



Office of the Secretary

UNITED STATES OF AMERICA  
FEDERAL TRADE COMMISSION  
WASHINGTON, D.C. 20580

January 24, 2008

Sandra F. Braunstein, Director  
Division of Consumer and Community Affairs  
Board of Governors of the Federal Reserve System  
Washington, D.C. 20551

Dear Ms. Braunstein:

This letter responds to your request for information regarding the enforcement activities of the Federal Trade Commission (“Commission” or “FTC”) under the Truth in Lending, Consumer Leasing, Equal Credit Opportunity, and Electronic Fund Transfer Acts (“Acts”) during the 2007 calendar year, for use in preparing the Federal Reserve Board’s (“Board”) Annual Report to Congress. You have asked for information regarding the Commission’s enforcement activities pursuant to those Acts, including methods of enforcement, and the extent to which compliance is achieved by entities subject to the Commission’s enforcement authority.<sup>1</sup> Also, you have asked whether the Commission recommends any changes to these laws or their implementing regulations or wishes to provide other comments or observations.

**I. THE COMMISSION’S 2007 ENFORCEMENT ACTIVITIES UNDER THE ACTS <sup>2</sup>**

**Truth in Lending Act<sup>3</sup>**

In calendar year 2007, the Commission continued its enforcement activities against unlawful lending practices. As discussed below, the Commission’s staff sent over 200 warning letters to mortgage brokers, lenders, and media outlets regarding mortgage advertising claims that

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<sup>1</sup> The Commission is charged with enforcement of the Federal Trade Commission Act (“FTC Act”) and various federal consumer financial laws and regulations, including the Truth in Lending Act (“TILA”), Consumer Leasing Act (“CLA”), Equal Credit Opportunity Act (“ECOA”), and Electronic Fund Transfer Act (“EFTA”), with respect to most nonbank entities in the United States. The Commission does not collect data regarding the extent of compliance by those numerous nonbank entities. As a result, this letter does not provide information on that issue.

<sup>2</sup> Information concerning the Commission’s enforcement and other activities discussed in this report is also available at the Commission’s Web site at <http://www.ftc.gov>.

<sup>3</sup> The Commission’s enforcement activities under the TILA in 2007 pertained to credit violations. The Commission did not initiate any enforcement actions alleging violations of the CLA, an amendment to the TILA.

may violate federal law, and has ongoing nonpublic investigations of potential TILA violations. The Commission also is continuing to litigate a case in federal district court for alleged violations of the TILA, Regulation Z, and the FTC Act.

**A. TILA Enforcement Efforts**

During the summer of 2007, the FTC staff conducted a nationwide review of home mortgage advertisements that focused on claims for very low monthly payment amounts or interest rates, without adequate disclosures of other important loan terms. The review included advertisements currently appearing in Web sites, newspapers, magazines, direct mail, and unsolicited e-mail and faxes, including some advertisements in Spanish. Thereafter, the FTC sent letters to more than 200 mortgage brokers and lenders, and media outlets that carried the advertisements, warning that some of the advertising claims may violate federal law.<sup>4</sup> In the warning letters, the FTC advised the advertisers and media outlets that some mortgage ads are potentially deceptive or in violation of the Truth in Lending Act. Letters to advertisers advised them to review their ads, and to read business and consumer education materials on the FTC's Web site to learn about relevant laws and requirements. Letters to media outlets advised them about the potentially deceptive advertising, with guidance on screening ads for questionable claims. At present, there are several ongoing nonpublic investigations of home mortgage advertisers for potential deceptive practices and violations of the TILA.

The Commission also continued its litigation in federal district court against a mortgage broker, Chase Financial Funding, and its principals, for alleged violations of the FTC Act, the TILA, and Regulation Z, in connection with advertisements for extremely low mortgage rates.<sup>5</sup> As described in previous reports, the defendants sent consumers spam and direct mail falsely offering consumers a "3.5% fixed payment" loan. According to the complaint, the defendants did not offer any such loan; in fact, if consumers chose to pay the advertised payment amounts, then their principal balances would increase, and after an introductory period, they would be forced to make higher monthly payments. The complaint alleged that the defendants violated the FTC Act by making various deceptive claims. The complaint further alleged that the defendants violated the TILA and Regulation Z by: (1) advertising credit terms other than those that actually are or will be arranged or offered by the creditor; (2) stating a rate of finance charge without clearly and conspicuously disclosing the APR or the fact that the APR may increase after consummation; (3) advertising a "payment rate" without making other required disclosures; and (4) failing to disclose the terms of repayment or the APR, as required. The complaint seeks consumer redress and other permanent equitable relief.

