

**Testimony of
Sally Greenberg, Executive Director, National Consumers League on**

S. 2998, the “Prepaid Calling Card Consumer Protection Act of 2008”

Before the U.S. Senate Commerce, Science and Transportation Committee

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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 Senate Committee on Commerce, Science, and Transportation to discuss the need for greater consumer protections in the purchase and use of prepaid calling cards. This largely unregulated consumer product is a “Wild West” of sellers and merchants who too often prey upon the most vulnerable consumers by promising minutes they don’t deliver and loading up on hidden or undisclosed charges and fees. In an industry like this, with low barriers to entry and a totally unregulated market, you can be sure there will be unscrupulous operators who will take the money and run.

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. (The NCL’s Fraud Center is described at www.fraud.org).

I want to commend you, Senator Nelson, for your leadership in offering S. 2998, the Prepaid Calling Card Consumer Protection Act of 2008. Consumers rely on you, an outspoken defender of consumer rights and protections, to look out for their 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’ll 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 your bill, S. 2998, and I’ll make some policy recommendations. Our written testimony also includes a timeline detailing the growth of the industry and the rise in fraud associated with that growth.

Let's start with the industry. It is illustrative that the shady practices of the prepaid calling industry were featured prominently on the HBO series, *The Sopranos*. In Episode 26, Tony is discussing the mob's work with prepaid cards. I've deleted the obscenities:

Tony Soprano: "So, telecommunications once again fails to disappoint. What's this thing? Telephone calling cards. You find a front man who can get a line of credit, you buy a couple of million units of calling time from a carrier. You become "acme telephone card company". "Acme". You're now in the business of selling prepaid calling cards. Immigrants especially, no offense. They're always calling back home to whoever (deleted) And it's expensive, right? You sell thousands of these cards to the (deleted), cards at a cut rate. But you bought the bulk time on credit, remember? The carrier gets stiffed. He cuts off the service to the card holders, but you already sold all your cards. That's (deleted) beautiful! (Laughing) it's a good one."

Of course, no one should conclude that the whole prepaid calling card industry is controlled by organized crime: we have no such evidence, but this vignette from *The Sopranos* demonstrates how easy it is to get into the industry, rip off consumers, and disappear with no accountability whatsoever. That must change.

Prepaid Calling Card Facts

- Prepaid cards are a \$4 billion a year industry, responsible for 11 billion calls in 2004^[1]
- The industry is estimated to reach \$6.4 billion in revenue in 2008.^[2]
- Examples of fraudulent practices used by the prepaid companies include "hang-up fees," periodic maintenance fees, destination surcharges, and high billing increments.^[5]
- Companies that try to "play by the rules" are often punished by a loss of market share due to fraudulent carriers.^[6]
- Only 11 states, including California, Connecticut, Florida, and Illinois, currently have laws pertaining to calling card fraud, specifically. Most turn to generic consumer protection statutes, but enforcement has been extremely light.^[7]
- Hispanic consumers may be losing up to \$1 million per day because of fraudulent phone cards.^[4]
- The average calling card delivers only 60% of the minutes promised, according to the Hispanic Institute, a non-profit research group.^[3]

- The FTC's 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 the prepaid cards, the cards delivered an average of only 50 percent of the advertised minutes.^[8]
- 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.^[9]

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.^[10]

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 scams, the most frequent victims of the fraud and deception are the most vulnerable consumers: immigrants and the working poor; and those lower income Americans who often cannot afford or obtain regular phone service. These consumers rely on calling cards to stay in touch with friends and loved ones in the US and abroad. Sadly, we believe that military families are also likely victims of be the prepaid card scams and rip-offs.

Yes, the cards provide these users with an alternative means of calling home, but many use false and deceptive practices in the process, and impose 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 –notably in your state of Florida, Senator Nelson - have done a commendable job in prosecuting fraudulent prepaid card companies. The Federal Trade Commission has also conducted investigations and brought important cases against individual

prepaid phone card providers. Unfortunately, these scattered efforts are insufficient. We need basic federal protections to stem the tide of the many deceptive practices in this industry.

