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Consumer News

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CONSUMER NEWS

by Charles R. Whitt
& Phillip Tortorich

Federal Trade Commission and Securities Regulators target business opportunity fraud on the Internet

The Federal Trade Commission ("FTC") and the North American Securities Administrators Association ("NASAA") recently announced that two hundred and fifteen Internet advertisers promoting business opportunities (i.e., fronting capital to start new business ventures) were sent notices of warning that state and federal

laws require more evidence supporting claims regarding their earnings. The Internet ads were identified by FTC officials, securities regulators, attorneys general offices from 24 states, the U.S. Postal Inspection Service, Canada, and Norway. In what officials dubbed "Business Opportunity Surf Day," the agencies spent a day

in March 1997 surfing the Internet for marketers extolling the potentially high earnings to be made by consumers who buy into business opportunity schemes. False or unsubstantiated earnings claims are violations of FTC regulations as well as state statutes prohibiting deceptive business practices.

Officials saved a copy of

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America Online wins court battle over E-mail blocking

America Online Inc. ("AOL") prevailed in a legal battle over electronic junk mail and ensured that its subscribers can block unsolicited messages. A federal court judge in the U.S. District Court for the Eastern District of Pennsylvania directed Cyber Promotions Inc. of Philadelphia to stop shifting its on-line identity in an attempt to circumvent AOL's junk E-mail filter. AOL offers members an option to block or receive unsolicited messages, also known as "spam," using a system that

filters out all E-mail from certain Internet addresses.

Cyber Promotions has been fighting for months with AOL over junk E-mail and originally challenged the move to block its E-mail on First Amendment grounds, however that argument was struck down last November in federal court. Sanford Wallace, Cyber Promotions president, sought to portray the latest order as a victory, saying that the agreement still does allow the company to send E-mail to AOL members.

AOL stated that it only wanted to offer its subscribers an effective blocking option and did not want to stop all Cyber Promotions E-mail. In addition to the Pennsylvania court ruling, a U.S. District Court Judge for the Southern District of Ohio granted CompuServe Corp. a preliminary injunction against Cyber Promotions, barring Cyber Promotions from flooding CompuServe members with unsolicited e-mails. •

each of the two hundred and fifteen sites that appeared problematic and made follow-up visits on April 21, 1997. Agents found that seven of the sites were changed to remove the earnings claims and another 37 sites had been dismantled completely. According to the FTC, 24 of the ads turned out to be messages that had been posted on forums and will disappear automatically. Of the 191 actual websites, 23 percent were changed or removed completely. The FTC would not confirm or deny whether it or other law enforcement authorities would investigate the remaining sites.

“The Surf Day approach to policing fraud on the Internet takes advantage of a vast new medium that, on the one hand, could make it easier to perpetuate a deceptive scheme and get away with it, and turns that medium into a tool for warning potential scammers that they can’t count on going undetected,” said Jodie Bernstein, Director of the FTC’s Bureau of Consumer Protection. “Part of our goal is to inform marketers about the law, which says that a company making earnings claims must have hard evidence to back them up. We encourage consumers surfing the web for a new business opportunity to insist on seeing substantiation for every objective claim a company makes, as well as a list of *every* person who has signed up for the business. While the Internet offers innovation, cutting-edge opportunities, it is still old-fashioned legwork—pouring over the numbers, and telephoning and visiting in-person sites of other participants—that will best protect consumers from becoming the victims of fraud,” Bernstein said.

Dan Cantone, chair of the NASAA Franchise and Business Opportunity committee and Assis-

tant Attorney General for the state of Maryland advises consumers to contact their state securities agency to find out which laws protect them before investing money with a company that promises to help set them up in a business. The NASAA also posts investor education information materials such as “Cyberspace Fraud and Abuse” on its website at www.nasaa.org. In addition, the FTC’s website at www.ftc.gov/opa/busops contains additional information to assist consumers checking into various business opportunities.

