Telephone Card Act.

II. Is Regulation Necessary? The Lessons from Economic Theory

Regulation is not necessary if consumers act reasonably and make efficient choices in the marketplace. Consumers can only make efficient choices if they are able to obtain the complete and accurate information needed prior to purchase without incurring excessive transaction costs. Such information may be contained in advertisements, in brochures accompanying the sale of the cards, on the packaging, or on the cards themselves. Another source of information is experience. Experience may come from the consumer's prior use of cards or from others, such as family and friends, who have used the cards. For the consumer to obtain enough information through experience, significant information search costs may arise, thereby raising the price of the product much like transaction costs. A consumer would incur significant search costs if he repeatedly paid for transportation to a store and spent money on a card that did not provide many minutes (though the advertising might state otherwise). Each time he must try a different card brand in order to find one that is cost-effective. However, he may be forced to try several cards before discovering a good card. Even then significant search costs continue if rates on the good card have changed.¹⁵

Theoretically, prepaid telephone cards come close to fitting the perfect competition model. Prepaid telephone cards are a homogenous product (consumers buy minutes), and there are many buyers and sellers due to the ease of entry into and exit from the market.¹⁶ However, in the perfect competition model, consumers have perfect information. Perfect information is rarely present, but consumers can typically search for information and make informed purchase decisions for many products.

The prepaid telephone card market is one where information could be made available to allow consumers to make better informed purchase decisions. Yet, investigations of the market indicate that either consumers cannot obtain information, or the information is inaccurate, contradictory or deceptive.¹⁷ Moreover, information is often not available from customer service, and consumers also may be misled by seller misconduct such as card issuers who sell defective cards.¹⁸ Consumers retain information from past purchase experience, but information from previous experience is likely to become outdated over time as terms and conditions of the cards change.

III. Problems Encountered by Consumers and Information Needed: Findings from an Empirical Study

Even if information is not available prior to purchase and customer service is inadequate, regulation may be unnecessary if prepaid telephone cards are inexpensive. In that situation consumers are able to learn what they need to know in order to avoid problems without incurring high costs. However, while each card is inexpensive, the unit price, or cost per minute, may be significant and consumers who rely on prepaid phone cards for many of their calls end up paying an excessive amount for telephone service. The prepaid phone card market has grown into a multi-billion dollar industry, and the cost to consumers as a group is tremendous, especially for certain segments of the population.

A qualitative study of forty-five Latino immigrants' experiences in an urban market in Georgia found that 78.7 percent of the immigrants complained about prepaid telephone cards.¹⁹ More specifically, consumers complained that they did not receive the number of minutes they expected and that customer service personnel could not be reached during available hours and often could not answer consumers' questions even when reached.²⁰ A follow-up study was conducted to verify these complaints.²¹ The follow-up study investigated the true costs of the cards and the information available from customer service.²² Minutes are often deducted for hidden fees, and consequently, consumers do not receive the number of minutes they are told are available. True cost is calculated by determining cost per minute using an accurate amount of minutes received.²³ In the study, over 250 prepaid telephone cards costing under eleven dollars were purchased and then used by bilingual data collectors to call Spanish-speaking countries from January until May 2004.²⁴

Before placing the calls, each data collector called the customer service number and asked a series of questions from a survey designed by the researchers.²⁵ Customer service personnel were asked about (1) the number of minutes the customer would have to call a specific city, (2) various kinds of fees that might be charged, (3) minute rounding, and (4) hours of customer service availability.²⁶ Data collectors then placed a call, using only one-half of the number of minutes that the recorded

message indicated was on each card.²⁷ This was done to ascertain if maintenance fees, hidden charges, or both were present.²⁸ After at least 1 week, a second call was placed to the same city.²⁹ The date and time were noted at the beginning and end of each call.³⁰ The number of minutes available was also noted.³¹ Each card was used until all minutes had expired.³² Calls were made to cities in Mexico, Colombia, Argentina, Peru, Spain, Uruguay, Guatemala, and Nicaragua.³³

The researchers computed expected cost by dividing the cost of the card by the initial number of minutes the consumer was told he or she had.³⁴ The actual cost of the card was computed by dividing the cost of the card by the actual number of minutes that a consumer obtained when using the card.³⁵ Cost was therefore computed as a unit price: cost per minute.³⁶ Findings from this research indicate that there is wide price dispersion with prepaid telephone cards.³⁷ The average actual cost of the cards was 87 percent higher than the average expected cost.³⁸

Data collectors also made three attempts to reach a customer service representative.³⁹ For two-thirds of the cards, it was possible to talk to a customer service representative.⁴⁰ The customer service representative answered on the first attempt for about one-half of the cards. For one-third of the cards, the consumers were not able to talk to a customer service representative, either because they were on hold for more than 5 minutes, no one answered, or there was only a recording.⁴¹ Furthermore, talking with a customer service representative was often not helpful.⁴² Although some customer service representatives were helpful, many times the customer service representative was not able to answer questions such as whether minute usage was rounded up or what fees were charged.⁴³

Subsequently, the researchers conducted an additional investigation of the information available on the cards.⁴⁴ One problem was that for some cards there was very little if any information about fees.⁴⁵ Another problem was that no standardized wording existed.⁴⁶ For example, in some instances a "service" fee appeared to be assessed per call much like a connection fee and in other instances what was called a "service" fee was assessed periodically in the same manner as a maintenance fee.⁴⁷ Additionally, the wording of some information was vague, such as the use of the terms "as may apply."⁴⁸ Stating that a maintenance fee "may apply" provides a warning for the consumer but does not tell the consumer if there is a maintenance fee or not.⁴⁹ Some maintenance periods are assessed after 2 days and others after 30 or 60 days.⁵⁰ A more serious offense was the use of contradictory or misleading wording.⁵¹ Many cards state that there is no connection fee but the fine print states that "connection fees may apply."⁵² Some brands of cards have no connection fee but they have a fee at the end of each call, called a "post-call" or "hang-up" fee.⁵³ Other information is also unclear and perhaps deceptive, such as information about taxes, pay phone surcharges and warranties.⁵⁴

More accurate information should be given on the number of minutes available when one places a call. When a consumer places a call, he or she is told how many minutes are available. However, a consumer typically does not receive all of those minutes.⁵⁵ Minutes are deducted for a variety of reasons such as connection costs and minute rounding penalties.⁵⁶ Determining the true cost per minute is unnecessarily complex because the consumer does not know how many minutes are deducted, and for which fees they are deducted.⁵⁷ The costs include activation fees, connection fees, minute rounding, extra pay phone fees, additional cell phone fees, charges even if no connection is made, maintenance fees, and service fees.⁵⁸ It would be helpful if companies provided information on which fees were applicable, even if the consumer would not know precise amounts.

Because of the great variation in the kinds of fees assessed, the difficulty in determining how the fees are assessed, and the lack of standardized wording, meaningful comparison shopping is impossible. Uniformity of information, disclosure and standardized names for fees would help consumers, much in the same way that nutritional labeling has provided a mechanism for uniform comparison. In some cases, outright consumer fraud may be present. Customer service representatives indicated that for some prepaid phone cards there were charges even if there was no connection. This is illegal in some states.⁵⁹ However, it was not possible to know if the consumer was charged for a call that was not connected.

IV. The Likelihood of Self-Regulation: The Nature of the Prepaid Phone Card Market

The third question addressed is whether the prepaid phone card industry can be expected to regulate itself. Self-regulation is probable when there are industry-wide standards available, the industry standards adequately protect consumers, and the industry is dominated by strong stable companies that are committed to those standards and can pressure other companies to comply.

Self-regulation is likely to occur if there are strict industry-wide standards. The industry's trade association, the International Prepaid Communication Association (IPCA) has adopted standards for its members.⁶⁰ One such standard requires that minute rounding be in 1 minute intervals.⁶¹ The problem is that there is no enforcement of the industry guidelines and no reason to believe that they are being followed by the majority of prepaid telephone card providers. According to Howard Segermark, Executive Director of the IPCA, only about 80 providers of the estimated 500 plus providers are members of the IPCA.⁶²

The IPCA standards are too limited to provide consumers with the protection that they need.⁶³ Even if the standards were satisfactory they could not serve as an adequate substitute for legal protections. For example, it is doubtful that the IPCA could pressure non-members of the association into complying with the standards unless the industry was dominated by stable companies who supported the IPCA standards. The prepaid phone card industry involves many different types of businesses such as: carriers, resellers, distributors, card issuers, and retailers. Absent rules having the force of law, compliance with voluntary standards is highly doubtful. Even if current businesses agreed to comply, someone would have to assume the responsibility to persuade the constant stream of new entrants who are enticed to enter the industry because of low start-up costs, and the general lack of compulsory registration or bonding, to comply with the standards. Additionally, even if the standards were satisfactory, there is no guarantee that they would not be changed without any prior notice to or input from consumer representatives. At the very least, contracts between issuers and consumers should incorporate the IPCA standards so consumers can sue in court for breach of contract if the issuers do not follow the standards.

Whether the industry can regulate itself hinges upon three factors: whether standards are available, whether they protect consumers, and whether the industry is dominated by strong stable companies. Although there are industry standards, they do not provide adequate protection for consumers because, as the empirical study indicates, the standards are not followed.⁶⁴ For example, information on minute rounding was available for less than half of the cards.⁶⁵ Of those for which information was available, slightly over half of the cards used more than 1 minute rounding.⁶⁶ Furthermore, the industry is not dominated by strong stable companies.⁶⁷ The fact that one can enter the market without incurring great costs means there are many providers. There is also evidence that the companies more likely to be considered stable, such as AT&T, MCI and Sprint actually cost more per minute than the other companies, and they do not give the consumer any better information than the lesser-known providers.⁶⁸ Our conclusion is that the industry cannot be expected to regulate itself.

Because of the problems consumers face in the marketplace and the dim prospects for adequate self-regulation, consumers need legal protection. The laws now on the books, however, fail to ensure that consumers receive the information, safeguards and remedies they require.

V. Adequacy of the Current Law

A review of current law demonstrates it is not adequate. No Federal law governs prepaid phone cards except the Federal Trade Commission Act (FTC Act).⁶⁹ It applies generally to all industries subject to FTC jurisdiction.⁷⁰ The FTC Act simply prohibits deceptive and unfair acts or practices.⁷¹ It does not require any disclosures and is not tailored to the needs of consumers who purchase prepaid phone cards.⁷² Rather, the Act only protects consumers from the most egregious conduct.⁷³ Because there is no private right of action, it protects only the customers of those companies against whom the FTC brings an action.

Most states have no statutes or regulations covering prepaid phone cards. Among the states that do regulate the cards, there is a great deal of variation in coverage and regulation ranges from minimal to comprehensive. However, no state adequately protects consumers.⁷⁴ Most states have laws prohibiting unfair and deceptive acts and practices in general.⁷⁵ While the laws provide for a private right of action,⁷⁶ many do not allow class actions,⁷⁷ which are crucial for cases involving purchases of inexpensive items. Also, the state laws suffer from the same deficiencies as the FTC Act.

Consumers may be able to attack the agreement between the seller and the consumer through general contract law avenues. For example, if the card does not work, or if there is no access number or authorization code, the consumer can claim failure of consideration. If the contract is too one-sided, a court may find it is unconscionable, but the doctrine of unconscionability has limited usefulness.⁷⁸ Contract law is totally inadequate to protect consumers because it only provides a remedy for rights that the contract grants to consumers.⁷⁹ Such contracts, one-sided agree-

ments presented by the card seller on a take-it-or-leave-it basis, impose few obligations on card sellers.⁸⁰

VI. Should Phone Cards Be Regulated at the State or Federal Level?

Strong arguments can be made to support both the position that regulation of phone cards should be through Federal law and the contrary position that it should be through state law. We recommend a combination of both state and Federal legislation. A consideration of the merits of legislation if it were administered either by the states or by Congress illustrates the issues that inform our proposal.

