Louisiana Law Review

Volume 48 | Number 2
Developments in the Law, 1986-1987: A Faculty Symposium
November 1987

Consumer Law

Ronald L. Hersbergen

CONSUMER LAW

*Ronald L. Hersbergen**

VIOLATIONS OF THE FTC ACT AS VIOLATIONS OF THE LOUISIANA UNFAIR TRADE PRACTICES AND CONSUMER PROTECTION LAW

It has been repeatedly recognized by Louisiana decisions that the Louisiana legislature patterned Louisiana Revised Statutes Title 51 section 1405(A) closely on the language of section 5 of the Federal Trade Commission Act.[1] Therefore, it is apparent that the legislature intended Louisiana courts to consider interpretations of section 5 by federal courts and by the Federal Trade Commission ("FTC") to determine the scope and application of Louisiana Revised Statutes 51:1405(A) so as to determine whether the Louisiana law has been violated.[2] In *Moore v. Goodyear Tire & Rubber Co.*,[3] for example, the Louisiana Second Circuit Court of Appeal looked to *Federal Trade Commission v. Sperry & Hutchinson Co.*,[4] and *Spiegel, Inc. v. Federal Trade Commission*,[5] to determine whether a certain creditor's acts and practices were "unfair" within the meaning of section 1405(A). Thus, if the FTC considers a practice to be "unfair" when it "offends established public policy and when the practice is immoral, unethical, oppressive, unscrupulous, or substantially injurious to consumers," and if Spiegel's practice of filing collection suits against its mail order customers in an inconvenient forum is held violative of that FTC standard, then it should follow that the act of Goodyear in entering its customer's home and repossessing property sold to him on credit, without the customer's consent or knowledge,

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* Professor of Law, Louisiana State University.

1. 15 U.S.C. § 45(a)(1) (Supp. 1987). Section 45(a)(1) states that "unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are declared unlawful." La. R.S. 51:1405(A) substitutes the language "in the conduct of any trade or commerce" for the federal language "in or affecting commerce," but is otherwise identical to the federal language.

2. Red Diamond Supply, Inc. v. Liquid Carbonic Corp., 637 F.2d 1001 (5th Cir.), cert. denied, 454 U.S. 827, 102 S. Ct. 119 (1981); Gour v. Daray Motor Co., 373 So. 2d 571 (La. App. 3d Cir. 1979); Moore v. Goodyear Tire & Rubber Co., 364 So. 2d 630 (La. App. 2d Cir. 1978); Guste v. Demars, 330 So. 2d 123 (La. App. 1st Cir. 1976). See generally Standard Oil Co. v. Collector of Revenue, 210 La. 428, 27 So. 2d 268 (1946); Moresi v. Burleigh, 170 La. 270, 127 So. 624 (1930); State v. Baddock, 170 So. 2d 5 (La. App. 1st Cir. 1964), writ denied, 170 So. 2d 867 (1965).

3. 364 So. 2d 630 (La. App. 2d Cir. 1978).

4. 405 U.S. 233, 92 S. Ct. 898 (1972).

5. 540 F.2d 287 (7th Cir. 1976).

is likewise a violation of section 1405(A) of Title 51 of the Louisiana Revised Statutes.[6]

The FTC has statutory power to prescribe "rules which define with specificity acts or practices which are unfair or deceptive acts or practices" within the meaning of 15 U.S.C. section 45(a)(1).[7] From this congressional grant of power has come, *inter alia*, the FTC's Preservation of Consumers' Claims and Defenses Rule,[8] by which it is an unfair or deceptive act or practice under 15 U.S.C. section 45(a)(1) for a seller to utilize a consumer credit contract which does not contain a prescribed provision,[9] destructive of negotiable form, and hence, destructive of holder in due course status.[10] The FTC has also used its power to prescribe the Credit Practices Rule,[11] by which it is an unfair act or practice under 15 U.S.C. section 45(a)(1) for a lender or retail installment seller to take, in a consumer credit transaction, a nonpossessory security interest in a consumer's household goods, other than a purchase money

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6. So held in Moore v. Goodyear Tire & Rubber Co., 364 So. 2d 630 (La. App. 2d Cir. 1978).

7. 15 U.S.C. § 57a(1)(B) (Supp. 1987).

8. 16 C.F.R. § 433 (1987).

9. The provision states as follows:

> Notice
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> Any holder of this consumer credit contract is subject to all claims and defenses which the debtor could assert against the seller of goods or services obtained pursuant hereto or with the proceeds hereof. Recovery hereunder by the debtor shall not exceed amounts paid by the debtor hereunder.