As reported in 2006, the stipulated preliminary injunction that the court previously entered in Chase Financial Funding remained in place. The Commission continued to receive

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<sup>4</sup> See Press Release, FTC Warns Mortgage Advertisers and Media That Ads May be Deceptive (September 11, 2007), available at <http://www.ftc.gov/opa/2007/09/mortsurf.shtm>.

<sup>5</sup> *Federal Trade Commission v. Chase Financial Funding, Inc.*, No. SACV 04-549 GLT (ANx) (C.D. Cal. filed May 12, 2004).

distributions from the defendant Chief Executive Officer James F. Berry's bankruptcy estate, after the defendant Berry filed for bankruptcy in 2006.<sup>6</sup> As of 2007, pursuant to our proof of claim, the Commission received total bankruptcy distributions exceeding \$325,000.<sup>7</sup> Litigation continues in the case.

## **B. Other Initiatives**

The FTC released a Bureau of Economics report presenting the results of a study on mortgage disclosures.<sup>8</sup> The study examined how consumers search for mortgages, how well consumers understand mortgage cost disclosures and the terms of their loans, and whether better disclosures can help consumers understand mortgage costs, shop for mortgage loans, and avoid deceptive lending practices. The report presented the findings that mortgage disclosure forms fail to convey key mortgage costs and terms to many consumers. The study concluded that better disclosures can be created to help consumers understand the costs and terms of mortgages to enable them to make informed decisions about mortgage products. The study's key findings also included that (1) with current disclosures, both prime and subprime borrowers misunderstood key loan terms, and both groups benefitted from better disclosures; and (2) for complex loans, where prime and subprime borrowers had the most difficulty understanding loan terms, better disclosures provided the greatest benefit.

Based in part on the above mortgage disclosure study, the FTC submitted staff comments to the Federal banking agencies in response to the agencies' request for comments on proposed illustrations of consumer information for subprime mortgage lending.<sup>9</sup> In the comments, the FTC staff supported the agencies' efforts to develop mortgage disclosures to help subprime borrowers make better informed decisions. The FTC staff also recommended that the agencies consider testing the effectiveness of their proposed new disclosures and consider undertaking a more comprehensive effort to improve federal mortgage disclosures. According to the comments, current mortgage disclosures frequently fail to convey key information to consumers, often are

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<sup>6</sup> Defendant Berry filed for bankruptcy following his agreement in 2005 to pay \$400,000 to the Commission, under a stipulated order releasing him from confinement for civil contempt of the stipulated preliminary injunction. *In re Berry*, No. 8:06-BK-10560-JR (Bankr. C.D. Cal. Apr. 20, 2006).

<sup>7</sup> *Id.* (Bankr. C.D. Cal. Oct. 17, 2006).

<sup>8</sup> See JAMES M. LACKO AND JANIS K. PAPPALARDO, FEDERAL TRADE COMM'N, BUREAU OF ECONOMICS STAFF REPORT, IMPROVING CONSUMER MORTGAGE DISCLOSURES: AN EMPIRICAL ASSESSMENT OF CURRENT AND PROTOTYPE DISCLOSURE FORMS (2007), available at <http://www.ftc.gov/os/2007/06/P025505mortgagedisclosurereport.pdf>. The Commission unanimously voted to issue the report.