Despite the fact that most states are not eager to tackle this problem,⁸¹ several factors indicate that state regulation might be superior to Federal regulation. State regulation can be tailored to the needs of that state's residents. For example, a state with a large immigrant population may want to enact more protective rules than others. This would be justified because many card sellers specifically target low-income, non-English speaking groups that may be especially vulnerable to unfair practices.⁸² Such a state may want to enact bilingual disclosure requirements, with special attention given to international calls. That state may also feel a need for strong substantive protections, such as rules guaranteeing a right to redeem unused value and setting a minimum time to use a card before it expires. Because of the tenuous or non-existent legal status of many consumers targeted by those who market phone cards, they often refuse to sue companies that engage in illegal practices or to complain to government agencies.⁸³ Special rules tailored to meet the needs of particular immigrant populations would have a better chance of being included in state law than in Federal legislation since lawmakers from states without large immigrant groups may not recognize or understand the importance of protecting them.

In addition, states have administrative agencies with expertise in drafting regulations and enforcing rules related to telecommunications.⁸⁴ Some states give the agencies crucial regulatory roles apart from issuing regulations. For example, in Illinois and Florida, providers of prepaid card services and resellers must receive a certificate of authority from a state agency.⁸⁵ Retailers selling the cards must have proof that the provider or reseller has obtained the certificate.⁸⁶ It is unlawful for companies to fail to comply with these requirements.⁸⁷

On the other hand, Federal legislation has several advantages over state regulation. The most obvious benefit is complete national coverage.⁸⁸ Another benefit is uniformity.⁸⁹ Complete and uniform national coverage helps both the industry and consumers. Many phone card companies sell cards in many states. Having one set of rules greatly lessens their regulatory burden. Furthermore, many companies sell cards on the Internet. A uniform set of rules greatly eases their regulatory burden since they are selling to consumers nationwide. The phone card industry may mount less opposition to a Federal law than to state laws because of the advantages of having to comply with only one law. They may actually support a Federal law in the belief it would discourage the majority of states that have not yet regulated phone cards from enacting their own laws.⁹⁰

In addition, uniform disclosures, standardized terms, and the same rights help produce educated consumers. This is especially important given the high mobility rates of people who live in the United States.⁹¹ Most will live in several states during their lifetimes. With a Federal law, they do not have to learn a new set of rules and definitions every time they move to a new state.

A Federal rule may also lead to more effective enforcement than state law. An individual state may have great difficulty enforcing its laws against companies operating from different states, especially those selling on the Internet. Jurisdictional issues may frustrate enforcement.⁹² Enforcement by a Federal agency would obviate many of these difficulties.

Lacking a Congressional mandate, no agency of the Federal Government has stepped forward to regulate this industry. Prepaid phone cards are payment devices.⁹³ The Federal Reserve Board (FRB) has substantial experience regulating payment devices, but lacks experience regulating the telecommunications industry.⁹⁴ Drafting regulations and enforcing them is better suited for an agency familiar with that industry. Prepaid phone cards provide access to telephone service. The agency with the most expertise in telecommunications, the FCC, has no experience dealing with payment devices. The FCC simply refers consumer complaints to the FTC, the Better Business Bureau, and state agencies.⁹⁵ Moreover, any Federal agency to which Congress delegates the responsibility for regulation would not be as attuned to local problems as are state agencies.

Although the FTC does not have a great deal of technical expertise in telecommunications, its Telemarketing Sales Rule indicates it is able to draft effective regulations related to telephone use.⁹⁶ It has brought enforcement actions against companies offering prepaid cards.⁹⁷ If Congress enacts Federal legislation to regu-

late prepaid phone cards, we believe the FTC is the most appropriate agency to issue regulations and enforce the Act.⁹⁸

As the above discussion demonstrates, there are substantial benefits to enacting legislation, either at the state or the Federal level. As we discuss in Part XI, we recommend that Congress enact Federal legislation. The Federal law, however, should not completely preempt state law. States would still be permitted to enact legislation tailored to the special needs of their consumers as long as that state law did not conflict with the Federal statute.⁹⁹

VII. Analysis of the Nature of Phone Cards and Implications for Drafting Applicable Law

In order to understand current laws regulating phone cards and draft a Model Act, it is necessary to determine the nature of phone cards. In part, the card is a payment device. It is a type of stored value card like a prepaid gift card.¹⁰⁰ But it is also a device that accesses a service. In this respect it is analogous to an ATM card that is used to access the financial services provided by ATMs.¹⁰¹ The prepaid phone card, however, is an integral part of a transaction for the provision of telecommunications services, a very specific type of service.¹⁰²

The fact that phone cards can be characterized in a variety of ways poses difficulties for evaluating current laws and choosing a body of law that may be appropriate for a Model Act. There is no general body of law governing stored value cards. Instead states have enacted laws that are very specific to the type of card regulated (gift card, phone card, payroll card), and there is great variation among the statutes governing each type of card. The phone card is used to access a service and there is no general law governing the sale of services. Those transactions are subject to the common law of contracts.¹⁰³ Therefore, the "law" is determined by what the particular contract provides. Like an ATM card, the phone card accesses a service that can result in using the consumer's funds. Because of that similarity, it may be appropriate to use the Electronic Fund Transfers Act, which governs ATM cards, as a model.¹⁰⁴ Indeed, the FRB recently has subjected another type of stored value card, the payroll card, to the same laws as ATM cards.¹⁰⁵ Because phone cards access telecommunications services, some states incorporate selected aspects of their rules for those services.¹⁰⁶

VIII. Analysis of Current Regulation

This section analyzes the current regulation of phone cards. The analysis illustrates the wide variety of problems some states have chosen to regulate. It also demonstrates that states have not selected any uniform approach to regulating the cards. Finally, it shows that they have not used regulation of other devices, such as gift cards or ATM cards, as models for their phone card laws.

There is no uniformity in the state law regulating phone cards. States have taken a wide variety of approaches. Some have imposed minimal regulation, while others subject the industry to many specific requirements.¹⁰⁷ Some have enacted statutes, while others have issued agency regulations.¹⁰⁸ However, as Part IX discusses, even the most comprehensive state laws completely ignore major issues.

Recent studies¹⁰⁹ demonstrate the need for adequate disclosure and for clearer explanations of the costs involved in making calls. Consumers need disclosures before they purchase cards in order to decide whether to buy a card and to compare prices among cards. The studies show, however, that cost of the card is a very complex matter. Consequently, consumers need standard terms that have a universal meaning and a standard format for presenting information, much like Truth in Lending. In addition, these studies show that consumers need access to customer service representatives who can answer specific questions and explain costs.¹¹⁰

The first point of consumer contact and often principal marketing effort is advertising. Generally, advertisements do not provide as much information as is already available on the cards. Advertisements typically state the number of minutes one obtains when calling a specific city, such as Mexico City. However, advertisements may also be misleading. For example, they may state that no connection fees are charged,¹¹¹ when in fact, there are many other hidden fees. Despite its importance, the Federal Government has not enacted rules regulating advertisements of prepaid phone card services.¹¹² Additionally, the FTC has not aggressively enforced violations of the FTC Act in this area.¹¹³

Consumer economic literature indicates that information from advertisements is often used by consumers in establishing reference prices.¹¹⁴ These reference prices are then used at the time of purchase.¹¹⁵ Misleading advertisements may negatively affect the consumer's purchase decisions. The FTC Act and state laws require ads to be truthful and not misleading, but consumers need more legal protection than merely a law that provides that an advertisement not be misleading. Consequently,

consumers need advertising provisions similar to those enacted in California, which is currently the only state with a statute specifically regulating the advertisement of phone cards.¹¹⁶ California law requires that any such advertisement “include a disclosure of any geographic limitation to the advertised price, rate, or unit value, as well as a disclosure of any additional surcharges, call setup charges, or fees or surcharges applicable to the advertised price, rate, or unit value.”¹¹⁷

On the other hand, a law requiring advertisements to include certain information is not sufficient either. Some consumers purchase cards without seeing an advertisement. Others who see ads also need information at the point of purchase. Such consumers may not remember the information in the advertisement, or they may remember it incorrectly. Furthermore, consumers need much more information than any advertisement could adequately convey. As a result, many of the states that regulate phone cards require disclosures at the point of purchase.¹¹⁸

Most states that regulate phone cards require very specific information to be disclosed on the card itself. One could argue that these laws are much too detailed, and that consumer choice in this competitive market should determine what information should be disclosed. However, the information that states require to be disclosed at the point of purchase reflects the problems consumers have encountered using the cards. The seller must print the name of the company on the phone card.¹¹⁹ Consumers need this information in order to contact the company when necessary, to complain about the company to law enforcement and to sue if a dispute cannot be resolved. State laws require the seller to print a toll-free customer service number on the card as well.¹²⁰ As studies show, consumers of this product need access to customer service.¹²¹ They often have reasonable questions, given the nature of the services provided. Because of the low cost of each card, requiring the seller to provide a customer service number that is not toll-free would discourage consumers from contacting customer service.

Some state laws also require the card seller to disclose a toll-free network access number if such a number is required in order to access service.¹²² Fundamental fairness requires the seller to inform the consumer of that number. For the seller not to disclose it would amount to fraud as the seller would have the consumer's money, but the consumer would not have any service. Requiring the number to be toll-free is justified because the access number merely permits the consumer to gain access to the system. Charges should not be imposed unless and until the consumer actually makes a call. The card also must disclose the authorization code if it is required to access service.¹²³ As with the requirement that the card contain the access number, failure to disclose the authorization code would be fraudulent since the consumer would have paid but would then be unable to make any calls.¹²⁴ Finally, states require the card to include the expiration date or policy, if any.¹²⁵ In California, Florida, Missouri, and New York, cards that do not include this information are considered to be active for at least 1 year from the date of purchase or the date of the last recharge.¹²⁶ In the State of Washington, if an expiration date is not disclosed on the card, it is considered “unexpired indefinitely.”¹²⁷

Other disclosures must be made either on the card or the packaging that comes with the card. It is necessary to give card sellers this choice because phone cards are small and all the required information may not fit. The manner of presentation is also important for disclosure to be meaningful. California, for example, requires the disclosure to be legible.¹²⁸ In addition, the required information must be made “available clearly and conspicuously in a prominent area immediately proximate to the point of sale of the . . . calling services.”¹²⁹ In Florida, if disclosures are not on the card or packaging, they must be displayed “visibly in a prominent area at the point of sale . . . in such a manner that the consumer may make an informed decision prior to purchase.”¹³⁰

In California, the required disclosures on the card or packaging include the “value of the card” as well as any surcharges, taxes or fees.¹³¹ The California statute provides a list of fees, illustrating the complexity of the product's pricing, and how sellers use a variety of different terms, all of which amount to additional cost to the consumer.¹³² Further, there are different requirements for disclosing surcharges for international calls.¹³³ The seller also must disclose the minimum charge per call, the billing decrement, the recharge policy, if any, and the refund policy, if any.¹³⁴

There is no national uniform format for disclosures on phone cards, unlike disclosure for credit and debit card transactions.¹³⁵ California, however, has tried to impose some uniformity on cards sold to consumers in its state.¹³⁶ The statute requires the value of the card and the amount of the charges to be disclosed on the card or its packaging all in the same format.¹³⁷ Moreover, if the value of the card is expressed in minutes, those minutes must be designated as either domestic or international.¹³⁸ Finally, that designation must be printed on the same line as the value of the card in minutes or on the line immediately following.¹³⁹

In addition to written disclosures at the point of sale, Texas requires verbal disclosures at the beginning of each call.¹⁴⁰ The consumer must be told the “domestic minutes, billing increments, or dollars remaining” on the prepaid account or card.¹⁴¹ In addition, when the balance on the credit card is almost depleted the company must provide a verbal announcement of that fact “at least 1 minute or billing increment before the time expires.”¹⁴²

California law recognizes that many sellers target specific ethnic groups.¹⁴³ It requires that if a language other than English is used in the advertising or promotion of the card, or is used on the card or packaging (other than for dialing instructions), the required information on the card or packaging must also be disclosed in the language used to advertise or promote the card.¹⁴⁴ If a language other than English is used on the card or packaging to provide dialing instructions for making a call or reaching customer service, the additional information required on the card or packaging must be disclosed in the language used to provide the dialing instructions or to reach customer service.¹⁴⁵ Similarly, Texas requires that if a card is marketed in a language other than English, certain disclosures must be made in the same language.¹⁴⁶ Bilingual cards are permitted as long as all of the required information is in both languages.¹⁴⁷

