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E-TAILING AND DIRECT MARKETING

Surveys and Sweepstakes May Run Afoul of "Do Not Call" Rules

In 2005, the National Do Not Call Registry, established pursuant to the FTC's Telemarketing Sales Rule, topped 100 million registered phone numbers. The FTC, the Department of Justice's Office of Consumer Litigation, and New York Attorney General Elliot Spitzer are taking action to pursue retailers who they contend attempt to circumvent the Do Not Call regulations through such methods as conducting surveys that lead to sales calls and including authorizations to call in the fine print of sweepstakes rules.

On December 29, 2005, the Department of Justice's Office of Consumer Litigation filed a Complaint against FMFG, Inc., d/b/a American Adjustable Beds, Tranquility Adjustable Beds, and California Sleep Research, in the United States District Court for the District of Nevada. The Complaint alleges that FMFG, Inc. violated the FTC's Telemarketing Sales Rule ("TSR") by calling consumers under the guise of conducting a legally permissible survey, but after asking consumers to "take a survey of their sleep habits [Defendants] then attempted to sell them adjustable beds." The government seeks \$11,000 for each alleged violation, and claims that there are more than 900,000 violations.

On February 22, 2006, Defendants moved to dismiss the Complaint for lack of specificity and failure to allege the proper number of violations. Defendants also claim that they are exempt from most of the TSR, and object to the "absurdity" of the potential \$9,900,000,000 fine.

In April 2005, New York Attorney General Elliott Spitzer entered

into an Assurance of Discontinuance with the Great Atlantic & Pacific Tea Company, Inc. (the "A&P") and Kitchen Magic, Inc. in which the A&P and Kitchen Magic agreed to discontinue calling sweepstakes entrants whose phone numbers were registered on the Do Not Call Registry. In 2004, the A&P conducted the "Kitchen Magic Sweepstakes" at participating locations. Customers who purchased any two of the promotional products (which included familiar products such as Cottonelle, Huggies, Glass Plus, Kleenex and Lysol) received a Kitchen Magic Make-Over game piece. A game board was provided in the store circular at participating stores during the first week of the promotion, and was also available on the A&P's website.

Participants were required to give their telephone number to participate in the sweepstakes. Attached to each game piece was an entry form that provided space for the entrant to print his name, address, and phone number and instructions for mailing the entry form. To the right of the provided space was printed language that gave Kitchen Magic permission to call the entrant. Also, the game board contained in fine print the following language:

By completing this form, entrant grants Kitchen Magic permission to place courtesy calls to their household to offer more information and a free estimate for Kitchen Magic products and services. This permission supersedes any previous or

subsequent registration on any state or federal "Do Not Call" lists.

Attorney General Spitzer claimed that Kitchen Magic and the A&P had engaged in deceptive practices by requiring consumers wishing to participate in the sweepstakes to relinquish their Do Not Call protection on the basis of a disclosure they may not have seen. The A&P and Kitchen Magic entered into an Assurance of Discontinuance with the Attorney General and agreed not to

- (1) Insert authorization clauses for calls to entrants' households on any entry forms for any game, contest, sweepstakes or chance promotions;
- (2) Utilize any telephone number information obtained from any game, contest, sweepstakes, or chance promotions submissions for any purpose whatsoever other than to notify the winner(s) of the sweepstakes; and
- (3) Insert language into the sweepstakes rules and regulations or on any entry forms used in conjunction with the sweepstakes which authorize calls to the sweepstakes' entrants notwithstanding the entrants' current or subsequent registration on any "Do Not Call" registry.

The A&P and Kitchen Magic also agreed to pay \$100,000 in penalties and costs.

DirectTV Will Pay the FTC \$5.3 Million for "Do Not Call" Violations

Satellite television provider DirectTV has agreed to pay \$5,335,000 to settle charges that it violated the Do Not Call provisions of the FTC's Telemarketing Sales Rule. The FTC's Complaint alleged that DirectTV, along with five telemarketing firms and their principals, were liable for calling Do Not Call registrants and for "call abandonment," a violation of the requirement that a live sales representative be on the line with a consumer within two seconds after the consumer's greeting.

In addition to the monetary penalty, the agreement: (i) requires DirectTV to terminate any telemarketer DirectTV "knows or should know" is making cold calls to consumers without express, written authorization from

DirectTV; (ii) requires DirectTV to monitor its telemarketers for compliance with FTC regulations, which includes among other things establishing a system to receive and retain complaints from consumers related to the telemarketing of DirectTV goods and services; and (iii) prohibits DirectTV from assisting any telemarketer DirectTV "knows or consciously avoids knowing" is violating the Telemarketing Sales Rule.

FTC Chairman Deborah Platt Majoras stated: "This multimillion dollar penalty drives home a simple point: Sellers are on the hook for calls placed on their behalf. The Do Not Call Rule applies to all players in the marketing chain, including retailers and their telemarketers."

