

FEDERAL TRADE COMMISSION
915 2nd Ave, Ste 2896
Seattle, WA 98174
Phone: 206.220.6350
Fax: 206.220.6366
Randall H. Brook (RB9033)
Robert J. Schroeder (RS0528)

UNITED STATES ATTORNEY
(Designated local counsel)
970 Broad Street, 7th Floor
Newark, NJ 07102
Phone: 973-645-2700
Fax: 973-645-2702
Susan J. Steele (SJS7042)

UNITED STATES DISTRICT COURT
DISTRICT OF NEW JERSEY

FEDERAL TRADE COMMISSION,

Plaintiff,

v.

THOMAS N. SALZANO and
PETER J. SALZANO,

individually and as officers of NorVergence,
Inc.,

Defendants.

CIVIL ACTION NO.

**COMPLAINT FOR INJUNCTIVE
AND OTHER EQUITABLE RELIEF**

Plaintiff, the Federal Trade Commission (“FTC”), by its undersigned attorneys, alleges:

1. This is an action under Section 13(b) of the Federal Trade Commission Act (“FTC Act”), 15 U.S.C. § 53(b), to secure permanent injunctive relief, including rescission of contracts,

cessation of collections and other equitable relief, for defendants' unfair and deceptive acts or practices in violation of Section 5(a) of the FTC Act, 15 U.S.C. § 45(a), in connection with the sale and financing of telecommunications services and related products.

2. The allegations against the defendants named in this complaint arise from the same practices and law violations as those alleged in a separate action previously filed in this district against NorVergence, Inc., ("NorVergence") (Docket No. CV- 04-5414-DRD). On July 22, 2005, a Default Judgment was entered against NorVergence. A typographical correction to the Default Judgment was filed August 8, 2005. NorVergence is also a debtor in a Chapter 7 bankruptcy proceeding in this district (Docket No. Bkr-04-32079-RG).

JURISDICTION AND VENUE

3. This Court has jurisdiction over this matter pursuant to 15 U.S.C. §§ 45(a) and 53(b), and 28 U.S.C. §§ 1331, 1337(a), and 1345.

4. Venue is proper in the United States District Court for the District of New Jersey under 15 U.S.C. § 53(b) and 28 U.S.C. §§ 1391(b) and (c).

PLAINTIFF

5. Plaintiff Federal Trade Commission is an independent agency of the United States Government created by statute. 15 U.S.C. §§ 41-58. The FTC enforces Section 5(a) of the FTC Act, 15 U.S.C. § 45(a), which prohibits unfair or deceptive acts or practices in or affecting commerce. The FTC may initiate federal district court proceedings by its own attorneys to enjoin violations of the FTC Act and secure appropriate equitable relief, including restitution and other equitable relief for injured consumers. 15 U.S.C. § 53(b). FTC suits under the FTC Act are law enforcement actions not barred by the automatic stay in bankruptcy, although distribution of assets and enforcement of any monetary judgment would be subject to the Bankruptcy Code

unless the bankruptcy is dismissed. 11 U.S.C. § 362(b)(4).

DEFENDANTS

6. Defendant Thomas N. Salzano was a founder and principal of NorVergence, a New Jersey corporation, and, at various times, was the Chief Management Officer of NorVergence. Individually or in concert with others, he has formulated, directed, controlled, or participated in the acts and practices of NorVergence, including the various acts and practices set forth herein. He resides in, and transacts or has transacted business in, the District of New Jersey.

7. Defendant Peter J. Salzano was a founder and principal of NorVergence, and, at various times, was the President of NorVergence. Individually or in concert with others, he has formulated, directed, controlled, or participated in the acts and practices of NorVergence, including the various acts and practices set forth herein. He resides in, and transacts or has transacted business in, the District of New Jersey. Defendant Peter J. Salzano is a debtor in a Chapter 11 bankruptcy proceeding in this district (Docket No. Bkr-05-11415-RG). The Commission's action against the defendant, including the enforcement of a judgment obtained in this action other than a money judgment against defendant Peter Salzano, is not stayed by 11 U.S.C. § 362(a)(1), (2), (3), or (6) because it is an exercise of the Commission's police or regulatory power as a governmental unit pursuant to 11 U.S.C. § 362(b)(4) and thus falls within an exemption from the automatic stay.

COMMERCE

8. At all times material hereto, defendants were engaged in the business of selling and financing telecommunications services and related products to small businesses and others, in or affecting commerce, as “commerce” is defined in Section 4 of the FTC Act, 15 U.S.C. § 44.

