UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF WASHINGTON
AT SEATTLE

FEDERAL TRADE COMMISSION, Plaintiff, v. JOHN STEFANCHIK, *et al.*, Defendants.	CASE NO. C04-1852RSM ORDER DENYING MOTION TO STRIKE AND GRANTING MOTION FOR PRELIMINARY INJUNCTION

I. INTRODUCTION

This matter comes before the Court on plaintiff's motion for preliminary injunction, and defendants' motion to strike. (Dkts. #2 and #35). Plaintiff argues that in numerous instances, in connection with the marketing, offering for sale, or sale of products and services about making money in the paper business, defendants have made representations that are false and misleading and constitute deceptive acts or practices in violation of section 5(a) of the FTC Act. In particular, plaintiff points to specific representations that consumers will make large amounts of money in their spare time, and will receive help from coaches who are substantially experienced in the paper business and are readily available. Plaintiff further argues that defendants did not possess or rely upon a reasonable basis that substantiated those representations. Finally, plaintiff argues that defendants, by making these false representations, also violated the Telemarketing Sales Rules.

Additionally, plaintiff asserts that both Stefanchik and Beringer should be held liable for the actions of Christensen and Atlas Marketing because Stefanchik actively participated in the telemarketing plan, and he is the sole shareholder and president of Beringer. Finally, as a result of these false and misleading representations, plaintiff alleges that consumers across the United States have suffered, and will continue to suffer, substantial monetary losses, and defendants will continue to reap unjust enrichment, unless this Court orders injunctive relief.

Defendants Stefanchik and Beringer oppose the motion. Defendants first respond with a motion to strike portions of the exhibits submitted by plaintiff in support of its motion for preliminary injunction. In particular, defendants object to numerous declarations containing statements about what a particular consumer was allegedly told by the telemarketing sales representative, asserting that those statements are inadmissible hearsay that should be excluded for purposes of the motion for preliminary injunction. Defendants also object to the declaration by plaintiff's witness Dr. Manoj Hastak, which contains the results of a survey given to a number of purchasers of Stefanchik's program. Defendants argue that much of the declaration contains inadmissible hearsay that should be excluded. Finally, defendants assert that if the court grants this motion to strike, then plaintiff cannot demonstrate the likelihood of success on the merits to justify the issuance of a preliminary injunction.

Defendant also argues that, should this Court reach the merits of the preliminary injunction motion, the FTC cannot establish that it is likely to succeed in demonstrating that Stefanchik and Beringer violated the FTC Act or the Telemarketing Sales Rules. First, defendants argue that authors are protected by the First Amendment Right to express opinions in their works, and the Mirror Image Doctrine, under which the FTC normally will not proceed against advertising claims which promote the sales of a book and other publications, protects Stefanchik because his statements regarding the alleged false earnings claims are taken directly from his book.

Second, defendants argue that consumers acting reasonably under the circumstances are

not likely to be misled by the opinions expressed by defendants because the comments, when viewed together, create a "net impression" that the representations contained in Stefanchik's materials are simply an attempt to convey to students the confidence that Stefanchik has in the program and its potential for success. Defendants further argue that formal training does not exist in the paper business; therefore, each of defendants' coaches is personally trained by Stefanchik. Thus, these factors, when taken together, form a reasonable basis for the assertion that students will receive expert coaching.

Third, defendants argue that they have a reasonable basis for the assertions in their program because Stefanchik's personal experience in creating substantial wealth supports the assertions.

Fourth, defendants argue that defendants Stefanchik and Beringer did not directly participate in the telemarketing program, and therefore, the actions taken by Christensen and Atlas Marketing cannot be imputed to them. Finally, defendants argue that any actions taken by Atlas Marketing are distinct and distinguishable, and independent from the authority and control of Stefanchik and Beringer.

II. DISCUSSION

A. Background

Plaintiff filed the instant case on August 24, 2004, following a two-year investigation of defendants' trade practices. Plaintiff alleges that defendants have violated section 5(a) of the Federal Trade Commission ("FTC") Act, and the FTC's "Telemarketing Sales Rule," through deceptive ads and marketing statements.