Philip Morris And Thirty Seven State Attorneys General Seek To Curb Illegal Internet Cigarette Sales

Tobacco giant Philip Morris USA has agreed to help the Attorneys General of 37 states and U.S. territories ensure that its products are not sold to retailers that break state or federal laws when they market cigarettes over the Internet. In January 2006, it signed a protocol designed to shut down illegal Internet cigarette traffickers by depriving them of the inventory they need to stay in business. The Attorneys General contend

that many such retailers break state age verification laws, state laws barring the shipment of cigarettes directly to consumers, state tax laws, federal mail and wire fraud laws, and the federal RICO Act.

The protocol refers to companies that buy directly from Philip Morris USA and resell online as "Direct Buying Customers." Under the protocol, an Attorney General whose state is a party to the protocol may notify Philip Morris when it believes a Direct

Buying Customer is violating state or federal law. The Attorney General must give Philip Morris a “reasonable legal and factual basis” for the position that particular sales are illegal. When Philip Morris receives such a notice from an Attorney General, it will suspend sales of its product to the Direct Buying Customer for a minimum of thirty days, and ultimately until the Direct Buying Customer provides “adequate assurance” to the Attorney General that it will abide by the law. The thirty-day minimum period applies unless the Direct Buying Customer can demonstrate that the Attorney General’s belief that the Direct Buying Customer was operating illegally was incorrect.

In addition, the protocol imposes sanctions on Direct Buying Customers that resell Philip Morris cigarettes to third-party vendors who in turn illegally sell the cigarettes over the Internet. Again, the Attorney General must give notice to Philip Morris and the Direct Buying Customer that the third-party vendors are selling Philip Morris cigarettes illegally. The Attorney General also must demonstrate that the Direct Buying Customer knew or should have known about the third-party vendor’s illegal conduct. Philip Morris will then reduce the volume of its sales to the Direct Buying Customer until the Direct Buying Customer assures the Attorney General that it has stopped doing business with the offending third-party vendor – or that the third-party vendor is complying with the law.

Finally, the protocol provides that Philip Morris will suspend from its incentive programs any retailer that an Attorney General deems to be acting in violation of state or federal law. Any such suspension remains in effect until the retailer provides adequate assurance to the Attorney General that it is complying with the law.

The protocol is the third step in a campaign by the Attorneys General to curb illegal Internet cigarette sales. In March of last year, major credit card companies agreed to stop processing payments for retailers who sell cigarettes on the Internet illegally. In addition, DHL and UPS agreed to stop shipping packages for Direct Buying Customers who engaged in illegal cigarette sales.

The participating states and U.S. territories are: Alabama, Arkansas, American Samoa, California, Colorado, Connecticut, Delaware, District of Columbia, Georgia, Hawaii, Idaho, Illinois, Iowa, Kentucky, Louisiana, Maryland, Massachusetts, Michigan, Montana, Nevada, New Hampshire, New Jersey, New Mexico, New York, Northern Marianas, Oklahoma, Oregon, Puerto Rico, South Carolina, South Dakota, Tennessee, Utah, Vermont, Washington, West Virginia, Wisconsin and Wyoming.

CONSUMER CREDIT

Ameriquest Enters \$325 Million Settlement with 49 States and D.C.

After two years of investigations by Attorneys General and prosecutors in 49 states and the District of Columbia, in January of this year California-based Ameriquest Mortgage Company settled allegations of consumer fraud arising from its home lending activities. The investigations were launched in response to numerous complaints and suits claiming that Ameriquest, the country’s largest privately held retail mortgage lender, systematically engaged in abusive and deceptive lending practices such as fraudulently inflating property appraisals, misrepresenting loan terms, charging unjustified fees and penalties, fabricating borrowers’ incomes, and using high pressure sales tactics. The settlement agreement provides for entry of stipulated judgments, consent decrees or administrative settlement documents, depending upon the jurisdiction, incorporating the settlement terms.

The settlement requires Ameriquest to pay a total of \$325 million, which includes \$295 million in restitution to consumers over the next year and \$30 million to the states for attorney’s fees and investigation costs. The settlement further requires Ameriquest

to make disclosures to prospective borrowers and limits Ameriquest’s lending practices.

Under the settlement, Ameriquest must fully and accurately disclose interest rate information, loan terms, points and other fees or charges, and the settlement provides sample scripts for the required oral disclosures. For example, if a proposed “non-prime” loan, defined as a mortgage loan above a certain rate, includes an adjustable rate provision, Ameriquest must provide an oral disclosure in substantially the following form:

- “The loan we have been discussing is an adjustable rate loan for \$[insert loan amount], with an initial interest rate of [insert initial interest rate]%. Your initial monthly payment would be \$[insert initial monthly payment], which does [or does not] include escrows for property taxes or insurance. Your loan does [or does not] include a prepayment penalty.
- Because this is an adjustable rate loan, the initial interest rate and monthly payment I quoted you are only guaranteed for the first [insert length of initial fixed rate period] of the loan. After that, your interest

rate can increase by up to [insert rate adjustment cap] percent each year. But, your interest rate can never be higher than [insert lifetime cap] percentage points over your initial interest rate.”