DEFENDANTS' BUSINESS ACTIVITIES

9. NorVergence's principal business since at least 2002, and continuing until shortly before its bankruptcy filing in July 2004, has been reselling telecommunications services, purchased from common carriers or others, principally to small businesses, non-profit organizations, churches, and municipalities. NorVergence marketed its services as integrated, long-term packages, including landline and cellular telephone service and Internet access.

10. NorVergence set its price for the service packages without regard to its cost of providing the services, which was likely to be much higher. Instead, it set a price based on a discount, usually 30%, from the amount the customer was previously paying for those services. It also typically promised unlimited free minutes for both long distance and cellular calls at no extra cost. The promised savings were laid out in writing so the customer could see what they would be paying and saving on a monthly and annual basis.

11. NorVergence explained to the customers that NorVergence could produce the dramatic savings and free minutes by installing a "black box" on the customer's premises. The most commonly offered black box was called the Matrix (or Matrix 850), and would supposedly route telecommunications in a manner to provide the savings. NorVergence's contract with its principal supplier of the Matrix set a price of \$1,500 for the box, although there are reports that the typical market price may have been as low as \$500.

12. In fact, the Matrix was a standard integrated access device, or IAD, commonly used to connect telephone equipment to a long-distance provider's T-1 or similar data line. It is wholly unrelated to cellular phone access. It does not establish or change the costs of the long distance service significantly, if at all. It cannot provide unlimited minutes, and NorVergence was actually obligated to pay its own suppliers, Qwest Communications Corporation, Sprint

Communications Company, and T-Mobile, USA, on a per minute basis.

13. A minority of NorVergence's customers were offered a Matrix Soho, a smaller device that is a standard firewall/router used to access Internet services. It did not provide access to telephone or cell phone services. NorVergence typically paid under \$350 for each Matrix Soho it provided to its customers.

14. NorVergence procured customers' signatures on a set of forms, including "non-binding applications" for services and a "rental agreement." The NorVergence sales pitch told customers they were signing up for long-term telecommunications services. In fact, what the customer usually received was a cancellable, price-variable service agreement or commitment, and a purportedly non-cancellable "rental agreement." The rental agreement purported to cover only the Matrix box.

15. Most of the customer's payment was allocated to the rental agreement for the Matrix (or similar product). Service applications or agreements signed at the same time as the rental agreement were for a small fraction of the rental amount and were unrelated to the actual costs of providing the telecommunications services.

16. While the price of the Matrix has been reported to be between \$500 and \$1,500, NorVergence rental agreements for the Matrix varied from \$400 to \$5,700 per month for the Matrix. Most rental agreements were for five years. They were titled simply "Rental Agreement," with the only indication that they were non-cancellable appearing in the fine print. The total cost to the customer was \$24,000 to \$340,000 for "renting" the \$1,500 Matrix box. Rental agreements for the \$350 Matrix Soho were lower priced, but could still total \$10,000 to \$30,000.

17. The price of the rental agreement had nothing to do with the cost of the Matrix.

NorVergence calculated the amount so the total charge for telecommunications services NorVergence promised to provide would add up to 30% less than the customers' previous bills.

18. After obtaining the customer's signature on the various "non-binding" applications, forms, and the rental agreement, NorVergence sold or assigned the rental agreement to a third-party finance company, either for the full five-year term or for some part of that term. The finance company paid NorVergence a discounted portion of the total rental price. The FTC believes that NorVergence received over \$200 million in upfront payments for the rental agreements it sold or assigned to various finance companies.

19. NorVergence included in the rental agreements various provisions that would make them more readily saleable. For example, they contained so-called "hell or high water" waiver of defenses clauses. These purport to require the customer to pay the full amount regardless of any fraud or deception perpetrated by NorVergence in making the original sale or in failing to provide the promised services. Typical language includes:

Your duty to make the rental payments is unconditional despite equipment failure, damage, loss or any other problem. If the equipment does not work as represented by the vendor, or if the vendor or any other person fails to provide any service, or if the equipment is unsatisfactory for any other reason, you will make any such claim solely against the vendor or other person and will make no claim against us.

In the example language above, the word "us" refers to the rentor, which could be NorVergence, a designated finance company, or an assignee not designated at the time of signing.

