

**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**

Mr. Chairman and Ranking Member Radanovich, I am Lois Greisman of the Federal Trade Commission (“Commission” or “FTC”).<sup>1</sup> Thank you for giving the Commission this opportunity to testify before the Committee about consumer protection issues associated with prepaid calling cards.

## **I. Executive Summary**

This testimony updates the Committee concerning the Commission’s and the States’ activities in this arena and offers comments on H.R. 3993, “The Calling Card Consumer Protection Act.”<sup>2</sup> On the enforcement front, since the spring of 2008, the Commission has brought three actions against major distributors of prepaid calling cards charged with deceptively marketing prepaid calling cards targeted at recent immigrants. Earlier this year, the Commission entered into multi-million dollar settlements in two of these cases, and the Commission is aggressively prosecuting the third case, which it filed in July of 2009. State participants in the FTC’s joint task force on fraud in the prepaid calling card industry have collectively brought over twenty law enforcement actions in this arena.

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<sup>1</sup> 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.

<sup>2</sup> 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 Representatives (Sept. 16, 2008), *available at* [www.ftc.gov/os/2008/09/P074406prepaidcc.pdf](http://www.ftc.gov/os/2008/09/P074406prepaidcc.pdf).

The Commission strongly supports the goals of H.R. 3993, which will provide better disclosures for consumers and will arm the Commission with stronger tools to combat fraud in the prepaid calling card industry. Most important, it will authorize the Commission to sue companies that provide telecommunications service for prepaid calling cards – many of which may profit handsomely from deceptive conduct. The bill would create a limited carve-out to the exemption to the FTC Act for common carriers subject to the Communications Act and would give us the authority to fine violators, which we believe is a critical deterrent. But, as explained below, the bill’s exemption of certain prepaid wireless phone services could create a loophole if the worst actors in the industry migrate their practices to prepaid wireless handsets to avoid the mandates of the bill. Finally, the Commission recommends the repeal of the common carrier exemption, which is an anachronistic jurisdictional impediment to effective consumer protection.

## **II. Background**

Over the last decade, the prepaid calling card industry has grown into a multi-billion dollar industry. Prepaid calling cards can serve as a convenient and inexpensive lifeline to connect consumers – particularly recent immigrants as well as members of the U.S. armed services – to their families. Such cards are typically sold in gas stations, newsstands, convenience stores, bodegas, groceries, military PX’s, as well as over the Internet. Unfortunately, however, purchasers of prepaid calling cards often receive only a fraction of the advertised number of calling minutes and are charged a welter of hefty and confusing fees and surcharges that are undisclosed or inadequately disclosed.<sup>3</sup>

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<sup>3</sup> See generally Mark E. Budnitz, Martina Rojo & Julia Marlowe, *Deceptive Claims for Prepaid Telephone Cards and the Need for Regulation*, 19 LOYOLA CONSUMER L. REV. 1 (2006); Jim Hays, *Fraud Plagues Prepaid Calling Card Market*, THE OREGONIAN, Oct. 5, 2008, available at

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

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[www.oregonlive.com/money/index.ssf/2008/10/fraud\\_plagues\\_prepaid\\_calling.html](http://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](http://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](http://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](http://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](http://www.nytimes.com/2002/08/11/nyregion/immigrants-see-path-to-riches-in-phone-cards.html).

FTC Act by misrepresenting the number of calling minutes provided by their cards and failing to disclose, or disclose adequately, fees and charges associated with their cards.<sup>4</sup> The FTC's extensive testing revealed that both the *Alternatel* and *Clifton Telecard Alliance* defendants' prepaid calling cards provided only about half the advertised calling minutes.<sup>5</sup>

The FTC recently obtained stipulated court orders resolving their charges against the *Alternatel* and *Clifton Telecard Alliance* defendants. In *Alternatel*, the final order entered on April 1, 2009 imposed a \$2.25 million judgment, and in *Clifton Telecard Alliance*, the final order entered on June 22, 2009 imposed a \$1.3 million judgment.<sup>6</sup> Both court orders contain strong and substantially similar injunctive relief, which permanently bars the defendants from misrepresenting the number of minutes of talk time a consumer will receive using their cards. The orders also require the defendants to clearly and conspicuously disclose all material terms and limitations, including card expiration dates, the existence and amounts of fees, and restrictions on the periods during which calling minutes are available. In addition, the final orders impose stringent and extensive obligations on the defendants to monitor the accuracy and

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<sup>4</sup> 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.