- [NOTE: If the Sales Person has not previously discussed a specific Fixed Rate Mortgage proposal with the Potential Borrower, the Sales Person shall also provide an additional oral statement in substantially the following form.]
- “You may be eligible for a loan with an interest rate that does not change.”

Ameriquest must also provide written disclosures. Early in the application process Ameriquest is required to present the borrower with a single page disclosure stating the terms of the proposed loan. In the event of a material change in the loan’s terms prior to closing, Ameriquest is required to supplement the initial disclosure.

The settlement prohibits Ameriquest from: (i) misleading a borrower regarding the competitiveness of the offered interest rate or other terms of the loan; (ii) encouraging the fabrication or misstatement of the borrower’s income; and (iii) soliciting a refinancing within the first two years after the loan’s origination.

The settlement also mandates revisions to Ameriquest’s compensation system, as for example by requiring Ameriquest to eliminate incentives that reward employees who include prepayment penalties or excessive fees or closing costs in loan documents.

The settlement provides for internal compliance monitoring by Ameriquest and for the appointment of an independent monitor.

Free Credit Reports For Only \$79.95/Year; Consumerinfo.Com Settles FTC Deceptive Trade Practice Action

After nearly two years of informal complaints and negotiations, in August 2005, the FTC sued Consumerinfo.com, Inc., an Experian company. The Commission charged that Consumerinfo.com engaged in deceptive trade practices by advertising free credit reports without adequately disclosing that access to the credit report was contingent upon enrollment in a credit monitoring service. The \$79.95 annual fee for the service was charged to the consumer’s credit card if the consumer did not cancel the service before the expiration of a thirty day trial period. Consumerinfo.com would then automatically charge the consumer’s credit card a renewal fee of \$79.95 every year thereafter unless the service was cancelled by the consumer.

Upon filing of the FTC Complaint, the parties agreed to a stipulated final judgment and order for injunction in which Consumerinfo.com, without admitting any wrongdoing, agreed to: (i) modify its advertisements and website to clarify that consumers must enroll in a credit monitoring service to receive a free credit report; (ii) disclose the means by which consumers may obtain free credit reports under federal law; (iii) cancel credit monitoring services for and provide refunds

to certain consumers who were enrolled in the service between November 1, 2000 and September 15, 2003; (iv) pay the FTC \$950,000 plus the proceeds of any refund checks uncashed after a certain period of time; (v) submit to monitoring and investigation by the FTC; and (vi) provide documentation of compliance with the order and injunction.

Consumerinfo.com has advertised free credit reports to consumers contingent upon enrollment in its various credit monitoring services since at least 1997, and has used descriptive URLs such as www.freecreditreport.com since 1999. However, in December 2004, the www.annualcreditreport.com website was launched as a means for west coast consumers to access free copies of their credit report as mandated by the Fair and Accurate Credit Transactions Act (“FACT Act”), amending the Fair Credit Reporting Act, 16 U.S.C. § 1681, et seq. The website and access to free credit reports online under the FACT Act became available to east coast consumers in September 2005. Thus, the FTC was likely spurred into action in large part due to the increase in the number of consumers attempting to obtain their credit reports online and the resulting confusion. In addition to the

Consumerinfo.com lawsuit, the FTC sent letters to entities maintaining approximately 130 websites warning against similar practices, and has issued consumer alerts on its own website.

It is too early to assess the impact of the FACT Act and the Consumerinfo.com settlement on private litigation involving advertisements for free credit reports.

New York Attorney General Prevails in Suit Against Sub-Prime Credit Card Issuer

In January 2006, a New York State trial judge ordered a sub-prime credit card issuer and its debt collector to pay nearly \$9 million in restitution and penalties. New York Attorney General Eliot Spitzer sued Cross Country Bank, Inc., a leading national sub-prime credit card issuer, and its debt collector Applied Card Systems, Inc. for engaging in fraud, false advertising, deceptive business practices and illegal debt collection practices. Both Cross Country Bank and Applied Card Systems have been under investigation for their business practices in several states across the country. The New York suit alleged that Cross Country Bank solicited consumers with poor credit histories, offering credit lines of up to \$2,500. The court found that these offers were deceptive as the vast

majority of consumers who applied received only about \$400 in credit. Thus far, there has been one reported class action lawsuit filed against Consumerinfo.com in federal court in Illinois. On December 15, 2005, the district court denied class certification, and the lawsuit is stayed pending appeal of the class certification issue to the Seventh Circuit.

majority of consumers who applied received only about \$400 in credit.