Laws which require sellers of prepaid telephone cards to provide a toll-free telephone number for customer service, and which establish requirements for that service are perhaps unique in the law of payment systems. If a person pays for goods and services with a check, the Uniform Commercial Code (UCC) does not require banks to provide any kind of customer service despite the importance of the financial services they provide.¹⁴⁸ If the consumer pays using a credit card or debit card, Federal law imposes certain error resolution procedures, but the seller of such cards is not required to provide a phone number for contacting the seller.¹⁴⁹ The seller is required only to resolve disputes, not provide information.¹⁵⁰ Phone cards are a type of stored value card. Many states regulate another type of stored value card, the gift card, but no gift card laws require sellers to provide consumers access to customer service, much less toll-free access.¹⁵¹ Thus, those states having phone card laws requiring the seller to provide a toll-free customer service number are going beyond what is normally mandated in consumer protection legislation.¹⁵²

Requiring the seller to disclose a toll-free customer service number does not help consumers unless informed customer service representatives are available to answer the consumers’ questions. The studies discussed previously illustrate the difficulties consumers have obtaining needed information from customer service.¹⁵³ States vary in the degree to which they impose quality standards for customer service. California and New York have the most consumer-friendly requirements. The seller’s customer service line must have live operators to answer calls twenty-four hours a day, 7 days a week.¹⁵⁴ Other states provide that the seller must have a live operator available or must record consumer calls and have a live operator return the call within a specified period of time.¹⁵⁵

In some states, phone card laws go further than what is required in most consumer protection statutes by setting minimum performance standards for the services that customer service must provide. For example, California and New York require the operator to permit consumers to file complaints.¹⁵⁶ In addition, the operator must be able to provide consumers with information about rates, surcharges, fees, policies on recharging cards, refunds, expiration dates, and the balance of usable minutes still available in the consumer’s account.¹⁵⁷

A few states have gone beyond disclosure and customer service by providing substantive protection as well. They impose detailed requirements on charges and fees.¹⁵⁸ These include mandating rules for rounding up to the next minute and prohibiting sellers from excessive rounding up.¹⁵⁹ Some laws provide that the value of the card cannot be reduced by more than the charges printed on the card or the packaging or display at the point of sale.¹⁶⁰

State statutes also impose a wide variety of refund requirements. California and New York require sellers to give the consumer a refund if the service fails to operate in a “commercially reasonable manner.”¹⁶¹ Although this is a vague standard, the statutes at least establish that consumers are entitled to refunds.¹⁶² In Florida, consumers are entitled to a refund if service is “rendered unusable for reasons beyond the consumer’s control.”¹⁶³ Missouri requires a refund if the company ceases operations¹⁶⁴ or can no longer provide service.¹⁶⁵ Alabama requires a refund if service is suspended.¹⁶⁶ Texas requires a refund if the company fails to provide service at the disclosed rates or the service fails to meet technical standards.¹⁶⁷ Florida requires companies to have a refund policy.¹⁶⁸ At a minimum, such a policy must provide for the consumer to receive a refund if the prepaid calling service is “unusable for reasons beyond the consumer’s control” and the services “have not [exceeded] the expiration period.”¹⁶⁹ Furthermore, the refund must be for the same amount as the

value still on the card.¹⁷⁰ Alaska requires a refund if the card does not work as represented or the required disclosures are not made to the customer.¹⁷¹ In addition, the Regulatory Commission of Alaska can direct that a refund be paid “for good cause.”¹⁷² In Florida, a company “may, but shall not be required to” provide a refund for lost or stolen cards.¹⁷³ States also require that the amount of the refund cannot be less than the value remaining on the card.¹⁷⁴ The refund must be provided within 60 days from the date the consumer notifies the company.¹⁷⁵

Some of the states that have enacted prepaid phone card laws have also imposed performance standards such as a minimum level of operational capacity for the service being provided. These requirements are in sharp contrast to the law governing other payment devices¹⁷⁶ as well as the laws governing the quality of goods and services.¹⁷⁷

In California, companies must “maintain access numbers with sufficient capacity to accommodate a reasonably anticipated number of calls without incurring a busy signal or undue delay.”¹⁷⁸ Apparently, failure to maintain that capacity would trigger California’s requirement that consumers are entitled to a refund if a company fails to provide service in a commercially reasonable manner.¹⁷⁹ Case law from other types of transactions may be useful in further defining what circumstances may be commercially unreasonable.¹⁸⁰ Florida law formerly required that every company ensure that at least 95 percent of all call attempts to the company’s toll-free customer service number be completed.¹⁸¹ Finally, there must be at least 97 percent accuracy of the length of the conversation.

Another substantive protection relates to expiration policies. For example, California, Florida, and New York provide that if the card does not state a specific expiration date or policy, a card is considered active for at least 1 year from the date of purchase.¹⁸² In addition, if the card has been recharged, it must be active for 1 year from the date of the last recharge.¹⁸³ Sellers who consider the 1-year minimum onerous can easily avoid its imposition simply by providing on the card that it expires within a shorter period of time.¹⁸⁴ However, if the seller establishes an expiration date that is too short, for example 1 week, the consumer may be able to convince a court that the expiration date is unconscionable, in bad faith, or commercially unreasonable.¹⁸⁵ Statutes do not impose a minimum period before a card expires.

State statutes and regulations of phone cards do not include specific provisions providing that consumers can sue the card companies for violating these laws. Nevertheless, consumers in some states may be able to sue under their “mini-FTC” acts, alleging that a violation of the phone card requirements constitutes a deceptive or unfair act or practice.¹⁸⁶ In other states, consumers may confront substantial barriers.¹⁸⁷ A government agency, such as the state’s public service commission, may be authorized to impose penalties for violation of the phone card laws,¹⁸⁸ but consumers have no assurance they will do so, especially if the commission lacks sufficient resources or strong proof that violations are widespread.

IX. The Inadequacy of Warranty Law

The UCC includes provisions on express and implied warranties that may be beneficial to consumers who purchase goods.¹⁸⁹ The UCC, however, does not apply to the sale of services, which would include the sale of telephone services. The Federal Magnuson-Moss Warranty Act prohibits the disclaimer of implied warranties once a seller provides a written warranty.¹⁹⁰ Unfortunately, the Act does not apply to the sale of services either.¹⁹¹

Because neither the UCC nor the Magnuson-Moss Warranty Act applies to the sale of phone services, general contract law applies. Under contract law, courts will enforce express warranties. The seller, however, can avoid that result by carefully drafting the contract so it does not include any express warranties regarding the quality of the service provided to the consumer. Some courts have held that service contracts include implied warranties.¹⁹² The cases, however, do not involve provisions of telephone services or comparable services.¹⁹³ Consequently, it is not at all clear how courts would apply those standards to prepaid phone service. Moreover, sellers most likely can avoid enforcement of the implied warranties by disclaiming them.¹⁹⁴

X. Problems Not Addressed in Regulations

As described above, while most states have not regulated phone cards at all, some which have enacted regulations have gone far beyond the protection accorded consumers using other types of payment devices. However, even the states with the most comprehensive regulations have failed to do anything to protect consumers who confront many serious problems. In order for our Model to accomplish its objective, it was necessary to identify the gaps in current law.

For example, regulations include many required disclosures,¹⁹⁵ but do not require sellers to inform consumers of their policy with regard to unilaterally changing the terms and conditions of providing service without prior notice to the consumer.¹⁹⁶ Statutes do not require disclosure of the seller's policy on lost, stolen, unauthorized, or malfunctioning cards.¹⁹⁷ Finally, statutes do not require sellers to inform consumers whether they can redeem unused value on their card, and if they can, how it can be redeemed and what charges may be imposed.¹⁹⁸

Statutes also fail to provide consumers with any protection if a card is lost or stolen.¹⁹⁹ In addition, consumers may lose the piece of paper or other record on which they have written their Personal Identification Number (PIN) and may not have their PIN memorized.²⁰⁰ Without the PIN, the card cannot be used and the consumer loses the value of the balance remaining on the card.²⁰¹ State law is deficient in not requiring the seller to replace the PIN. At the very least, statutes should require a warning to consumers about the consequences of losing their PIN. If the consumer cannot remember the PIN and the seller refuses to inform the consumer what the PIN is, or issue a new PIN, the balance of unused value remaining on the card becomes pure profit for the card issuer.²⁰²

A card may also be defective. For example, the access number or the PIN may not work,²⁰³ or the card may have some other defect making it impossible to operate as it should.²⁰⁴ Consumers will lose the entire balance on the card if the card issuer refuses to replace the card. Statutes do not require card issuers to replace cards. Even if the issuer does replace cards, it may charge such a high fee that it is not economically advisable for consumers to purchase a replacement.

Additionally, the card issuer may go out of business.²⁰⁵ The issuer may simply close its doors and disappear. Statutes provide purchasers of phone cards with no satisfactory remedy when this occurs. Alternatively, the issuer may file for bankruptcy, leaving consumers with unsecured claims that are unlikely to be satisfied.

States do not regulate the amount of charges and fees. Rather, states require an issuer who charges fees for various services, to inform consumers about the fees.²⁰⁶ However, the disclosure requirements of state laws are not adequate. For example, states do not require sellers to inform consumers of the extra charges they incur if they use their phone card at a pay phone.²⁰⁷

In states that have no laws regulating phone cards, the rights and obligations of the parties are governed by the contract between the card issuer and the consumer. In states with phone card laws, the many matters not regulated are subject to the terms of the contract. The contracts between issuers and consumers are not the result of a negotiated bargain between the parties, and, in fact the consumer never even signs the agreement. Rather, the law deems that consumers agree to the terms of the take-it-or-leave-it adhesion contracts by paying their money and using the card. The cards often include unilateral change of terms provisions under which the issuers can modify the contract's terms without notice to consumers.²⁰⁸ Those changes could deprive consumers of important rights they had under the contract when they originally bought the card or impose substantial new charges upon them. States have not enacted laws specifically governing this problem.

Finally, even states that have enacted strong phone card laws do not include in those statutes provisions granting consumers explicit causes of action and meaningful remedies for violation of the law such as those included in Federal consumer protection statutes.²⁰⁹ This is a serious omission that may make the protections in the laws largely illusory.

The Model Act described in the following section fills the gaps in current law by including provisions to deal with the issues identified above, that statutes do not address.

XI. Model Prepaid Telephone Card Act

Based on the foregoing analysis of the problems consumers of prepaid telephone cards encounter, the information they need, the nature of the marketplace, the dismal prospects for self-regulation, and the inadequacy of the states' responses to date, we propose that Congress enact a Federal law to regulate phone cards. As discussed previously,²¹⁰ a Federal statute provides benefits to both the industry and consumers that state laws cannot offer. Matters not included in the Federal statute are appropriate for individual states to adopt if they see fit to do so. Our proposal breaks very little new ground. Rather we have taken those features of state law that offer consumers needed protection and recommend that they be incorporated into a Federal law. Most of our suggestions represent approaches that states have already adopted. Therefore, it is reasonable to assume that they pose no significant technological or financial impediments to the prepaid phone card industry.

Our Model Act covers those matters that should be governed by a Federal statute. Some matters are not included in our Model Act because we believe they are best

left for the states to consider on an individual basis. These matters include licensing and registration of companies selling cards, the needs of residents with special needs, as well as regulation of rates and fees. If Congress refuses to pass phone card legislation, our Model Act should be enacted by each state.

