

Testimony of
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of the
National Consumers League

before the

United States House of Representatives
Subcommittee on Commerce, Trade, and Consumer Protection
of the Committee on Energy and Commerce

Hearing on Calling Card Consumer Protection Act (H.R. 3993)
December 3, 2009

Introduction

Good morning, Mr. Chairman. My name is Sally Greenberg and I am Executive Director of the National Consumers League. I appreciate this opportunity to appear before the House Committee on Energy and Commerce to again discuss the need for greater consumer protections in the purchase and use of prepaid calling cards. When we last appeared before this committee to discuss the issue, we equated the prepaid calling card marketplace with the “Wild West,” where unwary consumers too often fall victim to unscrupulous sellers and merchants. A little over one year later, we are sad to say that the situation for consumer remains more “Gunsmoke” than “Little House on the Prairie.”

The National Consumers League, whose founding in 1899 makes us the oldest consumer organization in the United States, has a longstanding interest in protecting consumers from fraudulent practices and is the only consumer group that operates a national fraud center. (NCL’s Fraud Center is described at www.fraud.org).

I want to applaud members of this Committee for the scrutiny and attention you have given to the issue of prepaid calling cards and commend Congressman Engel for introducing H.R. 3993 the “Calling Card Consumer Protection Act.” Consumers rely on members of this committee to defend consumer rights and protections and to look out for consumer interests. In my testimony, I will address some of the facts and figures describing the magnitude of the prepaid calling card industry and the large amounts of money involved. I will also discuss the fraud and deceptive practices associated with that industry and actions taken at the state and federal levels in response to fraud. I’ll discuss why NCL supports H.R. 3993, and I’ll make some policy

recommendations.

Part of the problem with the high incidence of fraud in the prepaid calling card business is the ease with which con artists can start a scam. According to Pablo Bressan, a Miami-based telecom consultant and prepaid calling card distributor, it costs as little as \$20,000 to buy the long-distance minutes and back-end computer platforms to get into the business. Some companies do not even go that far -- simply re-selling the cards made by others.¹

The potential for fraud in the prepaid calling card industry is so well-known that it even merited a mention as a preferred scheme on HBO's *The Sopranos*, with Tony Soprano calling fraudulent card schemes "(expletive) beautiful! It's a good one."

While we're not suggesting that the whole prepaid calling card industry is controlled by organized crime: we have no such evidence, this vignette from *The Sopranos* demonstrates how easy it is to get into the industry, rip off consumers, and disappear with no accountability. That must change.

Prepaid Calling Card Facts

- The North American prepaid calling card industry is estimated to reach \$2.14 billion in revenues by 2012.²
- Counting prepaid wireless products, the total prepaid telecommunications industry is estimated to reach \$22 billion in revenues by 2012.³
- Examples of fraudulent practices used by the prepaid companies include "hang-up fees," periodic maintenance fees, destination surcharges, and high billing increments.⁴
- Companies that try to "play by the rules" are often punished by a loss of market share due to

¹ Tessler, Joelle. "1-800 Scammer: Prepaid Calling Cards Rife with Fraud," Associated Press. October 7, 2008. Online: <http://www.msnbc.msn.com/id/27052474/>.

² "Growing Immigrant Population and International Visitors to Drive Sales of Calling Cards in North America," Press Release. September 12, 2006. Online: <http://www.frost.com/prod/servlet/press-release.pag?docid=81415399>. Retrieved on November 30, 2009.

³ Atlantic-ACM. "Prepaid Telecom Market to Reach \$22 Billion by 2012, New Atlantic-ACM Study Reveals," Press release. March 25, 2008. Online: http://www.atlantic-acm.com/index.php?option=com_content&view=article&id=396:pressrelease-03-25-08&catid=33:2008-press-releases&Itemid=5 Retrieved November 30, 2009.

⁴ Office of the Attorney General of Florida (June 11, 2008). "McCollum Announces Prepaid Calling Card Settlements, Industry-Wide Reform". Press release. Retrieved on July 24, 2008.