In addition, the bank immediately applied much of the credit granted to various fees, such as application fees, monthly maintenance fees and annual fees. The bank also added on fees for services such as “Applied Advantage” and “Credit Account Protection,” causing cardholders to exceed their credit limits within the first two billing cycles. The bank then applied overlimit fees and late fees.

The court found that all of the fees were not adequately disclosed and ordered that restitution be paid to thousands of New York consumers. While the bank argued that restitution could not be ordered without individualized determinations

of consumer reliance on the solicitations and representations, the court held that a presumption of actual reliance arose once the Attorney General showed that there were widely disseminated material misrepresentations that at least some consumers acted upon. The court noted that nearly 50,000 New York consumers received the deceptive credit solicitations and assessed a penalty accordingly. The court determined that a \$120 per consumer penalty was appropriate, and the resulting penalty was almost \$6 million.

Additionally, the “Credit Account Protection” program Cross Country Bank offered was advertised as providing several insurance benefits that New York customers who enrolled in the program did not actually receive. Upon enrolling in the program, New York consumers were sent an insurance certificate granting coverage for death and dismemberment, with no indication that these were the only eventualities for which there was coverage. The court stated that this was deceptive, as consumers could reasonably believe that they would receive the additional coverage described in the advertisements.

The court also addressed Applied Card System’s debt collection practices and awarded restitution and penalties for consumers whose accounts were “re-aged.” Applied Card Systems told many consumers that their accounts would be

made current and not subject to further late fees if they made a specified payment. However, Applied Card Systems failed to tell those consumers that the payment would be insufficient to avoid overlimit fees on any balance that exceeded their credit limits. The court also penalized Applied Card Systems for its “assumptive pay-by-phone” practice by which Applied Card Systems deceived consumers into erroneously believing they had authorized payments to their credit card accounts from their checking accounts.

Complaints against Cross Country Bank and Applied Card have been filed, or investigations launched, in at least eight other states. In West Virginia, for example, Cross Country Bank and Applied Card Systems were ordered to pay \$1.5 million in restitution last year based on allegations similar to those made in the New York suit.

Seventh Circuit Upholds Sanctions Against Illinois Law Firm For Frivolous FDCPA Claim

Recently, an aggressive response to a \$125 collection letter cost a Chicago law firm \$18,000 in sanctions. In a procedurally unusual case, the Seventh Circuit Court of Appeals held that the firm was properly sanctioned for making a frivolous threat to sue under the federal Fair Debt Collection Practices Act (FDCPA).

The case, *Riddle & Associates, P.C. v. Kelly*, 414 F.3d 832 (7th Cir. 2005), arose after a woman named Judith Kelly wrote a bad \$100 check to an Illinois riverboat casino. The casino retained Riddle & Associates, a Utah law firm, to collect the debt. After the Riddle firm sent a collection letter to Kelly demanding the \$100 plus a \$25 service fee, Kelly retained Edelman, Combs & Lattuner, a Chicago firm. The Edelman firm then sent the Riddle firm a letter threatening to sue the Riddle firm under the FDCPA and demanding \$3,000 in damages and attorney's fees. The Edelman firm claimed that the collection letter violated the FDCPA because the notice contradicted and overshadowed Kelly's right to dispute the debt.

Rather than waiting to see if the Edelman firm followed through with its threatened suit, the Riddle firm sought a declaratory judgment in federal court, requesting that the district court declare

that its collection letter did not violate the FDCPA. The district court granted summary judgment in favor of the Riddle firm, finding that the language in the collection letter was virtually identical to language in a collection letter which the Seventh Circuit had approved in another case. The court also characterized the Edelman firm's response to the collection letter as an attempt to "extort money from Riddle by saying it would go away for \$3,000, even though it could not have believed that its overshadowing argument had any chance of success in court." Thus, the court awarded sanctions of \$18,000. The Seventh Circuit affirmed the sanctions, noting that the Edelman firm was responsible for causing the Riddle firm to file suit because of the frivolous FDCPA claim made in its demand letter.

FALSE ADVERTISING

Recent NAD Decisions of Interest

The National Advertising Division of the Council of Better Business Bureaus has issued the following recent decisions of interest.

Manufacturer Must Support Claims of Product Efficacy with Clinical Testing of the Product as Formulated for Sale

The NAD, as part of its routine monitoring program, requested substantiation for claims made in television and Internet advertising for HeadOn Headache Relief products, which are manufactured by Miralus Healthcare. The products are pads saturated with homeopathic substances, which the consumer is to apply directly to the forehead.

The FDA recognizes the marketing of homeopathic pharmaceuticals in the United States, so long as the products meet certain conditions in the FDA's Compliance Policy Guide 7132.15 "Conditions Under Which Homeopathic Drugs May Be Marketed." The advertiser asserted that HeadOn Headache Relief products were manufactured, labeled, and marketed in compliance with that policy guide. All of the products' active ingredients were labeled as homeopathic and officially listed

and monographed in the Homeopathic Pharmacopeia of the United States, the official compendium of homeopathic drugs under Section 201(j) of the Food, Drug, and Cosmetic Act. The advertiser argued that as homeopathic drugs included in the Homeopathic Pharmacopeia, the active ingredients in their HeadOn Headache Relief products were determined to be effective by competent legal authority.