NCL believes that FTC regulations, as called for S. 2998, would help to level the playing field for all phone card providers. Such regulations 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 need a national floor of minimum requirements stating what industry practices won't be permitted. We applaud S. 2998'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 go forward with provisions that don't conflict with the federal law. That's a pro-consumer position and acknowledges the important role states have played in enacting and enforcing consumer protections.

NCL believes that both your bill Senator Nelson, S. 2998, and Congressman Elliot Engel's bill, H.R. 3402, would go far in addressing the false promises and deception associated with these cards. 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 your efforts, Senator Nelson, to require full disclosure of terms and conditions on these prepaid calling cards, we find that the terms themselves, when they are disclosed, are too often unconscionable.

For example, the text in fine print on the back of my \$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 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 “Majestic DMV” Card I purchased for \$2.00:

1) A .99 fee applies on the 1st day of use and every 5 days thereafter; 2) Calls made through tollfree 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 S. 2998'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. An open marketplace where all prepaid calling card companies are providing accurate information may do the trick; the market has a way of working very effectively consumers have accurate information upon which to compare rates.

NCL would like to suggest, however, that after passage of your bill, the FTC closely monitor the industry and in a year's time, report on whether disclosure is addressing the problem adequately.

Diogenes called the market "a place set apart where men can deceive each other." We must impose some limits on that paradigm. If after a year we still see failure to accurately disclose rates and unconscionable terms when the rates are disclosed, we would urge this Committee to consider stronger regulation of this industry.

NCL Policy Recommendations Related to Disclosure and S. 2998

The National Consumers League strongly supports S. 2998 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 FTC’s call to appoint a monitor to oversee the prepaid calling card business,^[14] and a requirement that the FTC report back to Congress on a periodic basis regarding the status of its efforts to enforce the terms of the proposed legislation.

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 S. 2998 requires that the disclosure text on the calling card itself, packaging, or other promotional material (including online) be in same language used to advertise the card, we would recommend expanding Sec 3.(b)(4) of the bill to require that prepaid phone card providers provide toll-free customer service lines staffed by customer service representatives able to converse in the languages that the cards are advertised in.

Further Recommended Action If Disclosure Requirements Are Not Sufficient

If after one year, the FTC reports back to Congress with 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, in a year's time, 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 and 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/or 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.”

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- 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 S. 2998 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 FTC, which will in turn report to the members of this Committee.

NCL also urges Congress to find a way to require that prepaid calling card companies go beyond simple disclosure of their onerous rates. The most vulnerable consumers—military families, immigrants, low income families—rely on these cards and spend their hard-earned money 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. If we need to take stronger action, this bill's requirements will represent an excellent first step.

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.

Issue Timeline

We have provided a timeline of enforcement actions and legal settlements pertaining to prepaid calling cards below.

- 1986** Prepaid calling cards introduced to the North American market.^[15]
- 1996** U.S. prepaid card sales reach \$1.1 billion^[16]
- April 2001** New York Attorney General Eliot Spitzer announces settlement with five companies accused of deceptively marketing prepaid telephone cards throughout upstate New York. This settlement was part of Spitzer’s ongoing efforts to combat illegal marketing practices of prepaid phone card companies dating back to 1999.^[17]
- 2006** Newark, NJ-based IDT Corp., the largest prepaid calling card company in the U.S. reports \$2.2 billion in total sales.^[18]
- 2007** U.S. prepaid market reaches \$4 billion in revenue
- January 2007** IDT Corp. settles federal class action suit brought on behalf of hundreds of phone card customers alleging fraudulent and deceptive advertising practices.^[19]
- March 2007** IDT files lawsuit against 9 competitors, alleging that they provide 40% less time than advertised. Epana Networks, Dollar Phone, and Locus Telecommunications quickly reach settlement with IDT, agreeing to cease any misleading marketing practices. Six other companies named in the suit, including CVT Prepaid Solutions Inc. issue an open letter to the industry, claiming that IDT’s suit is “nothing but an underhanded ploy to regain lost market share by intimidation.”^[20]