The Federal statute should establish a basic framework that ensures consumers a reasonable level of disclosure and protection. The statute should delegate to the FTC the task of issuing detailed regulations pursuant to the statute, filling in the details and responding to future changes in technology, marketing, and the marketplace.²¹¹ To assist card issuers in complying with the law and to reduce compliance costs, the statute should instruct the FTC to draft model disclosure forms for issuers to use if they wish.²¹² States would be permitted to enact their own laws as long as they were not inconsistent with the Federal statute.²¹³

The Federal statute should also regulate disclosures in advertising. As previously noted,²¹⁴ advertising is important in inducing consumers to buy a certain brand of card. In addition, a Federal law is appropriate because a radio or television commercial or Internet ad can be seen and heard across state borders. The Federal law should incorporate the provisions of California's law that requires phone card advertisements to disclose geographic limits to the advertised price, rate, or unit value, as well as to disclose additional surcharges, call setup charges, or fees applicable to the advertised price, rate, or unit value.²¹⁵ The FTC should be authorized to issue additional disclosures from time to time if it finds they are needed. This flexibility is appropriate given the new advertising avenues that emerging technologies continue to make possible.²¹⁶

The Federal law should require disclosures that are available to consumers prior to purchasing prepaid phone cards. Disclosure plays a crucial role in phone card transactions because of the manner in which consumers become bound by the terms of the contract. As is evident from the discussion in this article, the purchase and use of phone cards involves many elements. Some of the features of this service are complex and confusing, such as the calculation of fees and charges. Consumers and card issuers do not enter into a formal written contract that includes the terms of agreement, with consumers expressing their agreement to be bound in some manner, such as signing the contract. Instead, the card issuer notifies the consumer of rights, obligations, restrictions, limitations, and conditions on the card or in the packaging, and the consumer purchases the card. Therefore, the consumer does not participate in the negotiation of the terms. Courts uphold the enforceability of these types of contracts, finding that consumers have accepted and are bound by any terms of which they have notice if they use the product after having opportunity to discover those terms.²¹⁷ In order to ensure the fairness and reasonableness of the terms that bind the parties, it is essential that the law require certain disclosures that become part of the contract.

The Federal law should require certain disclosures on the card itself. This includes the name of the company issuing the card and a toll-free customer service number. The card also should give a toll-free network access number if that is required in order to access service. The card must disclose the authorization code if one is required to access service. Most states that have enacted legislation include these disclosure requirements.

The Federal statute should require that all cards have an expiration date, and that the date can be no shorter than 1 year after activation. This information is vital for the consumer to have. Therefore, there should be significant consequences if the card does not include that disclosure. The Federal statute should follow the laws enacted in Washington and Texas²¹⁸ and provide that if a seller fails to make that disclosure, the card is active indefinitely.

The Federal statute should follow the pattern of state law by requiring other disclosures, but permitting the issuer to make them either on the card or on the packaging that comes with the card. Additionally, the issuer should be required to make the disclosures available at the point of sale.²¹⁹ Disclosures should include all charges, taxes, and fees.²²⁰ The seller should disclose the minimum charge per call, extra charges imposed for calls from pay phones, the billing decrement, the recharge policy, if any, and the refund policy.²²¹ The FTC should have the authority to regulate further in this area. For example, phone card issuers may impose new types of charges and conditions. The statute should define charges and conditions in general terms so the FTC can issue regulations under its disclosure authority to include these new costs.

Surcharges for international calls deserve special attention. Those making international calls have a special need for clear and accurate information. Therefore, it is important that the surcharges for international calls not be buried in with the other disclosures. Consequently, the statute should provide that if international calls are a significant focus of the issuer's marketing or if a substantial portion of

the calls made on its cards are subject to surcharges for international calls, the issuer must make the disclosure of those surcharges in a prominent place on the card as well as on the packaging and at the point of sale. The statute should delegate to the FTC the responsibility to issue regulations further specifying the circumstances under which the special rules for international calls apply.

Consumers also need to know the balance remaining on their cards. Otherwise, when they have an important call to make, they may mistakenly believe they have more time than they actually have to make their call. The Federal law should follow Texas' lead by requiring verbal disclosures at the beginning of each call informing the consumer of the minutes, billing increments, or dollars remaining on the card.²²² When the balance on the card is nearly exhausted, the issuer should be required to inform the consumer verbally that the time is about to expire.²²³

Furthermore, the Federal statute should require several disclosures not mandated by state statutes. Sellers should have to inform consumers of their policy with regard to unilaterally changing the terms and conditions of providing service without prior notice to the consumer.²²⁴ Even better would be a provision requiring sellers to notify consumers beforehand of all proposed changes. Notification could be given verbally at the beginning of the consumer's call using the card.²²⁵ The consumer should be given the option of refusing to agree to the change. If the consumer refuses, she should be entitled to a refund of the unused value on the card. Sellers should be prohibited from charging a fee to obtain the refund.

Sellers should be required to disclose their policy on lost, stolen, unauthorized, and malfunctioning cards.²²⁶ In addition, the Federal statute should require sellers to inform consumers whether they can redeem unused value on their card, and if they can, how it can be redeemed and what charges may be imposed.

The statute should mandate the use of standard uniform terms that would be defined in the statute. This would enable consumers to comparison shop. Uniform terms would have uniform meanings, regardless of the state where the consumer purchased the card. In addition to requiring standard terms, certain terms should be prohibited to prevent the confusing and contradictory wording that many agreements contain.²²⁷ For example, some companies state there is no connection fee, leading consumers to believe there are no additional fees.²²⁸ This claim is misleading because instead of that fee they impose a fee at the conclusion of each call, called a "post-call" or "hang-up" fee. Sellers should be required to use a standard term that would apply to all fees imposed per call. Companies impose periodic charges for maintenance fees.²²⁹ The statute should require companies to use a standard term that would apply to all such maintenance fees. Companies should not be allowed to confuse consumers by using a variety of terms for such charges such as "administrative fee" or "service fee." The statute should require a standard format for charges imposed for taxes. Standard uniform terms would benefit card issuers as well as consumers because the standardization would be easier for issuers to comply with than various state laws with differing requirements and definitions. The statute should authorize the FTC to develop a standard format for disclosures and model forms.

The Federal statute should require that if the issuer uses a language other than English in advertising or promoting the card, or on the card or its packaging, then the required disclosures on the card or packaging must also be in that other language.²³⁰ If another language is used to provide dialing instructions for making calls or calling customer service, the disclosures required to be on the card or its packaging also must be in that other language.²³¹

Disclosure by card companies alone is not sufficient.²³² The Federal statute should also require dispute resolution procedures and substantive rights and protections. The Federal statute should ensure the effectiveness of customer service or else consumers will be at a severe disadvantage in learning essential information and seeking solutions for problems that arise. Issuers should be required to provide a toll-free telephone number for customer service, with that number clearly disclosed on the card itself. The issuer should be required to have an adequate number of trained, live operators available at least Monday through Friday, 8 hours each day.²³³ The statute should require that the issuer record all calls made at other times, and that the recorded calls be returned no later than the end of the next business day.²³⁴ Consumers should have the right to file complaints when they call customer service,²³⁵ and the issuer should be required to investigate within ten business days, crediting the consumer's card or providing a refund if the consumer's complaint is justified.²³⁶ Consumers also need information when they call, and the issuer's customer service operators should have the capacity to provide information about rates, surcharges, fees, refunds, expiration dates, recharging cards, and the available balance.²³⁷

The Federal statute should include rules for rounding charges up to the next minute and should prohibit excessive upwards rounding.²³⁸ Federal law should also prohibit the issuer from reducing the value of the card by more than the charges printed on the card or the packaging or information displayed at the point of sale.²³⁹ Moreover, the seller should be prohibited from imposing a fee if there is no connection made to the party dialed.

The Federal statute should require the issuer to provide a refund when the issuer fails to provide service at the disclosed rates or charges more than disclosed or allowed.²⁴⁰ In addition, the consumer should receive a refund if the phone service fails to meet certain technical standards.²⁴¹ Refunds are warranted if service is suspended, terminated,²⁴² or unusable.²⁴³ Consumers should be entitled to a refund if the service does not work as represented, the required disclosures are not made,²⁴⁴ or the card is defective. Consumers should also be able to receive a refund of the unused balance on their card if they report their card as lost or stolen and the issuer has the capacity to block all future use of the card after receiving the consumer's notice.²⁴⁵

There may be other circumstances under which refunds should be required. Therefore, the statute should include more general standards as well. California and New York's models require a refund of at least the value remaining on the card if the service fails to operate in a "commercially reasonable manner."²⁴⁶ Other examples of general standards are provisions requiring a refund if the issuer fails to exercise ordinary care, acts in bad faith, or uses a contract that includes unconscionable terms.²⁴⁷

The Federal statute should impose minimum performance standards. The seller should be required to have the capacity to accommodate a reasonably anticipated number of calls without consumers encountering a busy signal or unreasonable delay.²⁴⁸ The FTC should set requirements for what percentage of calls must be completed and the accuracy of the company's calculation of the conversation time.²⁴⁹

The Federal statute should also include a guaranty stating that both the card and the service provided meet minimum standards. Accordingly, it should provide that there is an implied warranty of merchantability in every phone card transaction. This is the law under the UCC with regard to the sale of goods.²⁵⁰ Unlike the UCC, however, the issuer should not be allowed to disclaim that implied warranty.²⁵¹

The Federal statute should establish a maximum cap on a consumer's liability as long as the card issuer has the ability to block access so the thief cannot continue to use the card.²⁵² If the issuer does not have that ability, the law should require a prominent disclosure on the card or its packaging that the purchaser will lose the entire balance on the card if it is lost, stolen, or used in an unauthorized fashion, if that is the issuer's policy.

Consumers may lose their PINs rendering the card useless and resulting in the loss to the consumer of the value remaining on the card.²⁵³ A seller should be required to supply a new PIN if the consumer notifies the seller and the seller has the ability to block access to anyone using the lost PIN. If the seller lacks the ability to block access and does not want to provide consumers any relief, the Federal statute should require the seller to clearly warn consumers either on the card or its packaging that they have no protection if the PIN is lost.

Additionally, the statute should require sellers to replace defective cards.²⁵⁴ Consumers will lose the entire balance on the card if the card issuer refuses to replace it. The law should prohibit sellers from charging more than a reasonable fee for a replacement.²⁵⁵ If sellers can charge exorbitant replacement fees, it will be economically inadvisable for the consumer to order a replacement.

Consumers need meaningful remedies otherwise they have no means for recovering the losses they incur as a result of violations of the law. The Federal statute should include the remedies contained in Federal consumer protection laws, providing for actual damages, statutory damages, costs and attorney's fees.²⁵⁶ Class actions should be expressly permitted, or else litigation will not be feasible, given the small amount of each individual's damages. Predispute mandatory arbitration should be prohibited.²⁵⁷

The recommendations made thus far should be in a Federal statute or accompanying FTC regulations. They involve national problems that are best dealt with on a uniform nationwide basis both to ensure that consumers can enjoy a basic level of protection wherever they live and to lower compliance costs for the industry. If Congress fails to enact a law, however, states should pass their own statutes, using the above as a model, and delegating regulatory authority to the appropriate state agency.

Some issues are best dealt with on a state basis rather than through a Federal law. Examples of this include the licensing and registration of companies. Some states require this already, and the rest should be encouraged to consider it. States

also should require companies to post a bond so consumers will have a fund from which they can be compensated in case a company goes out of business. Some states require phone card companies to file tariffs listing all of their rates and fees, with a state agency empowered to reject those rates.²⁵⁸ We believe it best to leave that decision to the states rather than establish a Federal bureaucracy to oversee rate regulation for all sellers. While lawmakers generally are reluctant to regulate fees, regulation of phone card fees is warranted because of the low income and vulnerable status of many of the consumers who are specifically targeted by the industry. Consequently, states should consider enacting laws prohibiting rates above a certain amount, as states already do for consumer credit. There is a great deal of diversity in the demographic characteristics of various states. Individual states may find it necessary to enact special protections for vulnerable groups within their states, such as immigrants.

Finally, Federal and state laws governing phone cards should prohibit waiver of the requirements mandated in the laws. Strong consumer protection laws do not benefit consumers if sellers can enforce contractual provisions by which consumers agree to waive provisions in those laws intended to benefit and protect them.

XII. Conclusion

Empirical studies indicate that consumers have difficulty obtaining necessary information about prepaid telephone cards before purchase. Information is often unavailable, misleading, and confusing. There is no Federal regulation of prepaid phone cards. Although numerous states have statutes or administrative regulations, they vary widely and many states have no laws regulating phone cards. Both card issuers and consumers could be better served with Federal legislation.