While the NAD took no issue with the advertiser's assertion that its products were manufactured, labeled, and marketed as a homeopathic drug in full compliance with the policy guide, the NAD found problematic the advertiser's general claims of product efficacy for the treatment of headaches, migraines, and sleeplessness. These claims included the following: "An entirely new and advanced headache treatment applied directly to the forehead;" "...providing consumers with a...way of treating some of their most common health problems: headaches, migraines, and pain with sleeplessness;" and "HeadOn provides Fast, Safe, effective [headache] relief... ."

The NAD stated that as a general rule, health-related advertising claims must be supported by competent and reliable scientific evidence. This evidence typically takes the form of well-controlled studies,

the results of which relate directly to the performance promised in the advertising. The NAD found that “notwithstanding the advertiser’s submissions regarding the ‘clinical provings’ in support of [the ingredients], the record is devoid of any testing (clinical or otherwise) on any of the HeadOn products as formulated for sale for use as directed.” Furthermore, the advertiser was found to have “failed to provide any evidence permitting extrapolation from the clinical provings to the specific claims made for its product as formulated for sale.”

In its statement following the issuance of the NAD’s decision, the advertiser maintained that the NAD’s decision that advertisers are required to substantiate the efficacy of their marketed products as formulated for sale “is entirely inconsistent with FTC precedent that indicates that there is no precise standard for what constitutes ‘competent and reliable scientific evidence’ and that studies conducted on a specific active ingredient (or ingredients) may be sufficient to substantiate claims for a product as formulated for sale.”

Consumer Use Testing Found to be Proper Method of Substantiating Claims of Product Superiority in the Tampon Market

Proctor & Gamble, the manufacturer of Tampax tampons, challenged superiority and exclusivity claims made by Playtex

Products, Inc. in its television commercials for Gentle Glide tampons.

The first claim Proctor & Gamble challenged was “Get Playtex Gentle Glide... for unbeatable...protection.” To substantiate this claim, Playtex submitted the results of a synerga test, a test mandated by the FDA to test tampon absorbent capacity. Proctor & Gamble asserted that measuring a tampon’s ability to prevent leakage is very different from measuring how much liquid a tampon can absorb in a laboratory setting. Proctor & Gamble asserted that several elements of a tampon’s design affect the tampon’s ability to protect against leakage, and that absorbency is only one of those factors. The NAD agreed with Proctor & Gamble, and held that “absorbency is one aspect of protection and the advertiser itself considered them two components in the prevention of leaks.” The NAD found that relying on a synerga test “would not suffice to support an ‘unbeatable protection’ claim.” Instead, the NAD found that “consumer use testing is better suited to substantiating the advertiser’s ‘unbeatable protection’ claim.” Since Playtex had no consumer use testing data, the NAD recommended that Playtex discontinue its use of its “unbeatable protection” claim.

Proctor & Gamble also challenged the claim in Playtex’s Gentle Glide tampon television commercial: “The only one that blooms to fit.” The claim was shown

simultaneously with an image of a flower, before and after blooming. Proctor & Gamble asserted that this claim was false because all tampons expand to prevent leakage, and thus, Playtex’s Gentle Glide is not unique. The NAD found that one reasonable interpretation of the advertisement was that “the Gentle Glide, unlike other tampons, opens up like a flower.” However, the NAD found that another reasonable interpretation “is that [the Gentle Glide tampon] is the only one that expands to fit inside...because flowers necessary expand when they ‘bloom.’” The NAD found that this interpretation could reasonably “imply that competing tampons do not so expand and thus provide less protection against leaks.” The NAD agreed with Playtex that the Gentle Glide “is unique in that, unlike other tampons, it has two absorbent pads, and that the pads, when removed from the applicator and unfolded, form a flower-like shape.” Playtex is permitted to distinguish its product, and it “can (and should) underscore that its product contains two absorbent pads instead of one.” But, since all tampons expand, once inside, in order to prevent leaks, the NAD recommended that Playtex discontinue the use of the term “only” in connection with its “blooms to fit” claims.

Avon Advertisements for “At-Home” Skin Care Products Mislead Consumers by Using Language Commonly Associated with Medical Procedures

Anew Clinical Lift and Tuck, and Anew Deep Crease Concentrate, both produced by Avon Products, Inc., were the subject of a four-page advertisement that was reviewed by the NAD as part of its routine monitoring program. The NAD requested substantiation from Avon for certain express and implied performance claims made in the advertisement.

