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TRIAL

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Fair Play for Consumers

by U.S. Senator Joseph D. Tydings (D.-Md.)

For most of Anglo-American legal history, the law has uncompassionately insisted: "Caveat emptor—the buyer beware!" [1]

Whatever justification there may have been for such a policy in the early stages of our economic development, its chief effect in today's complex market is to place an undue burden on the contractual party least capable of carrying it. Too often the modern consumer is unable to assess the technical qualities of the product he purchases, to resist sophisticated sales campaigns, or to comprehend the multitude of credit plans and financial "deals" that he may be offered. Every year billions of dollars are wasted by consumers through the purchase of misrepresented goods.

Although the least educated and the more impoverished segments of society—those who can least afford it—suffer the most, all levels of society are affected. Commissioner Mary Gardiner Jones of the Federal Trade Commission characterized the situation this way:

"No matter how informed and sophisticated the consumer, deception will take its toll and the very morality of the community is at stake when there is no effective legal action to be taken against such dishonest merchants." [2]

Fortunately, in the last few years private groups, legislatures and law enforcement officers have begun to recognize the importance of protecting consumer interests.

Campaigns against those who defraud and deceive consumers have intensified. Consumer councils have developed on state and local levels across the country, and the voice of the consumer has begun to receive a hearing in legislative halls.[3]

Public awareness of the need for consumer-protection programs has had some salutory effects, but has not significantly reduced the incidence of fraud. False advertisers, loan sharks and others of their ilk are still making exorbitant profits at the expense of the unwary consumer.

In sum, despite good intentions and the proliferation of consumer protection laws and agencies, our society continues to require that the "buyer beware."

Ralph Nader estimates that "at least 95% of illegal consumer abuses are never adjudged to be such by our legal system. The arm of the law . . . never reaches these abuses, thereby permitting an 'overworld' of corporate crime which reaps billions yearly from the defenseless consumer." [4]

The activities of the Federal Trade Commission indicate the weaknesses of the "agency" approach to the prevention of consumer frauds. Commissioner Ralph Elman, of the Federal Trade Commission, recently charged that his agency is marked by "waste, inefficiency and indifference to public interest." [5]

The 29 years it took the FTC to bring the Holland Furnace Company to task demonstrates clearly the ineffectiveness of administrative agencies in providing consumer remedies.

Complaints about high pressure tactics were made against the company as long ago as the early 1930's.[6] In December 1936, the company agreed to an FTC consent order against certain misleading advertising claims.[7] Although complaints against the company continued,[8] a second proceeding was not initiated by the FTC until 1954.[9]

Four years later, a cease and desist order was issued prohibiting Holland "from engaging in a sales scheme . . . whereby its salesmen gain access to homes by misrepresenting themselves as official 'inspectors' and 'heating engineers' and thereafter dismantling furnaces on the pretext that this is necessary to determine the extent of necessary repairs." [10] For seven years, Holland Furnace Company ignored the court decree enforcing the cease and desist order. Finally in 1965, the company was heavily fined for contempt of court.[11]

The danger of overdependence on public enforcement agencies is obvious:

- Delay is inherent in a bureaucracy.
- Administrative budgets and personnel are limited and in some cases the statutory structure or powers of an agency may inhibit its effectiveness.
- More often than not, such agencies lack effective sanctions to enforce their decrees.[12]

The consumer may, of course, initiate a private action for fraud or for rescission of a sales contract on the basis of misrepresentation. In most cases, however, this ability is more theoretical than real. Law suits are costly. The financial loss to a single consumer is not usually large enough to make individual litigation practicable. His court costs and attorney's fees may far exceed the restitution he is likely to receive even if he prevails in his suit.

But while administrative agencies may be ineffective and the cost of an individual suit may be prohibitive, many persons acting together as a defrauded class could afford to enforce their individual rights.[13] A consumer class action compensates for the inability of individual consumers to litigate small individual losses by enabling one or more representatives of a group of consumers with similar injuries to place group injury in issue.

The aggregate group claim is generally large enough to warrant the outlay of the necessary expenses and, more significantly, to make it possible to obtain private counsel on reasonable terms.

In addition to being economically infeasible, individual suits, even if their success is assumed, are unlikely to prove an effective deterrent to the dishonest company. In fact, many irresponsible companies probably treat the loss of an occasional small judgment as one of the risks of the trade; a risk made worthwhile by their continued high profits through misrepresentation or other deceit.

It is noteworthy that Holland Furnace Company continued its depreda-

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tions notwithstanding a number of instances in which it was successfully sued for common law fraud by individual home owners[14] and a number of other instances in which individual home owners successfully defended contract actions by Holland Furnace Company on the grounds that their contracts had been induced by fraud.[15]

The consumer class action, on the other hand, has beneficial effects that extend beyond the restitution of individual damages to the injured consumers. The mere existence of an effective class action remedy will deter improper conduct. The potential defendant is forced to consider not only the possible direct economic loss from a class action, but also the potential visibility, publicity, and public reaction and the resulting loss of good will.[16]

Although the dishonest merchant may be able to safely ignore the separate complaints of many individuals, he cannot afford to disregard the public criticism of many voices in unison.