<sup>9</sup> See FEDERAL TRADE COMM'N, STAFF COMMENTS TO JENNIFER J. JOHNSON, SECRETARY, BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM, October 2007, available at <http://www.ftc.gov/be/v080000.pdf>. The comments present the views of the staff of the Bureau of Economics, Bureau of Consumer Protection, and the Office of Policy Planning. The Commission unanimously voted to file the comments.

misunderstood, and may contribute to information problems in the mortgage market.<sup>10</sup> These findings apply to both prime and subprime borrowers, and to the evaluation of simple, fixed-rate mortgages. Based on staff's research, the comments state that consumers likely would benefit from one clear disclosure document that alerts them to the major costs and features of a mortgage. This document should significantly reduce the cost of obtaining information about the true value of different mortgage options, be noticeable and easy to read and understand, summarize key loan features up-front to facilitate informed comparison shopping, and make clear what a consumer is getting into before signing. The comments also note the importance of consumer research and express the staff's readiness to participate with other federal agencies in a more comprehensive effort to improve federal mortgage disclosures.

In addition, the FTC submitted staff comments on the Department of Defense's ("DoD") proposed regulation to implement the military lending consumer protections of the John Warner National Defense Authorization Act of Fiscal Year 2007, section 670, "Limitations on Terms of Consumer Credit Extended to Service Members and Dependents" ("Act").<sup>11</sup> The proposed regulation required oral and written disclosures, a 36 percent rate cap, and other lending limitations, including prohibitions or restrictions on refinances and renewals by the same creditor, mandatory arbitration, creditor demands for certain notices from borrowers, creditor use of vehicle titles as security, and prepayment penalties and fees. Violators would be subject to criminal prosecution, and contracts in violation of the proposed regulation would be void. The FTC supported the proposed regulation, and, in particular, DoD's proposal to: (1) focus the regulation on those products that it had found most problematic for Service members – payday loans, title loans, and refund anticipation loans; and (2) apply the regulation to all types of lenders of these products, rather than exempting banks and similar entities.<sup>12</sup>

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<sup>10</sup> See *supra* note 8. The comments also discussed an earlier study on mortgage disclosures. See JAMES M. LACKO AND JANIS K. PAPPALARDO, FEDERAL TRADE COMM'N, BUREAU OF ECONOMICS STAFF REPORT, THE EFFECT OF MORTGAGE BROKER COMPENSATION DISCLOSURES ON CONSUMERS AND COMPETITION: A CONTROLLED EXPERIMENT (2004), available at <http://www.ftc.gov/os/2004/01/030123mortgagefullrpt.pdf>.

<sup>11</sup> Pub. L. 109-364, codified at 10 U.S.C. § 987 (2007). The proposed amendments are found at 72 Fed. Reg. 18,157-18,170 (Apr. 11, 2007). The comments are titled FEDERAL TRADE COMM'N, BEFORE THE DEPARTMENT OF DEFENSE, IN THE MATTER OF REQUEST FOR COMMENT ON PROPOSED REGULATION IMPLEMENTING LIMITATIONS ON TERMS OF CONSUMER CREDIT EXTENDED TO SERVICE MEMBERS AND DEPENDENTS, DOCKET NO. DOD-2006-OS-0216, June 2007, available at <http://www.ftc.gov/os/2007/06/070614dodcomm.pdf>. The comments present the views of the staff of the Bureau of Consumer Protection, Office of Policy Planning, and the Bureau of Economics. The Commission unanimously voted to file the comments.

<sup>12</sup> The final regulation was issued in August 2007 and is consistent with the above staff comments. See 72 Fed. Reg. 50,580 (Aug. 31, 2007) (codified at 32 C.F.R. Part 232). The Act and regulation became effective October 1, 2007. See 10 U.S.C. § 987 Note (2007).

### **C. Consumer and Business Education**

The Commission's consumer and business education efforts for consumer credit and consumer leasing are vital to achieving its mission and enforcement goals. In 2007, the Commission released mortgage related consumer brochures, including "Deceptive Mortgage Ads: What They Say; What They Leave Out," "Mortgage Payments Sending You Reeling? Here's What to Do," "Buying a Home: It's a Big Deal," and "How to Manage Your Mortgage if Your Lender Closes or Files for Bankruptcy."<sup>13</sup> In 2007, the Commission also issued updates to various publications relating to the TILA, including "Home Equity Credit Lines" and "Understanding Vehicle Financing."<sup>14</sup> In furtherance of its Hispanic Outreach Program, the Commission published Spanish-language versions of certain publications: "La Compra de una Vivienda (Buying a Home: It's a Big Deal)" and "Anuncios de Hipotecas Engañosas: Lo que Dicen y lo que Omiten (Deceptive Mortgage Ads: What They Say; What They Leave Out)."<sup>15</sup> All of the Commission's consumer protection materials are made available to the public through the Commission's Web site.<sup>16</sup>

