

PREPARED STATEMENT OF
THE FEDERAL TRADE COMMISSION ON
**"CONSUMER PROTECTION IN CYBERSPACE:
COMBATING FRAUD ON THE INTERNET"**

Before the

**TELECOMMUNICATIONS, TRADE, AND CONSUMER PROTECTION
SUBCOMMITTEE**

of the

**HOUSE COMMITTEE ON COMMERCE
UNITED STATES HOUSE OF REPRESENTATIVES**

Washington, D.C.

June 25, 1998

Mr. Chairman and members of the Committee: I am Eileen Harrington, Associate Director in the Bureau of Consumer Protection at the Federal Trade Commission ("FTC" or "Commission"). I appreciate this opportunity to present the Commission's views on the important issue of fraud on the Internet.⁽¹⁾

I. Introduction and Background

A. FTC Law Enforcement Authority

The Commission pursues its mission of promoting the efficient functioning of the marketplace by seeking to protect consumers from unfair or deceptive acts or practices and to promote vigorous competition. As you know, the Commission's responsibilities are far-reaching. Its primary legislative mandate is to enforce the Federal Trade Commission Act, which prohibits unfair methods of competition and unfair or deceptive acts or practices in or affecting commerce.⁽²⁾ With the exception of certain industries, this statute provides the Commission with broad law enforcement authority over virtually every sector in our economy,⁽³⁾ commerce on the Internet falls within the broad sweep of this statutory mandate.

B. Fraud in Cyberspace

The advent of the Internet -- with its new methods of communicating through web sites, electronic mail, news groups, chat rooms, electronic bulletin b

totaled approximately \$301 million in 1996 -- will reach \$7.7 billion by the year 2002.⁽⁸⁾

of online service providers and threatens the development of the Internet as a conduit for commerce. For example, America Online ("AOL") has reported that it currently handles 60 million electronic messages per day, up from 5 million messages per day only 18 months ago. Moreover, AOL estimates that UCE comprises as much as one-third of its e-mail traffic.⁽¹⁷⁾

The United States Secret Service assisted staff in ascertaining how this "Trojan horse" viewer software worked, and AT&T lent further assistance in tracing the software back to specific web sites. With this help, the Commission's staff completed its investigation, filed a complaint, and obtained an *ex parte* temporary restraining order and asset freeze against the defendants within just 31 days of learning about the alleged scam. The lawsuit was recently resolved by entry of a stipulated permanent injunction against the main defendants named in the Commission's complaint and the issuance of a virtually identical administrative order against additional parties found to have played a role in the alleged scam. Under the two orders, the defendants and administrative respondents are barred from engaging in the alleged unlawful practices, and over 38,000 consumers should

Food and Drug Administration ("FDA"), and the National Highway Traffic Safety Administration ("NHTSA"). The U.S. Consumer Gateway provides the public with "one-stop shopping" for federal information on a broad spectrum of consumer issues, ranging from auto recalls to drug safety to investor alerts.⁽²⁴⁾ Since early February 1998, the site has received over 1.8 million hits from 88,000 visitors.

B. "Teaser" Pages

Extending a hand to consumers at their most vulnerable point -- when they are surfing in areas of the Internet likely to be rife with fraud and deception -- the staff of the Commission has posted several "teaser" web sites. The "Ultimate Prosperity Page" is one example advertising a fake deceptive business opportunity. The "Ultimate Prosperity Page" uses "buzz words" and promises of easy money common to many such scams.

result, the Interactive Services Association, a leading online trade association, and companies such as AT&T, NetCom, America Online, Circuit City, Compaq, Micron, Borders, and American Express have helped circulate public service announcements over the Internet, cautioning consumers to avoid particular scams and "hot linking" consumers to the Commission's web site where they can find "Cybershopping" guides, "safe surfing" tips, and other helpful information.

IV. Business Education

A. Surf Days

At the forefront of its business education efforts, the Commission has conducted nine different "Surf Days" aimed at providing information to new entrepreneurs who may unwittingly violate the law. The first Surf Day was conducted in December 1996 and focused on pyramid schemes that had begun to proliferate on the Internet. Commission attorneys and investigators enlisted the assistance of the SEC, the U.S. Postal Inspection Service, the Federal Communications Commission, and 70 state and local law enforcement officials from 24 states. This nationwide *ad hoc* task force surfed the Internet one morning, and in three hours, found over 500 web sites or newsgroup messages promoting apparent pyramid schemes. The Commission's staff e-mailed a warning message to the individuals or companies that had posted these solicitations, explaining that pyramid schemes violate federal and state law and providing a link back to FTC.GOV for more information. In conjunction with the New York Attorney General's Office and the Interactive Service Association, the Commission announced the results of Internet Pyramid Surf Day at a televised press conference held during the Internet World '96 convention in New York City. A month later, the Commission's investigative staff checked on the status of web sites or newsgroups identified as likely pyramids during Surf Day and found that a substantial number had disappeared or been improved.⁽²⁸⁾ The Commission has employed this technique several times since, conducting additional Surf Days focused on Internet web sites or newsgroup messages that promoted potentially problematic business opportunities, credit repair schemes, and "miracle cure" health products.