Defendant John Stefanchik is an entrepreneur who made his money through the process of buying and selling privately held mortgages, commonly known as paper mortgages. He is the author of the book "Wealth Without Boundaries," in which he describes how other individuals can become involved in the paper mortgage industry. Stefanchik formed defendant Beringer Corporation in Washington State in 2002. The corporation holds the copyrights to all of

Stefanchik's books, videos and other publications. Stefanchik is the president, manager, and sole shareholder of Beringer Corporation.

Defendant Atlas Marketing, Inc., is a Nevada corporation doing business in Utah. Defendant Scott Christensen is the sole shareholder and president of Atlas. Atlas conducts all of the telemarketing and promotion of Stefanchik's materials.[1]

Defendants market and sell course materials, in-person workshops, videotapes, audio tapes, and other products and services that purport to teach consumers how to purchase and/or sell privately held mortgages or promissory notes that are secured by real estate. Stefanchik has marketed and sold these products since the early 1990s; however, he has marketed and promoted his products through Atlas since 2001 and also through Beringer since 2002.

Defendants begin targeting consumers through direct mail pieces and internet advertising offering Stefanchik's book for sale. Consumers who respond to the ads and purchase the book are then called by telemarketers who attempt to sell the consumer Stefanchik's additional products and services, such as seminars, workshops, videotapes and personal coaches. Defendants are typically charged between $5000 and $8000 for these products and services, depending on the particular package the consumer chooses. Consumers who balk at the price are apparently encouraged to spread the charges over several credit cards, or encouraged to open new credit cards to pay for the program. Consumers are also apparently told that they will make their money back by the time the credit card bills are due.

Plaintiff alleges that to induce consumers to purchase Stefanchik's products and services, defendants represent to the consumers that they will learn how to become wealthy using Stefanchik's techniques. Plaintiff further alleges that defendants represent to consumers that

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[1] Plaintiff's motion for a preliminary injunction was initially brought against all defendants, both Stefanchik and Christensen in their individual capacities, and both Beringer Corporation and Atlas Marketing. However, on October 15, 2004, Christensen and Atlas Marketing voluntarily agreed to the entry of a preliminary injunction against themselves. (Dkt. #16). The preliminary injunction was entered by the Court on October 20, 2004. (Dkt. #19). Thus, plaintiff's motion continues only against Stefanchik and Beringer Corporation.

they will make large amounts of money in their spare time, as much as $10,000 every 30 days, or $2,700 for only five or six hours of work. Plaintiff asserts that, contrary to these representations, most consumers who purchase the products and services do not make large sums of money in their spare time, and many don't make any money at all.

In their telemarketing pitches, defendants also offer a one-year coaching service that defendants represent is staffed by coaches who are substantially experienced in the paper business, and who are readily available by telephone to assist consumers in finding and completing paper transactions. Plaintiff asserts that defendants' coaches do not have substantial experience in the paper or real estate business, and many times, are not readily available to assist consumers at all. Defendants claim that all coaches are personally trained by Stefanchik.

B. Motion to Strike

Defendants move to strike portions of certain exhibits submitted by the FTC in support of its motion for preliminary injunction, including: (1) the declarations of numerous consumers who purchased the Stefanchik program; (2) transcripts of recorded telephone conversations submitted with one consumer declaration; (3) statements made in telemarketing scripts; and (4) the expert declaration of Dr. Manoj Hastak. The Court will address each dispute in turn.

1. Consumer Declarations

Beyond making conclusory statements that the portions they wish to have stricken are inadmissible hearsay, defendants provide no authority or support for their request. Moreover, defendants do not even identify why they believe the statements are hearsay. Plaintiff, on the other hand, notes that the law is well-settled that evidence submitted in support of a motion for preliminary injunction need not be admissible at trial to be considered by the Court. *See, e.g.*, *Flynn Distrib. Co. v. Harvey*, 734 F.2d 1389, 1394 (9th Cir. 1984); *Ross-Whitney Corp. v. SmithKline & French Laboratories*, 207 F.2d 190, 198 (9th Cir. 1953).

