Federal Trade Commission

ABI Winter Leadership Development Conference
Scottsdale, Arizona

Remarks of David C. Vladeck[1]
Director, FTC Bureau of Consumer Protection
December 10, 2010

Most of you are probably more familiar with the FTC in your role as consumers than as lawyers, judges, accountants or financial professionals. If you registered for the Do Not Call Registry and now enjoy dinner uninterrupted by telemarketers, well, the FTC is responsible for that. If you monitor your credit by getting a free credit report every year, the FTC brought that to you, too. Or if you've used the yellow Energy Guide label to help buy a major appliance, that's also us. However, given that many of you are not as familiar with the agency in your professional capacity, I want to start with a quick overview of what the FTC is and what we do, before I turn to current consumer protection issues and our bankruptcy work.

In 1914, Congress created the FTC as part of its battle to "bust the trusts." Our consumer protection mission did not fully appear until 1938 when Congress passed a broad prohibition against "unfair and deceptive acts or practices." Those laws, along with many other rules under the agency's purview, give us the unique distinction as the only general jurisdiction federal

[1] The views expressed here are my own and do not necessarily represent the views of the Federal Trade Commission or any Commissioner.

consumer protection agency. Our mission and actions are determined by a set of five Commissioners, representing both political parties. Each Commissioner is nominated by the President, subject to Senate confirmation, and serves a seven-year term.

The Agency is divided into three bureaus – the Bureau of Competition, the Bureau of Economics, and the Bureau of Consumer Protection. I serve as the Director of the Bureau of Consumer Protection, which does the most of the agency's bankruptcy work. In the Bureau of Consumer Protection, we accomplish our mission with three tools: law enforcement; consumer and business education; and rulemaking.

Today, I'd like to share some of our current priorities – several of which relate to issues you may find in both individual and corporate bankruptcy cases.

Mortgage assistance relief scams

One area of particular concern to us has been mortgage assistance relief scams. I am sure you have seen the ads: companies promise to prevent foreclosure or obtain a loan modification in exchange for a hefty up-front fee. In reality, they do little but collect the fee.

The FTC has launched an aggressive enforcement initiative against these pervasive, pernicious scams – bringing 32 cases against more than 180 individuals and corporations. In addition, we have partnered with numerous state and federal law enforcement agencies to bring two nationwide sweeps: Operation Stolen Hope and Operation Loan Lies. These sweeps involved more than 200 lawsuits against loan modification and foreclosure rescue providers. To date 64 defendants have settled with the Commission, agreeing to lifetime bans on providing mortgage assistance relief.

In addition to this enforcement work, we have commenced several rulemakings aimed at cleaning up the mortgage marketplace. Just last month, the Commission issued the final Mortgage Assistance Relief Services (MARS) Rule. The Rule, among other things, includes a ban on advance fees for mortgage relief services. Many, if not most, mortgage assistance and loan modification services charge consumers a large fee prior to providing any services. Under the new Rule, this practice is prohibited, and those service providers can only collect a fee after they have provided the service they advertise. Specifically, the mortgage relief service must give consumers a written offer from their lenders and the consumers must accept that offer prior to collection of a fee. In addition, the Rule requires mortgage relief companies to disclose key information to consumers, like the fact that the lender may not agree to change the loan, and that if a company tells consumers to stop paying their mortgages, the consumers could lose their homes and damage their credit ratings. The advance-fee ban will take effect on January 31 of next year. The Rule's required disclosures, however, will be effective this December 29th.

Job and grant scams

Given the current economic condition, it is no surprise that lately we have also seen a rise in job and grant scams. These scams promise grant money or guaranteed employment in exchange for a payment. After making the payment, consumers very rarely hear back from the soliciting company.

To halt these scams, in the last year, the FTC has coordinated two major law enforcement sweeps – Operation Short Change and Operation Bottom Dollar. Along with our state and federal partners, we collectively filed over 190 law enforcement actions.

Moreover, to help consumers protect themselves, the FTC released two videos. The first features a former scammer who hawked phony business opportunities and served prison time for deceiving investors. The second video – available in both English and Spanish – warns consumers against paying anyone who promises to find them employment. Monster.com and Craigslist both link to the video on their sites, and Microsoft Bing has worked with the FTC to have public service announcements, with a link to ftc.gov/jobscams, pop up when key terms are searched.

