

Top 10 Consumer Complaints:

Strengthening consumer protections in the 21st century marketplace

*Background Paper for A Special Consumer Protection Hearing
Of the Assembly Judiciary Committee*

**July 17th, 2007
9:30 – 12:00
Room 4202, State Capitol**

Executive Summary

The Committee will examine some of today's most prevalent and egregious consumer fraud problems. The purpose of the hearing is to identify new trends in consumer fraud, receive updates on long-running scams, review the effectiveness of current law, and discuss suggestions for new ways of combating rip-offs in the marketplace.

Committee staff asked deputy district attorneys from throughout the state who specialize in consumer protection to compile a list of the most troubling consumer fraud issues, and from that list staff chose the "top 10" consumer complaints that serve as the topic of the hearing. The "top 10" list is not based on a statistical analysis of consumer calls into DAs' offices; rather, the list reflects the consensus of prosecutors and committee staff about what constitute the most pressing types of fraud.

All of the "top 10" subjects potentially fall within the Committee's jurisdiction, and the hearing is intended, in part, to provide background for legislation that will come before the Committee for consideration. The top 10 consumer complaints that the committee will examine include the following:

1. Identity Theft
2. Elder Fraud
3. Immigration Consulting Fraud and Unauthorized Practice of Law
4. High Tech and E-Commerce Fraud
5. Predatory Lending Tactics
6. Contractor Fraud and Failure
7. False Advertising and Deceptive Sales
8. Auto Sales/Leasing Practices
9. Health and Diet Products
10. Government Mimicry and Phony Assessor Scams

The hearing will focus on four of the 10 items on the list: ID theft; elder fraud; immigration consulting fraud; and high-tech crime. The Committee chose to “drill down” on these four items for various reasons. ID theft is the subject of numerous bills that have and will come before the Committee. Elder fraud is a perennial legislative issue that will only grow more important as the percentage of elderly residents in this state expands. Immigration consulting fraud – a problem for many years – is timely as the federal government continues to consider immigration policy reform. And high-tech crimes allow the committee to focus on emerging and complex consumer threats.

This paper combines the research and writing of committee staff and district attorneys from throughout the state, with special credit going to the Los Angeles District Attorney’s Office. Committee staff and DA’s offices shared the writing and research in the “problem” sections. The “strategies and solutions” sections of the paper are drafted entirely by DA’s offices,¹ and serve as discussion topics for the hearing rather than specific endorsements of policy by the Assembly Judiciary Committee.

The Top Ten Consumer Complaints

1. Identity Theft

The Problem

Identity theft — the wrongful use of the personal identifying information of another — is a serious crime, most often occurring in a high tech context, which ruins a victim’s credit and good name, causes enormous financial and emotional harm, and costs honest businesses over \$50 billion annually nationwide. In many cases, victims are charged with crimes they did not commit because the thieves use the victims’ identity to commit a crime.

Identity theft is widely regarded as the largest-scale and fastest growing crime in the County of Los Angeles, the state of California, and the nation. A 2003 study the Federal Trade Commission indicated that almost 10 *million* Americans discovered they were victims of some form of identity theft in the preceding year.² In the County of Los Angeles, more than 27,000 identity theft reports were received in 2005 alone. Based on Federal Trade Commission studies suggesting that only 40% of victims report ID thefts, it is estimated that at least 65,000 ID thefts take place each year in Los Angeles County, and this general pattern is replicated in virtually every community in California.³

From earlier simple cases of “dumpster diving” and one-on-one credit card fraud, modern identity theft has grown troublingly complex and sophisticated, greatly increasing its

¹ With the exception of the Elder Fraud section (Section 2), which was drafted by Committee staff.

² Federal Trade Commission, *Identity Theft Survey Report* (2003), at p.4.

³ *Id.*

potential for societal harm. Identity theft has become an organized crime usually characterized by multiple defendants. The investigation of one of these large-scale cases often requires many detectives, and then may occupy the full efforts of a prosecutor to prepare and prosecute. Interviews with and assistance to the victims may require hundreds or even thousands of contacts. Examples include the LADA prosecution in *People v. Hamilton*, a 22-defendant ID theft fraud and merchant scam, and LADA's ChoicePoint database intrusion case with 189,000 victims' information accessed (*People v. Oluwatosin*).

ID theft has become increasingly sophisticated in its use of high technology and system knowledge:

- **E-mail scams, phishing and pfarming schemes**, and the use of skimmers, encoders and other technological methods to collect and harvest victims personal identifying information have become commonplace, employing such means as modified ATM PIN pads, pocket-size skimmers, and devices placed in gas station pumps.

- **Identity thieves are collecting larger amounts of data** from numerous victims, keeping personal information longer, and storing it for use long after the initial theft, in a phenomenon known as **“profiling.”**

- **These organized scammers use jurisdictional limitations** to frustrate law enforcement. Information is collected in one part of the county and only used in another. For example, one crook steals victim information via skimming, data mining or mail theft. He/she provides the information to other conspirators who access others credit by encoding cards, engaging in unlawful balance transfers of manufacturing credit card checks. Still other participants are recruited to use the fraudulent cards or checks to obtain goods or services. The activities are planned for separate locations, often in different jurisdictions, to make prosecution difficult.

- **Identity theft now reaches deeply into the high-volume world of credit** and banking information. Up to 75% of all ID theft reports made to the Los Angeles Sheriff's Department today are for credit or banking fraud. This type of identity theft has a large local loss, in that items purchased on stolen credit are a direct loss to county merchants and financial institutions. Fraudulently purchased items are losses that directly reduce tax revenue for the county.