This article presents a case for Federal legislation and a proposed model act which would draw upon the best of current state regulations. The Federal Trade Commission is the suggested avenue for administrative agency regulations and enforcement of the proposed legislation. The Federal legislation also must provide a private right of action for consumers, providing them with meaningful remedies when they are injured due to a company's failure to comply with the law. However, a few issues should be left to the states' discretion. If Congress fails to enact legislation, the states should pass the model act.

Footnotes

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³ Mitch Morrison, *Paying Dividends: The Prepaid Category Continues to Grow and it's Not Just Phone Cards Anymore*, 39 CONVENIENCE STORE NEWS 48 (2003).

⁴ Brian Cook, Thomas K. Crowe & Jo Ann Scott Cullen, *Experts Predict—Prepaid Forecast 2002*, INTELECARD NEWS, Jan. 2001, http://www.intelecard.com/story_home.asp?StoryID=342 (last visited Sept. 11, 2006); Richard Gutwillig, *Calling on Savvy*, 55 SUPERMARKET BUS. MAG. 89 (2000).

⁵ Michael Browne, *Generally Speaking: Selling a Variety of General Merchandise Draws Customers, High Margins*, 40 CONVENIENCE STORE NEWS 37, 37 (2004).

⁶ Howard Segermark, *Why Market Phone Cards?* 30 NAT'L PETROLEUM NEWS 30, 30 (June 2002).

⁷ Cook, Crowe and Cullen, *supra* note 2, at 14; Gutwillig, *supra* note 2 (reporting that card sellers are targeting home-based businesses and traveling salespersons). Military personnel also are major users of prepaid calling cards. *FCC Taps Calling Cards for Access, USF Payments*, TELECOM POL'Y REP., July 10, 2006.

⁸ Gutwillig, *supra* note 2. Digitac sells computers and computer services. *Id.* <http://www.digitac.com.aa> (last visited Sept. 27, 2006).

⁹ Mary Louise Pickel, *Phoning Mexico . . . for profit*, ATL. J.-CONST., June 8, 2006; Cook, Crowe and Cullen, *supra* note 2; Gutwillig, *supra* note 2.

¹⁰ Alan R. Andreasen, *Disadvantaged Hispanic Consumers: A Research Perspective and Agenda*, 16 J. OF CONSUMER AFF. 46, 48 (1982); Jinkook Lee & Horacia Soberon-Ferrer, *Consumer Vulnerability to Fraud: Influencing Factors*, 31 J. OF CONSUMER AFF. 70, 72 (1997).

¹¹ Julia Marlowe, *Investigation of Pre-Purchase Information on Prepaid Telephone Cards*, Report to the Georgia Governor's Office of Consumer Affairs 1 (Sept. 2005); Julia Marlowe and Martina Rojo, *Consumer Problems With Prepaid Telephone Cards*, 51 CONSUMER INTS. ANN. 126, 128-30 (2005).

¹⁰The Mexico Tri Color card, purchased in 2005, provides an example of misleading information. The card reads “sin cargo de conexión” on the front in large print, but the small print on the back reads “cargos de conexión aplicaran.” The statement on the front informs the consumer there are no connection charges, but the statement on the back says the opposite. Marlowe and Rojo, *supra* note 9, at 127. Customer service representatives sometimes provide confusing information. For example, one told a consumer the phone card had a “maintenance fee of \$0.50 every one or 2 days.” *Id.*

¹¹*AT&T v. Ting*, 182 F. Supp.2d 902, 930 (N.D. Cal. 2002), *aff’d* 319 F.3d 1126 (9th. Cir. 2003), *cert. denied*, 124 S. Ct. 53 (2003); *see* Jean Sternlight, *As Mandatory Binding Arbitration Meets the Class Action, Will the Class Action Survive?* 42 WM. & MARY L. REV. 1 (2000).

¹²According to the U.S. Census Bureau, 37 million people in the United States live in poverty. Bradley R. Schiller, *Fluid Poverty*, ALBANY TIMES UNION, Sept. 24, 2006 (noting that more than 20 percent of Hispanics in the United States live in poverty).

¹³*See, e.g.*, Press Release, FTC, Marketer of Pre-Paid Cards Agrees to Settle Charges of Failing to Disclose Actual Cost of Using Card; Additional Charges Per Call Added, Some Cards Incurred Monthly Maintenance Fee (Mar. 4, 1999).

¹⁴*Phone Card Issuers Must Pay Access Fees*, N.Y. TIMES, July 4, 2006, at C9 (reporting that the FCC ruled AT&T must make Universal Service Fund payments on its prepaid calling card transactions).

¹⁵*See* Phillip Nelson, *Information and Consumer Behavior*, 78 J. OF POL. ECON. 311, 312 (1970).

¹⁶Segermark, *supra* note 4, at 30.

¹⁷Marlowe, *supra* note 9, at 4–5; Marlowe and Rojo, *supra* note 9, at 128.

¹⁸Nancy Luna, *Phone Card or PhonyCard?* ORANGE COUNTY REG., Aug. 20, 2005 (reporting experience of consumer who was never able to use her defective card to make a call).

¹⁹Julia Marlowe and Jorge H. Atilas, *Consumer Fraud and Latino Immigrant Consumers in the United States*, 29 INT’L J. OF CONSUMER STUD. 391, 395–96 (2005).

²⁰*Id.* at 395–96.

²¹Marlowe and Rojo, *supra* note 9, at 130–31.

²²*Id.* at 132–33.

²³*Id.* at 133.

²⁴*Id.* at 130.

²⁵*Id.*

²⁶Marlowe and Rojo, *supra* note 9, at 130.

²⁷*Id.*

²⁸*Id.*

²⁹*Id.*

³⁰*Id.*

³¹Marlowe and Rojo, *supra* note 9, at 130.

³²*Id.*

³³*Id.* at 132.

³⁴*Id.* at 133.

³⁵*Id.*

³⁶Marlowe and Rojo, *supra* note 9, at 133.

³⁷*Id.*

³⁸*Id.*

³⁹*Id.* at 130.

⁴⁰*Id.*

⁴¹Marlowe and Rojo, *supra* note 9, at 130.

⁴²*Id.* at 131.

⁴³*Id.*

⁴⁴Marlowe, *supra* note 9, at 18–19.

⁴⁵*Id.* at 4.

⁴⁶*Id.*

⁴⁷*Id.* at 4–5.

⁴⁸*Id.* at 4.

⁴⁹Julia Marlowe and Francisco Diaz, *Verification of Advertised Claims for Prepaid Phone Cards* (Working Paper, 2006).

⁵⁰Marlowe, *supra* note 9, at 4.

⁵¹*Id.*

⁵²*Id.*

⁵³*Id.*

⁵⁴*Id.* at 5.

⁵⁵Marlowe and Rojo, *supra* note 9, at 132.

⁵⁶*Id.*

⁵⁷Marlowe, *supra* note 9, at 4.

⁵⁸*Id.* at 4–5.

⁵⁹CAL. BUS. & PROF. CODE § 17538.9(12) (West 2006) (a customer is not considered connected if the customer receives a busy signal or the call is unanswered); AL. PUB. SERV. COMM’N RULE T-18.1(7) (1997) (usage rates can be charged only for connected minutes); 16 TEX. ADMIN. CODE § 26.34(e)(2) (2000) (account may be decreased only for completed calls; busy signals and unanswered calls are not considered completed).

⁶⁰ITA Phonecard Disclosure Guidelines, The Int’l Telecard Ass’n Standards Comm., June 5, 2000.

⁶¹*Id.*

⁶²Howard Segermark, Executive Director, International Prepaid Communications Association, personal interview with Julia Marlowe and Martina Rojo, at the offices of the Association, 904

Massachusetts Avenue, Washington, D.C., March 29, 2004. The International Prepaid Communications Association is the successor organization to the International Telecard Association.

⁶³ Compare ITA Phonecard Disclosure Guidelines, *supra* note 60, with the Model Act discussed *infra* in Part XI. For example, the IPCA standards do not include any rules on advertising. They do not require a minimum period before the card expires or redemption of unused value. Card issuers are not required to replace defective cards.

⁶⁴ Marlowe and Rojo, *supra* note 9, at 131.

⁶⁵ *Id.*

⁶⁶ *Id.*

⁶⁷ Gutwillig, *supra* note 2.

⁶⁸ Marlowe, *supra* note 9, at 3.

⁶⁹ 15 U.S.C. § 45(a)(1) (2006).

⁷⁰ *Id.* § 45(a).

⁷¹ *Id.* § 45(a)(1).

⁷² *Id.*

⁷³ The FTC Act merely declares unfair and deceptive acts to be unlawful. 15 U.S.C. § 45(a)(1) (2006). It does not establish any requirements for disclosure of essential information, levels of performance, customer service or error resolution.

⁷⁴ See *infra* Part X discussing problems not dealt with in any laws.

⁷⁵ MICHAEL M. GREENFIELD, CONSUMER LAW: A GUIDE FOR THOSE WHO REPRESENT SELLERS, LENDERS, AND CONSUMERS 160, 559 (Little, Brown 1995).

⁷⁶ Courts in some states have made it very difficult for consumers to bring actions under these laws. See, e.g., *Zeeman v. Black*, 273 S.E.2d 910, 915 (Ga. Ct. App. 1980) (imposing a “public interest” requirement that is not included in the statute).

⁷⁷ E.g., GA. CODE ANN. § 10–1–399(a) (2006).

⁷⁸ Most courts require consumers to prove both procedural and substantive unconscionability. Greenfield, *supra* note 75, at 529–34. To prove procedural unconscionability the consumer must show the process under which the consumer entered into the contract was unconscionable. To prove substantive unconscionability, the consumer must prove the terms in the contract were unconscionable. Some courts allow the doctrine to be raised only as a defense, which means consumers can challenge a contract as unconscionable only if the seller has sued them. They cannot use it affirmatively as the basis of their own lawsuit against the seller. *Rosboro Lumber Co. v. Employee Benefits Ins. Co.*, 672 P.2d 1336, 1338 (Or. Ct. App. 1983), *rev'd on other grounds*, 680 P.2d 386 (Or. 1984).

⁷⁹ See generally Official Comment U.C.C. § 1–203 (2005). The Comment provides that “failure to perform or enforce, in good faith, a specific duty or obligation under the contract, constitutes a breach of that contract. . . . [T]he doctrine of good faith merely directs a court toward interpreting contracts within the commercial context in which they are created, performed and enforced, and does not create a separate duty of fairness and reasonableness which can be independently breached.”

⁸⁰ See generally *Discover Bank v. Superior Court*, 30 Cal. Rptr. 3d 76, 113 P.3d 1100, 1109–10 (Cal. 2005) (stating that adhesion contracts are unconscionable, “at least to the extent they operate to insulate a party from liability that otherwise would be imposed under [state] law”).

⁸¹ This is in contrast to gift cards. Far more states have enacted laws regulating that type of stored value card. MARK BUDNITZ & MARGOT SAUNDERS, CONSUMER BANKING & PAYMENTS LAW CREDIT, DEBIT & STORED VALUE CARDS, CHECKS, MONEY ORDERS, E-SIGN, ELECTRONIC BANKING AND BENEFIT PAYMENTS 178–79 (National Consumer Law Center 3rd ed. 2005).

⁸² Prepaid phone cards have been identified as a key problem area for Hispanics. Federal Trade Commission, Hispanic Outreach Forum & Law Enforcement Workshop: A Summary of the Proceedings, at 8 (Oct. 2004), <http://www.ftc.gov/reports/hispanicoutreach/hispanicoutreach.pdf> (last visited Sept. 11, 2006). Fraudulent practices involving the cards are “likely to be targeted to immigrant populations.” *Id.* at 9. “Hispanics are noted for their trusting nature, which means they may be easier prey for scam artists.” *Id.* at 8. See generally Hoover’s In-Depth Company Records, Ace Cash Express, Inc. Aug. 24, 2005 (reporting that Ace Cash Express, Inc. targets consumers who do not have bank accounts, selling them prepaid phone cards, and controversial products such as payday loans).