To support its claims concerning Anew Clinical Lift and Tuck, Avon produced an independent, randomized, twelve-week, baseline-controlled, efficacy study. The study showed statistically significant results, primarily for the “laxity parameter for the abdomen, buttocks, hips, and thighs.” Based on these results, the NAD found that the advertisement’s general performance claims (i.e., “Anew Clinical Lift and Tuck reduces jiggle and sag;” “With Vacu-Shape Technology, it tightens the skin;” and “96% of the women had tighter skin of the abdominal area and 100% had a more lifted rear”) were substantiated.

The NAD, however, found that other claims in the advertisement “convey[ed] the unsupported message that [Avon’s] product[s] can confer performance benefits comparable to those achieved by surgical procedures.” These claims included

statements like “Put your tummy and butt in their place” and “Proven to tuck the tummy and lift the rear.” The NAD found that this second claim “clearly reference[s] product performance in the terms of the actual surgical procedures (tummy tuck; buttock lift) that the advertiser contends are not points of comparison.” This was particularly the case, the NAD concluded, because the advertisement included a visual reference to a hypodermic needle, along with the tagline “Needle? Knife? Lipo? No.”

The advertisement referred to the product as an “alternative” and not a “substitute” for a cosmetic procedure. However, the NAD found that claims like “Put your tummy and butt in their place” and “Proven to tuck the tummy and lift the rear,” when combined with the visual of the hypodermic needle, “could reasonably communicate that [the product] produces results similar to plastic surgery, a message the advertiser may not have intended to convey but nevertheless could not support.” The NAD also found the language of “restor[ing]” a tighter tummy” and “reshap[ing]” your rear to be problematic, because they suggest that “one can turn back the clock, achieving a pre-cellulite, pre-sagging look the surgical procedures are intended to produce and which [the product’s] testing results do not demonstrate.”

Similarly, the NAD found that Avon’s Anew Deep Crease Concentrate

advertisement falsely “impli[ed] that [Avon’s] product performs an equivalent function to Botox and/or collagen injections.” The NAD noted that the advertisement’s claim that the product is an “alternative” to “line-relaxing” injections was, standing alone, non-problematic. However, this claim was linked to another claim that the product “relaxes and levels lines in a single concentrated drop.” The NAD found that this claim latter “speaks to product performance using the same terms (“relaxes” lines) that describes the effects of the cosmetic procedure it is not intended to compare.” While statistically significant results were seen in the product’s testing, “none of the evidence in the record shows that one drop of the product can level lines.”

Serta Must Improve its Substantiation and Modify its Comparative Claims in its Advertisements for Serta FireBlocker Mattresses

Serta, Inc. ran a series of Internet, print, and broadcast advertisements for its line of “FireBlocker” mattresses. The claims in these advertisements were challenged by Sealy, Inc., a competing mattress manufacturer.

Among other things, Sealy argued that Serta’s claims inflated the number of children’s deaths caused by bedroom fires each year. Sealy asserted that the advertising campaign conveyed the

false message that mattresses by Serta’s competitors would “go up in flames and kill your sleeping children” and that “only” a mattress with Serta’s FireBlocker could save your children. Sealy challenged exclusivity claims in the advertisements, arguing that it also sells “nationally branded mattresses with an open-flame retardant system.” In addition, Sealy also argued that the term FireBlocker was literally false, and used to imply fire-proof capabilities; that the fibers contained in the Serta FireBlocker mattress only slow down, and do not block, the spread of flames; and that Serta’s advertisements imply the literally false notion that a “small flame” coming into contact with a mattress sold by a Serta competitor will become a “roaring fire” in less than three minutes.

The NAD found several problems with Serta’s claims. First, Serta’s advertisements claimed that “Hundreds of [i.e., 200 or more] children die in bedroom fires every year.” Because there was no single study that analyzed the number of children who died each year from bedroom fires, Serta pooled data obtained in the 1990’s to obtain its figure that “hundreds of children” die. The NAD was “troubled” by Serta’s reliance on “out of date” data, and by its “pooling of disparate databases.” The NAD held that “[i]t is well established that when used for advertising substantiation, methodologies and study populations must be sufficiently consistent so that pooling of

results is consistent.” The NAD found no evidence that the data relied upon was sufficiently similar to permit such pooling, and thus, the NAD determined that Serta had no reasonable basis for this claim and recommended that Serta discontinue its use of the claim.

Serta’s “Your Current Mattress” television spot displayed two bare mattresses, one burning with flames and identified as “Your Current Mattress.” The other mattress is only scorched, and it is identified as a “SERTA®FIREBLOCKER” mattress. The spokesman stated that “[t]his is a Serta mattress with FireBlocker after the same amount of time...[FireBlocker] assures valuable escape time. Only Serta has FireBlocker—not Sealy, not Simmons, only Serta! Why would you buy any other mattress?” The NAD found that it was “undisputed” that Sealy also made open-flame fire-resistant mattresses, sold nation-wide. While Serta argued that “your current mattress” was probably non-compliant with the new California open-flame flammability standard, because the standard was so new, the NAD found that this claim was no longer accurate. Serta was cautioned not to equate the absence of Serta’s FireBlocker technology with being “unprotected,” as it did in both the “Your Current Mattress” advertisement, and in its claim that “[w]ithout FireBlocker technology, an unprotected mattress ignited by a small flame can easily become

a roaring fire in less than three minutes.” The NAD determined that the comparative claim should be modified to “clearly specify as a basis of comparison a mattress without open-flame fire resistant protection like FireBlocker technology.” However, the NAD did find that Serta could continue to use the claim “Only Serta has FireBlocker,” because FireBlocker is the registered trademark for Serta’s proprietary technology.