Strategies and Solutions

1. Vertical prosecution of, and investigative assistance for, the following crimes:

- **Identity theft crimes**, including crimes committed via check, ATM, access card fraud, and other electronic or computer related thefts. *See* list of crimes in Penal Code § 13848 (b)(1).

- **Computer crimes**, including the unlawful access, destruction or misuse of government, corporate, and private computers, the theft of data from computers, and the use of computers to defraud, extort or commit other crimes. *See* list of defined computer crimes in Penal Code section 13848 (b)(2):.
- **Theft of intellectual property**, including movie, music and software piracy, theft of trade secrets, Theft of telecommunication, cable or satellite signals or components, counterfeit of trademarks on music, movies and computer components, and the theft of high technology components. *See* list in Penal Code § 13848 (b)(4,5,6,7 and 8).
- **Money laundering accomplished with the aid of computers or electronic banking transfers**. *See* list in Penal Code § 13848 (b)(3).

2. Legislative Solutions. California's Legislature and law enforcement community should continue to play a leadership role in analyzing, drafting, and advocating for improved legislation in the fields of computer crime and identity theft. Updated laws to deal with new forms of identity theft and computer crime, such as pfarming and pfishing, will always be needed. And California and the federal government should consider appropriate legislative efforts to ensure a steady source of increased funding for investigation, prosecution, and consumer education in this arena.

3. Law Enforcement and Public Cooperation, Outreach, and Training. The many prosecutors' offices and investigative agencies active in this field must recognize the common nature of this problem and must develop a coordinated strategy for combating it. Examples of this approach to agency cooperation are numerous and must be expanded. In Southern California, for example, a number of such efforts are underway and should be expanded, including the Southern California High Tech Crime Task Force, the Southern California Identity Theft Task Force, the Los Angeles Electronic Crime Task Force, and efforts by other groups or individual agencies with high tech crime or ID theft sections.

The legislature and the law enforcement community should play leadership roles in projects now underway to promote regional and national strategies on identity theft and computer crime. One example is an undertaking by the National District Attorneys Association and its affiliated American Prosecutors Research Institute (APRI) to establish a national training center and clearinghouse for identity theft matters. The newly established National Center for Prosecution of Identity Crime (NCPIC), located in Alexandria, Virginia, is envisioned as the first stage of a national strategy that would expand to regional centers to improve identity theft training and to exchange legal research, statistics, and case information. The proposed division would continue and expand on our current efforts with NDAA/APRI and similar ventures.

2. Elder Fraud and Abuse

Seniors are a favorite target of rip-off artists who play on their victims' age, isolation, and financial worries to raid their life savings. The scams are myriad but share a common pattern of misplaced trust. The best advice to seniors is to beware of anyone with access to your finances. Here are some examples of what can go wrong:

The Problem

Caregivers can take more than they give. Your elderly parents are in pretty good health but need help around the house with everyday tasks like bathing, dressing, cooking, and walking. You turn to the Yellow Pages for a list of agencies that provide home care services, and you choose one that claims to run "background checks" on its caregiver employees (but doesn't say what sort of background check). The caregiver starts work in your parents' home, but after a couple of months, suddenly disappears. You find a statement from your parents' bank showing thousands of dollars are missing.

Beware the fancy title. You get knock on the door from a sharply-dressed salesman who shows you a business card with the title, Registered Elder Specialist. He invites himself inside and convinces you that his special certification in senior financial products makes him a trusted partner in your retirement planning. What you don't find out until after you've signed his contract is that there's no such thing as a "Registered Elder Specialist" – and what did all those papers you just signed really say, anyway?

The lunch is free, but now you're not. You see an add in the paper for a financial planning seminar on living trusts, free lunch included, and you gladly attend. Before lunch is served, someone describing himself as a paralegal circulates a questionnaire for you to fill out – including your name, address, and financial information. A couple of days later, the paralegal comes to your door and strongly encourages you to convert your current savings into an annuity. The paralegal seems to know what he's doing so you agree to sign his papers. But what he didn't tell you is that now if you want access to your assets – including for an emergency medical need – you'll be paying huge withdrawal penalties.

Strategies and Solutions

Though fraud against senior citizens takes place over the telephone, through the mail, and by other means of remote communication, experts often identify the elderly person's doorstep as the front line in the battle against financial abuse: if a con artist can insinuate himself or herself into the senior's home, the risk of a successful scam skyrockets.

Current state law protects seniors in their homes by, for example, requiring that before an in-home meeting with a senior, a life insurance agent must provide 24-hour advance written notice of the purpose of the meeting, the identity of the agent, the fact that the senior has the right to have other people present, and the fact that the senior has the right

to end the meeting at any time, among other disclosures.⁴ Seniors should be educated about their existing rights, and resources should be available for enforcing them through various regulators such as the Department of Insurance and district attorneys' offices.

As the problem of caregiver fraud and abuse illustrates, however, there may be need for further laws protecting seniors from scams in their homes. For example, there is no requirement that private in-home care providers screen their employees for past criminal conduct. Deputy District Attorney Paul Greenwood of the San Diego DA's Office will testify at today's hearing that failure to weed out caregivers with past felony and other criminal convictions has exposed seniors in his county and throughout the state to intolerable levels of fraud and abuse. The Committee may choose to discuss the best method of protecting against caregiver fraud, including consideration that mandatory employee background screening be performed by private home care agencies.⁵

3. Immigration Fraud and Unauthorized Practice of Law

The Problem

"Immigration fraud" in this context refers to complaints from individuals who are not U.S. citizens but who reside in the U.S. that they have been deceived or defrauded in their efforts to adjust their immigration status, usually by someone paid to prepare immigration paperwork or otherwise present their cases to immigration authorities.