⁸³ Hispanic Outreach Forum & Law Enforcement Workshop: A Summary of the Proceedings, *supra* note 82, at 10. “. . . the concept of the government protecting consumers may be foreign to many Hispanics.” *Id.*

⁸⁴ Administrative agencies in the following states have regulations pertaining to prepaid phone cards. AL. PUB. SERV. COMM’N RULE T–18.1 (2000); FLA. ADMIN. CODE ANN. r. 25–24.900–935 (2006); MO. CODE REGS. ANN. tit. 4, §240–32.160–70 (2006); 16 TEX. ADMIN. CODE § 26.34(e)(4) (2000).

⁸⁵ 815 ILL. COMP. STAT. 505/2QQ (2006); FLA. ADMIN. CODE ANN. r. 25–24.910 (2006). Some states require providers of the service to file tariffs. FLA. ADMIN. CODE ANN. r. 25–24.915 (2006); 16 TEX. ADMIN. CODE § 26.34(e)(1) (2000).

⁸⁶ *Id.*

⁸⁷ *Id.*

⁸⁸ “. . . Federal law applies nationally.” *Salt Lake Tribune Publ’g Co. v. Mgmt. Planning, Inc.*, 390 F.3d 684, 688 (10th Cir. 2004).

⁸⁹ “Because Federal law applies nationally,” courts should assume “that Congress desires national uniformity in the application of its laws.” *Id.* See Laura S. Langlely, *Sperm, Egg, and a Petri Dish*, 27 J. LEG. MED. 167, 206 (2006) (proposing Federal legislation because it would create uniformity among the states).

⁹⁰ See, for example, the industry’s response to state laws requiring companies to notify consumers when there is a security breach resulting in the possible exposure of personal information about consumers. Katie Kuehner-Hebert, *Data Privacy Now Issue for States*, 170 AM. BANK-

ER 1, Mar. 28, 2005 (noting how businesses prefer a Federal statute over a patchwork of state laws).

⁹¹ Fourteen percent of the people in the United States, totaling 40 million people, move or change their address every year. Stephanie Fiereck, *Focus on Class Action*, NEW JERSEY LAW., Oct. 31, 2005 (relying on data from the U.S. Census Bureau's Geographical Mobility Study 2002–2003).

⁹² *E.g.*, *Neogen Corp. v. Neo Gen Screening, Inc.*, 282 F.3d 883, 887 (6th Cir. 2002); *Gator.com Corp. v. L.L. Bean, Inc.*, 341 F.3d 1072, 1075 (9th Cir. 2003).

⁹³ Prepaid phone cards are analogous to payment devices such as credit cards, that are defined as devices for “the purpose of obtaining . . . property . . . or services.” 15 U.S.C. § 1602(k) (2006).

⁹⁴ The Federal Communications Commission has authority to regulate interstate telephone service. 47 U.S.C. § 201 (2006). See *AT&T Corp. v. Iowa Util. Bd.*, 525 U.S. 366, 384 (1999) (clarifying the FCC's rulemaking authority under the Telecommunications Act).

⁹⁵ FCC, Prepaid Phone Cards: What Consumers Should Know, <http://ftp.fcc.gov/cgb/consumerfacts/prepaidcards.html> (last visited Sept. 11, 2006).

⁹⁶ FTC Telemarketing Sales Rule, 16 C.F.R. § 310 (2006).

⁹⁷ *FTC v. PT-1 Commc'ns, Inc.*, Civ. Action No. 99-1432 (S.D.N.Y. 1999) (stipulating final judgment and order for permanent injunction and consumer redress against defendant PT-1 Communications, Inc.).

⁹⁸ As discussed *infra* in Part XI, we propose that states be allowed to enact their own legislation if it is not inconsistent with the Federal law. State administrative involvement may be needed if a state wishes to require sellers to register or follow the example of some states that require sellers to obtain a certificate of authority or certificate of public convenience. *E.g.*, AL. PUB. SERV. COMM'N Rule T-18.1 (2000); FLA. ADMIN. CODE ANN. r. 25-24.910 (2006); MO. CODE REGS. ANN. tit. 4, § 240-32.150(1) (2006); 815 ILL. COMP. STAT. 505/2QQ(b) (2006).

⁹⁹ Other Federal consumer protection laws demonstrate how consumers can get the benefit of national coverage as well as protection for special local needs. These laws establish a national floor of minimum requirements. Rather than completely preempting state law, they permit states to enact laws that provide consumers with greater protection as long as the state's law is not inconsistent with the Federal law. *E.g.*, Truth in Lending Act, 15 U.S.C. § 1666(j) (2006); Electronic Fund Transfers Act, 15 U.S.C. § 1693(q) (2006); Fair Debt Collection Practices Act, 15 U.S.C. § 1692(n) (2006).

¹⁰⁰ Christopher B. Woods, *Stored Value Cards*, 59 CONS. FIN. QTLY. REP. 211, 211 (2005). One commentator suggests that the card issuer has special legal duties that arise from the fact that the card is prepaid. “And a fiduciary responsibility is involved for those who take money prior to providing service.” Howard Segermark, *Ensuring Fair Competition Remains Regulatory Challenge for Prepaid*, PHONE PLUS MAG., Mar. 2001, available at: <http://www.phoneplusmag.com/articles/131soap.html> (last visited Sept. 11, 2006). Segermark is Executive Director of the International Prepaid Communications Association.

¹⁰¹ ATMs can be used to perform a variety of services including cash deposits, cash withdrawals, balance inquiries, and transfers from one account to another. Candace Heckman, *Getting Money Back After ATM Theft Proving To Bank You're A Victim Is The Hard Part*, SEATTLE POST INTELLIGENCER, Aug. 9, 2006 (describing thefts involving ATM balance inquiries and ATM withdrawals); Citibank Home Page, <http://www.citibank.com> (describing ATM features enabling customers to withdraw cash and make transfers from one account to another) (last visited Sept. 27, 2006); Bank of America Home Page, <http://www.bankofamerica.com> (describing ATM features enabling customers to make withdrawals, make transfers from one account to another, and make balance inquiries (last visited Sept. 27, 2006).

¹⁰² See *e.g.*, 47 U.S.C. § 251 (2006) (prescribing the duties of telecommunications carriers).

¹⁰³ *E.g.*, *Cont'l Dredging, Inc. v. De-Kaizerred, Inc.*, 120 S.W.3d 380, 394 (Tex. Ct. App. 2003).

¹⁰⁴ The applicable law is the Electronic Fund Transfers Act, 15 U.S.C. § 1693 *et seq.*

¹⁰⁵ 71 Fed. Reg. 51437 (2006) (to be codified at 12 C.F.R. pt. 205) (Final Rule, effective July 1, 2007).

¹⁰⁶ *E.g.*, in Texas, prepaid calling card services companies are required to register with the Public Service Commission. 16 TEX. ADMIN. CODE § 26.34 (2000).

¹⁰⁷ Compare AL. PUB. SERV. COMM'N RULE. T-18.1 (1997) (requiring only the disclosure of essential information), with CAL. BUS. & PROF. CODE § 17538.9(b)(1) (West 2006) (covering advertising, disclosures, refunds, and customer service).

¹⁰⁸ *Id.*

¹⁰⁹ Marlowe and Rojo, *supra* note 9, at 134–35; Marlowe, *supra* note 9, at 9.

¹¹⁰ *Id.*

¹¹¹ Marlowe, *supra* note 9, at 4.

¹¹² See Federal Trade Commission, <http://www.ftc.gov>, listing all the FTC's guides and policy statements on advertising, none related directly to prepaid phone card services. (last visited Sept. 27, 2006).

¹¹³ Chester S. Galloway, Herbert Jack Rotfield and Jef I. Richards, *Holding Media Responsible for Deceptive Weight-Loss Advertising*, 107 W. VA. L. REV. 353, 383 (2005) (stating that the FTC does not have the resources to investigate many cases of deceptive advertising). The FTC, however, has brought at least one action against a phone card company. See *supra* text at note 97.

¹¹⁴ Edward A. Blair, Judy Harris and Kent B. Monroe, *Effects of Shopping Information on Consumers' Responses to Comparative Price Claims*, 78 J. OF RETAILING 76 (2002); Larry D. Compeau, Dhruv Grewal and Rajesh Chandrashedaran, *Comparative Price Advertising: Believe it or Not*, 36 J. OF CONSUMER AFF. 287–88 (2002); Valarie A. Zeithaml, *Consumer Perceptions of Price, Quality, and Value: A Means-End Model and Synthesis of Evidence*, 52 J. OF MARKETING 2–3 (1988).

¹¹⁵ Blair, Harris and Monroe, *supra* note 114, at 76.

¹¹⁶Truth in Lending imposes requirements for ads that mention specific credit terms. 12 C.F.R. § 226.24 (2006).

¹¹⁷CAL. BUS. & PROF. CODE § 17538.9(b)(1) (West 2006).

¹¹⁸States require disclosures on the card itself. *See e.g.*, CAL. BUS. & PROF. CODE § 17538.9(b)(2)(A) (West 2006). Some states require other disclosures on the card or its packaging. *See e.g.*, *Id.* § 17538.9(b)(3).

¹¹⁹CAL. BUS. & PROF. CODE § 17538.9(b)(2)(A) (West 2006). California law defines “company” as “an entity providing prepaid calling services to the public using its own or a resold telecommunications network.” CAL. BUS. & PROF. CODE at § 17538.9(a)(1) (West 2006). Other states that require the name of the company on the card include the following: Alaska, *see* ALASKA ADMIN. CODE tit. 3, § 52.377(d)(1)(A) (2006); Alabama, *see* AL. PUB. SERV. COMM’N Rule. T–18.1 (1997); Florida, *see* FLA. ADMIN. CODE ANN. r. 25–24.920(1)(a) (2006); Illinois, *see* 815 ILL. COMP. STAT. 505/2QQ(d)(1)(A) (2006); Missouri, *see* MO. CODE REGS. ANN. tit. 4, § 240–32.150(2) (2006); New York, *see* N.Y. PUB. SERV. LAW § 92–f2)(a) (McKinney 2006); Texas, *see* 16 TEX. ADMIN. CODE § 26.34(f)(1)(B)(ii) (2000); and Washington, *see* WASH. ADMIN. CODE 480–120–264(5)(a)(ii) (2006).

¹²⁰CAL. BUS. & PROF. CODE § 17538.9(b)(2)(B) (West 2006); FLA. ADMIN. CODE ANN. r. 25–24.920(1)(b) (2006); ILL. COMP. STAT. 815 505/2 QQ(d)(1)(B) (2006); MO. CODE REGS. ANN. tit. 4, § 240–32.160(2)(B) (2006); N.Y. PUB. SERV. LAW § 92–f2)(b) (McKinney 2006); 16 TEX. ADMIN. CODE § 26.34(f)(1)(A)(i) (2000).

¹²¹Marlowe and Rojo, *supra* note 9, at 134–35; Marlowe, *supra* note 9, at 9.

¹²²CAL. BUS. & PROF. CODE § 17538.9(b)(3)(C) (West 2006); FLA. ADMIN. CODE ANN. r. 25–24.920(1)(c) (2006); 815 ILL. COMP. STAT. 505/2 QQ(d)(1)(C) (2006); MO. CODE REGS. ANN. tit. 4, § 240–32.160(2)(C) (2006); N.Y. PUB. SERV. LAW § 92–f2)(c) (McKinney 2006).

¹²³CAL. BUS. & PROF. CODE § 17538.9(b)(2)(D) (West 2006); FLA. ADMIN. CODE ANN. r. 25–24.920(1)(d); MO. CODE REGS. ANN. tit. 4, § 240–32.160(2)(D) (2006); N.Y. PUB. SERV. LAW § 92–f2)(d) (McKinney 2006).

¹²⁴The situation is analogous to the person who issues a check drawn on an account that doesn’t exist or that contains no funds, providing the payee with an action in deceit. *See* Greenfield, *supra* note 75, at 12.