16 C.F.R. § 433 (1987). A similar provision must be placed in consumer credit contracts made in connection with a purchase money loan by a lender "affiliated with" the seller or to whom the seller refers consumers for such loans; unless the provision is placed in such purchase money loan contracts (by the lender), the *seller's* acceptance of the loan proceeds is violative of the rule.

10. The prescribed provision conditions the consumer's promise to pay within the meaning of La. R.S. 10:3-104(1)(b) (1983). See Thomas v. Ford Motor Credit Co., 48 Md. App. 617, 429 A.2d 277 (Md. Ct. Spec. App. 1981). Lacking negotiable form, the possessor of the contract cannot be the holder and therefore not a holder in due course of it, so as to cut off the consumer's claims or defenses under La. R.S. 10:3-305 (1983). This result is obtained because only a "holder" may be a holder in due course under La. R.S. 10:3-302(1) (1983), and only through the process of "negotiation" can a party subsequent to the payee be a holder, under La. R.S. 10:3-202(1) (1983); but only a writing in negotiable form may be "negotiated," and both sections 3-202(1) and 3-302(1) use the word "instrument," which La. R.S. 10:3-102(1)(e) (1983) defines to mean a negotiable instrument.

Even if one could argue that the FTC rule does not destroy the negotiable form of an otherwise negotiable consumer credit contract, the holder of it would find it difficult to qualify for holder in due course status under La. R.S. 10:3-302 (1983) in the face of the FTC provision. See Jefferson Bank & Trust Co. v. Stamatiou, 384 So. 2d 388 (La. 1980); Hersbergen, Developments in the Law, 1979-1980—Banking Law, 41 La. L. Rev. 313-319 (1981).

11. 16 C.F.R. § 444 (1987).

security interest.[12] Thus, a violation of such an FTC rule is a violation of 15 U.S.C. section 45(a)(1), whether the failure to heed the rule was intentional or unintentional[13] and whether or not the failure actually deceived anyone, so long as the act or practice had the tendency or capacity to deceive.[14]

Logically, a violation of an FTC Trade Regulation rule should be viewed as a presumptive violation of Louisiana Revised Statutes 51:1405(A);[15] however, the recent decision of the Louisiana First Circuit Court of Appeal in *LeBlanc v. Belt Center, Inc.*,[16] does not so hold. At issue in *Belt Center* was whether a failure to comply with the FTC's Franchising Disclosure Rule[17] was per se violative of 51:1405(A). The first circuit held that the failure of compliance with the Rule's requirements was not an unfair trade practice under Louisiana Revised Statutes 51:1405(A), there being no showing of fraud, misrepresentation, decep-

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12. The Rule defines the key terms "lender," "retail installment seller," and "household goods."

13. Proof of intention to deceive is not a requisite to a finding of a violation of 15 U.S.C. section 45(a)(1) (Supp. 1987). See, e.g., Beneficial Corp. v. Federal Trade Comm'n, 542 F.2d 611 (3d Cir.), cert. denied, 430 U.S. 983, 96 S. Ct. 1679 (1976); Montgomery Ward & Co. v. Federal Trade Comm'n, 379 F.2d 666 (7th Cir. 1967); Federal Trade Comm'n v. Sterling Drug, Inc., 317 F.2d 669 (2d Cir. 1963). Indeed, the FTC, the federal courts, and a number of state courts have ruled that a failure to disclose pertinent information may be as deceptive an act as an affirmative misrepresentation, and that it is often necessary for a seller to disclose unfavorable facts to avoid misleading purchasers. See, e.g., Simeon Management Corp. v. Federal Trade Comm'n, 579 F.2d 1137 (9th Cir. 1978); Warner-Lambert Co. v. Federal Trade Comm'n, 562 F.2d 749 (D.C. Cir. 1977); Heller v. Silverbranch Constr. Co., 376 Mass. 621, 382 N.E.2d 1065 (1978).

14. Federal Trade Comm'n v. Algoma Lumber Co., 291 U.S. 67, 54 S. Ct. 315 (1934); Beneficial Corp. v. Federal Trade Comm'n, 542 F.2d 611 (3d Cir.), cert. denied, 430 U.S. 983, 96 S. Ct. 1679 (1976); General Motors Corp. v. Federal Trade Comm'n, 114 F.2d 33 (2d Cir. 1940), cert. denied, 312 U.S. 682, 61 S. Ct. 550 (1941). Section 45(b) does require a showing of public interest in an FTC proceeding. See Federal Trade Comm'n v. Standard Oil of Calif., 449 U.S. 232, 101 S. Ct. 488 (1980); Federal Trade Comm'n v. Klesner, 280 U.S. 19, 50 S. Ct. 1 (1929); Exposition Press, Inc. v. Federal Trade Comm'n, 295 F.2d 869 (2d Cir. 1961), cert. denied, 370 U.S. 916, 82 S. Ct. 1554 (1962).