Immigration fraud takes many forms, including:

- ***The "notario = lawyer" hoax.*** In many Latin American countries the title "notario publico" means someone licensed to practice law, but in California a notary is only a person designated to witness the signing of documents. Unscrupulous immigration consultants often advertise themselves as "notorios," hoping to mislead immigrants from Latin America into believing they are dealing with attorneys. In fact, it is illegal for an immigration consultant to call himself a "notario" in California because of this inherent capacity to mislead as to this crucial distinction.
- ***The asylum gambit.*** Scam artists will sometimes suggest pathways to citizenship that cost a lot and are guaranteed to fail. Some convince clients to apply for asylum – at a standard charge of about \$5,000 – knowing that because applicants must demonstrate that deportation back to their native countries would result in persecution, their applications won't be successful. Mexican nationals, in particular, are often misled in this way with phony promises of political asylum, which is never granted in cases of immigration from that nation.

⁴ See Section 789.10 of the Insurance Code.

⁵ See AB 853 (Jones, 2007) – Currently in the Assembly Appropriations Committee.

In these cases, clients have effectively exposed themselves to federal authorities and may face deportation as a result. A client's deportation allows the consultant to continue defrauding other client's without consequence.

Some may see immigration fraud as a matter for the federal authorities to handle exclusively, but this is often not the case. Typically federal authorities will only investigate and prosecute individuals who actually file paperwork with the U.S. Citizenship and Immigration Services (USCIS), and then the case must meet other filing guidelines as well.

Immigration fraud is a problem throughout the state of California and ongoing criminal prosecution of such fraud is vital. Statutes used in these enforcement efforts include Penal Code sections 484/487 (grand theft by false pretenses), Business and Professions Code section 6126 (unauthorized practice of law), and California's detailed Immigration Consultants Act (ICA), Business and Professions Code sections 22440 *et seq.*

The ICA applies to anyone who engages in the business of giving non-legal advice or assistance in an immigration matter. Thus, if the suspect is not a lawyer and has not practiced law, but has merely offered to complete immigration forms, translate answers on the forms, secure supporting documents for the person preparing forms, submit the forms to the federal government, or refer people to others for legal representation about an immigration matter, the suspect must comply with this law.

The most troublesome aspect of an immigration fraud case for the prosecutor is uncertainty over whether the victim will be available to testify once the matter is presented to the court. The concern is that the victim may be deported or may simply be too afraid to testify. USCIS, in its prior INS configuration, had a witness protection program for such victims. However, in the past this program sometimes presented problems, in that the former INS would agree not to deport an undocumented person while the matter proceeds through the courts, but then it must, by its own rules, deport the person at the conclusion of the case. Victims of immigration fraud view this as punishment for coming forward. Some district attorneys prefer not to use the federal immigration witness protection program and instead explain to victims that cooperation will not result in any impact on their immigration status. Most victims were willing to testify under these conditions.

Strategies and Solutions

Although in most respects we have substantial laws to punish immigration fraud, there remain obstacles to successful investigation and prosecution, including insufficient law enforcement resources and a lack of public awareness.

1. Legislation. In 2002 the State Bar and other public agencies sought legislation to increase penalties for the unlicensed practice of law and the Legislature responded by passing SB 1459 (Romero) which increased the punishment for this crime to one year in county jail or a \$1,000 fine or both. If the defendant commits a subsequent violation and

is convicted, the court must impose a 90-day jail sentence or state on the record the reasons for a lesser sentence. Other legislation in this vein has followed, including last year's AB 630 (Chu). This kind of legislative support will be important in combating immigration and UPL fraud as they go through the usual permutations of fraud schemes. The efforts of the Legislature and the law enforcement community should continue to be focused on our fight against immigration fraud.

2. Increased Investigator and Prosecutor Resources. Investigating immigration fraud usually requires detective work by someone who is bilingual or who has a translator available. Investigators or detectives must invest a good deal of time to coax frightened victims to report these crimes and to reassure the victims that coming forward will not lead to deportation. To investigate and prosecute these cases it is often necessary to go through a time-consuming process of obtaining documents from the federal government to establish whether the suspect filed documents improperly on behalf of victims. Most local police agencies and district attorneys find prosecutors and investigators with this kind of expertise in very short supply.

3. Increased Enforcement Cooperation. Multi-agency cooperation will also be important in this effort. As an example of this approach, law enforcement agencies in San Diego are combating immigration fraud by increasing the resources devoted to it and by educating law enforcement officers about the problem. The San Diego District Attorney's Office belongs to a regional Immigration Fraud Task Force headed by the U.S. Attorney's Office. The task force consists of representatives from USCIS, ICE, the FBI, the U.S. Attorney's Office, the District Attorney, the City Attorney, police officers, and the Mexican Consulate. This task force meets to discuss complaints their offices have received and to ensure that the agencies work together efficiently.

In this same vein, the continuing concern of victims' reluctance to testify in such matters (for fear of revealing undocumented status) can sometimes be eased by building a rapport with the national consulate at issue. For example, Mexican nationals often feel much more comfortable telling their stories while sitting in a room at the Mexican Consulate with a representative of the Consulate present. State and local agencies have had success with developing a rapport with the staff at the Consulate, so that Consulate staff can vouch for agency officials, placing the victims at ease.

4. Public Education Focusing on Prevention and Solutions. Undocumented non-citizens often do not know their rights and do not know whether to complain or where to complain when they are victimized. The organizations to which they turn are frequently unaware that police agencies and prosecutors are available to assist in these cases. Individual police officers may not recognize complaints of this nature are criminal in nature and may not take a police report when called. Finally, prosecutors may be reluctant to invest resources to prosecute these cases for fear that witnesses will no longer be available when it is time to prove the case at trial.