The NAD also found problems with the claim that “FireBlocker is a blend of...fibers... that block the spread of an open flame into the mattress.” While Serta asserted that the claim describes exactly how its proprietary technology works, the NAD determined that Serta “did not provide a reasonable basis for its unqualified claim that its FireBlocker mattresses ‘block’ the spread of fire.” Instead, “[a]s the advertiser concedes, its FireBlocker technology is intended to slow down and delay the spread of an open flame.” Thus, the NAD recommended that the claim “be modified to more accurately describe the technology.”

Advertisements for Johns Manville’s “Formaldehyde-Free” Insulation Falsely Implied that Formaldehyde-Bonded Fiberglass Insulation is Unhealthy

The Formaldehyde Council, Inc., an association of leading formaldehyde producers and users, challenged a series of print advertisements for Johns Manville’s

“formaldehyde-free” insulation. The Formaldehyde Council argued that the tests supporting the “formaldehyde-free” claim were not sufficiently precise because they did not test whether the product emitted any formaldehyde at all. In support of the claim, Johns Manville submitted the results of two independent laboratory tests, both of which indicated that there were no detectable levels of formaldehyde emissions from the product. The NAD noted that “[w]hen reviewing advertising claims about a product’s ability to eliminate a particular substance, NAD has held that the detection of de minimis amounts of that substance will not necessarily bar the advertiser from making the elimination claim.” In this case, the NAD noted that the amount of formaldehyde that a person is exposed to outdoors is more than three times greater than the amount emitted by the product in the laboratory tests. Furthermore, the amount emitted by the product in the laboratory tests was a tiny fraction of the maximum recommended exposure levels. Thus, the NAD determined that Johns Manville provided a reasonable basis for the claim.

However, the NAD did find other problems with the ads. One advertisement depicted a sleeping child clutching a teddy bear, along with the copy: “We got rid of formaldehyde in the insulation. So now all you have to worry about is getting rid of the monsters underneath the bed.” The

advertisement also read: “It’s easy to get rid of the formaldehyde that lurks behind the walls of your children’s rooms,” and “Who knows, this insulation may even help you sleep better.” The NAD found consumers could reasonably take away from the advertisement as a whole the implication that standard formaldehyde-bonded insulation, in and of itself, is a health risk. In fact, insulation containing formaldehyde is only one of many formaldehyde-emitting products found in the home. The NAD determined that this advertisement was more about disparaging a competing product than about simply alerting consumers to a product benefit. The NAD therefore determined that Johns Manville should discontinue this advertisement.

Similarly, the NAD was troubled by an advertisement that stated: “On June 15, 2004, the International Agency for Research on Cancer (IARC) designated formaldehyde as a known human carcinogen (cancer causing).” The NAD noted that “[i]t is well established that even literally true claims may be misleading based upon the context in which they are presented.” Here, consumers “could reasonably take away the message that the formaldehyde found in standard fiber glass insulation has carcinogenic effects.” However, this classification of formaldehyde, in and of itself, “cannot support a claim about the health effects of the substance in the amounts it appears in insulation.” Thus, the NAD determined that this claim should be discontinued.

DECEPTIVE TRADE PRACTICES

H&R Block Sued for Consumer Fraud (Again)

On March 15, 2006, New York Attorney General Eliot Spitzer sued H&R Block, the nation’s largest tax preparation company, for failing to disclose the high cost of maintaining savings accounts. The Complaint alleges deceptive business practices, common law fraud, and breach of fiduciary duty. According to the Complaint, H&R Block advised clients to buy an “unsuitable, fraudulently marketed, poorly performing, fee-ridden ‘retirement vehicle’ called the

Express IRA that actually shrinks over time.”

Between 2001 and 2005, H&R Block attempted to expand its business by offering financial services to its customers, including more than 500,000 “Express IRA” accounts. H&R Block marketed these accounts to low-income clients, many of whom had never had a savings account, and advertised them as “a better way to save,” promising “great rates.” By 2002, according to the Complaint, H&R Block knew that

high maintenance fees and penalties resulted in negative rates of return for its Express IRA account customers. In most cases, the required maintenance fee exceeded the interest. The Complaint refers to an e-mail from an H&R Block district manager to the company's CEO, advising of fundamental deficiencies in the Express IRA accounts and the detriment to customers. The CEO forwarded the e-mail to the Express IRA product manager, adding his own concerns. However, the company made no changes to the accounts.