Consumer debt collection

As economic conditions impact an increasing number of consumers, we have also seen an increase in consumer debt collection efforts. While most of these efforts are lawful, others are not. The law is clear that debt collectors may not deceive, harass, or abuse consumers. In 2009, the FTC received nearly 120,000 complaints from consumers about the conduct of debt collectors – more complaints than the agency received about any other single industry. This number is troubling, and the Commission will continue to make enforcement of the Fair Debt Collection Practices Act (FDCPA) a priority. As I will discuss later, we recently intervened in a bankruptcy case to ensure consumers would have all of the important protections contained in the FDCPA as part of a Trustee's proposed collection on accounts.

Unfortunately, we have too many instances where debt collectors get any number of things wrong in trying to collect the debt – they call the wrong person, attempt to collect the wrong amount, or both. If you think this is a problem only for small, unsophisticated collection companies, you are wrong. Just this fall the Commission settled a case against one of the nation's largest debt collectors – Allied Interstate – because it was doing all of those things. Allied Interstate now holds the distinction of paying the second largest civil penalty ($1.75 million) obtained by the FTC in a debt collection case.

Consumer debt relief services

With credit card delinquencies at historic highs, we are seeing the emergence of many companies that falsely claim they can reduce or eliminate consumers' interest rates or balances. In the last seven years, the FTC has brought 23 cases against credit counseling firms that are sham nonprofits, against debt settlement services, and against debt negotiators, whose practices harmed many thousands of consumers.

In addition to suing the companies that promise, but don't deliver, these debt relief schemes, the FTC recently amended the Telemarketing Sales Rule to curb deception and abuse by for-profit providers of debt relief services. These amendments also prohibit such providers from charging a fee until they settle or reduce a customer's credit card or other unsecured debt. This ban on advance fees protects all consumers who enroll in a for-profit debt relief service after October 27, 2010.

Negative options

Another area that we are keeping a close eye on is negative option marketing. I am sure you are familiar with this practice; you may even have fallen victim to a negative option scam. It occurs whenever a marketer takes a consumer's silence as agreement to continue a transaction, such as billing monthly for membership in an Internet discount buying club. While these offers can provide benefits to consumers, they also pose a high risk of deception. Unscrupulous marketers use negative options that are not adequately disclosed to trap consumers in a cycle of recurring charges for goods or services they do not want and never knew they purchased.

For example, one business falsely claimed ties to Google in marketing a bogus work-at-home scheme under names like "Google Money Tree," "Google Pro," and "Google

Treasure Chest." Consumers were lured into giving financial account information to this phony business to pay a small shipping fee for the work-at-home kit. Defendants did not adequately disclose, however, that buying this kit would also trigger recurring monthly charges of $72 for another product. The FTC sued the company and obtained an order banning it from using negative option features and requiring it to turn over $3.5 million in assets.

That case is but one example of the aggressive action taken by the FTC to stop deceptive negative option marketing. Indeed, in the last 10 years, the Commission has initiated 60 cases against negative option marketers selling everything from dietary supplements to buyers' clubs. In addition, the FTC has developed consumer and business education to help consumers avoid negative option scams and to help businesses comply with the law.

Privacy

Privacy has been one of my main priorities at the Commission, and we have been very active on behalf of consumers in this area. Just last week, the FTC issued a privacy report, which contains our ideas for how to meet the privacy challenges posed by the vast array of 21st century technology and business practices that collect and use consumer data. Even if you don't use these new technologies, I'm sure you've heard of some of them. They include social networking, cloud computing, online behavioral advertising, mobile marketing, and the collection and use of information by retailers, data brokers, third-party applications, and other diverse businesses. Our goal in issuing the report is to provide a framework that promotes consumer choice along with privacy, transparency and business innovation. In an effort to strike the right balance on the Internet, we have recommended a "Do Not Track" mechanism that will allow consumers to choose whether to allow companies to target them with ads or collect data about their online searching and browsing activities. The Commission is collecting comments on "Do Not Track" and the other recommendations described in the report through the end of January.

We also continue to be active in protecting consumers from new and emerging data security challenges. Earlier this year, we announced a new initiative involving breaches related to peer-to-peer (P2P) software. We sent almost 100 letters advising companies, schools, and local governments that the personal information they maintained – in some cases, Social Security numbers, driver's license numbers, and health records – had been exposed on P2P networks. This information is a potential gold mine for identity thieves. Once a file is shared on a P2P file-sharing network, it cannot be pulled back. To make sure other organizations do not suffer the same fate, we have prepared a guide for businesses on how to secure computer networks and how to educate employees about the risks of P2P software.