The Rules of Civil Procedure reflect that principle. For instance, Rule 56, which governs motions for summary judgment, provides that affidavits "shall set forth such facts as would be

admissible in evidence." Fed. R. Civ. P. 56(e). In contrast, Rule 65, governing preliminary injunctions and temporary restraining orders, contemplates that both admissible and inadmissible evidence may be submitted. Rule 65 simply notes that "any evidence received upon an application for a preliminary injunction which would be admissible upon the trial on the merits becomes part of the record on the trial and need not be repeated upon the trial." Fed. R. Civ. P. 65(a)(2).

Finally, the Court is not convinced that the disputed statements are actually hearsay. Plaintiff notes that the statements are offered as evidence of what the telemarketers said, not for the truth of the matter asserted, and therefore, would not be hearsay if the consumers testified to the statements. For all of these reasons, the Court denies the motion to strike portions of the consumer declarations.

B. Transcripts of Recorded Telephone Records

Defendants argue that the declaration of William F. Kelly, which contains portions of transcribed telephone conversations between Kelly and an Atlas Marketing representative, contains inadmissible hearsay and has not been properly authenticated. Defendants assert that, because the taping begins mid-conversation, and there is no indication when the conversations took place, the evidence cannot be properly refuted. Plaintiff answers that the declaration itself authenticates the transcriptions, and the declarant has set forth specific dates and other details of each call. The Court agrees with plaintiff. By declaring under penalty of perjury that the transcripts are true and accurate, the witness can authenticate the transcript. *See* Fed. R. Evid. 901(a). The specific dates and details of each call set forth by the declarant support the transcripts' reliability. Thus, the Court denies the motion to strike this declaration.

C. Statements Made in Telemarketing Script

Defendants argue that Exhibit 21, which contains copies of Atlas Marketing telemarketing scripts, contains inadmissible hearsay that should be excluded. In particular, defendants object to the following portion:

> My name is _____ and my phone number is _____. Write down 5-10 hours per week. That's how much time you will need to spend. Each deal may be worth between $3,000 to $5,000 to you. You could be making money in 90 days if you do this the Stefanchik way and put in the time and effort.

Defendants do not state why they believe this constitutes inadmissible hearsay.

Plaintiffs, on the other hand, note that the script quoted was produced to plaintiff by former counsel for the defendants, Gary Hailey. In his cover letter to plaintiff, counsel represented that the script was being used to telemarket the Stefanchik program. Thus, the script is a document used in the ordinary course of business of defendants' telemarketing activities. The Court agrees with plaintiff that the script is a business record relied upon in the ordinary course of business, and as such, the statements are admissible. *See* Fed. R. Evid. 803(6).

D. Dr. Hastak's Declaration

Finally, defendants argue that portions of Dr. Hastak's declaration, which contains the results of a survey of purchasers of the Stefanchik program, should be stricken as inadmissible hearsay. Defendants based their argument primarily on the fact that they had not had the opportunity to prepare or present a rebuttal expert.

As discussed above, hearsay evidence is admissible in a preliminary proceeding. Moreover, the Court has since granted defendants' motion for time to conduct limited discovery, and defendants have presented the Court with a rebuttal expert and her opinions of the survey. Therefore, the Court agrees with plaintiff that the disputed portions of the declaration should not be stricken, and the Court denies defendants' request to do so.