- July 2007** Florida Attorney General Bill McCollum announces investigation of 10 prepaid calling card companies for fraudulent or deceptive advertising.^[21]
- August 2007** Representative Eliot Engel (D-NY) introduces H.R. 3402 “Calling Card Consumer Protection Act.”^[22]
- March 2008** FTC asks U.S. District Court for the District of New Jersey to halt allegedly illegal marketing practices of prepaid card companies CTA Inc., Clifton Telecard Alliance One LLC, and Mustafa Qattous.^[23]
- May 8, 2008** Senator Bill Nelson (D-FL) introduces S. 2998 “Prepaid Calling Card Consumer Protection Act of 2008.”^[24]
- May 23, 2008** Texas Attorney General Greg Abbott announces filing of legal enforcement action against prepaid calling card company Next-G Communications, Inc. over allegedly deceptive marketing practices employed by the company.^[25]

Footnotes

[1] “THI Praises FTC for Standing Against Calling Card Fraud,” The Hispanic Institute. 2007. Retrieved on July 24, 2008.

[2] “Prepaid Calling Cards: Market Dynamics and Forecast 2003-2008,” ATLANTIC-ACM. February 2003. Retrieved on July 25, 2008.

[3] *Ibid.*

[4] “Facts and Figures,” *The Hispanic Institute*. Retrieved on July 24, 2008.

[5] *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.

[6] Holden, Diana. “Calling Out Prepaid Phone Cards,” *BusinessWeek*. July 9, 2008. Retrieved July 24, 2008.

[7] “Facts and Figures,” *The Hispanic Institute*. Retrieved on July 24, 2008.

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[10] *Ibid.*

[11] "Calling Card Questions & Answers," The Hispanic Institute. Retrieved on July 25, 2008.

[12] Marshalian, Jonathan. "You've Come a Long Way, Baby," *The Prepaid Press*. September 17, 2007. Retrieved July 25, 2008.

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

[14] Federal Trade Commission (March 26, 2008). "FTC Asks Court to Halt Prepaid Calling Card Scam; Alleges Consumers Receive Fewer Calling Minutes Than Advertised and Pay Hidden Fees". Press release. Retrieved on July 24, 2008.

[15] Frost and Sullivan. "North American Prepaid Calling Cards Market," August 10, 2006. Retrieved on July 25, 2008.

[16] "Prepaid Phone Cards: The Facts," State of New York Attorney General. Retrieved on July 25, 2008.

[17] Office of the New York State Attorney General (April 11, 2001). "Prepaid Phone Card Sweep Cleans Up Deceptive Posters". Press release. Retrieved on July 25, 2008.

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[19] IDT Corporation (January 25, 2007). "IDT Reaches a Settlement in Calling Card Class Action Lawsuit". Press release. Retrieved on July 25, 2008.

[20] Hatcher, Monica. "McCollum probes calling card deceptions," *The Miami Herald*. July 24, 2007.

[21] Hatcher, Monica. "McCollum probes calling card deceptions," *The Miami Herald*. July 24, 2007.

[22] U.S. House. 110th Congress, 1st session. *H.R. 3402, Calling Card Consumer Protection Act*. ONLINE. Thomas.gov. Available at <http://www.thomas.gov/cgi-bin/bdquery/z?d110:HR03402:@@L&summ2=m&> [Retrieved on July 25, 2008].

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[24] U.S. Senate. 110th Congress, 2nd session. *S. 2998, Prepaid Calling Card Consumer Protection Act of 2008*. ONLINE. Thomas.gov. Available at <http://www.thomas.gov/cgi-bin/query/F?c110:1:/temp/~c110YZkszS:e930>: [Retrieved on July 25, 2008].

[25] Attorney General of Texas (May 23, 2008). "Attorney General Abbott Takes Legal Action Against Prepaid Calling Card Company". Press Release. Retrieved on July 25, 2008.