fraudulent carriers.⁵

- Eleven states, including California, Connecticut, Florida, Illinois, and New Jersey currently have laws pertaining to calling card fraud, specifically. Most turn to generic consumer protection statutes, but enforcement has been extremely light.⁶
- Hispanic consumers may be losing up to \$1 million per day because of fraudulent phone cards.⁷
- The average calling card delivers only 60% of the minutes promised, according to the Hispanic Institute, a non-profit research group.⁸
- The Federal Trade Commission's (FTC) survey of prepaid calling cards confirms the Hispanic Institute's findings. For instance, one calling card tested by the FTC claimed to offer 360 minutes to Panama, but only delivered 23 minutes of calling time. The FTC said that in 87 tests of prepaid cards, they delivered an average of only 50 percent of the advertised minutes.⁹
- The cost-per-minute rates for prepaid phone cards can be up to 87 percent higher than expected. An expected call rate of 15 cents per minute, for example, may end up costing 28 cents per minute.¹⁰
- Customer service representatives for prepaid calling cards are often unavailable or not knowledgeable regarding the prepaid phone cards their employers are selling. A 2005 University of Georgia study found that in a third of the calls to prepaid calling card customer service lines, callers couldn't reach a representative. When they did make contact, the representative often was unable to answer basic questions about fees or rounding up of minutes.¹¹

⁵ Holden, Diana. "Calling Out Prepaid Phone Cards," *BusinessWeek*. July 9, 2008. Retrieved July 24, 2008.

⁶ "Facts and Figures," The Hispanic Institute. Retrieved on July 24, 2008.

⁷ "Facts and Figures," *The Hispanic Institute*. Retrieved on July 24, 2008.

⁸ "Prepaid Calling Cards: Market Dynamics and Forecast 2003-2008," ATLANTIC-ACM. February 2003. Retrieved on July 25, 2008.

⁹ Dang, Dan Thanh. "Avoid These Prepaid Calling Cards, FTC says," *Baltimore Sun*. June 6, 2008. Retrieved July 24, 2008.

¹⁰ Horton, Denise. "Prepaid Phone Cards: Caller Beware," *University of Georgia Research Magazine*. Fall 2005. Retrieved on July 24, 2008.

¹¹ *Ibid.*

Why We Need To Protect Users of Prepaid Calling Cards

The rapid growth of the prepaid calling card industry combined with, until recently, a lax enforcement of consumer protection statutes at the state and federal levels, has enabled consumer fraud to flourish. Like so many other fraudulent practices, the most frequent victims are the most vulnerable consumers: immigrants and the working poor; and those lower income Americans who don't have or cannot afford regular phone service. These consumers rely on calling cards to stay in touch with friends and loved ones in the US and abroad. We believe that military families are also likely victims of certain deceptive industry practices.

Yes, the cards provide these users with an alternative means of calling home, but many use false and deceptive practices in the process, along with imposing unconscionable terms. Fraud is fraud—if an automobile is sold with the promise of a sun roof and chrome wheels, it better have a sunroof and chrome wheels—if a phone card promises 500 minutes to call El Salvador, it should deliver those 500 minutes.

Some state attorneys general have done a commendable job in prosecuting fraudulent prepaid card practices, including in Florida and Texas. The Federal Trade Commission has also conducted investigations and brought important cases against individual prepaid phone card providers. While these efforts are important, they are too diffuse to reign in the frequently deceptive promises made by the industry selling these cards. We need basic federal protections to stem the tide of the many deceptive practices in this industry.

NCL believes that giving the FTC greater authority, as called for in H.R. 3993, would help to level the playing field for calling card providers. As called for in H.R. 3993, regulations should include requirements that prepaid phone card providers and distributors disclose the terms and conditions of the cards and list the per minute rates, preferred international destination rates, and any fees or surcharges in their advertising,

We applaud the leadership of the FTC and state attorneys general have shown in cracking down on unscrupulous calling card operators. Beginning in February of this year, the FTC, working with the states, began a series of investigations that have resulted in numerous fraudulent calling card companies being fined millions of dollars. While the FTC and state actions in this area have benefitted consumers, we fear that millions of dollars in losses continue to flow from unwary consumers into the pockets of scammers in the calling card industry.

To address this issue, we support a national floor of minimum requirements stating what industry practices won't be permitted. We applaud H.R. 3993's provisions preserving the rights of states

to go forward with their own civil cases—as Florida did. The federal government should set minimum standards and permit states to act on behalf of their citizens with stronger standards if they so choose. That pro-consumer language acknowledges the important role states have played in enacting and enforcing consumer protections.

Federal legislation may have other positive effects. Anecdotal evidence suggests that the simple threat of regulation has already increased pressure on the prepaid calling card industry to reform its marketing practices.¹² We've also seen evidence through the IDT settlement in Florida that if one company is forced to disclose accurately how many minutes a card will provide and what the surcharges and fees will be, they will lose market share to the other firms who are shading the truth. Therefore, we need to create a level playing field where all participants are required to provide accurate information.