The Attorney General alleges that in

addition to charging fees that resulted in a net loss for customers, the company also failed to adequately disclose those fees, by not providing customers with a written document describing all of the Express IRA's fees in a comprehensible format before the customer decided to open an account. The Complaint also alleges that the company negligently misrepresented the Express IRA accounts by failing to ensure that its tax professionals understood the complex product.

H&R Block has stated that it "believe[s] in the Express IRA product and [is] proud of the opportunities it presents" to clients.

PRIVACY

Shoe Retailer DSW Settles FTC Charges of Failing to Protect Customer Data

In March 2005, shoe retailer DSW issued a press release stating that credit card and other purchase information concerning some 1.4 million customers had been stolen from its computer networks. A month later DSW began sending customer notification letters alerting them of this security breach. Among the recipients of these letters was FTC Chairman Deborah Platt Majoras.

The FTC filed an administrative complaint against DSW for failing to take reasonable security measures to protect sensitive customer data. The FTC has

brought a total of seven data security cases, but the import of this case lies in the Commission's change of strategy. Whereas the first five cases charged "deception," which requires the FTC to find examples where a company made promises of data security to its customers but failed to provide that security, the two latest cases (against DSW and BJ's Wholesale Club, Inc.) charged "unfairness," which requires the FTC to show: "(1) the practice is likely to cause substantial injury to consumers that is not offset by countervailing benefits to consumers or competition and (2) the

harm cannot reasonably be avoided by consumers."

The complaint alleges that DSW engaged in practices that when taken together, constituted a failure to provide reasonable and appropriate security. Among other things, DSW: (i) "created unnecessary risks to the information by storing it in multiple files when it no longer had a business need to keep the information;" (ii) "did not use readily available security measures to limit access to its computer networks through wireless access points on the networks;" (iii) "stored the information in unencrypted files that could be accessed easily by using a commonly known user ID and password;" (iv) "did not limit sufficiently the ability of computers on one in-store network to connect to computers on other in-store and corporate networks;" and (v) "failed to employ sufficient measures to detect unauthorized access."

The FTC and DSW entered into a settlement on March 10, 2006. The settlement requires DSW to maintain a comprehensive information security system and specifically requires DSW to: (i) "Designate an employee or employees to coordinate and be accountable for the information security program;" (ii) "Identify material internal and external risks to the security, confidentiality, and integrity of consumer information that

could result in unauthorized disclosure, misuses, loss, alteration, destruction, or other compromise of such information, and assess the sufficiency of any safeguards in place to control these risks;" (iii) "Design and implement reasonable safeguards to control the risks identified through risk assessment, and regularly test or monitor the effectiveness of the safeguards' key controls, systems, and procedures;" and (iv) "Evaluate and adjust its information security program in light of the results of testing and monitoring, any material changes to its operations or business arrangements, or any other circumstances that DSW knows or has reason to know may have a material impact on the effectiveness of its information security program."

The settlement also requires DSW, within 180 days, to obtain an independent third-party audit of its comprehensive security program. DSW must have the security program assessed by the third-party auditor biennially for the next 20 years to ensure that the comprehensive security program remains effective in protecting customer information.

CONTRACT LAW

New York Court Rules That Stores Cannot Keep Gift Card Balances

In a decision that could encourage retailers to stop placing expiration dates on gift cards, in January a New York court ruled that money left unspent on expired gift cards escheats to the state as unclaimed property. A suburban Albany business, “Kimberly’s...A Day Spa,” which disputed that it was required to turn over the balance of expired gift cards, brought the case against the state Comptroller.

Kimberly’s argued that the sale of a gift card is a contract between the business and the customer and that under the terms of the contract, if the customer does not spend the card before the expiration date, the business has the right to keep the profit on the sale. The state Supreme Court in Albany County, however, agreed with the Comptroller that New York’s abandoned property law requires that a gift card unspent on its expiration date must be reported and escheats to the state five years after issuance.

The New York Attorney General’s office commented that the court’s decision eliminates the incentive for businesses to impose short expiration dates so they can pocket the unspent funds. The ruling applies to any retailer in New York state that issues gift cards with expiration dates. Corporate businesses not organized under

the laws of New York will not be affected by the ruling because unclaimed property escheats to the gift card issuer’s state of incorporation.

Sales of gift cards in the U.S. have increased dramatically in recent years and it is estimated that last year sales exceeded \$110 billion. New York law allows expiration dates on gift cards if the issuer makes certain disclosures before the sale of the gift card. Gift card laws vary significantly from state to state and in recent years these laws have been changing. California, for example, has banned the use of expiration dates except in certain very limited circumstances. In February, FTC Chairman Majoras told Congress that gift card issuers who fail to make clear and conspicuous disclosures may be engaging in deceptive practices and thus fall within the FTC’s jurisdiction.

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