Spanish Language Initiative

The FTC started its Hispanic Law Enforcement and Outreach Initiative in 2002 to address the growing problem of consumer fraud against Hispanics. The 2004 FTC Staff Report on Consumer Fraud in the United States confirmed our initial belief that consumer fraud against Hispanics is a significant problem, revealing that Hispanics are about twice as likely as non-Hispanic whites to be victims of consumer frauds. As a part of this initiative, the FTC has moved aggressively to combat consumer fraud against Hispanics, filing 53 actions against 187 businesses and individuals. For instance, we just shut down a California-based mortgage rescue scam, Dinamica Financiera, aimed at Spanish-speaking consumers.

While our law enforcement activities are ongoing, the FTC continues to stay on top of what is happening in the Spanish speaking market and to work closely with partners throughout the country to protect Hispanics from unfair and deceptive practices. Specifically, over the next year, the FTC plans to convene a series of regional workshops with community organizations, legal service providers, and others that provide services to Spanish speakers. In addition, FTC staff will be monitoring local Spanish-language television, radio, and print advertising to better target our law enforcement efforts.

Green Guides

Another area we are continuing to monitor is how companies market products using environmental or green marketing claims. To assist the marketers, the Commission has issued Environmental Marketing Guides, which are commonly referred to as the Green Guides. These Guides demonstrate how the Commission might apply the FTC Act's prohibition on unfair or deceptive practices to environmental marketing claims. They cover claims such as "renewable energy" claims, "renewable materials" claims, and "carbon offset" claims.

The FTC issued its Green Guides in 1992 and then revised them in 1998. The world of environmental marketing, however, has not remained static. The last few years have seen a virtual explosion of green claims. Therefore, this fall, the Commission published new proposed modifications to the Guides and sought public comment. Updating the Guides should help businesses better align their product claims with consumer expectations.

When business guidance fails, however, the Commission is not shy about bringing law enforcement actions. Most recently, the FTC initiated seven such suits challenging deceptive biodegradable, "environmentally friendly," and bamboo claims. Most, if not all, bamboo textiles are in fact rayon. Rayon is made from a relatively environmentally unfriendly process and therefore many consumers are not getting what they think they are paying for.

Consumer education

Because consumers are the first line of defense against fraud and deception, we place a high priority on consumer education. Those of you with children may want to take a look at our Net Cetera guide, which gives you tips on how to talk to your kids about a whole host of issues, from socializing on the Internet, to mobile phones (including both texting and sexting), how to protect your computer, and parental controls.

Additionally, earlier this year, we released an interactive video game called AdMongo. It's designed to teach kids from third to sixth grade about advertising – how to recognize it and how to think critically about it. In addition, we have countless guides to help consumers of all ages evaluate offers ranging from credit counseling and debt settlement, to loan modification services, to franchise and business opportunity offers, to car financing and leasing arrangements. Check out ftc.gov and you'll find all these guides (and more) under our consumer protection and consumer information pages.

Consumer Financial Protection Bureau (CFPB)

As you all know, Congress recently passed legislation creating a new bureau within the Federal Reserve Board. While the FTC has retained most of its authority over consumer financial products and services, we will share many responsibilities with the new CFPB and have been meeting regularly with CFPB staff and management. In addition to creating the CFPB, the Dodd-Frank legislation authorized the FTC to promulgate consumer protection rules concerning motor vehicle dealers using streamlined authority. We have begun and will continue to pursue an inclusive process to determine what, if any, new rules might be needed to protect consumers, particularly with regard to auto financing issues.

Bankruptcy issues

For those of you who have not represented clients in connection with a FTC action, I am sure you are wondering what all this consumer protection talk has to do with bankruptcy. Well, we actually find ourselves dealing with bankruptcy issues quite frequently. In general, the FTC appears in bankruptcy cases in two ways: 1) to deal with claims related to a defendant in one of our enforcement cases; or 2) to address issues that are core to our consumer protection mission, which may or may not relate to our status as a creditor in the case.

Sometimes an individual or corporate defendant will file a bankruptcy petition in the midst of defending an FTC enforcement or contempt action. Other times, defendants file after we have obtained either a litigated or stipulated judgment. In either situation, our objectives remain the same: 1) to preserve any interim orders, such as an asset freeze; 2) to protect our judgments by contesting a debtor's discharge or by recovering assets; and 3) to protect consumers from further harm from the debtor/defendant.