Beyond Disclosure: What More Can We Do To Protect Consumers

While NCL supports efforts requiring full disclosure of terms and conditions on these prepaid calling cards, we find that the terms themselves, even when disclosed, are too often unconscionable.

For example, the text in fine print on the back of a \$5.00 “Africa Sky” card states the following:

All of the following fees will reduce the number of available minutes and the value of the card. Use of a toll free number from a pay phone will incur a \$.99 per call fee. Per minute rate will be .02 higher for calls placed using toll free access numbers. Call time for multiple calls is calculated by rounding the last minute up to the closest multiple of 3 and then adding 1 minute except that if your call lasts less than 1 minute you will be charged only for a minute. If available minutes are not all used up on the first call the following fees will apply (1) the multiple call rate will be 40% higher and will apply to all calls (see poster for details) (2) a fee per call of \$.59 will apply to each call; and 3) on midnight after the first call a fee of \$.69 will be deducted and then weekly thereafter. Card Expires Three Months After First Use. . . Rates and Fees are Introductory and are subject to change anytime. . . .

The same or similar text is found on most of the cards. So, though we have the terms disclosed, albeit in fine print, we have a company that is rapidly subtracting money from the user's original purchase. A 40% higher rate is imposed after the first call; a fee of 59 cents per call will apply to each one after the first call; and after midnight of the first call, the fee is 69 cents, which will be

¹² Marshalian, Jonathan. “You’ve Come a Long Way, Baby,” *The Prepaid Press*. September 17, 2007. Retrieved July 25, 2008.

deducted weekly thereafter. This is from an original \$5.00 card. No wonder users find that two or three weeks—or sooner—after first use, the card has no credit remaining. Notice the card also contains this catch-all phrase “*Rates and Fees are Introductory and are subject to change anytime...*” leaving the card distributors the option of changing the rules whenever they wish.

Worse still is the \$2.00 “Majestic DMV” Card :

- 1) *A .99 fee applies on the 1st day of use and every 5 days thereafter;*
- 2) *Calls made through toll free access numbers are subject to a fee of up to 4 cents a minute*
- 3) *Payphone surcharge of .99¢*
- 4) *A destination surcharge of between 20-60% of the total call; and/or 5) a fee of .10-.99 for connected calls, .15/minute maximum domestic call rate (before applicable charges and fees); minutes and/or seconds are billed at a minimum of one minute and up to 5 minute increments, plus any applicable fees. Card expires 3 months after first use or 12 months after activation.*

As a consumer advocate, I’ve often found it useful to look at consumer protection measures in other countries. I lived in Australia two years ago and used prepaid cards for calls to the United States. My experience was uniformly positive—the Australian prepaid cards tended to deliver the minutes they promise, and they were good for multiple uses. *Choice Magazine*, Australia’s counterpart to our *Consumer Reports*, tested these international calling cards and found that indeed, many delivered good value and low rates without connection fees or added charges. When I arrived back in the United States and began buying cards here, I found that their value tended to disappear after the first call. When I read the fine print, I understood why.

I also consulted the document *Consumer Protection in the European Union—Ten Basic Principles*—and note that the Fifth Principle is relevant to our discussion of prepaid calling cards:

Contracts Should Be Fair To Consumers

Have you ever signed a contract without reading all the small print? What if the small print says the deposit you just paid is non-refundable – even if the company fails to deliver its side of the bargain? What if it says you cannot cancel the contract unless you pay the company an extortionate amount in compensation? EU law says these types of unfair contract terms are prohibited. Irrespective of which EU country you sign such a contract in, EU law protects you from these sorts of abuses.

We could apply the EU’s notion of contract fairness to this issue. NCL supports H.R. 3993’s

disclosure requirements and hopes that they will satisfactorily address the problem of consumers paying good money for a prepaid calling card that fails to deliver the service, but we don't think it goes far enough. Our recommendations for better consumer protections are laid out below. At the same time, we acknowledge the importance of an open marketplace where all prepaid calling card companies are required to provide accurate information.

NCL Policy Recommendations Related to Disclosure and H.R. 3993

The National Consumers League strongly supports H.R. 3993 and its provisions to give enforcement authority to the Federal Trade Commission under the "unfair or deceptive act or practice," clauses of the Federal Trade Commission Act. While prepaid calling cards generally offer savings on international long distance calling versus traditional "Dial 1," 10-10 dial-around and wireless long distance calling,¹³ these savings are no excuse for fraud or deception. We also support H.R. 3993's requirement that a Government Accountability Office study of the effectiveness of the Act be conducted.