Among the tips that the NASAA and the FTC offer consumers investigating business opportunities advertised on the Internet:

(1) Do not accept a list of references selected by the company offering the business opportunity as a substitute for a complete list of franchise or business owners.

(2) Avoid any plan which includes commissions for recruiting additional distributors because it may be an illegal pyramid scheme that ultimately will collapse for lack of new recruits. Many state laws prohibit pyramiding by allowing commissions to be paid only for retail sales of goods or services, not for recruiting new distributors.

(3) Ask for disclosure documents if you are investing in a franchise; it is required by law and should provide detailed information to help investors compare one business to another.

(4) Check out the company with the state securities agency, attorney general’s office or other consumer protection agency in the state where the advertisement is posted and the state where the company is headquartered. •

Media groups bring action against TotalNews alleging web page republishing

A group of the nation's largest media companies sued the host of a new World Wide Web site called TotalNews Inc., accusing the company of illegally republishing and repackaging on-line Web pages for a profit. The suit addresses the extent to which certain companies can control who profits from their Web sites. The plaintiffs include the Washington Post Co., Time Warner Inc.'s Cable News Network, and Dow Jones & Co., publisher of the Wall Street Journal.

The suit alleges trademark and copyright infringement. The plaintiff's asked a federal court judge in Manhattan to order Phoenix-based TotalNews to stop misappropriating the respective media groups' material.

A core issue in the lawsuit is whether it is legal for a Web directory to take a finder's fee, in this case ad revenue, when it links a computer user to another company's home page. TotalNews president Roman Godzich said his company has

done nothing wrong and says his site posts a disclaimer stating that TotalNews is not affiliated with the sites in its directory. According to one of the plaintiffs in the suit, TotalNews helps consumers access over 1,000 sites operated by other media companies and TotalNews covers up as much as a third of the space by "framing the located site with its own paid advertisements and logo."

Pornographic web site secretly rerouted users to Eastern Europe

Federal regulators shut down three pornographic Internet sites after thousands of subscribers complained that all they received were phone bills for calls to Moldova, a former Soviet republic. A federal court in New York granted the Federal Trade Commission's request for a temporary restraining order against two Long Island companies, Audiotex Connection Inc. and Promo Line Inc., and three individuals. A lawyer representing the companies and the individuals denied the allegations.

According to investigators, the alleged scam was both high-tech and international. The three sites—*www.beavisbutthead.com*, *www.sexygirls.com*, and *www.ladult.com*—required Internet visitors to download a special computer program onto their personal computer before letting them see the adult material. The program lowered the volume on the computer modem and then silently hung up on the visitor's own local Internet service provider before redialing a phone number in Moldova.

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Visitors to the Web sites remained connected to the Moldova number until they turned off their computers, FTC officials said. The charge on the international phone call kept increasing—at more than \$2 a minute—while the computer users accessed other sites or merely used their own programs. According to the agency, some bills ran as high as \$3,000. Overall, more than 800,000 minutes of calling time were billed to U.S. consumers, according to Eileen Harrington, the FTC's associate director of its marketing practices division. More minutes were billed to customers from Canada, New Zealand and other nations.

AT&T Corp. said it will make some special arrangements but has not promised to pay all of the charges. "Ultimately we expect all consumers to pay their bills," said Richard Petillo, AT&T corporate security manager. AT&T may be re-

quired under international agreements to pay some of the foreign charges. Sprint Corp. and MCI Communications Corp. said complaints would be handled case by case.

Joel Dichter, a New York lawyer representing the companies and the three individuals—owners Anna Grella, Bill Gannon and David Zeng, who wrote the suspect program—said in a statement that the FTC "has sued the wrong individuals and entities." "The web sites," he said, "gave consumers a clear warning that international phone charges would apply." According to FTC officials, phone scams involving developing nations are on the rise. Some state-owned phone companies that have installed high-tech telephone systems charge exorbitant rates to international callers and reward companies with a share of the profits if they can generate calls. •

Supreme Court hears arguments on the Communications Decency Act

On March 19, 1997, the Supreme Court heard arguments on a case of first impression regarding the Internet and free speech. The argument centered on the constitutionality of the Communications Decency Act ("CDA"). The case before the Court is a combination of two cases from the reviewing courts which barred enforcement of the CDA due to its unconstitutional vagueness.

