Cano is under an order issued in *FTC v. Credit Development Int'l*[16] which prohibits her from offering for sale the right to participate in a Ponzi scheme, or a pyramid scheme in which participants purchase the opportunity to derive income primarily from recruitment or payments by recruits, and prohibits her from misrepresenting material facts in connection with the sale of business opportunities. Her criminal case is ongoing, and her prior conduct likely will play some role in the trial and/or at sentencing.

Calculating Criminal Contemnors' Sentences and Other Recent Decisions

The teeth of Project Scofflaw, of course, are the likelihood of significant prison time. In the past, there has been disparity in the sentences handed down. A number of changes in the last 20 months, however, brought first clarity then disarray to the issue. The FTC staff is now in a "wait and see" mode.

In December 2002, as discussed in greater detail in the Staff's Second Annual Report to the Commission on Project Scofflaw,[17] the staff submitted a comment to the U.S. Sentencing Commission identifying, under the existing federal sentencing guidelines, a potential for disparate sentences for similar conduct by defendants convicted of criminal contempt. The comment noted that the sentencing guidelines direct courts to apply the guideline for the offense most analogous to the conduct that gave rise to the contempt. Courts, however, differed on what constituted the most analogous guideline for violations of an order involving fraudulent behavior; some used the fraud guideline, while others used the obstruction of justice guideline. Thus, the comment recommended implementing changes to lessen the disparity.

In July 2003, the Eighth Circuit addressed head-on which guideline to apply for contemptuous fraud. In *United States v. Robert Ferrara*,[18] the appellate panel reviewed and upheld defendant Ferrara's 125 month sentence for six counts of criminal contempt. Ferrara was subject to a 1983 federal court order prohibiting him from making false representations in connection with offering business opportunities and requiring him to comply with the FTC's Franchise Rule. On appeal, Ferrara contended that the district court erred by sentencing him pursuant to the fraud guideline rather than the guideline applicable to obstruction of justice, which would have resulted in a six to eight month sentence. The Eighth Circuit noted that Ferrara admitted he had made and caused others to make false representations to encourage the sale of the franchises involved in the six counts of the indictment and that the disclosure statements given to the six individuals had been inaccurate and contained material omissions. It then concluded "this is the type of conduct commonly sentenced under [the fraud guideline],"[19] and affirmed the district court's choice of that guideline.

Subsequently, in November 2003, the Sentencing Commission added to the contempt guideline an application note clarifying that the fraud guideline is the most analogous one in a case involving a violation of an order enjoining fraudulent behavior.[20] The application note further clarifies that using the fraud guideline for contemptuous fraud and including the fraud guideline's two-level upward adjustment for violating an order is not double counting. In addition, the Sentencing Commission amended the obstruction of justice guideline itself to ensure that defendants serve prison time, not just probation or home detention.

All of this is now in limbo. In its recent *Blakely v. Washington*[21] opinion, the Supreme Court declared unconstitutional state sentencing laws that allow an increase or enhancement in the sentence based on findings of fact made by a judge by a preponderance of the evidence rather than by a jury beyond a reasonable doubt. Although the Court expressly stated that "the Federal Guidelines are not before us, and we express no opinion on them,"[22] several appellate courts have applied the *Blakely* analysis to the federal guidelines and declared them unconstitutional either in whole or in part.[23] Others have ruled that *Blakely* does not render the federal guidelines unconstitutional,[24] and one decided to certify the question to the Supreme Court.[25] In light of this upheaval, the Supreme Court heard oral argument on the constitutionality of the federal sentencing framework in the first week in October, and likely will render its opinion shortly. Even if the Court were to overturn the sentencing guidelines, however, the last 20 months has done much to educate courts about the seriousness of contemptuous fraud.