Some progress is being made in the area of consumer education. For example, many district attorneys have focused training efforts on local police agencies to engender

greater understanding of these crimes and higher enforcement priority. Improved press contacts and releases have helped to inform members of the public that law enforcement agencies can and will prosecute immigration fraud.

4. High-Tech Crime and E-Commerce Fraud

The Problem

The scope of high technology crime and its rate of increase are difficult to exaggerate. Recent studies conducted by the federal government and business groups indicate that computer-related crime has grown exponentially since 1997, costing the nation billions of dollars in economic harms and losses and overwhelming existing law enforcement efforts to address it.⁶ A 2004 study suggested that perhaps two-thirds of the estimated \$16 billion in annual worldwide economic harm from digital attacks (such as Penal Code section 502 unauthorized access violations) occurs in the United States.⁷

Los Angeles County is widely recognized as one of the key centers of the wave of high technology-related crime sweeping the country. In 2005 the Federal Trade Commission recorded 15,984 Internet crime and ID theft reports for the greater Los Angeles Area, ranking that community second in the nation only to the New York City in the rate of incidence of these crimes.

The California High Technology Crimes Task Force reported some 552 high tech crime cases involving 15,588 victims and \$305,914,885 in total monetary loss for fiscal year 2004-2005 statewide, and Los Angeles cases comprised the single largest component of these.⁸ The Joint Council data (above) suggest that economic losses from computer crime in Los Angeles County now exceed \$300 million each year. Similar harms in proportional amounts are experienced by every California community. And the non-economic harms of computer systems invaded and lives disrupted may be an even greater societal toll.

Today computer crime takes many forms and mutates rapidly as new technologies are introduced. Commonplace among California computer crimes in 2006 are computer intrusion or “hacking” to defraud or deceive others (Penal Code § 502(c)(1)), computer intrusion to take, copy or use the data of others (Penal Code § 502(c)(2)), unauthorized use of computers (Penal Code § 502(c)(3)), computer intrusion to alter or destroy data (Penal Code 502(c)(4)), the malicious introduction of computer viruses, worms, Trojan horses, and other “malware” (Penal Code 502(c)(6)), the tidal wave of spam and otherwise annoying e-mails (Penal Code 643m and other provisions), the theft of

⁶ Joint Council on Information Age Crime, *Computer-Related Crime Impact: Measuring the Incidence and Cost* (2004), at p.5.

⁷ *Id.*, at 8.

⁸ High Technology Theft Apprehension and Prosecution Program, *High Technology Crime in California* (2005), at p.14.

telecommunications services by computer means (Penal Code 502.7), Internet auction fraud (Penal Code section 535), and various forms of intellectual property theft (*see, e.g.*, Penal Code section 499(c)).

Some specific examples of these new forms of computer crime include:

- ***Employment opportunity Web sites*** may allow job seekers to search for work opportunities, but may also be bogus companies trying to lure the unsuspecting. Overseas investment and employment opportunities may require an immediate “return” of an initial overpayment, but the consumer soon discovers that the initial check was worthless and the return payment is a complete loss.
- ***Online auction sites*** (such as eBay) have revolutionized consumer marketing, but can also subject the unwary to scams such as:

“*Bid siphoning*” where con artists lure customers off of the official auction site, promising the same products at much lower prices, but later the customers find that protections like insurance are absent, and the seller may never ship the product.

“*Second chance offers*” come from fraudsters once the buyer has lost on a bid. Again, the buyer is lured off the official site, losing any of its protections, with promise of a “second chance” to purchase the item.

“*Escrow service fraud*” occurs after the buyer has won on a bid and the seller requests that the buyer use a certain escrow service for payment. The way legitimate escrow services work is that the buyer sends payment to a third-party escrow company that holds onto the funds until the buyer receives and accepts the merchandise. But if the seller convinces the buyer to send payment to a bogus escrow service, the seller has the money and the buyer never sees the product.

“*Parcel courier e-mail schemes,*” a variation on the escrow scam, take place after the customer has bought the item online. The seller contacts the buyer to say the purchased item will be sent to UPS, and held there until the seller receives payment. Soon afterwards, someone purporting to be “UPS” contacts the buyer informing him or her that the item has arrived and is being held pending payment. This causes the buyer to transfer the funds to the seller, only later to realize that it wasn’t UPS that called and there are no items to pick up.

- ***Nigerian money transfer schemes*** are bogus too-good-to-be-true profit opportunities. An e-mail arrives from a purported Nigerian government official or citizen offering a generous percentage to US citizens willing to help liberate funds held there. The dupe is told that he or she must pay some “modest fees” in order to make the transaction go through, which fees of course disappear into the hands of a scammer living in a country without an extradition treaty with the US.

- **Online bulletin boards** allow investors to trade tips and advice on stock buys, but may also be subject to insider manipulation and harm.

Strategies and Solutions

The geometric growth of these scams and frauds calls for California to step up its leadership in the battle against high tech crime by expanding and reorganizing its resources devoted to (1) investigating and prosecuting computer crimes and ID theft, (2) advancing the state of the law in this field, and (3) educating law enforcement, businesses, and consumers on means of addressing this challenge.

The strategies and solutions listed for the Identity Theft topic (above), including vertical prosecution, legislative updating, and law enforcement/public cooperation and training, are equally appropriate for the closely related problem of High Tech and E-Commerce Fraud.

5. Predatory Lending Practices

The Problem

Most lenders are honest and closely follow federal and state lending guidelines. But in recent years shady or unscrupulous lenders have turned home mortgages, auto loans, or emergency payday loans into traps for the unwary.

