

**PREPARED STATEMENT OF
THE FEDERAL TRADE COMMISSION**

on

PREPAID CALLING CARDS

Before the

**SUBCOMMITTEE ON COMMERCE,
TRADE, AND CONSUMER PROTECTION**

of the

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

WASHINGTON, D.C.

December 3, 2009

¹ The written statement presents the views of the Federal Trade Commission. Oral statements and responses to questions reflect the views of the speaker and do not necessarily reflect the views of the Commission or any Commissioner.

² In testimony last year, the Commission provided background information about the prepaid calling card industry, the Commission's and the States' recent law enforcement actions against distributors of prepaid calling cards, the Commission's establishment of a joint federal-state task force to combat fraud in the prepaid calling card industry, the FTC's consumer education and outreach efforts in this area, and, more generally, the FTC's support for the full repeal of the FTC Act's exemption for common carriers subject to the Communications Act of 1934. *See* Prepared Statement of the Federal Trade Commission on Prepaid Calling Cards Before the Subcommittee on Commerce, Trade, and Consumer Protection of the of the Committee on Energy and Commerce, U.S. House of Representa

The FTC has been at the forefront of federal efforts to protect consumers from deceptive practices in the prepaid calling card business. The FTC combats this problem in three ways: (1) the FTC investigates and vigorously prosecutes individuals and entities within its jurisdiction for deceptive marketing of prepaid calling cards; (2) it established and leads a joint federal-state task force on fraud in the prepaid calling card industry; and (3) it conducts public outreach and education to assist consumers of prepaid calling cards.

III. FTC Enforcement Actions

The heart of the FTC's law enforcement authority is Section 5 of the FTC Act, 15 U.S.C. § 45(a)(2), which prohibits deceptive or unfair acts or practices in or affecting commerce. Under Section 13(b) of the FTC Act, 15 U.S.C. § 53(b), the Commission may initiate federal district court proceedings to enjoin deceptive or unfair practices and obtain other equitable relief, such as restitution and disgorgement of ill-gotten gains.

In 2008, the FTC used this authority to file two similar cases against major distributors of prepaid calling cards and their principals: *FTC v. Alternatel, Inc.*, No. 08-01433-CIV-Jordan/McAliley (S.D. Fla.) (Compl. filed May 19, 2008), and *FTC v. Clifton Telecard Alliance One LLC*, 2:08-CV-01480-PGS-ES (D.N.J.) (Compl. filed Mar. 25, 2008). In both cases, the FTC alleged that the defendants, which marketed cards chiefly to recent immigrants, violated the

www.oregonlive.com/money/index.ssf/2008/10/fraud_plagues_prepaid_calling.html; Herb Weisbaum, *Prepaid Phone Card Industry Under Attack*, MSNBC, Oct. 23, 2008, available at www.msnbc.msn.com/id/27327684/business-consumerman; Joelle Tessler, *Fraud is a Hang-Up for Prepaid Calling Card Market*, USA TODAY, Oct. 5, 2008, available at www.usatoday.com/tech/products/2008-10-05-calling-card-fraud_N.htm; *Talk Isn't So Cheap on a Phone Card*, BUSINESS WEEK, July 23, 2007, available at www.businessweek.com/magazine/content/07_30/b4043079.htm; Susan Sachs, *Immigrants See Path to Riches in Phone Cards*, N.Y. TIMES, Aug. 11, 2002, available at www.nytimes.com/2002/08/11/nyregion/immigrants-see-path-to-riches-in-phone-cards.html.

⁴ In *Clifton Telecard Alliance*, the FTC also alleged that the defendants violated the FTC Act by failing to disclose that consumers could be charged even for unconnected calls.

⁵ The FTC collectively tested over 100 calling cards of the *Alternatel* and *Clifton Telecard Alliance* defendants by using the cards to place calls to a variety of countries in Latin America and Africa. The tests were comprised of “single-call” and “multiple-call” testing. In single-call testing, the FTC sought to exhaust the value of the card in a single call, whereas in multiple-call testing, the FTC attempted to use each card to place a series of calls. In all cases, the total number of calling minutes provided by each card was compared to the number of calling minutes promised on the defendants’ poster advertisements.