On another note, the Seventh Circuit has issued a decision that makes it more difficult for a successful fraud perpetrator to use fraud proceeds to mount an expensive legal defense on the shoulders of the defrauded victims. In a decision penned by Judge Posner, the Seventh Circuit held that a defendant has no Sixth Amendment right to spend another person's money for a legal defense, even if those funds are the only way to retain the attorney of the defendant's choice.[26] The district court judge had granted summary judgment and ruled that all of the proceeds of the fraud were held by the defendant in constructive trust on behalf of the victims. Nonetheless, the court released from the constructive trust $25,000 for attorneys fees in a parallel criminal action. The appellate panel wrote that once the court found that all of the defendant's assets were proceeds of the fraud, the defendant had no right to use those assets, even to mount a defense to a criminal prosecution.

Lessons for Practitioners

The FTC's message is clear: Just like the Monopoly® player drawing the "Go to Jail" card, the consequences for a scofflaw are serious. Practitioners should advise their clients who are under a federal court order in an FTC action that the FTC will use its compliance monitoring techniques to identify scofflaws, and when a scofflaw has been identified, prosecute the scofflaw through civil contempt and, where appropriate, criminal contempt actions. Practitioners further should advise their clients about the risks of violating an order, including significant time in prison and the forfeiture of the proceeds of the contemptuous conduct. In other words, non-compliance will cost more than a lost turn and $200 for not passing "Go."

The Voluntary Payment Doctrine: A Potential Bar to Restitution Claims

by Steven B. Malech*

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It is common practice for businesses, ranging from credit card issuers to cable television providers, to impose late fees on consumers who fail to pay for goods and services in a timely fashion. Over the past several years, however, consumers have attacked such fees under various consumer protection laws, particularly those imposed on cable television subscribers,

claiming that the fees are illegal because they are not reasonably related to the actual costs incurred as a result of the late payment.[1] In response to purported class action lawsuits initiated by consumers seeking the return of a portion of such fees, cable television operators and other businesses have successfully invoked a decades, if not centuries, old defense called the Voluntary Payment Doctrine ("VPD"),[2] which provides that "money paid with knowledge of all the facts, and without fraud or duress, cannot be recovered merely on account of ignorance or mistake of the law."[3] By contrast, however, a small minority of courts has held that the VPD does not bar claims for monetary relief brought by consumers challenging allegedly illegal late fees or other alleged violations of public policy.[4]

This article considers justifications for applying the VPD to bar claims for restitution in consumer litigation, reasons for rejecting the use of the VPD in consumer litigation and the potential impact that the successful invocation of the VPD may have on the resolution of actions brought by the FTC and state enforcement agencies seeking restitution remedies, actions that conceptually (if not intuitively) may be affected by the VPD.

Applying the VPD: Putnam v. Time Warner

In *Putnam*, the plaintiffs alleged that a $5.00 late payment fee assessed by Time Warner to customers who failed to pay their monthly cable bill by the time specified in their contract constituted an unlawful liquidated damages provision because the amount of the fee was not reasonably related to the actual costs incurred by the company as a result of the late payments. The plaintiffs alleged that they paid the late fee without knowing that Time Warner's actual costs from a late payment were less than 50 cents and that the company concealed material information regarding those costs. The plaintiffs sought restitution with respect to fees that had already been paid, and declaratory and injunctive relief to prevent the assessment of such fees in the future. Time Warner moved to dismiss the claims on the basis of the VPD, among other grounds. The trial court granted the motion and the plaintiff's appealed.

The Wisconsin Supreme Court affirmed the dismissal of the claims for monetary relief.[5] The Court noted that the "voluntariness in the doctrine goes to the willingness of a person to pay a bill without protest as to its correctness or legality."[6] The Court also explained that "[t]here are two primary reasons why courts have adopted the voluntary payment doctrine. First, the doctrine allows entities that receive payment for services to rely upon these funds and to use them unfettered in future activities . . . . Second, the doctrine operates as a means to settle disputes without litigation by requiring the party contesting the payment to notify the payee of its concerns. After such notification, a payee who has acted wrongfully can react to rectify the situation."[7] Based on these principles, the Court held that the VPD barred a claim for monetary relief on behalf of a person who paid a late-payment fee without protest and who thereafter alleged that the fee was based on unlawful liquidated damages.[8]