¹²⁵CAL. BUS. & PROF. CODE § 17538.9(b)(3)(I) (West 2006); FLA. ADMIN. CODE ANN. r. 25–24.920(2)(c) (2006); 815 ILL. COMP. STAT. § 505/2 QQ (d)(2)(F) (2006); MO. CODE REGS. ANN. tit. 4, § 240–32.160(1)(C) (2006); N.Y. PUB. SERV. LAW § 92–f2)(e) (McKinney 2006); 16 TEX. ADMIN. CODE § 26.34(f)(1)(B)(iv) (2000); WASH. ADMIN. CODE 480–120–264(5)(a)(v) (2006).

¹²⁶CAL. BUS. & PROF. CODE § 17538.9(b)(8) (2006); FLA. ADMIN. CODE ANN. r. 25–24.920(7) (2006); MO. CODE REGS. ANN. tit. 4, § 240–32.170(8) (2006); N.Y. PUB. SERV. LAW § 92–f2)(f) (McKinney 2006).

¹²⁷WASH. ADMIN. CODE 480–120–264(5)(a)(v) (2006). Texas has the same policy; if the expiration date or policy is not disclosed, on the card, it is considered active “indefinitely.” 16 TEX. ADMIN. CODE § 26.34(f)(1)(B)(iv) (2000).

¹²⁸CAL. BUS. & PROF. CODE § 17538.9(b)(3) (West 2006).

¹²⁹*Id.*

¹³⁰FLA. ADMIN. CODE ANN. r. 25–24.920(2) (2006).

¹³¹CAL. BUS. & PROF. CODE § 17538.9(b)(3) (West 2006).

¹³²Fees include “monthly or other periodic fees, maintenance fees, per-call access fees, surcharges for calls made on pay telephones, or surcharges for the first minute or other period of use. . . .” *Id.* § 17538.9(b)(3)(A).

¹³³*Id.* § 17538.9(b)(3)(B).

¹³⁴*Id.* Illinois’ and New York’s requirements on disclosure of fees are similar. 815 ILL. COMP. STAT. § 505/2QQ(d)(2) (2005); N.Y. PUB. SERV. LAW § 92–f3) (McKinney 2006).

¹³⁵12 C.F.R. § 226.12 (1994) (regarding credit cards); 12 C.F.R. § 205.4 (2001) (regarding debit cards).

¹³⁶CAL. BUS. & PROF. CODE § 17538.9(b)(13) (West 2006).

¹³⁷*Id.*

¹³⁸*Id.*

¹³⁹*Id.*

¹⁴⁰16 TEX. ADMIN. CODE § 26.34(g)(1) (2000).

¹⁴¹*Id.*

¹⁴²*Id.* § 26.34(g)(2) (2000).

¹⁴³CAL. BUS. & PROF. CODE § 17538.9(b)(4) (West 2006).

¹⁴⁴*Id.*

¹⁴⁵*Id.*

¹⁴⁶16 TEX. ADMIN. CODE § 26.34(f)(1) (2000).

¹⁴⁷*Id.*

¹⁴⁸*See* U.C.C. § 4–406 (2002) (requiring customers to report check forgeries and alterations to the bank, and if timely reported the non-negligent customer is not liable, but the UCC does not require any dispute resolution procedure. If the bank refuses to investigate the customer’s claim and recredit the customer’s account, the customer’s only recourse is to sue. The bank’s refusal to investigate and recredit does not violate the UCC).

¹⁴⁹12 C.F.R. § 226.13 (1994) (regarding credit cards); 12 C.F.R. § 205.11 (2001) (regarding debit cards).

¹⁵⁰*Id.*

¹⁵¹Budnitz and Saunders, *supra* note 81, at 178–79.

¹⁵²*Id.*

¹⁵³Marlowe and Rojo, *supra* note 9, at 130–31.

¹⁵⁴CAL. BUS. & PROF. CODE § 17538.9(b)(6) (West 2006); N.Y. PUB. SERV. LAW § 92–f(4) (McKinney 2000).

¹⁵⁵ See, e.g., AL. PUB. SERV. COMM'N Rule T-18.1(5) (2000) (requiring that customer service be manned 8 hours per day, 5 days per week); FLA. ADMIN. CODE ANN. r. 25-24.920(4) (2006) (requiring live operator 24/7 or electronically recorded and attempt to contact the next business day); MO. CODE REGS. ANN. tit. 4, § 240-32.140(4) (2001) (requiring availability 24/7); 16 TEX. ADMIN. CODE § 26.34(i) (2000) (requiring live operator 24/7 or electronically recorded and attempt to contact the next business day); WASH. ADMIN. CODE 480-120-264(2)(a) (2003) (requiring ability to respond 24/7).

¹⁵⁶ CAL. BUS. & PROF. CODE § 17538.9(b)(6)(B) (West 2006); N.Y. PUB. SERV. LAW § 92-f(4) (McKinney 2006).

¹⁵⁷ N.Y. PUB. SERV. LAW § 92-f(4) (McKinney 2006). New York also requires that the operator be able to provide information about the "terms and conditions of service and monthly service charges." *Id.* § 92-f(4)(iv).

¹⁵⁸ FLA. ADMIN. CODE ANN. r. 25-24.920(9) (2006); CAL. BUS. & PROF. CODE § 17538.9(b)(7) (West 2006); N.Y. PUB. SERV. LAW § 92-f(5) (McKinney 2006).

¹⁵⁹ FLA. ADMIN. CODE ANN. r. 25-24.920(9) (2006).

¹⁶⁰ CAL. BUS. & PROF. CODE § 17538.9(b)(7) (West 2006); N.Y. PUB. SERV. LAW § 92-f(5) (McKinney 2006).

¹⁶¹ *Id.*

¹⁶² *Id.*

¹⁶³ FLA. ADMIN. CODE ANN. r. 25-24.925(1)(a) (2006).

¹⁶⁴ MO. CODE REGS. ANN. tit. 4, § 240-32-170(5)(B) (2006).

¹⁶⁵ *Id.* § 240-32-170(6)(A).

¹⁶⁶ AL. PUB. SERV. COMM'N Rule T-18.1(4) (1998).

¹⁶⁷ 16 TEX. ADMIN. CODE § 26.34(j) (2000).

¹⁶⁸ FLA. ADMIN. CODE ANN. r. 25-24.925(1)(a).

¹⁶⁹ *Id.*; see also MO. CODE REGS. ANN. tit. 4, § 240-32.170(6) (2006) (requiring a company to refund the unused value remaining on the card if the "company is no longer able to provide service.")

¹⁷⁰ FLA. ADMIN. CODE ANN. r. 25-24.925(1)(a) (2006). The company can choose whether to make the refund in cash or by means of a replacement service. It must be provided within 60 days of when the consumer notifies the company. *Id.* r. 25-24.925(1)(b).

¹⁷¹ ALASKA ADMIN. CODE tit. 3, § 52.377(e) (2006).

¹⁷² *Id.*

¹⁷³ FLA. ADMIN. CODE ANN. r. 25-24.925(2) (2006). Compare the rules for lost and stolen credit cards. Under Federal law, a consumer has a maximum liability of \$50. The liability will be less if the consumer notifies the card issuer before the thief charges less than \$50 prior to the consumer providing the notification. 12 C.F.R. § 226.12(b) (2006).

¹⁷⁴ CAL. BUS. & PROF. CODE § 17538.9(b)(7) (West 2006); FLA. ADMIN. CODE ANN. r. 25-24.925(1)(a) (2006); MO. CODE REGS. ANN. tit. 4, § 240-32.170(6)(A) (2006); N.Y. PUB. SERV. LAW § 92-f(5) (McKinney 2006).

¹⁷⁵ *Id.*

¹⁷⁶ Credit card law provides a limited remedy if there is a failure in the goods or services purchased. Consumers can dispute the charges and refuse to pay for those goods or services. 12 C.F.R. § 226.12(c) (2006). The card issuer will charge the amount back to the merchant and leave the consumer and merchant to resolve the dispute on their own. Budnitz & Saunders, *supra* note 81, at 152. Debit card law does not provide any remedy. *Id.* at 82.

¹⁷⁷ In regard to the sale of goods, the Uniform Commercial Code includes rules on express and implied warranties, but a merchant can avoid these by disclaiming them in the contract between the parties. U.C.C. § 2-316 (2003). The Federal Magnuson-Moss Warranty Act provides limited protection. 15 U.S.C. §§ 2301-2312 (2006). The warranty laws regarding the provision of services are even more problematic. See *infra* at Part IX.

¹⁷⁸ CAL. BUS. & PROF. CODE § 17538.9(b)(10) (West 2006).

¹⁷⁹ *Id.* § 17538.9(b)(7).

¹⁸⁰ Many laws require parties to act in a commercially reasonable manner. See, e.g., U.C.C. §§ 3-103(a)(6)-(9) (2002), 9-607(c), 9-608(a)(3), 9-610 (2000).

¹⁸¹ FLA. ADMIN. CODE ANN. r. 25-24.930 (repealed 2005).

¹⁸² CAL. BUS. & PROF. CODE § 17538.9(b)(8) (West 2006); N.Y. PUB. SERV. LAW § 92-f(6) (McKinney 2006).

¹⁸³ N.Y. PUB. SERV. LAW § 92-f(6) (McKinney 2006).

¹⁸⁴ *Id.*

¹⁸⁵ See generally *Borowski v. Firststar Bank Milwaukee*, 579 N.W.2d 247 (Wis. Ct. App. 1998) (upholding a bank's contract requiring a customer to notify the bank of any unauthorized signature or alteration of a check within 14 days as reasonable, and rejecting the dissent's view that such a short time period was contrary to customers' reasonable expectations and conduct).

¹⁸⁶ Greenfield, *supra* note 75, at 160 (describing how legislation prohibiting deceptive practices has been enacted in every state). See also, *id.* at 559 (most states have prohibited unfair practices).

¹⁸⁷ See, e.g., *Taylor v. Jacques*, 292 B.R. 434, 434 (Bankr. N.D. Ga. 2002) (holding that consumer cannot sue under Georgia's Fair Business Practices Act if the industry is regulated, even if the regulations do not address the problem the consumer alleges violates the Act). Consumers also face formidable barriers to obtaining judicial relief if a company stops doing business. Alternatively the company may stop doing business in one state, then resume business in another state under a different name. See generally, Pickel, *supra* note 7 (reporting that companies lose consumer loyalty with their unfair and deceptive practices, but then market the cards with a new brand name, cheating consumers who do not realize it is the same company).

¹⁸⁸ 16 TEX. ADMIN. CODE § 26.34(m) (2000) (explaining that the commission can order the company to take corrective action, impose administrative penalties, and coordinate with the Office of the Attorney General).

¹⁸⁹ Once a seller makes an express warranty, it cannot disclaim that warranty. U.C.C. § 2-316(1) (2003). However, the seller is not required to make any express warranties. Certain implied warranties arise by operation of law, U.C.C. § 2-314 & 2-315 (2003), but the seller can easily disclaim these. U.C.C. § 2-316(2) & (3) (2003).

¹⁹⁰ 15 U.S.C. § 2308(a) (2006).

¹⁹¹ 16 C.F.R. § 700.1(h) (2006). Even if the Act did apply, the Act prohibits only the disclaimer of implied warranties that are created by state law; the Act itself does not create any implied warranties.

¹⁹² “[A] duty is implied in every service, repair or construction contract to perform it skillfully, carefully, diligently, and in a workmanlike manner.” *Alco Standard Corp. v. Westinghouse Elec. Corp.*, 206 Ga. App. 794, 796, 426 S.E.2d 648, 650 (Ga. Ct. App. 1992).

¹⁹³ *Id.*

¹⁹⁴ No cases were found addressing this issue, but since the UCC permits disclaimers of implied warranties for the sale of goods, presumably courts also would allow it for the sale of services. See generally Richard M. Alderman, *Warranty Disclaimers and the Texas Deceptive Practices Act*, 29 HOUS. LAW. 14, 15 (Jan./Feb. 1992) (discussing express warranty disclaimers in service contracts).

¹⁹⁵ See Budnitz and Saunders, *supra* note 81, at 177–178.