<sup>5</sup> 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.

<sup>6</sup> 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 their financial condition, they will be liable for the full \$24,445,252.

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 equitable monetary relief likely in the form of restitution and/or disgorgement of ill-gotten gains.

#### **IV. State Law Enforcement Actions**

The FTC works closely with the offices of State Attorneys General and other state agencies to protect consumers of prepaid calling cards. In the fall of 2007, the FTC established a joint federal-state task force concerning deceptive marketing practices in the prepaid calling card industry. The task force members include representatives from the offices of more than 35 State Attorneys General and other state and local agencies, and the Federal Communications

Commission (“FCC”). Working cooperatively allows the FTC and other state, local, and federal agencies to share information and coordinate law enforcement activity in this arena.<sup>7</sup>

Collectively, states have brought over 20 enforcement actions against prepaid calling card companies for allegedly deceptive marketing practices. Leading the way is the Office of Florida Attorney General Bill McCollum, which has entered into Assurances of Voluntary Compliance (“AVCs”) with 13 prepaid calling card companies.<sup>8</sup> These settlements are the culmination of a broad investigation into the prepaid calling card industry launched by the Florida Attorney General in July of 2007. Likewise, the Office of the Illinois Attorney General is actively investigating a number of prepaid calling card companies. The New Jersey Attorney General recently has entered into AVCs with seven prepaid calling card providers.<sup>9</sup> The Texas Attorney General has an ongoing enforcement action against Next-G Communication, a

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<sup>7</sup> 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.

<sup>8</sup> See, e.g., Press Release, *McCollum Announces Prepaid Calling Card Settlements, Industry-Wide Reform* (June 11, 2008), available at [www.myfloridalegal.com/newsrel.nsf/newsreleases/79C6666DB24608D785257465004EC901](http://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.; Cinco Telecom; and Touch-Tel USA.

<sup>9</sup> See Press Release, *New Jersey Calls ‘Time Out’ on Prepaid Calling Cards* (Mar. 17, 2009), available at [www.consumeraffairs.com/news04/2009/03/nj\\_calling\\_cards.html](http://www.consumeraffairs.com/news04/2009/03/nj_calling_cards.html). The companies subject to the New Jersey AVCs are: CVT Prepaid Solutions, Inc.; Dollar Phone Enterprises, Inc.; Epana Networks, Inc.; IDT Corp.; Locus Telecommunications, Inc.; STi PhoneCard, Inc.; and Total Call International, Inc.

telecommunications service provider that produces and sells prepaid calling cards.<sup>10</sup> The California Attorney General also has recently obtained a consent decree against Total Call International, Inc.<sup>11</sup>

The FTC commends the actions of the Florida, Illinois, New Jersey, Texas, and California Attorneys General and is grateful for their participation and the participation of all of our law enforcement partners in the FTC's joint federal-state calling card task force.

## **V. The Proposed Legislation**

The FTC supports the goal of H.R. 3993 to provide better disclosures to consumers and believes that it would give the FTC and the states powerful new tools to combat fraud in this area. The FTC appreciates Representative Engel's leadership in protecting consumers of prepaid calling cards.