Predatory mortgage or auto lending are today the subjects of major consumer protection lawsuits brought by state and local prosecutors in California. In this type of scheme, the fast-talking loan salesman makes attractive promises of easy loan terms for a new or refinanced home loan or auto purchase. Often the victim is an elderly person with some home equity but modest fixed income. But when the smoke clears, the borrower has been tricked into an adjustable loan instead of a fixed one, or faces huge undisclosed prepayment penalties or other unfavorable terms. Elderly and low-income borrowers are particularly vulnerable, and sometimes even lose their homes as a result.

An important recent example is the 2006 judgment in *People v. Ameriquest Mortgage Co., et al.* (RG06260804, Mar.31, 2006) involving allegations of misrepresentations of loan terms and other unfair practices by Ameriquest Mortgage of Orange, California. More than 70,000 California borrowers, many of them elderly or unsophisticated, were injured by the unfair business practices at issue. Believed to be the second-largest such consumer restitution program in a California law enforcement case, this lawsuit was part of a nationwide action which resulted in a total national judgment of \$325 million.

In recent years, the payday loan industry has come under increasing scrutiny for the conduct of some industry members who prey on the vulnerable. In this scheme, the consumer works hard to make ends meet for his or her family, but can't put enough aside for a rainy-day fund. When the consumer's car breaks down and needs major repairs, he

or she turns to a “fast bucks” payday lender. The victim gives the lender a post-dated check and receives cash at an annual interest rate of 400%. In two weeks, the consumer begins to get phone calls from the lender asking for repayment. Soon the lender is coming to the consumer’s office and starts calling the borrower’s friends and family. The lender then offers the option of renewing the loan and paying the interest fee again. Now the vulnerable consumer is in a vicious loan and interest rate cycle which may end in ruined credit or bankruptcy.

Strategies and Solutions

1. Law Enforcement Priorities. Both regulatory agencies charged with lending laws and consumer protection prosecutors must assign higher priority to addressing these difficult problems. Cases like *People v. Ameriquest Mortgage Co.* are complex and resource intensive but their deterrent impact on unfair lending practices, and their prospects for real consumer relief, can be profound. Increasingly close cooperation among the Department of Corporations, other state lending regulators, the Attorney General, and local prosecutors is called for. Payday loan cases involving highly vulnerable consumers, including those serving overseas in the US military, should also be a higher priority for police agencies and other law enforcers.

2. Consumer-Friendly Regulation of Lending Practices. The regulatory and legislative environment must be evaluated to ensure that consumer interests remain paramount. A troubling trend in recent federal regulatory policy and case law assigns a preemptive role to federal regulation and seeks to oust state consumer laws from their traditional police powers role in protecting local consumers. Given the leadership that many states have demonstrated in curbing unfair lending practices, federal preemption should be opposed, especially unless it is accompanied by provable and lasting commitment to vigorous consumer protection policies addressing problems such as predatory mortgage lending and unscrupulous payday lending. Further California legislation to increase consumer protections in the payday loan industry, although no doubt controversial, should again be revisited.

3. Borrower Education. Consumer understanding of the proper uses of credit and the pitfalls of the borrowing process has never been complete, and remains a key problem underlying these schemes. Better and more comprehensive borrower education efforts should be considered. A simple and short brochure on payday lending, for example, might be an effective mechanism for assisting those vulnerable consumers in a time of stress. Point-of-sale disclosures for all transactions should be reviewed for readability and simplicity, as the current welter of disclosure documents (in such transactions as today’s real estate loans) tends to confuse as much as it clarifies. More lasting long-range solutions, such as addressing sound borrowing practices in school curricula, should be evaluated.

6. Contractor and Home Repair Fraud

The Problem

Each year Californians file more than 25,000 complaints with the Contractors State License Board, involving allegations of enormous aggregate losses from unscrupulous or unlicensed contractors. Estimates of annual consumer loss range from \$60 million to \$100 million, and these are almost certainly understated as many consumers do not know how to file complaints with CSLB or choose not to do so.⁹

Contractor fraud often follows a simple formula: The homeowner pays the contractor for a job that the contractor never begins, never finishes, or performs to fraudulently poor standards of quality. Equally prevalent is the contractor who claims to be licensed and bonded, with all those qualifications imply for consumer protection, when in fact the contractor is unlicensed and outside our state's system of consumer protection.

Unlawful contracting violations often harm some of our most vulnerable consumers, including the elderly and those who do business in languages other than English. Even small jobs can have a major impact on homeowners. One Southern California case started with a \$30,000 roofing job, which an elderly couple contracted with an unlicensed contractor. The unlicensed contractor abandoned the job after removing the original roof. The subsequent weather damage required a complete rebuild of the home, costing over \$488,000.

Con artist contractors can use sophisticated methods to make sure they get paid. The "home improvement loan scam" offers a classic example. The fraudster comes to the homeowner's door and offers to re-tile the kitchen floor at a good price. But if the homeowner can't readily afford to pay cash for the job, the contractor offers to put him or her in touch with a lender. The work on the kitchen begins, and a couple days later, the consumer is asked to sign some papers without really understanding their terms. Later, it turns out that the homeowner signed up for a home equity loan at extremely high rates of interest. The contractor and the lender colluded to take advantage of an unwary consumer, and now that the trap is sprung, the contractor walks away from the job. The customer is stuck with a half-finished kitchen floor and an unconscionable loan.