15. In addition to the rule of statutory construction applicable to "borrowed" statutes referred to in the cases cited at note 2, supra, the language of La. R.S. 51:1406(4) (1987), "[a]ny conduct which complies with section 5(a)(1) of the Federal Trade Commission Act [15 U.S.C. § 45(a)(1) (Supp. 1987)], as from time to time amended, any rule or regulation promulgated thereunder and any finally adjudicated court decision interpreting the provisions of said Act, rules and regulations [are exempt from La. R.S. 51:1405(A) (1987)]," is, by negative implication, supportive of the proposition.

16. 509 So. 2d 134 (La. App. 1st Cir. 1987).

17. The FTC Rule in question is entitled "Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures." 16 C.F.R. § 436 (1987).

tion, or unethical conduct.[18] The *Belt Center* decision is not only at odds with the rule of statutory construction aforementioned,[19] it also engrafts elements of proof nowhere found in section 1405(A). Moreover, given the difficulty of proving fraud, and given that there is no private right of action under the FTC Act,[20] the decision is a virtual invitation for overreaching by franchisors, and by sellers and lenders operating under Trade Regulation rules as to consumers' claims and defenses,[21] door-to-door selling,[22] credit practices[23] and used car sales.[24]

A franchise agreement does not involve a consumer in the sense of one who undertakes an obligation primarily for personal, family, or household purposes; rather, the franchisee has a profit motive.[25] The FTC, however, has documented the similarities between franchisees and

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18. 509 So. 2d at 137. Cf. Martin v. International Dryer Corp., 637 F. Supp. 101 (E.D.N.C. 1986) (a violation of a disclosure rule of the Consumer Product Safety Commission did not establish per se that the product in question presented an unreasonable or substantial risk of harm). Ironically, a showing of fraud in the *Belt Center* case would not have been impossible. The case of Westbury Small Business Corp. v. Ballarine, 125 A.D.2d 462, 509 N.Y.S.2d 569 (N.Y. App. Div. 1986), affirmed a finding of franchisor fraud premised on a knowing failure to disclose material facts.

19. See supra text accompanying notes 1-5 and 15. The court's decision is at odds with the decision of the New Jersey Supreme Court in Morgan v. Air Brook Limousine, Inc., 211 N.J. 101, 510 A.2d 1197 (1986), which reached the conclusion that a failure of compliance with the Franchising Disclosure rule was a per se violation of the New Jersey consumer fraud law:

> The Rule establishes basic minimum standards for lawful business conduct in the sale, offer for sale and advertising of franchises or business opportunity ventures. It is designed to prevent deception or unfairness in such transactions by prohibiting certain conduct and by imposing affirmative obligations upon those who engage in such transactions. The Rule is a recognition that such transactions often involve consumer commitment of substantial dollars in an attempt to secure self-reliance and security in an independent business, often without the availability of reliable, meaningful and adequate information to make an informed investment decision. Without such information, the consumer's attempt to share in the "American Dream" could result in a nightmare of significant personal and financial proportions.

510 A.2d at 1205. See also Bailey Employment Sys. v. Hahn, 545 F. Supp. 62 (D. Conn. 1982), aff'd, 723 F.2d 895 (2d Cir. 1983) (the FTC rule specifically declares the failure to disclose to be an unfair or deceptive act or practice, and no proof of reliance, or of intent to deceive is required; a violation of the state's unfair trade practices act may arise from a failure to disclose material information).

20. See Holloway v. Bristol-Myers Corp., 327 F. Supp. 17 (D.D.C. 1971), 485 F.2d 986 (D.C. Cir. 1973).

21. 16 C.F.R. § 433 (1987).

22. 16 C.F.R. § 429 (1987).

23. 16 C.F.R. § 444 (1987).

24. 16 C.F.R. § 455 (1987).