20. NorVergence's rental agreements also provided, in very fine print, that any disputes under the contract would be resolved in a forum distant from the customer's place of business and, in many cases, unknown at the time the customer signed the contract:

This agreement shall be governed by, construed and enforced in accordance with the laws of the State in which the Rentor's principal offices are located or, if the lease is assigned by Rentor, the laws of the state in which the assignee's principal offices are located, without regard to such State's choice of law considerations and all legal actions relating to this lease shall be venued exclusively in a state or federal court in that State, such court to be chosen exclusively at Rentor or Rentor's assignee's sole option.

In some cases, NorVergence may have made multiple assignments of the same contract, adding to the ambiguity of what forum might apply.

21. NorVergence also failed to disclose to customers material facts about the transaction that would lead them to question whether they should enter into it. For example, it did not tell customers that it had no long-term commitment from any service provider for the long-term services it was promising to provide to its customers. It also did not tell them that the Matrix box would be of little or no value to the customer if NorVergence failed to provide the promised telecommunications services.

22. In selling the rental agreements, NorVergence was left with its only ongoing income being payments on telecommunications service agreements with its customers. That income was only a small fraction of the cost of providing the promised services. NorVergence could not meet its long-term obligations to customers from this income, but would instead have had to set aside most or all of the income from the assignment or sale of the rental agreements to do so, and even that would likely have been insufficient. Based on the Chapter 7 case, it appears that NorVergence did not set aside any substantial portion of the rental contract income to cover promised services.

23. Initially, NorVergence did provide those below cost services to some of its early customers. For others the Matrix installation or connection was never completed and functional.

Delays or problems in installation or connection began as early as fall 2003. By mid-2004, NorVergence had stopped installing or connecting the black boxes it had sold and ceased paying the common carriers or other service providers and its employees. It was then placed into involuntary bankruptcy in this district. Initial filings from the Chapter 7 trustee indicate that virtually none of the hundreds of millions of dollars in up-front payments received by NorVergence can be found and there are no other substantial assets.

24. NorVergence's customers are no longer receiving any services from NorVergence. Many of the finance company assignees are insisting on full payment under the rental agreements despite the fact that they know or should know that the black boxes are essentially worthless without the promised services, and that customers are receiving no services. Some of the finance companies are filing collection suits in forums distant from the customer.

25. In deciding to do business with NorVergence based on information provided by or available from NorVergence, the finance companies knew or should have known that NorVergence was primarily selling a discounted package of telecommunications services and the Matrix was an incidental part of the promised services. Additionally, in receiving contracts from Norvergence where the total price might vary from \$24,000 to \$340,000 for the exact same \$1,500 product, those finance companies knew or should have known that the contracts might have been part of a scheme to defraud consumers.

26. NorVergence had more than 1,000 rental agreements not yet assigned to any finance company at the time of its bankruptcy filing. NorVergence is providing none of the promised services associated with those agreements. If these contracts had been assigned or sold, either by the Chapter 7 trustee or by NorVergence if the bankruptcy action had been dismissed, the customers could have been subject to the same type of collection actions by

assignees as for the contracts already assigned. They could have been forced to pay tens or hundreds of thousands of dollars for a worthless black box and services they will never receive.

27. NorVergence also has a residual interest in an unknown number of rental agreements that were assigned to finance companies for limited terms. These finance companies would be expected to return the rental agreements to NorVergence, who theoretically could then begin collecting on the contracts or resell the contracts to other third parties who might attempt collection while still providing none of the promised services.

VIOLATIONS OF SECTION 5 OF THE FTC ACT

COUNT I

28. In numerous instances, in connection with the sale and financing of telecommunications services and related products, defendants represented, expressly or by implication, directly or indirectly:

- a. That payment on the rental agreement and associated service agreements would result in the customer receiving the promised discounted telecommunications services for a long term.
- b. That NorVergence would treat the applications, forms, and rental agreement consumers were signing as a unified agreement under which NorVergence would provide telecommunications services in exchange for consumers' payments.
- c. That the equipment listed in the rental agreement would create the promised substantial savings in the customer's total cost of telecommunications services.

29. In truth and in fact:

- a. Payment on the rental agreement and associated service agreements would not and did not result in the customer receiving the promised discounted

telecommunications services for a long term.

b. NorVergence did not treat the applications, forms, and rental agreement consumers were signing as a unified agreement under which NorVergence would provide telecommunications services in exchange for consumers' payments.