The Contractors State Licensing Law (CSLL) reflects a strong tradition of the law in California to protect consumers from incompetence and dishonesty by unlicensed contractors who provide building materials and construction services. In 2003, at the request of the CSLB Enforcement Monitor, the Legislature passed amendments to the CSLL which substantially enhanced the enforcement provisions of the law. Some of the key legislative enhancements included an extension of the statute of limitations for prosecutions of unlicensed contractors pursuant to section 7028 of the Business and

⁹ Papageorge and Fellmeth, *Initial Report of the CSLB Enforcement Program Monitor* (Oct. 1, 2001); *Second Report of the CSLB Enforcement Program Monitor* (Apr. 1, 2002), at 49, and *passim*.

Professions Code, increased penalties for multiple violations of the law, required fingerprinting for contractor license applicants, and greater bonding requirements.

Strategies and Solutions

1. Legislation. A clarification of restitution rights could assist in insuring that victims are made whole. Penal Code section 1202.4 provides that a victim of crime who incurs any economic loss as a result of the commission of a crime shall receive restitution directly from any defendant convicted of that crime. However, the amount of loss may be subject to dispute if an unlicensed contractor argues that work that he or she did for the victim had some value. In enacting section 7031 of the Business and Professions Code, the Legislature specifically precluded an unlicensed contractor from recovering the “value” of any work completed. Section 7031 provides that a person who utilizes the services of an unlicensed contractor may bring an action in any court of competent jurisdiction in this state to recover *all compensation* paid to the unlicensed contractor for performance of any act or contract. Statewide, various prosecutors’ offices have worked to recover such compensation on behalf of the victims in criminal restitution hearings, with uneven results. It seems clear that for reasons of judicial efficiency and restitution to the victims, criminal sentencing courts should be required to provide complete restitution to victims as provided in section 7031. Such a result could be mandated by specific reference of necessity for criminal restitution in the amount of all compensation paid to the unlicensed contractor in section 7031 of the Business and Professions Code or in section 1202.4 of the Penal Code.

On another front, the CSLB will frequently impose administrative fines levied by citation against unlicensed contractors as a method of enforcing licensing requirements. Business and Professions Code section 7028.17 makes it a misdemeanor not to pay such fines after the citation becomes final. Frequently, the CSLB attempts to give the contractor time to pay the fine, delaying the time within which they finally refer the case to the local prosecutor. Sometimes, this results in the case being referred to the prosecutor beyond the one year general statute of limitations for misdemeanors. Just as other offenses against unlicensed contractors have extended statutes of limitations (four years for the basic charge of contracting without a license) the statute of limitations for collection of fines should also be extended to no less than two years and preferably the same four years as the underlying charges.

2. New Enforcement Strategies. New multi-jurisdictional enforcement strategies must also be developed. By way of example, the Los Angeles City Attorney’s Office has addressed the troubling unlicensed contracting problem by forming a partnership with the Contractors State License Board staff to expedite investigations of unlicensed contractors and bring more cases to my office. Many of the numerous cases prosecuted have involved significant amounts of money. In one recent example, the defendant collected nearly \$200,000 from the victim before abandoning the project. This left the victim despondent and financially unable to complete the job.

7. False Advertising and Deceptive Sales Practices

The Problem

The classic wisdom tells us that “if it seems too good to be true, it probably is.” Nowhere is this more accurate than in the world of advertising and sales practices. Most businesses realize that truthful sales efforts build better customer loyalty in the long run. But all too many sellers succumb to the temptation to gain a competitive edge by exaggeration, half-truths, or flat-out lies to sell their wares.

Complaints about deceptive, misleading, or unfair sales practices are perennial candidates for any list of top consumer problems. A 1974 national study by the U.S. Chamber of Commerce put the total annual economic harm from deceptive practices at \$21 billion, which would be more than \$88 billion in inflation-adjusted terms.¹⁰

False advertising and deceptive point-of-sale business practices take many forms:

- **“Bait and switch” practices.** Advertisers or sellers offer unrealistically low prices to lure customers into their stores, only to use product disparagement and claims of unavailability as the tools to switch consumers to higher profit items. Auto dealers, camera stores, and stereo and appliance centers are often involved in such cases.

- **Perpetual sales.** Newspaper, TV and radio ads make claims of phony price comparisons and too-good-to-be-true discount prices to create the false impression of a special sale with a limited duration. “WAS \$99.99 – on sale THIS WEEKEND ONLY for \$59.99!!!” But in fact the product can be bought at that store for \$59.99 all year long. Often associated with this practice are carpet merchants, window blind stores, and some home furnishing businesses.

- **Phony “going out of business” advertising.** Commonplace, especially during economic downturns, are ads claiming “LOST OUR LEASE” or “GOING OUT OF BUSINESS – LIQUIDATION SALE” in banner terms when in fact the business or chain of stores has no intention of permanent closure. In another variation, liquidator companies bring in new merchandise from out of state and use phony mark-downs to mislead customers as to the extent of sales savings. Rug merchants, furniture stores, and jewelry stores have often been charged with this tactic.

- **False representations about product quantity or features.** Consumers trust what merchants say, and often don’t check to see if they actually receive what the seller promised. High technology short-measure sales at gas stations and computer monitor screens which have smaller-than-advertised viewable area are examples of cases prosecuted under this theory.

- **Supermarket and department store scanner accuracy.** Scanner technology has helped to speed checkstand operations but it has been accompanied by a continuing

¹⁰ U.S. Chamber of Commerce, *White Collar Crime* (1974), at 6.

problem of overcharges when the store's computer registers a full price when the former sale price sticker is still on the shelf. Millions of dollars can be taken from the public a few dollars at a time through negligence or poor pricing practices.