Importantly, the Court also held that its decision was supported by "the principles of public policy and equity that gave birth to the doctrine."[9] In particular, the Court explained that "[p]rivate businesses such as Time Warner should be able to incorporate into their revenue stream payments made by their customers without dispute."[10] The Court further explained that the doctrine "provided stability and certainty once funds have been transferred without notice of dispute, thereby decreasing the transaction costs that would accrue if payments received long ago could be demanded back."[11] Noting that a customer could avoid the application of the VPD by making some form of protest prior to or contemporaneous with the payment, the Court held that "[a]bandoning the voluntary payment doctrine here would open the door for a wide array of challenges to past payments in the name of protecting persons who were tardy in inquiring into and contesting demands for payment. The equities of cable customers who fail to make timely protests against allegedly unlawful late-payment fees must be weighed against the fiscal interests of cable providers in the certainty of payments received without dispute. We find this balancing favors the latter interest and the preservation of the voluntary payment doctrine in this context."[12]

Rejecting the VPD: Time Warner Entertainment v. Whiteman

In a case with strikingly similar facts but an opposite result, the plaintiffs in Whiteman alleged that the late fees (either $4.40 or $4.60) assessed by the company on their monthly cable television bills were unlawful because they exceeded the cost of collection. The plaintiffs sought to recover the fees paid in excess of Time Warner's actual damages and sought declaratory and injunctive relief preventing further assessment of the allegedly inflated fee. Time Warner moved to dismiss the claims for monetary relief on the grounds that they were barred by the VPD. The trial court ultimately rejected Time Warner's argument and allowed the case to proceed on the merits. The Indiana Court of Appeals affirmed the trial court's ruling with respect to the claims for declaratory and injunctive relief, but reversed with respect to the claims for monetary relief.

The Indiana Supreme Court, however, held that the VPD did not bar the plaintiffs' claims for monetary relief. The Court based its decision on several factors. First, the Court determined that the payment of the late fees was not "voluntary" under Indiana law because the plaintiffs were "put in the position by Time Warner of having to pay in order to receive cable service" and that "[t]he plaintiffs against whom the voluntary payment doctrine was enforced faced no immediate deprivation of good or services if they did not pay."[13]

Second, the Court interpreted "the current tentative draft of a new Restatement of Restitution & Unjust Enrichment" as limiting the application of the VPD "to situations where a party has voluntarily paid a disputed amount . . . in the face of a recognized uncertainty as to the existence or extent of an obligation" to do so.[14] The Court found that there was a genuine issue of material fact in that regard that precluded the dismissal of the action.

Third, while acknowledging that the majority of cases from other jurisdictions favored Time Warner's position, the Court noted that the authority was not unanimous. Rather, it cited the dissent in Putnam for the proposition that a customer had no reason to protest the payment of a fee if he or she had no reason at the time of payment to believe that the fee was unreasonable or unconscionable.[15]

Fourth, the Court expressly rejected the public policy arguments that the Wisconsin Supreme Court found persuasive in Putnam. The Whiteman Court noted that it did not "believe that it is appropriate to favor a private enterprise over private individuals."[16] Rather, the Court concluded that, if the fee is unlawful, Time Warner should not be able to benefit from its own wrongdoing.[17]

Pratt v. Smart Corporation

In a decision similar in effect to Whiteman, plaintiff Pratt alleged that Smart Corporation charged her attorneys $28.50 to provide a copy of a four-page medical record pertaining to treatment that she received in a hospital for injuries resulting from a car accident. Pratt claimed that the charge was excessive and, therefore, violated a statute requiring hospitals to furnish such records without unreasonable delay and the requesting parties to pay reasonable costs of copying.[18] The trial court granted Smart's motion for summary judgment on the grounds that there was no "factual dispute about anything happening in this case" and "that the statute in question . . . does not allow for recovery."[19]