C. Motion for Preliminary Injunction

The FTC seeks a preliminary injunction to redress the consumer injury caused by defendants' alleged deceptive and illegal business practices. Section 13(b) of the FTC Act and Rule 65 of the Federal Rules of Civil Procedure allow this Court to grant such preliminary relief in "proper cases." *See* 15 U.S.C. § 53(b). A proper case includes any matter involving an

alleged violation of a law which the FTC enforces. Under section 13(b), a district court may grant the FTC a preliminary injunction "upon a proper showing that, weighing the equities and considering the Commission's likelihood of ultimate success, such action would be in the public interest." 15 U.S.C. § 53(b). "Section 13(b), therefore, 'places a lighter burden on the Commission than that imposed on private litigants by the traditional equity standard; the Commission need not show irreparable harm to obtain a preliminary injunction.' Under this more lenient standard, 'a court must 1) determine the likelihood that the Commission will ultimately succeed on the merits and 2) balance the equities.'" *FTC v. Affordable Media, LLC*, 179 F.3d 1228, 1233 (9th Cir. 1999). The FTC argues that it meets both prongs of that test. For the reasons set forth below, the Court agrees.

A. Likelihood of Success on the Merits

Plaintiff argues that defendants have acted deceptively in marketing the Stefanchik program. An act or practice is "deceptive" within the meaning of the FTC Act if there is a representation, omission, or practice that is likely to mislead consumers acting reasonably under the circumstances and that representation, omission, or practice is material to the consumer's payment decision. *FTC v. Pantron I Corp.*, 33 F.3d 1088, 1102 (9th Cir. 1994). Reasonable consumers are not required to doubt the veracity of express representations, and the Court may presume express claims to be material. *Id.* at 1095-96. Implied claims are presumptively material where there is evidence that the seller intended to make the claim go to the heart of the solicitation or the characteristics of the product or service offered. *See Kraft, Inc. v. FTC*, 970 F.2d 311, 322 (7th Cir. 1992); *see also Southwest Sunsites, Inc.*, 105 F.T.C. 7, 149 (1985), *aff'd*, 785 F.2d 1431 (9th Cir. 1986); *FTC v. Figgie Int'l, Inc.*, 994 F.2d 595, 604 (9th Cir. 1993) (explaining that the law does not protect people who merely imply their deceptive claims). Furthermore, a consumer's reliance on such false claims is presumptively reasonable.

Plaintiff also argues that claims that purchasers of the Stefanchik program can make large amounts of money in their spare time are false and unsubstantiated earnings claims. Plaintiff

asserts that defendants are unable to demonstrate that they have a reasonable basis for their earnings claims. Plaintiff's argument is supported by the survey results presented by Dr. Hastak, and the numerous consumer declarations attached to the motion for preliminary injunction. In addition, plaintiff argues that defendants falsely represent in their telemarketing calls that their personal coaches are substantially experienced in the paper business and are readily available by telephone to assist consumers in finding and completing paper transactions. Plaintiff argues that these claims also violate the Telemarketing Sales Rule. Finally, plaintiff argues that Stefanchik should be held individually liable for the violations because he is involved in the daily operation of the business, and has actual knowledge of the direct mail pieces and telemarketing scripts used to sell the Stefanchik program.

Defendants first answer that the U.S. Constitution protects an author's right to express opinions in his works; therefore, advertising that restates or describes the contents of the book should also be protected. Defendants further argue that the Mirror Image Doctrine, under which the FTC will ordinarily not proceed against advertising claims which promote the sale of books and other publications, protects the Stefanchik materials. The Court finds this argument misplaced.

The FTC does not challenge the book itself, or defendants' efforts to sell the book by quoting from it; rather, the FTC seeks to halt defendants' deceptive and misleading claims made about the program that the book and other materials are used to sell. Moreover, this Court has previously determined that defendants may not assert First Amendment protection as an affirmative defense to the Complaint because the law is well settled that, once speech is deemed to be false, misleading, and commercial, it is not constitutionally protected. *See, e.g.*, *Central Hudson Gas & Elec. Corp. v. Public Service Comm. of New York*, 447 U.S. 557, 563-64 (1980); *Zauderer v. Office of Disciplinary Counsel*, 471 U.S. 626, 638 (1985); *United States v. Schiff*, 379 F.3d 621, 629-30 (9th Cir. 2004). Accordingly, the Court rejects defendants' argument.