Rather, NorVergence treated the rental agreement as a separate hardware financing document so it could sell that agreement and receive the rental income up front regardless of whether it actually delivered the promised telecommunications services.

c. The equipment listed in the rental agreement would not and did not create the promised substantial savings in the customer's total cost of telecommunications services. It could provide only minimal savings, if any.

30. Therefore, the representations set forth in Paragraph 28 above are false or misleading and constitute deceptive acts or practices in violation of Section 5(a) of the FTC Act, 15 U.S.C. § 45(a).

COUNT II

31. In numerous instances, in connection with the sale and financing of telecommunications services and related products, defendants represented, expressly or by implication, directly or indirectly, that NorVergence would provide substantially discounted telecommunications services for a long term.

32. Defendants failed to disclose:

a. That it had no long-term commitment from any service provider for the services it was promising to provide to its customers.

b. That the equipment covered by the rental agreement would be of little or no

value to the customer if NorVergence failed to provide the promised telecommunications services.

33. These facts would have been material to consumers in their contracting with NorVergence for services and rental of the equipment. The failure to disclose these facts, in light of the representations made in Paragraph 31 above, is a deceptive act or practice in violation of Section 5(a) of the FTC Act, 15 U.S.C. § 45(a).

COUNT III

34. In numerous instances, in connection with the deceptive sale and financing of telecommunications services, as described in Paragraphs 9-27 above, defendants' practice of including in NorVergence's rental agreements provisions authorizing NorVergence or its assignees to file lawsuits in specified or unspecified venues other than the customer's location or the location where the customer executed the contract was likely to cause substantial injury that could not have been reasonably avoided, and that was not outweighed by countervailing benefits to consumers or competition.

35. Therefore, defendants' practices, as alleged in paragraph 34, are unfair and in violation of Section 5(a) of the FTC Act, 15 U.S.C. § 45(a).

COUNT IV

36. By furnishing third-party finance companies with rental agreements that may allow the finance companies to:

- a. Misrepresent that consumers owe money regardless of whether NorVergence provides the promised telecommunications services; and
- b. File collection suits in distant forums,

Defendants provided others with the means and instrumentalities for the commission of

deceptive or unfair acts or practices.

37. Therefore, defendants' practices, as set forth in paragraph 36, constitute deceptive or unfair acts or practices in violation of Section 5(a) of the FTC Act, 15 U.S.C. § 45(a).

CONSUMER INJURY

38. Consumers throughout the United States have suffered substantial monetary loss as a result of defendants' unlawful acts or practices. In addition, defendants have been unjustly enriched as a result of their unlawful practices. Absent injunctive relief by this Court, and depending on the proceedings in and outcome of the bankruptcy cases, defendants may continue to injure consumers and to harm the public interest.

THIS COURT'S POWER TO GRANT RELIEF

39. Section 13(b) of the FTC Act, 15 U.S.C. § 53(b), empowers the Court to grant injunctive and other ancillary relief, including restitution, reformation or rescission of contracts, and cancellation of purported debts, to prevent and remedy violations of any provision of law enforced by the FTC, although distribution of assets and enforcement of any monetary judgment would be subject to the Bankruptcy Code unless the bankruptcy proceeding against defendant Peter J. Salzano is dismissed.

40. The Court, in the exercise of its equitable jurisdiction, may award other ancillary relief to remedy injury caused by defendants' violations.

PRAYER FOR RELIEF

Plaintiff requests that the Court, as authorized by Section 13(b) of the FTC Act, 15 U.S.C. § 53(b), and pursuant to its own equitable powers:

1. Enter judgment against defendants and in favor of the FTC for each violation alleged in this complaint.

2. Permanently enjoin and restrain defendants from violating the FTC Act.
3. Award such relief as the Court finds necessary to redress injury to consumers resulting from the defendants' violations of the FTC Act, including but not limited to restitution, reformation or rescission of contracts, and the cancellation of purported debts.
4. Award plaintiff the costs of bringing this action, as well as such other and additional equitable relief as the Court may determine to be just and proper.

Respectfully submitted,

Dated: June 23, 2006

WILLIAM BLUMENTHAL
General Counsel

/s Randall H. Brook
RANDALL H. BROOK (RB9033)

/s Robert J. Schroeder
ROBERT J. SCHROEDER (RS0528)

Attorneys for the
Federal Trade Commission
915 2nd Avenue, Ste. 2896
Seattle, WA 98174
Tel 206.220.6350
Fax 206.220.6366