The Commission has now taken its Surf Day concept to the private sector, the global law enforcement community, and sister agencies as well. In August 1997, the Coupon Information Center, a private trade association, and its members from the national merchandising community joined Commission staff in surfing for fraudulent opportunities that promoted coupon certificate booklets. Then on October 16, 1997, the Commission helped coordinate the first "International Internet Surf Day." Agencies from 24 countries joined this effort and targeted "get-rich-quick" schemes on the Internet.⁽²⁹⁾ Australia's Competition and Consumer Commission oversaw the world-wide effort while the FTC led the U.S. team consisting of the SEC, the Commodities Futures Trading Commission ("CFTC") and 23 state agencies.

In November 1997, the Commission used the Surf Day concept to help the Department of Housing and Urban Development ("HUD") target unscrupulous "HUD Tracers." These

"tracers" track down consumers to whom HUD may owe a refund for FHA mortgage insurance. Consumers can claim their refund for free by contacting HUD directly; however, unscrupulous "tracers" may falsely claim that refunds cannot be secured without their assistance (and they may charge up to 30 percent in commissions), may falsely claim an affiliation with the government, and may falsely represent to other entrepreneurs how much money they can make as "HUD tracers." The HUD Tracer Surf Day not only helped to generate publicity to inform consumers about HUD's refund program, but it also helped eliminate many potentially deceptive solicitations from the Internet. A month after sending out warning messages, the Commission's staff checked on suspect tracer sites and found that 70 percent had shut down entirely or removed questionable claims about earnings potential or their affiliation to HUD.

In early February, the Commission announced yet another innovative use of the Surf Day concept, this time targeting deceptive UCE messages. Commission staff conducted a "fall harvest" by surfing the Commission's large database of UCE solicitations, topic by topic, and identifying over 1000 individuals or companies potentially responsible for misleading e-mail solicitations, for example, for pyramid or other get-rich-quick schemes. Ironically, most of these UCE messages did not allow any reply by e-mail, due to inaccurate or deceptive "sender" information, so in January through the U.S. Postal system the Commission sent out letters warning the sources of the UCE that their messages may be in violation of the law.

B. Outreach to Internet Businesses

Our messages to businesses on the Internet are straightforward -- *e.g.*, don't lie or make misleading statements; don't make product or earnings claims that you can't support; don't mislead consumers with unrealistic testimonials. The difficulty lies in finding a way to get these basic messages to new entrepreneurs who may have no prior business or

Endnotes

1. My oral testimony and responses to questions you may have reflect my own views and are not necessarily the views of the Commission or any Commissioner.

2. 15 U.S.C. § 45(a). The Commission also has responsibilities under approximately 40 additional statutes, *e.g.*, the Clayton Act, 15 U.S.C. § 12, which prohibits various anticompetitive practices; the Truth in Lending Act, 15 U.S.C. §§ 1601 *et seq.*, which mandates disclosures of credit terms; the Fair Credit Billing Act, 15 U.S.C. § 1666 *et seq.*, which provides for the correction of billing errors on credit accounts; and the Fair Credit Reporting Act, 15 U.S.C. § 1681 *et seq.*

administrative orders or trade regulation rules, and may file those actions on its own behalf if the Department of Justice declines to do so in the name of the United States. 15 U.S.C. § 56.

12. *America Online, Inc.*, FTC File No. 952-3331 (consent order subject to final approval, May 1, 1997); *CompuServ, Inc.*, FTC File No. 962-3096 (consent order subject to final approval, May 1, 1997); *Prodigy Services Corp.*, FTC File No. 952-3332 (consent order subject to final approval, May 1, 1997). These respondents allegedly made "free trial" offers to consumers without adequately disclosing that consumers would automatically be charged if they did not affirmatively cancel before the end of the trial period. (The Commission also alleged that AOL failed to inform consumers that 15 seconds of connect time was aduww 35.88 T0 1 Tf (ad)-7(u

19. *FTC v. Internet Business Broadcasting, Inc., et al.*, Civil No. WMN-98-495

(D. Md., filed February 19, 1998); *FTC v. Dixie Cooley, d/b/a DWC*, Civil No. CIV-98-0373-PHX-RGS
(D. Ariz., filed March 4, 1998)

20. Civil No. 98-8194 CIV HURLEY (M.D. Fla., filed March 30, 1998).