⁶ The full judgment imposed on the *Clifton Telecard Alliance* defendants was \$24,445,252. However, all but \$1.3 million of this amount was suspended based on the defendants’ inability to pay. If the defendants are found to have misrepresented

lawfulness of their calling cards and associated marketing materials as well as the conduct of their business partners – including their telecommunications service providers – to ensure that consumers actually receive the advertised number of calling minutes. For example, the defendants must routinely test the cards they distribute, implement procedures to ensure the distribution of accurate and up-to-date point-of-sale materials, and confirm that only such materials are displayed by retailers.

Most recently, the FTC sued Diamond Phone Card, Inc., a New York-based company that has sold prepaid calling cards throughout the country, and the company's principals. *FTC v. Diamond Phone Card, Inc.*, 09-CV-3257 (E.D.N.Y.) (Compl. filed July 29, 2009). The FTC alleges that the *Diamond* defendants violated the FTC Act by misrepresenting the number of calling minutes consumers could obtain using Diamond prepaid calling cards and by failing to adequately disclose fees associated with Diamond phone cards. As in *Clifton Telecard Alliance* and *Alternatel*, the FTC's extensive testing showed that Diamond calling cards delivered only roughly half the advertised calling minutes. The FTC seeks a permanent injunction as well as

⁷ The task force includes representatives from the following Offices of Attorneys General: Alabama, Arizona, Arkansas, California, Colorado, Connecticut, District of Columbia, Florida, Georgia, Hawaii, Idaho, Illinois, Indiana, Iowa, Kansas, Kentucky, Maryland, Maine, Massachusetts, Minnesota, Missouri, Montana, New Mexico, Nevada, New Hampshire, New Jersey, New York, North Carolina, North Dakota, Ohio, Oregon, Pennsylvania, Rhode Island, South Dakota, Tennessee, Texas, Virginia, Washington, and Wisconsin. In addition, the New York State Consumer Protection Board, the New York City Department of Consumer Affairs, and the City of Chicago Department of Consumer Services are also task force members.

⁸ See, e.g., Press Release, *McCullum Announces Prepaid Calling Card Settlements, Industry-Wide Reform* (June 11, 2008), available at www.myfloridalegal.com/newsrel.nsf/newsreleases/79C6666DB24608D785257465004EC901. The companies subject to the Florida AVCs are: ADMA Telecom, Inc.; Blackstone Calling Card, Inc.; IDT Corp.; Union Telecom Alliance; Total Call International, Inc.; CVT Prepaid Solutions, Inc.; Dollar Phone Enterprise, Inc.; STi Prepaid, LLC; Alternatel, Inc; Cristel Telecommunications, LLC; Locus Communications, Inc.; and others.

¹⁰ *State of Texas v. Next-G Commc'n, Inc.*, No. 2008CI08149 (Bexar County, Tex.) (Pet. filed May 23, 2008); *see also* Press Release, *Attorney General Abbott Takes Legal Action Against Prepaid Calling Card Company* (May 23, 2008), available at www.oag.state.tx.us/oagNews/release.php?id=2479.

¹¹ *See* Press Release, *Brown Prevents Calling Card Company From Boosting Profits By Charging Hidden Fees*, available at www.ag.ca.gov/newsalerts/release.php?

prosecution by the FTC. Significantly, H.R. 3993 would create a limited carve-out from the

¹² Some participants in the prepaid calling card industry have begun to offer prepaid wireless services. As the cost of providing cellular phones and calling minutes continues to decrease, the incentive to move consumers to prepaid wireless accounts from more traditional prepaid calling cards has increased.