- **Prize and premium promotions.** “CONGRATULATIONS!!! You have won one of the following FABULOUS prizes!!” So says the spam advertisement on the consumers' computer screen or the unsolicited post card in the mail. All the consumer has to do is supply the \$49.95 shipping (for the worthless “gold plated” silverware) or provide credit card information (which may be used for identity theft).

Strategies and Solutions

1. Cooperative Law Enforcement/Regulator Strategies. Deceptive sales practices, especially by larger businesses or chains, seldom stop at county boundaries. The endemic shortage of consumer protection investigators and prosecutors can be partially eased by increased use of cooperative law enforcement strategies, where state regulators (Dept. of Consumer Affairs and its boards and bureaus, Dept. of Motor Vehicles, Division of Measurement Standards) work on teams or joint venture investigations to bring more effective enforcement actions on a regional or statewide basis. California's consumer prosecutors are making important strides in this direction. This trend should be encouraged and state agencies incentivized to participate further.

2. Intensive Education on Wise Consumer Shopping Behaviors. Consumer fraud/deception is perhaps the most preventable of crimes, and consumer education remains the cornerstone of this prevention. It is impossible to overemphasize the importance of the message of wise consumer shopping behaviors — such as doing careful pre-buying research, checking receipts for accuracy, and complaining effectively when violations occur. A variety of new or underutilized consumer education formats should be tried or expanded, including Web sites, public service announcements, point-of-sale checklists and brochures, and improved consumer education in school curricula.

3. Business Community Outreach. Greater emphasis should be placed on outreach to the business communities through trade associations, chambers of commerce, and other community-based organizations. Most businesspersons are honest. And even those who may be tempted to use “lowest common denominator” sales practices can be educated to understand that gaining customer trust is a more successful long-term marketing strategy than the unscrupulous fast-buck approach. Many business groups already broadcast this message, but much more can be done in this vein.

8. Auto Sales and Leasing Fraud

The Problem

Transportation by automobile is for most Californians not a luxury but a necessity of life. Auto purchases or leases generally represent the second-largest financial transaction in the lives of most consumers.

Auto sales fraud is as old as the car itself. Schemes can be simple or more complex, but in either case it often takes much more than a good kick to the tires to figure out whether the deal the consumer is being offered is really worth taking. Auto sales and leasing complaints are consistently among the top consumer complaints fielded by consumer agencies in California. Examples of common scams include:

Undisclosed car problems. The dealer fails to tell the buyer about prior accidents and damage, or the dealer covers up the fact that the vehicle was salvaged and rebuilt, or that it was a rental.

Contract language issues. The dealer may negotiate the terms of a contract orally in one language and then ask the buyer to sign a contract containing additional terms in another language.

Sales or lease “packing.” Most of the negotiations to purchase or lease a car take place as a conversation between the buyer and the auto dealer’s representative. The buyer discusses desired features and options (including navigation systems, audio components, extended warranties, etc.) and is quoted a purchase or lease price, often in monthly payment terms. When the time comes to sign the written contract, the customer signs on the dotted line expecting to have bought or leased just the car discussed. But instead, the seller has manipulated or “packed” the purchase or lease contract, which now contains undisclosed or poorly disclosed extras and additional charges, often buried in fine print.

“Yo-Yo” financing scams. The consumer drives off the lot as the proud owner of a new car, and spends the next two weeks showing it off to friends and coworkers. Shortly thereafter the dealership calls the consumer to that the bank declined the contract’s financing. But now the dealer offers alternative financing at much higher rates, leaving the purchaser with no real option but to pay more.

Balance pay-off frauds. A chronic and serious problem, involving a small but significant number of car dealers, arises when an unscrupulous dealer takes an auto trade-in for a new purchase or lease, and neglects or fails to pay off the existing balance on the trade-in, perhaps later filing bankruptcy and leaving the buyer with two car loans and one car.

Strategies and Solutions

1. Legislation. Last year’s AB 68 (Lieber), the “Car Buyer’s Bill of Rights,” represented an important step in the right direction toward consumer relief from sharp and unscrupulous car dealer practices. This bill provides, among other remedies, a limited contract cancellation option, a clearer prohibition on certain of the “packing” practices, and new limitations of certain forms of deceptive auto advertising. A product

of extensive compromise, AB 68 and its impact should be carefully studied, with input from consumer organizations and law enforcement officials, to make sure the bill accomplishes its laudable objectives. Further amendments to the relevant Vehicle Code provisions may prove necessary if packing and other deceptive practices are not adequately reduced. This year's SB 729 (Padilla), which would address the serious problem when auto dealers fail to pay off balances owed on trade-ins, merits the Legislature's full support and the Governor's prompt approval.

2. Enforcement Priorities. Successful enforcement cases like the Los Angeles District Attorney's 2001 criminal and civil prosecution in *People v. Gunderson Chevrolet* (resulting in seven criminal convictions and \$2.3 million in consumer restitution and monetary relief) have sent important deterrent messages to the car dealership community in California. These cases have helped change business practices statewide. Police agencies must respond promptly and enthusiastically to consumer complaints about these practices, and should work closely with equally committed DMV investigators and prosecutors to bring appropriate criminal and civil enforcement cases.

9. Health and Diet Products

The Schemes

Health-conscious Californians are often the targets of scam artists and snake oil salesmen whose goal is to exploit our concerns over weight loss, beauty, and good health. The health and diet businesses are part of a multibillion-dollar industry composed of many legitimate vendors and a troublingly large number of quacks and con artists.

Some of these scammers focus on consumers worried about diets and better looks. Most of us know that real and lasting weight loss can only be achieved through a careful balance of safe dieting and exercise. But many consumers are lulled into believing that a "miracle" diet or process will produce easy and instantaneous results.