### **Equal Credit Opportunity Act**

Although the Commission did not initiate any enforcement actions in 2007, as the Commission stated in Congressional testimony in July 2007, it is engaged in several ongoing, non-public fair lending investigations of mortgage lending companies.<sup>17</sup> The testimony

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<sup>13</sup> See FEDERAL TRADE COMM'N, DECEPTIVE MORTGAGE ADS: WHAT THEY SAY; WHAT THEY LEAVE OUT, at <http://www.ftc.gov/bcp/edu/pubs/consumer/alerts/alt023.pdf>, FEDERAL TRADE COMM'N, MORTGAGE PAYMENTS SENDING YOU REELING? HERE'S WHAT TO DO, at <http://www.ftc.gov/bcp/edu/pubs/consumer/homes/re04.pdf>, FEDERAL TRADE COMM'N, BUYING A HOME: IT'S A BIG DEAL, at <http://www.ftc.gov/bcp/edu/pubs/consumer/alerts/zalt001.pdf>, and FEDERAL TRADE COMM'N, HOW TO MANAGE YOUR MORTGAGE IF YOUR LENDER CLOSES OR FILES FOR BANKRUPTCY, at <http://www.ftc.gov/os/2007/12/071219mortgage.pdf>.

<sup>14</sup> See FEDERAL TRADE COMM'N, HOME EQUITY CREDIT LINES, at <http://www.ftc.gov/bcp/edu/pubs/consumer/homes/rea02.pdf> and FEDERAL TRADE COMM'N, UNDERSTANDING VEHICLE FINANCING, at <http://www.ftc.gov/bcp/edu/pubs/consumer/autos/aut04.pdf>.

<sup>15</sup> See FEDERAL TRADE COMM'N, LA COMPRA DE UNA VIVIENDA, at <http://www.ftc.gov/bc/edu/pubs/consumer/alerts/zsalt001.pdf> and FEDERAL TRADE COMM'N, ANUNCIOS DE HIPOTECAS ENGAÑOSAS: LO QUE DICEN Y LO QUE OMITEN, at <http://www.ftc.gov/bc/edu/pubs/consumer/alerts/salt023.pdf>. Numerous additional materials for Hispanic consumers are also available. See <http://www.ftc.gov/ojo>.

<sup>16</sup> See <http://www.ftc.gov/bcp/consumer.shtm>.

<sup>17</sup> *Home Mortgage Disclosure Act Data and FTC Lending Enforcement Before the House Committee on Financial Services, Subcommittee on Oversight and Investigations* (statement of Lydia B. Parnes, Director of Bureau of Consumer Protection, Federal Trade Comm'n, July 25, 2007, at 7-9) available at <http://www.ftc.gov/os/testimony/P064806hdma.pdf>.

summarized how the Commission uses Home Mortgage Disclosure Act (“HMDA”)<sup>18</sup> data as a screening or targeting tool for fair lending compliance investigations. According to the testimony, although some pricing data and loan applicant information are available, the HMDA data overall are limited and insufficient to establish a law violation. Instead, the Commission uses the reported data to identify lenders with differences in outcomes for protected classes, and in particular for minorities compared to non-minorities.<sup>19</sup> The testimony observed that, consequently, the principal goal of a fair lending investigation is to determine whether or not the differences in outcomes persist after legitimate underwriting criteria are taken into account, and that the Commission uses the HMDA data as a screening or targeting tool for fair lending compliance investigations. The testimony also noted that the Commission has a strong commitment to enforcing the fair lending laws and will pursue vigorously any violations revealed by its investigations.

### **Electronic Fund Transfer Act**

In 2007, the Commission entered into one settlement, and continued litigation in another case, for alleged violations of the EFTA, Regulation E, the FTC Act, and other Federal statutes. Other nonpublic investigations of potential EFTA violations are ongoing.