On appeal to the Tennessee Court of Appeals, Smart Corporation's primary argument was that Pratt's claim was barred by the VPD. The Court, however, held that "the State has an interest in transactions that involve violations of statutorily-defined public policy, and, generally speaking, in such situations, the voluntary payment rule will not be applicable."[20] Accordingly, the Court held that "the voluntary payment rule presents no impediment to Pratt's cause of action, and thus does not provide an adequate basis for sustaining the trial court's grant of summary judgment in favor of Smart."[21]

The Implications of the VPD to Government Enforcement

The FTC and state enforcement agencies often investigate the circumstances under which consumers were charged certain fees, including late fees and early termination fees. Where the agencies believe that a business or individual has illegally, deceptively or unfairly imposed and obtained payment for such fees, they often seek to obtain restitution on behalf of the consumers who paid the challenged fees. In doing so, the agencies effectively step into the shoes of the consumers themselves.

While an old doctrine, the VPD doctrine seldom has been offered as a defense to either a federal or state enforcement action in which restitution was sought. Clearly, an argument can be made that the agencies should not be allowed to obtain monetary relief for consumers who would be barred from such a recovery if they pursued a lawsuit on their own. In jurisdictions in which businesses have successfully invoked the VPD to obtain dismissal of restitution claims brought by consumers, it appears that the agencies might likewise be barred from recovering a portion of the fees voluntarily paid by those consumers. Businesses facing this scenario would be well served to at least pursue the defense.

On the other hand, the agencies seek to enforce laws designed to promote clear and conspicuous disclosure of the material terms governing a consumer relationship. Like the consumers in *Whiteman*, the agencies faced with a VPD challenge are likely to assert that businesses should not be allowed to profit from illegal fees that a consumer might not have had any reason to believe was being improperly charged. The agencies are also likely to assert that, like the interests recognized in *Whiteman and Pratt*, the strong public policy underlying unfair and deceptive trade practices laws should trump any such policy benefit by which businesses can unlawfully impose and collect certain fees because of mistake or insufficient consumer awareness.

As the number of enforcement actions brought by the FTC and the various state enforcement agencies continues to grow, there is a significant possibility that more defendants will assert the VPD whenever the agencies seek restitution as a remedy. It seems self-evident that the agencies will vigorously oppose such efforts to use the doctrine. How the courts (and possibly Congress and state legislatures) resolve this issue in the coming years undoubtedly will have a major impact on the ability of the agencies to recover money for consumers and, thus, alter the manner in which the agencies and business approach such issues.

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FTC v. D Squared Solutions: An On-Line Application of The FTC's Unfairness Doctrine

by Deborah Matties*

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In a common 1950s scam, unscrupulous door-to-door salesmen represented themselves as "heating engineers" and offered homeowners free furnace "inspections." While "inspecting" a furnace, they dismantled and refused to reassemble it until the homeowner submitted to extortionate demands for "repair" fees. The FTC successfully challenged that scam as an unfair trade practice in *Holland Furnace*.[1]

In its recent case against software marketer D Squared Solutions, the FTC alleged that the defendants engaged in a 21st Century variation on this classic scheme. On July 28th, a federal judge in Baltimore entered a stipulated permanent injunction against D Squared Solutions and its two principals, settling FTC charges that they had interfered with the operation of consumers' computers by barraging them with repeated Windows Messenger Service "pop up" spam that advertised software that would stop the pop up spam at a cost of $25 to $30.[2]

According to the FTC, the defendants assaulted consumers with an estimated 135,000 pop up ads ***per hour***, with many consumers receiving them at a rate of one every ten minutes. Consumers from across the country testified that they lost data and work productivity. Others reported that their computers crashed or froze as a result of the pop ups. The defendants' purpose in sending so many ads so frequently was apparent: by maximizing the disruption to consumers' computers, they hoped that consumers would ultimately buy their pop up-blocking software.

According to the FTC complaint, the defendants also operated a synergistic side business whereby they licensed the pop up-sending software to other electronic marketers so that they could send the same kind of pop ups to the same consumers. In addition to profiting directly from these licensing arrangements, the defendants increased demand for their pop up-blocking software by encouraging others to engage in the same disruptive practice. Thus, the FTC's complaint also alleged that by selling pop up-*sending*