Some examples of this kind of diet or beauty scam include:

"Plug in the ShockAb electrical muscle toners, sit back, and watch that six-pack grow!"

"Roll back the clock 10 years! New all-natural HGH anti-aging pill guarantees a return of energy and vitality!"

"Eat all you want and still lose weight!"

"Lose weight and keep it off – permanently!"

Other fraud schemes target even more vulnerable consumers who suffer from serious illnesses which should be treated by competent medical professionals. These sad cases

often involve naïve consumers who are tricked into the use of quack remedies and thus forego proven medical treatments which could help them recover. Examples include:

“Anti-Cancerlin – the new drug that suppresses or reverses pancreatic cancer.”

“Herbal anti-depression treatment. Welcome to natural happiness!”

“Miracle tea will cure your diabetes!”

As long as there are consumers who suffer health problems or want to lose weight, there will be a vigorous market for products to address those concerns. And this market will continue to be plagued by nostrums and phony remedies.

Strategies and Solutions

1. Pro-Consumer Regulatory Environment. A fundamental challenge for consumer protection officials in this arena is the changing – and often deteriorating – federal regulatory environment for food and drug products. Federal regulatory changes like the DSHEA legislation (permitting unsubstantiated claims on some food supplements as long as minimal disclaimers are included) and others have greatly opened the field of health and diet advertising to dubious practices and abuses. California’s legislative and executive leadership should speak out, and lobby in Washington DC, for consumer-friendly regulations and pro-consumer enforcement policies by the federal agencies.

2. Law Enforcement Commitment. The complexities of cases involving expert medical testimony often serve as a deterrent to state and local law enforcement officials in their evaluation of prospective actions in this arena. Identification of expert witnesses willing to assist on a *pro bono* or limited-fee basis, and greater commitment of resources by state and local police agencies and prosecutors, will be needed before we see a marked increase in the number and success of prosecutions against health and diet scammers.

10. Government Mimicry and Phony Assessor Scams

The Problem: Simulated Government Mailings

Recently, prosecutors have seen an increase in the number of consumer complaints regarding letters they receive that appear to be from government agencies, but are really solicitations by private businesses. These complaints involve: (1) letters warning that the law requires some action by the recipient and requiring the recipient to respond with a fee; (2) letters that offer to file a homeowner’s exemption or homestead with the County; (3) letters that offer to appeal the assessed value of a property; and (4) letters that refer to current mortgage information on file with the Recorder and offer a better mortgage.

A typical scenario in this regard is as follows: The homeowner opens a letter from a company that offers a special service. The solicitation claims that the assessed value of the homeowners' house is higher than the current market value, meaning that the consumer is paying higher property taxes than required by law. For a fee, the company will make sure the assessed value of the house is reduced, lowering the property taxes. In the most common scam, the letter either misrepresents the true valuations, or implies that special assistance is required when in fact a simple call from the homeowners to the County Assessor's office can have the same effect, and for free.

Solicitors are aware of these provisions and are producing solicitations that appear to be from the government, but do not necessarily run afoul of the expressed provisions of these code sections. Business and Professions Code §17537.8(a)(3)(B) prohibits a homestead exemption filing service from using a name that contains both the words "assessor" and "homeowners' exemption" or "exemption." So a company may use "assessor" but not one of the other words, and comply with the letter, but not the spirit, of the law.

Also prevalent are new services that send solicitations to corporations suggesting that they must file documents (e.g. corporate minutes) with the Secretary of State and offering to do so for a fee. The outside envelope indicates in bold print "BUSINESS MAIL—IMPORTANT NOTICE ENCLOSED. THIS IS NOT A GOVERNMENT DOCUMENT." By placing the required disclosure in a sentence, the disclosure is less likely to be noticed by the recipient. Although the company does not use a government seal, the solicitation bears the seal of the business, which the casual observer may mistake for an official seal.

The harm done to the public tends to be that people open junk mail and waste their time wading through confusing solicitations before realizing the document is not a government document. On occasion, the solicitation, although true and complying with the specific provisions of the law, is misleading as a whole. In those situations, recipients are misled and part with their money.

Strategies and Solutions

1. Clarification of Law Relating to Misleading Mailers. Although California's Business and Professions Code contains useful provisions addressing these problems, some of the utility of our general purpose consumer protection laws has been undermined by poorly reasoned federal court decisions. In *Haskell v. Time, Inc.* (E.D.Cal.1994) 857 F.Supp.1392, and the related *Freeman v. Time, Inc.* (9th Cir.1995) 68 F.3d 285, a District Court judge took it upon himself to determine for all Californians that misleading representations on junk mail envelopes constituted only a *de minimis* invasion of consumer rights and thus were not actionable (even though California's Legislature deems these practices offensive). Legislative or judicial directions which clarify or supersede these holdings would help in the effort to bring successful actions against junk mail marketers who choose to lie or mislead in order to get past the consumer's defenses.

2. Criminal and Civil Enforcement Strategies. Many of the perpetrators of these scams are itinerant fraud artists – the lineal descendants of the aluminum siding salesmen of the 1950s. They move from county to county plying their particular junk mail scheme until the authorities crack down. Both civil consumer protection lawsuits and criminal misdemeanor prosecutions should be employed rigorously in multiple jurisdictions throughout California to address these fraud artists and their scams. We can and should make California as a whole a hostile environment for these fraudsters.

3. Consumer Education. Many of these schemes – and the homestead scam in particular – are successful only because of consumer ignorance about these relatively arcane topics (such as the homestead exemption) that are involved. Greater consumer education efforts by tax assessors and other county and state authorities would greatly undercut the preconditions for these successful scams.

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