25. Under the Louisiana deceptive practices provisions, the protection of section 1405(A) is not limited to those "consumers" who have a non-profit motivation. See La. R.S. 51:1402(1) (1987).

consumers in its Statement of Basis and Purpose for the Franchising Disclosure Rule.[26] At best, the *Belt Center* decision only imposes a

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26. In its investigation the FTC reported:

> It is the nature and context of this setting which has permitted the abuses detailed below to flourish. Specifically, it is apparent from the record that a serious informational imbalance exists between prospective franchisees and their franchisors. This imbalance has been shown to exist, "even with the best intentions for fair treatment" of franchisees by franchisors. As noted by Professor Urban Ozanne, in a statement presented to the commission on the first proposed rule:
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> "The prospective franchisee does not approach the contract negotiations with the franchisor as an equal. The usual tremendous economic disparity between the parties to the franchise agreement is obvious. Moreover, a severe informational disparity exists as well. First, the franchisor or his franchise salesman sets before the franchisee a franchise agreement that is long and complicated. The franchisee or his attorney is seldom in a position to fully evaluate this document or its implications. Second, the franchisor has substantial experience in negotiating with franchisees, while this may be the franchisee's one and only contract negotiation. Third, the franchisor presents the information about the franchise and its sales and profits. Unlike the franchisee, he knows how much of the information is fact and how much puffery. . ."
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> The impact of this "informational imbalance" is particularly acute in franchising where many prospective franchisees possess a low level of business sophistication. The relative lack of business sophistication is demonstrated by numerous material and comments on the public record. For example, in *The Economic Effects of Franchising*—a detailed study of "fast food" franchising undertaken by Professors Ozanne and Hunt—it was reported that ". . . 68% of our sample of franchisees did not own a business prior to their franchised business and half the franchisees had incomes below $10,000 prior to buying their franchise." This relative lack of business experience and low capitalization is quite striking in light of the nature of franchising—a "highly complex, dynamic and changing area, with varied sophisticated business, financial and legal techniques and complications." Given the complex nature of most franchising operations, it is somewhat surprising that a group of relatively "unsophisticated" persons enter a field which requires such a significant degree of business acumen. One of the reasons accounting for the involvement of such persons in franchising is the "get rich quick" claims utilized by many franchisors in advertisements and other promotional materials. As indicated by numerous franchisee complaints, such claims often induce a person who has had little or no formal business training into believing that he or she may earn a great deal of money with little effort and in spite of a lack of experience. As further illustrated by such complaints and related public record materials, such "get rich quick" claims frequently either are unsubstantiated by the franchisor, or they misrepresent material facts with regard to the "potential earnings" of a particular franchise business. . . In this regard, the susceptible nature of prospective franchisees to such claims of "instant success" created the potential for serious economic injury as a result of concealment or misrepresentation of the material terms of the franchise business under consideration.

Statement of Basis and Purpose Relating to Disclosure Requirements and Prohibitions Concerning Franchising and Business Opportunity Ventures, CCH Business Franchise Guide para. 6304.

difficult burden of proof on franchisees and consumers in cases involving violations of FTC Trade Regulation rules; at worst, the decision imposes an across-the-board requirement that private litigants under Louisiana Revised Statutes 51:1405(A) prove fraud, scienter, reliance (and therefore deception) or unethical conduct—none of which are statutorily required.

In *Pizzaloto v. Hoover Co.*,[27] by contrast, the Fifth Circuit Court of Appeal of Louisiana, citing favorably *Hinchliffe v. American Motors Corp.*,[28] a decision under the Connecticut Unfair Trade Practices Act, has recognized what the *Belt Center* decision does not: that state unfair trade practices acts have been adopted so as to eliminate the difficult proof problems in fraud cases—the plaintiff in an unfair trade practices act need not prove misrepresentation or other fraudulent conduct, nor reliance thereon, nor that the representation or suppression of the truth became part of the basis of the bargain. Indeed, the judicial-legislation of such requisites has the effect of blue-penciling the word "unfair" from Louisiana Revised Statutes 51:1405(A) for, given that any *deceptive* act or practice is inherently unfair, the use of the word "unfair" in section 1405(A) must have been intended to mean something beyond "deception." If one accepts the correctness of the *Moore v. Goodyear Tire & Rubber*/FTC definition of unfair,[29] a requirement of proof of intent by the defendant emasculates the remedy of the Louisiana Deceptive Practices Act.

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27. 486 So. 2d 124 (La. App. 5th Cir.), writ denied 488 So. 2d 202 (1986).

28. 184 Conn. 1216, 440 A.2d 810 (1981). See also Urling v. Helms Exterminators, Inc., 468 So. 2d 451 (Fla. Dist. Ct. App. 1985). Cf. D.D.D. Corp. v. Federal Trade Comm'n, 125 F.2d 679 (7th Cir. 1942) (holding that the FTC Act itself does not require that a violation of the act rise to the level of fraud).

29. See supra text accompanying notes 3-6.