¹³ Civil penalty actions are filed by DOJ on behalf of the FTC. In general, under the FTC Act, the Commission must notify the Attorney General of its intention to commence, defend, or intervene in any civil penalty action under the Act. 15 U.S.C. § 56(a)(1). DOJ then has 45 days to commence, defend, or intervene in the suit. *Id.* If DOJ does not act within the 45-day period, the FTC may file the case in its own name, using its own attorneys. *Id.*

¹⁴ More generally, the Commission has recommended that Congress authorize the FTC to seek civil penalties for violations of Section 5 of the FTC Act, and, to promote efficiency and expediency, to seek civil penalties in its own right across the board, without being required to refer enforcement of civil penalty proceedings to DOJ. *See, e.g.*, Prepared Statement of the Federal Trade Commission Describing the Commission's

exemption, and indeed, every commissioner – Democrat, Republican, and Independent going back to at least 2003 – believes it should be repealed.¹⁵

The common carrier exemption originated in an era when telecommunications services were provided by highly-regulated monopolies. However, Congress and the FCC have dismantled much of the economic regulatory apparatus formerly applicable to the industry, in which firms are expected to compete. Removing the exemption from the FTC Act would not alter the jurisdiction of the FCC, but would give the FTC the authority to protect consumers against unfair and deceptive practices by common carriers in the same way that it can protect against unfair and deceptive practices by non-common carriers involved in the provision of similar services.

Prepaid calling cards are a case in point. In contrast to the State Attorneys General, who are able to bring enforcement actions to stop both telecommunications providers and distributors offering prepaid calling cards from engaging in unfair and deceptive practices, the FTC has targeted only the deceptive practices of prepaid calling card distributors, because of the FTC Act common carrier exemption. Furthermore, even when the Commission has identified and brought enforcement actions against non-common carriers, the common carrier exemption has imposed additional litigation costs on the FTC. For example, in both the *Clifton Telecard Alliance* and *Alternatel* cases against prepaid calling card distributors, the defendants moved to dismiss the

¹⁵ See, e.g., Prepared Statement of the Federal Trade Commission Before the Committee on Commerce, Science, and Transportation, U.S. Senate (Apr. 8, 2008), *available at* www.ftc.gov/os/testimony/P034101reauth.pdf; Prepared Statement of the Federal Trade Commission Before the Subcommittee on Competition, Foreign Commerce, and Infrastructure of the Committee on Commerce, Science, and Transportation, U.S. Senate (June 11, 2003), *available at* <http://www.ftc.gov/os/2003/06/030611reauthsenate.htm>.

FTC's cases on the grounds that the FTC had not sued the underlying carriers. While the *Alternatel* court rejected the argument that the common carriers that provided telecommunications service for the calling cards at issue were indispensable parties, the burden of responding to such motions can be substantial.¹⁶

The FTC has extensive expertise with advertising, marketing, billing, and collection – areas in which significant problems have emerged in the telecommunications industry.¹⁷ In addition, the FTC has powerful procedural and remedial tools that could be used effectively to address developing problems in the telecommunications industry if the FTC were authorized to reach them.

VII. Conclusion

The Commission will continue its aggressive law enforcement and consumer outreach and education programs in the prepaid calling card arena. The Commission thanks this

¹⁶ The *Clifton Telecard Alliance* court did not rule on the defendants' motion to dismiss prior to the settlement of the case.

¹⁷ For example, the FTC has brought numerous cases involving the cramming of unauthorized charges onto consumers' phone bills. *See, e.g., FTC v. Nationwide Connections, Inc.*, 06-80180-CIV-Ryskamp/Vitunac (S.D. Fla. 2006); *FTC v. Webservice Media, LLC.*, Civ. No. H-06-1980 (S.D. Tex. 2006); *FTC v. Verity Int'l Ltd*, 335 F. Supp. 2d 479 (S.D.N.Y. 2004), *aff'd in part, rev'd in part*, 443 F.3d 48 (2d Cir. 2006), *cert. denied*, 127 S. Ct. 1868 (2007); *FTC v. Epixtar Corp.*, 03-CV-8511 (DAB) (S.D.N.Y. 2003); *FTC v. Mercury Marketing of Del., Inc.*, 00-CV-3281 (E.D. Pa. 2000); *FTC v. Sheinkin*, 2-00-363618 (D.S.C. 2000); *FTC v. Int'l Telemedia Assocs., Inc.*, 1-98-CV-1925 (N.D. Ga. 1998); *FTC v. Audiotex Connection, Inc.*, C-97 0726 (DRH) (E.D.N.Y. 1997).