As a general proposition, we applaud the requirements included in the Florida Attorney General's June 2008 settlement with prepaid card companies, such as:

- Ceasing all deceptive advertising
- Providing 100% of the minutes advertised
- Not using hidden fees or misleading minute calculations to increase their profits at consumers' expense
- Printing disclosures for a given card in any language used to advertise that card
- Printing the exact number of minutes available and the card's expiration date (if applicable) on the card
- Prohibiting naming of card surcharges to resemble taxes
- Requiring one-minute increment billing

While H.R. 3993 requires disclosure of the name of the prepaid calling card service provider, we recommend that this section of the bill be expanded to include requiring the mailing address of the card originator. In addition, we would like every calling card provider to be required to publish a website (whose address is printed on the card) listing all rates, taxes, fees, and surcharges associated with the card. Currently, Section 3(a) of H.R. 3993 only requires that the provider list rates *if* they maintain a website. With more consumers turning to the Internet every day, we believe it to be imperative that card providers maintain a website with relevant

¹³ "Facts and Figures," The Hispanic Institute. Retrieved on July 24, 2008.

information about the card, especially if they currently do not do so.

Further Recommended Action If Disclosure Requirements Are Not Sufficient

If the GAO study mandated in Section 8 of the bill presents evidence indicating that greater disclosure is not reducing the consumer abuses in the industry, we recommend that further action be considered by this Committee, with the Federal Trade Commission given the authority to enforce these provisions:

- Require all market entrants to be licensed and post a bond before marketing cards to consumers. That bond would go into a fund to compensate consumers who are victims of fraud. Those companies that market prepaid calling cards should also be required to provide a name, address and place of incorporation. Right now, the barriers to entry are so low and the penalties for not making good on the value of the cards are so minimal that it's simply open season on consumers. We believe requiring a bond will act to keep many bad actors out of the industry.
- Require all market entrants to have a 24 hour, 7 days a week toll free number that has a live person on the other end who must be knowledgeable about the use of the card.
- Require that fees and surcharges imposed be related to actual costs. Congress has imposed rules on other industries that were charging consumers outrageous fees – the moving van industry, payday lenders, and funeral homes, to name a few. If this Committee finds that disclosure is not easing the deception and rip-offs that plague this industry, the Committee should consider imposing stronger regulations on prepaid calling card companies to curb the many fees and surcharges they impose on consumers.
- Require that all cards have an expiration date and that this date be no shorter than one year after activation. If a seller fails to make a disclosure on expiration, the card should be valid indefinitely.
- Require sellers to list the minimum charge per call and the balance in minutes and dollars remaining on the card.
- Require sellers to inform consumers, via a website or toll-free phone number, of any proposed changes in terms and conditions, with consumers given the chance to reject these changes and receive a refund on the card with no fee imposed for requesting such a refund within an appropriate grace period of no less than 30 days after posting of the proposed

change. Prepaid calling card providers should also be required to prominently list a mailing address to which customers can direct refund requests and a website with a refund form that the consumer can access easily.

- Require uniform terms in all prepaid calling card contracts so that consumers can comparison shop. Companies should not be allowed to confuse consumers by using a variety of terms for charges such as “administrative fee” or “service fee.”
- The amounts involved in prepaid phone card transactions are too small for any one individual to bring a case to court. The only meaningful way to allow consumers to hold prepaid card sellers accountable is through use of the class action process. Consumers need to be guaranteed a private right of action and the ability to band together as a class to bring cases against dishonest prepaid phone card providers.

Conclusion

We strongly support H.R. 3993 and commend this Committee for holding the hearing today. By requiring much better disclosure on prepaid calling cards, this bill will help to mitigate the deception and fraud associated with these cards. We also support further monitoring of the industry by the GAO, which will in turn report to the members of this Committee.

NCL also urges Congress to investigate ways that consumers can be protected from prepaid calling card industry abuses beyond disclosure requirements. The most vulnerable consumers—military families, immigrants, low income families—rely on these cards and spend their hard-earned money, often only to see the value of the cards disappear quickly after first use. NCL believes we can do better by consumers. We support the disclosure required under this bill and hope that it works. We urge the members of this committee to remain vigilant and ready to act should enhanced disclosure not be sufficient to reign in industry abuses.

Thank you, Mr. Chairman, for giving the National Consumers League this opportunity to comment on your bill. We commend you for your pro-consumer record and look forward to working with you and your staff to see this bill enacted into law.

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