The FTC also may have a direct impact on a bankruptcy case, or on services related to bankruptcy proceedings and individual debtors, due to the very nature of our consumer protection work. In the three examples I am going to discuss, the FTC acted on issues core to its mission: 1) protecting consumers' privacy; 2) preventing false and unsupported claims on consumer home mortgages; and 3) monitoring and reviewing practices in the consumer debt buying industry. Before I get to those big issues, let's first talk about what happens when one of our defendants files a bankruptcy petition.

Preserving an asset freeze

In some enforcement cases, we obtain orders from the district courts freezing defendants' assets. When a defendant under such a freeze subsequently files for bankruptcy, issues can arise that require the FTC to get involved in the bankruptcy proceeding. For example, in the Cynergy Data bankruptcy case in Delaware, we recently intervened to protect frozen funds for victimized consumers. Specifically, the debtor attempted to settle the claims of several of its payment processors by moving frozen funds in the hands of one processor. The Commission objected and the debtor and payment processor ultimately agreed to new terms that did not involve moving frozen assets.

Protecting against discharge

In many of our enforcement cases, we are able to resolve our litigation with stipulated orders that protect the FTC from discharge of its judgment in a pending bankruptcy matter. Specifically, for individual defendants, the stipulated orders include a separate order in which the debtor agrees to except our judgment from his or her discharge under the fraud debt exception (Section 523(a)(2)(A)). If the defendant/debtor continues to litigate in the underlying FTC case, the Commission will use the findings in that case as the basis for an adversary proceeding and litigate nondischargeability based on the fraud debt exception.

A few years ago, two debtor/defendants learned this lesson the hard way. In that case, we filed an enforcement case alleging false representations by the debtors in marketing their purported invention promotion services. We won that case, but later filed a contempt action against these two debtor/defendants and others. In the contempt case, we obtained a $59 million litigated judgment. Two defendants filed for bankruptcy protection and fought us on nondischargeability issues in their bankruptcy cases. In the first debtor's case, we prevailed on summary judgment by using both principles of collateral estoppel from the District Court's ruling and evidence discovered as part of our enforcement and contempt cases. Shortly after that victory, the second debtor/defendant agreed to a nondischargeability order.

Recovering a defendant's assets

In some cases, the FTC must take action in bankruptcy cases to collect on a judgment – including cases where a defendant tries to shelter assets by abusing the corporate form. For example, we recently filed a complex adversary proceeding against a limited liability company named Warwick Properties that had filed a bankruptcy petition. That LLC held title to a $5 million, waterfront home on Mercer Island outside Seattle. The home was, of course, listed as property of the debtor's estate, and the debtor estimated it had well over $1 million in equity in the property.

The home also happened to be the personal residence of John Stefanchik, an individual defendant in an FTC enforcement action. The Commission had a $17.8 million judgment against Stefanchik for deceptively marketing a program to make easy money at home by buying and selling promissory notes and mortgages. It turns out, the putative manager of the now-bankrupt LLC was Stefanchik's wife. In reality, Stefanchik effectively directed and controlled the activities of the LLC. To collect its judgment, the Commission filed an adversary proceeding, asserting reverse veil-piercing and fraudulent transfer claims, against the bankrupt LLC, Stefanchik, and his wife. The proceeding is ongoing, but the FTC's goal is to recover whatever equity remains in the home after the bank loans and property taxes are paid.

Protecting consumers from harm

Finally, the FTC often appears in bankruptcy matters to protect consumers from harm that may arise from the bankruptcy process itself. For example, the sale of a debtor's assets in bankruptcy may raise a variety of issues related to debt collection, competition, and privacy.

The FTC recently addressed a trustee's collection on consumer accounts receivable in two separate cases. In the first case, the debtor's chapter 7 trustee requested permission to hire a collections attorney to collect the debtor's consumer accounts. The debtor in the case, a company named BlueHippo, filed its bankruptcy petition shortly after we filed our third contempt action against it. This particular debtor had a history of offering financing and lay-away programs for consumers to purchase computers, but then rarely provided the computers. After numerous state Attorneys Generals and the FTC objected to the collection process and proposed collections attorney, we obtained the Trustee's agreement not to collect on accounts of consumers who failed to receive a computer. Furthermore, we obtained an order from the bankruptcy court denying the trustee's application to retain that particular debt collector, due in large part to the number of consumer complaints filed against the proposed debt collector and the fact that those complaints raised serious questions about whether he was violating the Fair Debt Collection Practices Act (FDCPA). The Court also ordered the Trustee to consult with the FTC and state Attorneys General on any subsequent proposed collections agent and to work with those law enforcement entities to ensure a fair collections process.