The FTC believes the proposed elimination of the common carrier exemption with respect to the providers of telecommunications service for prepaid calling cards is essential to the FTC's ability to protect consumers in this arena. The FTC Act exempts common carriers subject to the Communications Act from its prohibitions on unfair and deceptive acts or practices and unfair methods of competition. 15 U.S.C. §§ 44, 45(a)(2). The common carrier exemption has forced the FTC to focus its enforcement efforts on distributors of prepaid calling cards. As a consequence, the telecommunications service providers for such cards have eluded

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<sup>10</sup> *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](http://www.oag.state.tx.us/oagNews/release.php?id=2479).

<sup>11</sup> See Press Release, *Brown Prevents Calling Card Company From Boosting Profits By Charging Hidden Fees*, available at [www.ag.ca.gov/newsalerts/release.php?id=1732](http://www.ag.ca.gov/newsalerts/release.php?id=1732).



prosecution by the FTC. Significantly, H.R. 3993 would create a limited carve-out from the common carrier exemption to the FTC Act, to permit the FTC to bring enforcement actions against the common carriers that provide telecommunications service for prepaid calling cards. The FTC strongly supports this extension of FTC authority, which will ensure that a significant segment of the prepaid calling card industry no longer will be shielded from FTC enforcement actions. Notably, there is precedent for granting the Commission authority over telecommunications service providers for the purpose of protecting consumers of a particular service or product. In the Telephone Disclosure and Dispute Resolution Act, 15 U.S.C. § 5701, *et seq.*, Congress authorized the FTC to promulgate regulations concerning advertising for, operation of, and billing and collection procedures for pay-per-call or “900 number” telephone services. *See* 16 C.F.R. Part 308.

Critically, however, the bill’s exemption of certain prepaid wireless phone services from its coverage raises concerns. This exception could provide a powerful incentive for the worst actors in the prepaid calling card industry to migrate their business practices to prepaid wireless handsets and refill cards in an effort to avoid the mandates of the proposed law.<sup>12</sup>

The FTC also supports the proposed authorization of civil penalties for violations of the FTC Act, which will give the agency a powerful new remedy in this arena. To enable the Commission to address problems with deceptive conduct involving prepaid calling cards more effectively, the Commission also recommends that Congress give the Commission authority to bring actions seeking civil penalties in its own right against prepaid calling card providers and

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<sup>12</sup> 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.

distributors rather than through the Department of Justice (“DOJ”).<sup>13</sup> Giving the FTC authority to bring its own civil penalties cases in this area would help ensure that the Commission does not have to forego quick relief in order to seek civil penalties.<sup>14</sup>

The Commission recognizes that the agency and the Committee share the same goal: stopping unscrupulous calling card companies from defrauding vulnerable consumers. The Commission looks forward to working with the Committee regarding the legislation as the Committee moves forward.

## **VI. The Common Carrier Exemption**

The Commission appreciates the proposed extension of its authority over prepaid calling card providers, but nonetheless, the Commission respectfully recommends that Congress repeal altogether the FTC Act exemption for common carriers subject to the Communications Act. On several occasions, the Commission has testified in favor of the repeal of the common carrier

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<sup>13</sup> 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.*

<sup>14</sup> 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 Anti-Fraud Law Enforcement Program and Recommending Changes in the Law and Resources To Enhance the Commission’s Ability to Protect Consumers Before the Subcommittee on Consumer Protection, Product Safety, and Insurance of the Committee on Commerce, Science, and Transportation, U.S. Senate (July 14, 2009), *available at* [www.ftc.gov/os/2009/07/P094402antifraudlawtest.pdf](http://www.ftc.gov/os/2009/07/P094402antifraudlawtest.pdf). Commissioner Kovacic has dissented from the Commission’s endorsement of across-the-board civil penalty authority. *See id.* at 3 n.4.

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

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

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<sup>15</sup> 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](http://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.<sup>16</sup>

The FTC has extensive expertise with advertising, marketing, billing, and collection – areas in which significant problems have emerged in the telecommunications industry.<sup>17</sup> 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 Committee for focusing attention on this important issue and for the opportunity to discuss its law enforcement program.

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

<sup>17</sup> 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).