¹⁹⁶ *Id.*

¹⁹⁷ *Id.*

¹⁹⁸ *Id.*

¹⁹⁹ See FLA. ADMIN. CODE ANN. r. 25–24.925(2) (providing that a company “may, but shall not be required to, provide a refund” for lost or stolen phone cards). Compare credit card and debit card law that imposes specific caps that limit the consumer’s liability if a thief makes charges on a lost or stolen card. 15 U.S.C. § 1643(a) (2006) (credit cards); *Id.* § 1693(g) (debit cards and other electronic fund transfers).

²⁰⁰ See Cheryl Johnson, *Faux Williams makes rounds; Star impersonator leaves trail of angry victims*, STAR TRIB., Dec. 26, 2004 (reporting consumer’s allegations of unauthorized use of phone card after he lost the piece of paper on which he had written his PIN).

²⁰¹ *Id.*

²⁰² The card issuer may be required to transfer those funds to the state under abandoned property or escheat laws. Christopher B. Woods, *Stored Value Cards*, 59 CONSUMER FIN. L. Q. REP. 211, 219 (2005); Anita Ramasastry, *State Escheat Statutes and Possible Treatment of Stored Value, Electronic Currency, and Other New Payment Mechanisms*, 57 BUS. LAW. 475, 480–81 (2001) (stating that North Carolina and Arizona exclude prepaid phone cards from their escheat laws). Even where those laws apply to prepaid phone balances, the seller has the use of those funds until they are paid to the state.

²⁰³ Marlowe & Rojo, *supra* note 9, at 130.

²⁰⁴ Luna, *supra* note 18 (highlighting an instance where a consumer reported that her card was cutoff immediately after making her first call, and the card did not work thereafter). The New York Attorney General persuaded eighteen retailers to agree to deactivate and reissue damaged gift cards. *Big Retailers Agree to Replace Gift Cards*, DETROIT FREE PRESS, Mar. 3, 2003.

²⁰⁵ See <http://www.ftc.gov/bcp/online/pubs/products/buytime.htm>; <http://www.fcc.gov/cgb/consumerfacts/prepaidcards.html>; see also Mark E. Budnitz, *Stored Value Cards and the Consumer: The Need for Regulation*, 46 AM. U. L. REV. 1027, 1035, n. 54 (1997) (reporting that issuers of prepaid phone cards have gone out of business after selling tens of thousands of cards which thereafter became worthless).

²⁰⁶ See Getting the Best Value from Prepaid Phone Cards, Consumer Action (April 1, 2001), available at <http://www.consumeraction.org> (last visited Oct. 5, 2006).

²⁰⁷ *Id.*

²⁰⁸ Budnitz and Saunders, *supra* note 81, at 172–173. See *infra* text accompanying note 200.

²⁰⁹ See, e.g., the Electronic Fund Transfers Act, 15 U.S.C. § 1693(m) (2006) (providing actual damages, statutory damages, costs, and reasonable attorney’s fees).

²¹⁰ See *infra* Part VI.

²¹¹ As discussed above, the FRB and FCC might be appropriate agencies as well. See *supra* text accompanying notes 89–94. The FTC, however, seems best suited. The FRB deals with financial institutions, and sellers of phone cards are not financial institutions. The FCC’s focus is on the telecommunications industry, not on payment devices such as phone cards, or the types of problems consumers face when they use phone cards.

²¹² As provided in other statutes, using the agency-approved form would be deemed compliance with the disclosure requirements. Electronic Fund Transfers Act, 15 U.S.C. § 1693(m)(d)(2) (2006).

²¹³ See Electronic Fund Transfers Act, 15 U.S.C. § 1693(q) (2006) The Act does not annul, alter, or affect state law except to the extent it is inconsistent with the Act. Furthermore, a state law is not inconsistent if it affords consumers greater protection than is provided in the Act.

²¹⁴ See *supra* text accompanying note 108. See also *FTC v. Pt-1 Comm’ns*, Civ. Action # 99–1432 (S.D.N.Y. 1999) (stipulated final judgment and order for permanent injunction and consumer redress; permanent injunction in connection with phone card company’s advertising). See also Hispanic Outreach Forum & Law Enforcement Workshop: A Summary of the Proceedings, *supra* note 82, at 9 (discussing how phone cards and other various types of media, excluding direct mail, are sources of deceptive claims targeted at Hispanics).

²¹⁵ CAL. BUS. & PROF. CODE § 17538.9(b)(1) (West 2006).

²¹⁶ See Federal Trade Commission, *Facts for Business: DotCom Disclosures*, available at <http://www.ftc.gov/bcp/online/pubs/buspubs/dotcom> (last visited May 31, 2006).

²¹⁷ See e.g., *Boomer v. AT&T Corp.*, 309 F.3d 404 (7th Cir. 2002) (holding that the consumer accepted a contract when using the service after he received agreement). See generally Ronald J. Mann, *Panel One: Boilerplate In Consumer Contract: “Contracting” For Credit*, 104 MICH. L.

REV. 899, 910 (2006) (discussing the credit card issuer's use of contract terms providing that notice and continued use bind consumers when issuers unilaterally change contract terms). As Howard Segermark, the Executive Director of the International Prepaid Communications Association, has commented regarding the special nature of phone card contracts, "handing over a package—a phone card or prepaid cellular—does not provide an opportunity for a formal contract." Segermark, *supra* note 100.

²¹⁸ 16 TEX. ADMIN. CODE § 26.34(f)(1)(B)(iv) (2006); WASH. ADMIN. CODE § 480-120-264(5)(a)(v).

²¹⁹ CAL. BUS. & PROF. CODE § 17538.9(b)(3) (West 2006).

²²⁰ Examples of fees include "monthly or other periodic fees, maintenance fees, per-call access fees, surcharges for calls made on pay telephones, or surcharges for the first minute or other period of use[.]" *Id.* § 17538.9(b)(3)(A).

²²¹ *Id.*; Illinois' and New York's requirements on disclosure of fees are similar. 815 ILL. COMP. STAT. 505/2QQ(d)(2) (2006); N.Y. PUB. SERV. LAW § 92-f(3) (McKinney 2006).

²²² 16 TEX. ADMIN. CODE § 26.34(g)(1) (2006).

²²³ *Id.* § 26.34(g)(2).

²²⁴ See Budnitz and Saunders, *supra* note 81 at 172-73.

²²⁵ Notification should not create technical problems. Texas requires sellers to inform consumers verbally when their balances are nearly exhausted. 16 TEX. ADMIN. CODE § 26.34(g)(2) (2006).

²²⁶ See *supra* text accompanying notes 184-186 discussing the requirements for lost and stolen cards that the Federal statute should impose.

²²⁷ See *supra* text accompanying notes 46-56.

²²⁸ Marlowe, *supra* note 9, at 4.

²²⁹ *Id.* at 4-5.

²³⁰ CAL. BUS. & PROF. CODE § 17538.9(b)(4) (West 2006).

²³¹ *Id.*

²³² Alan M. White and Cathy Lesser Mansfield, *Literacy and Contract*, 13 STAN. L. & POL'Y REV. 233, 264-65 (2002). ". . . disclosure statements . . . may not be able to aid most consumers in understanding the terms of their agreement." *Id.* at 261.

²³³ California and New York require live operators twenty-four hours a day and 7 days a week. CAL. BUS. & PROF. CODE § 17538.9(b)(6)(A) (West 2006); N.Y. PUB. SERV. LAW § 92-f(4) (McKinney 2006).

²³⁴ See FLA. ADMIN. CODE ANN. r. § 25-24.920(4) (2006); MO. CODE REGS. ANN. tit. 4, § 240-32.160(5) (2006), 16 TEX. ADMIN. CODE § 26.34(i) (2000). Alabama requires that the number be manned 8 hours per day, 5 days per week. AL PUB. SERV. COMM'N Rule 18.1(5) (1997).

²³⁵ Consumers in New York and California can file complaints with customer service. CAL. BUS. & PROF. CODE § 17538.9(b)(6)(C) (West 2006); N.Y. PUB. SERV. LAW § 92-f(4) (McKinney 2006).

²³⁶ This scheme is similar to that in the Electronic Fund Transfers Act, 15 U.S.C. § 1693(f) (2006).

²³⁷ N.Y. PUB. SERV. LAW § 92-f (4) (McKinney 2006). New York also requires that the operator be able to provide information about the "terms and conditions of service and monthly service charges." *Id.* § 92-f (4)(iv).

²³⁸ FLA. ADMIN. CODE ANN. r. § 25-24.920(3)(c) (2006).

²³⁹ CAL. BUS. & PROF. CODE § 17538.9(b)(1) (2006); N.Y. PUB. SERV. LAW § 92-f (McKinney 2006).

²⁴⁰ CAL. BUS. & PROF. CODE § 17538.9(b)(7) (2006); N.Y. PUB. SERV. LAW § 92-f (McKinney 2006).

²⁴¹ *Id.* The Federal statute should allow the FTC to describe technical standards because the description requires a high level of technical expertise and specificity. Moreover, the standards may need to be adjusted as technology advances over time.

²⁴² AL. PUB. SERV. COMM'N Rule T-18.1(4)(1997).

²⁴³ FLA. ADMIN. CODE ANN. r. § 25-24.925(1)(a) (2006). See also MO. CODE REGS. ANN. tit. 4, § 240-32.170(6) (2006) (providing that a company must refund the unused value remaining on cards when the "company is no longer able to provide service").

²⁴⁴ ALASKA ADMIN. CODE tit. 3, § 52.3771(e) (2006).

²⁴⁵ FLA. ADMIN. CODE ANN. r. § 25-24.925(2) (2006) (permitting, but not requiring, a refund for lost or stolen cards).

²⁴⁶ CAL. BUS. & PROF. CODE § 17538.9(b)(7) (West 2006); N.Y. PUB. SERV. LAW § 92-f (McKinney 2006).

²⁴⁷ Commercial reasonableness, failure to exercise ordinary care, good faith, and unconscionability are all standards included in the Uniform Commercial Code. Consequently, including them in the proposed statute is not a novel approach. See U.C.C. §§ 3-103(a)(6) & (9) (2002); U.C.C. § 2-302 (2003); U.C.C. § 9-610(b) (2000).

²⁴⁸ CAL. BUS. & PROF. CODE § 17538.9 (b)(7) (West 2006).

²⁴⁹ FLA. ADMIN. CODE ANN. r. § 25-24.930 (repealed 2005).

²⁵⁰ U.C.C. § 2-314 (2003).

²⁵¹ *Id.* § 2-316 (2003) (allowing sellers to disclaim implied warranties). See, e.g., MD. CODE ANN., COM. LAW § 2-316.1 (West 2006) (illustrating that some states prohibit sellers from disclaiming implied warranties in consumer transactions).

²⁵² See Budnitz and Saunders, *supra* note 81, at 7.7.1.

²⁵³ David Wood, *Tips on Using Prepaid Phone Cards*, MILITARY MONEY MAG., available at <http://www.militarymoney.com/lifestyle/1065704890> (last visited Oct. 5, 2006).

²⁵⁴ Examples of defects include access numbers or PINs that do not work and other defects making it impossible for the card to operate as it should. A lost PIN may never be found. In that situation the consumer has paid money for the card and the seller never has to provide any more value. The card issuer may be required to transfer those funds to the state under

abandoned property or escheat laws. Even where those laws apply to prepaid phone balances, the seller has the use of those funds until they are paid to the state. *See* Luna, *supra* note 18; *Big Retailers Agree to Replace Gift Cards, supra*, note 204.

²⁵⁵The statute should delegate to the FTC the authority to study the actual costs to sellers of replacing cards in order to establish more specific guidelines for what would constitute a reasonable fee.

²⁵⁶*E.g.*, Electronic Fund Transfers Act, 15 U.S.C. § 1693 (2006).

²⁵⁷A comprehensive critique of mandatory predispute arbitration in phone card contracts is beyond the scope of this article. *See* Symposium, *Mandatory Arbitration*, 67 LAW & CONTEMP. PROBS. 1 (2004) (showing that mandatory arbitration agreements are a substantial barrier to consumers' ability to obtain meaningful relief).

²⁵⁸16 TEX. ADMIN. CODE § 26.34(e)(4) (2000) (requiring that prepaid calling card service companies register with the Public Service Commission).