In the second case, the FTC worked with the Trustee to halt collections from consumers who never received the services promised by a debtor. The debtor in that case, Apply2Save, operated a sham home loan modification business. It charged consumers $595 to $995, up front, for supposed loan modification and foreclosure relief services. The vast majority of consumers who enrolled in the Apply2Save program never received any assistance, and several consumers have since lost their homes, due, in no small part, to the fact that consumers would often pay the Apply2Save enrollment fee instead of their mortgage. Shortly after the FTC sued Apply2Save, its CEO and a related entity named Sleeping Giant filed chapter 7 bankruptcy petitions. The FTC worked with the chapter 7 Trustee to resolve the FTC's enforcement action. That stipulated order contains provisions that prohibit any future collection of the consumer accounts – all of which were included among the debtor's list of assets – and enters judgment against the defendants in the amount of $4.1 million.

Privacy

As I mentioned earlier, the Commission is also concerned about protecting consumers' privacy. This past summer, FTC staff became aware of a potential privacy problem in an individual's chapter 7 bankruptcy case. The debtor in the case was a man named Peter Cummings – he was the former head of a magazine named XY Magazine, which was oriented predominantly towards gay male youth and published from about 1996 to 2007. The magazine contained articles on how to get into college, suicide prevention, and other topics of interest to gay teenagers. XY Magazine also operated a website, XY.com, which featured the magazine content as well as online profiles of its members as part of a dating service. Both the magazine and website collected a substantial amount of personal information from their subscribers, including names, street and email addresses, bank or credit card information, and personal photos. The enterprise had amassed profiles of over 100,000 magazine subscribers and over 500,000 website members, but explicitly promised all its subscribers that their information would not be sold, or otherwise made public, without their permission.

The business eventually became insolvent and terminated its operations. Two of Mr. Cummings's former business partners were interested in buying some of the magazine's assets through his bankruptcy case, which included the potentially valuable profiles.

Given the promises made to consumers and the particular circumstances in this case, sale of these profiles was at the very least troubling. To address the situation, I wrote a public letter to Mr. Cummings laying out our concerns. In addition, we sent the letter to the founder's former business partners as they were negotiating an asset sale with the bankruptcy trustee. Within days, the U.S. Trustee's Office became involved and requested appointment of a privacy ombudsman. The court appointed an ombudsman and ultimately approved the sale. The asset sale, however, did not involve the transfer or sale of assets containing the personal information. Rather, the court abandoned that information to the founder, with instructions that it be destroyed.

False or unsupported claims

In our loan servicer cases, the FTC had a direct impact on information available to Chapter 13 debtors. Earlier this year, the FTC sued two of Countrywide's main loan servicers. Those servicers inflated rates for normal default-related services, including property inspections, lawn mowing and other services designed to protect the lender's interest in the property. In addition, we discovered that those servicers were making false or unsupported claims in Chapter 13 cases about the amounts debtors owed and the status of their loans. The loan servicers agreed to settle the FTC's claims and turn over $108 million to the FTC, which will be paid back to consumers harmed by these practices. Those stipulated orders also require Countrywide to make changes to its Chapter 13 practices. Among other things, it now must send debtors monthly notices containing information about the amounts the debtors owe and implement a data integrity program to ensure the accuracy of data used in Chapter 13 cases. We hope that those of you who work with Chapter 13 debtors are seeing the benefits of these new requirements in your cases.

Consumer debt buying industry study

Over the last few years, the FTC has also found major problems in the flow of information among creditors, debt buyers and collectors. Some of these problems lead to collectors who try to collect from the wrong consumers, make collection attempts in the wrong amount, or both. As a result, last winter, the Commission ordered nine companies to turn over information about their purchase and collection of consumer debt practices. These nine companies collectively buy about 75 percent of the debt sold in the United States. The FTC will use this data for a study of the debt-buying industry, with the hope that the information flow problems we have already identified can be remedied with concrete action on the part of the whole industry.

Before finishing, I want to thank Sam Gerdano and ABI for inviting me to speak to you today. I hope I have been able to give you some greater insight into the priorities of the FTC and how we might interact with you in bankruptcy cases. Although we are a small agency, we have a big mandate. As the nation's consumer protection agency, the FTC remains vigilant in protecting consumers wherever and whenever the need arises.