Government Contends CDA Provisions Not Vague

The CDA was enacted in order to protect minors from viewing indecent material on the Internet. The challenged provisions relate to two areas of the CDA. One of the provisions related to the specific child and transmissions provisions. Under these provisions a person is in violation of the CDA when

they knowingly transmit indecent material to a minor. According to the Government, if you do not know that you are transmitting to a minor, then these provisions do not apply. However, the second area of provisions concern the display of patently offensive material through the Internet. This provision of the CDA is much broader and consequently more difficult to enforce. Under the

latter provision, minors should not be able to access a web site containing patently offensive material. The burden is on the supplier of the information (the creator of the site) to ensure that children cannot obtain access to the site. According to the Government, blocking technology is available and, therefore, feasible to require site owners to screen for age.

There was a concern among the justices about whether non-commercial sites would be unduly burdened by the regulations. The concern is that if the cost is too excessive, then these provisions would in effect be limiting the free speech of others. However, the Government argued that the technology exists for noncommercial sites to provide adults with a verification code that allows them to access adult-only sites at no cost to those who post information on those sites. It was accepted by the justices and the parties whose commercial sites have been using age verification and adult access codes for some time.

According to the Government, the question should not center on the meaning of patently offensive. This term has been held by the Federal Communications Commission

(“FCC”) and the other courts not to be constitutionally vague. Presently, a jury instruction exists to determine what constitutes whether something was patently offensive under a jurisdiction’s prevailing community standards. Finally, the Government argued that if the CDA is vague in areas, the Supreme Court maintains the authority and can limit those areas found to be unconstitutional. Further, if sections are declared unconstitutional, then those sections should be severed from the law, while keeping the remaining law intact.

ACLU Contends CDA Bans Speech

The American Civil Liberties Union (“ACLU”) and some 50 other companies and groups have challenged the CDA. They claim that (1) the CDA bans free speech; (2) it will not be effective; there are less-restrictive alternatives; (3) and it will chill much speech that is not indecent because of the threat of criminal sanctions. The ACLU argued that the Government’s methods of handling the situation are not feasible. While a minuscule portion of the World Wide Web may be able to use the methods proposed by the

Government (i.e., the use of CGI script to verify age), the majority of the Internet is not capable of using the program. Further, it was argued, that the 40 million people who use the news groups to engage in interactive discussions would be prevented from such discussions if required to post messages in a static web site. The ACLU said that free discussion would consequently be adversely affected. Moreover, they argued that it is impossible to screen for age concerning the news groups because they exist in cyberspace on over 200,000 different news group servers. It would be necessary for each of the separate owners of the news groups to screen for age.

The justices inquired as to why the Internet should not be viewed as similar to radio and television, where there are numerous enforcement standards which must be complied with. In addition, since only a limited number of corporations can use broadcast radio and television because of the inordinate cost, the justices questioned why the Internet should not be similarly constricted. The ACLU argued that the speech they were challenging was not that of obscenity or child pornography, but rather, a much different subset

of speech that is called patently offensive or indecent speech.

The ACLU stated that the CDA would be ineffective because approximately 50 percent of the communications targeted come from foreign sources not subject to the provisions of the CDA. Because of these problems, the ACLU believes that the Court should not consider

the severance argument as severance would not solve the problems with the language of the CDA.

Lastly, the ACLU argued that Congress could have (1) drafted a statute that did not apply at all to noncommercial speakers; (2) drafted a statute which only applied to visual material; and (3) limited the speech targeted to

prurient speech which lacked serious value. In closing, the ACLU stated that since Congress chose not to take any of these actions, the CDA cannot be severed but should be held unconstitutional in its entirety. The Supreme Court is expected to decide the issue in late June. •