The Commission settled charges against Remote Response Corporation, its marketing and management company, and various principals for, among other things, alleged violations of the EFTA, Regulation E, and the FTC Act.<sup>20</sup> According to the complaint, the defendants marketed to Spanish-speaking consumers and sold products under the name “Amerikash.”<sup>21</sup> The complaint alleged that defendants made promises of a guaranteed, pre-approved MasterCard for an advance fee ranging from \$138-\$200 (along with free items such as an ATM card and phone card) and a free trial membership in a discount health plan. The complaint alleged that many consumers never received a MasterCard, and instead received only a random combination of the free items, and that many consumers received nothing. The complaint also alleged defendants charged consumers’ credit cards, or debited their bank accounts for the discount health plan on a recurrent basis, without obtaining their authorization for preauthorized electronic fund transfers in violation of the EFTA and Regulation E.

The stipulated final orders ban the defendants from telemarketing and from ever selling credit, debit, stored value, ATM or phone cards, travel or gas vouchers, vacation package

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<sup>18</sup> HMDA is at 12 U.S.C. § 2801 *et seq.*

<sup>19</sup> The Federal Reserve Board provides to the Commission information and analysis regarding HMDA data reported by the lenders within the FTC’s jurisdiction. The Commission staff reviews this analysis and also performs its own, independent analysis of the data.

<sup>20</sup> *Federal Trade Commission v. Remote Response Corp.*, No. 06-20168-CIV (S.D. Fla. Aug. 23, 2007).

<sup>21</sup> *Id.* (S.D. Fla. Jan. 23, 2006). The complaint was later amended to include additional principals of Remote Response Corp. *Id.* (S.D. Fla. June 5, 2006).

discounts, or health discount plans.<sup>22</sup> The orders also entered judgments totaling \$4,164,558 (the total amount of consumer injury) against each of the defendants. The court also prohibited defendants from making misrepresentations about the goods and services they sell, from charging consumers improperly, and from misrepresenting the terms and conditions of free-trial offers. In connection with obtaining payment for “free-to-pay” offers, the orders prohibited the defendants from improperly debiting consumers’ bank accounts or charging their credit or debit cards.

The Commission continued its litigation in federal district court against Berkeley Premium Nutraceuticals, Inc. and other corporate and individual defendants for, among other things, alleged violations of the EFTA, Regulation E, and the FTC Act.<sup>23</sup> According to the complaint, the defendants offered consumers “free” samples of their dietary supplements and enrolled them in a program that automatically shipped them more pills and billed them for the shipments, even though most consumers never agreed to participate in the program. The complaint charged that after consumers provided credit or debit card information to pay the \$4.50 shipping and handling fee for the “free” samples, the defendants used that information to bill consumers for future shipments that they sent automatically. The defendants enrolled consumers in the continuity program, according to the complaint, and automatically billed them on a recurring basis without obtaining their authorization for the recurring debits in violation of the EFTA and Regulation E. The complaint seeks, among other things, permanent injunctive relief and consumer redress.

## **II. ANY SUGGESTIONS FOR CHANGES IN THE ACTS OR THEIR IMPLEMENTING REGULATIONS**

The Commission has no suggestions for changes in the Acts or their implementing Regulations at this time beyond the staff comments referenced above.

The Commission hopes that the information contained in this letter responds to your inquiry and will assist in preparation of the Board’s Annual Report to Congress. If any other information would be useful or if you wish to request additional assistance, please contact Peggy Twohig, Associate Director, Division of Financial Practices, at (202) 326-3224.

By direction of the Commission.

Donald S. Clark  
Secretary

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<sup>22</sup> The orders applied to defendants: Remote Response Corporation; Alberto Salama, Samuel Salama, Elias Salama and Joseph Bensabat, co-owners of Remote Response; and German Espitia, president of Instant Way Corp. As reported last year, the court previously entered an order of default judgment and permanent injunction against defendant Instant Way Corp. on August 2, 2006. *Id.* (S.D. Fla. Aug. 1, 2006).

<sup>23</sup> *Federal Trade Commission v. Warshak*, No. 1:06-cv-00051-SJD (S.D. Ohio filed Jan. 30, 2006). The order staying this case, pending the outcome of the criminal trial, remains in effect. *See id.* (S.D. Ohio Dec. 27, 2006).