Defendants next argue that neither Stefanchik nor Beringer can be held liable for the actions of Christensen or Atlas Marketing. Specifically, defendants argue that they cannot be held vicariously liable for Christensen and Atlas Marketing's actions because they are not agents for Stefanchik and Beringer. However, that argument is without merit. The FTC argues that Stefanchik and Beringer are directly liable for the misrepresentations they knew of and allowed to be dissemination to the public. Stefanchik reviewed the scripts used by Atlas Marketing, and therefore, was aware that the telemarketers were informing consumers that they could be making $3,000 - $5,000 per deal in just 5-10 hours per week.

Individuals are personally liable for restitution for corporate misconduct if they "had knowledge that the corporation or one of its agents engaged in dishonest or fraudulent conduct, that the misrepresentations were the type upon which a reasonable and prudent person would rely, and that consumer injury resulted." *FTC v. Publishing Clearing House, Inc.*, 104 F.3d 1168, 1171 (9th Cir. 1996). The knowledge requirement can be satisfied by showing that the individuals had actual knowledge of material misrepresentations, were recklessly indifferent to the truth or falsity of a misrepresentation, or had an awareness of a high probability of fraud along with an intentional avoidance of the truth. *Id.* The Commission, however, "is not required to show that a defendant intended to defraud consumers in order to hold that individual personally liable." *Id.*; *see also Affordable Media, LLC*, 179 F.3d at 1234. In addition, under the Telemarketing Sales Rule, sellers are strictly liable whether they make the sales themselves or arrange for another to make the sales. *See* 16 C.F.R. § 310.

The FTC has provided sufficient evidence that the telemarketers led consumers to believe that they could make large amounts of money in the paper business. (Dkts. #3 and #4, Exs. 7-23). Moreover, defendants' own advertising and direct marketing pieces make the same claims. (Dkt. #3, Ex. 6). Defendants have provided only one expert witness to rebut plaintiff's survey results, but have provided no consumer declarations or survey information of their own with contrary information. Although defendants argue that all of Stefanchik's representations are

based on his own success in the paper industry, and that all of his representations are qualified with words such as "if you put in the time and effort you could . . ." or "these results are not typical," the Court finds, in light of the representations as a whole, a reasonable consumer's net impression would be that he or she could make large amounts of money in a short amount of time, and defendants' qualifications do not overcome that net impression. Furthermore, plaintiff has provided evidence that defendants' claims were material to the consumers' purchasing decisions, and defendants have shown no basis for asserting otherwise. (*See* Dkts. #3 and #4, Exs. 7-23).

The same is true for defendants' coaching claims. Defendants represented that their coaches were knowledgeable about the paper business, and had experience in the industry. Yet, defendants admit that no formal training in the paper business is available, and therefore, the coaches were all trained by Stefanchik himself. While the FTC acknowledges that formal training is not always necessary, the consumer declarations show that many of the coaches did not even have a basic knowledge of the real estate industry, and were unable to assist the consumers with their questions. For all of these reasons the Court finds that the FTC has shown a sufficient likelihood of success on the merits to warrant preliminary relief.

B. Balancing of Equities

Defendants argue that a preliminary injunction is not necessary at this time because the telemarketing defendants have already submitted to an injunction, and Stefanchik and Beringer are using no other telemarketers at this time. Defendants also argue that requiring them to shut down their business would cause financial hardship.

Defendants misunderstand the scope of plaintiff's request. Nothing in the proposed preliminary injunction requires defendants to stop conducting business. Rather, the injunction prevents them from making misrepresentations about the program. Furthermore, at this time, nothing prevents defendants from hiring another telemarketing company to do the business that Atlas and Christensen were formerly conducting. Thus, the Court finds that the equities balance

in favor of granting preliminary relief.

III. CONCLUSION

Defendants' Motion to Strike (Dkt. #35) is DENIED.

Plaintiff's Motion for Preliminary Injunction (Dkt. #2) is GRANTED. The Court will enter plaintiff's proposed preliminary injunction upon entry of this Order.

The Clerk shall direct a copy of this Order to all counsel of record.

DATED this 16 day of December 2004.

/s/ Ricardo S. Martinez
RICARDO S. MARTINEZ
United States District Judge