Experience in states whose courts are amenable to consumer class actions reveals the potential protection for consumer rights that this procedural device can provide.

In California, for example, the courts permitted an action to be brought by a taxicab customer on behalf of himself and others similarly situated to recover allegedly excessive charges by a taxicab company accumulating over a four-year period.[17] The court ruled that the action could properly be brought as a class action since the complaint showed the existence of an ascertainable class as well as a defined community of interest in the questions of law and fact affecting the parties to be represented.

Although the plaintiffs' individual claims were relatively negligible, the aggregate claim of over $100,000 made litigation feasible. The court, recognizing that fact, stated:

"[A]bsent a class suit, recovery by any of the individual taxicab users is unlikely. The complaint alleges that there is a relatively small loss to each individual class member. In such a case separate actions would be economically infeasible. Joinder of plaintiffs would be virtually impossible in this case. It is more likely that, absent a class suit, defendant will retain the benefits from its alleged wrongs. A procedure that would permit the allegedly injured parties to recover the amount of their overpayments is to be preferred over the foregoing alternative.[18]

An Illinois court has similarly ruled proper a class action brought on behalf of an estimated six million Montgomery Ward charge-account holders who claim to have unwittingly subscribed to a credit life, disability and dismembership insurance plan on their accounts with Ward.[19]

A class action brought on behalf of the charge account holders was held to be a proper form of action by the court on the ground that the plaintiff had stated a good cause of action, that he adequately represented the class involved and that the class action was "singularly appropriate to the controversy presented by the complaint." [20] The class action was the only practicable way to litigate the claims, as the Illinois court saw.

Class actions would appear to be an invaluable weapon in the consumer's arsenal, but the class action procedure of many of the states is outmoded and archaic. All states provide some form of class actions, but the manner in which they define the procedure often makes it unavailable in the usual consumer-fraud situation.

The New York cases, for example, require a unity of interest among the members of a class that approximates the test for compulsory joinder of parties.[21] They also require that class members desire identical remedies.[22] The result of this view is that to date consumer class actions are summarily dismissed in New York.[23]

Similarly, in *Spear v. H. V. Greene Co.*,[24] a Massachusetts court refused to allow 40 plaintiffs to bring a suit on behalf of 60,000 others although the alleged facts indicated that the defendant company had employed similar fraudulent methods to swindle many individuals out of sums aggregating to a substantial amount.

The court recognized that "the frauds charged in the bill are great in magnitude and peculiarly vicious in their nature in that they were designed chiefly to victimize the ignorant and frugal poor." [25] Nevertheless, the court dismissed the class action, the only feasible means of suit, on the ground that the common interest required for a common-law class action was not satisfied. The court interpreted that requirement to mean that the plaintiffs must have suffered virtually identical wrongs. Fortunately for the citizens of Massachusetts, that state has recently enacted strong consumer class action legislation,[26] but the climate for such actions remains inhospitable in most other states.

Moreover, as a result of a recent U.S. Supreme Court decision, *Snyder v. Harris*,[27] the federal courts appear to be even less hospitable to consumer class actions than state courts. Prior to *Snyder v. Harris* the provisions of Rule 23 of the Federal Rules of Civil Procedure, as amended in 1966,[28] appeared to establish a procedural basis for the maintenance of consumer class actions in those cases where a basis for federal jurisdiction existed.[29] But in that decision the Supreme Court ruled that separate and distinct claims cannot be aggregated to meet the required $10,000 jurisdictional amount.

This ruling in effect makes the Rule 23 action, in itself the most modern class action procedure in the United States, unavailable to the defrauded consumer who has a claim of less than $10,000, even if he can satisfy the necessary diversity of citizenship or federal question requirements for federal jurisdiction.

It has been suggested that, except for the effects of *Snyder v. Harris*, diversity forms a sufficient basis for bringing most instances of mass fraud into federal court.

I cannot agree that a reversal of *Snyder v. Harris* would in itself be sufficient.

First, much mass fraud is perpetrated in localized urban areas and may not involve any diversity of citizenship. A usurious finance company operating in Cleveland may never loan money to anyone who is not domiciled in Ohio. Moreover, even if a borrower from another state could conceivably be located, a lawyer both practically and ethically must work with the client who enters his office. He cannot finance a search for such a borrower or solicit his business.

In the spring of 1969, I introduced legislation to establish a meaningful private consumer remedy. S. 1980 provided for consumer class actions in federal courts in cases where state consumer protection laws have been violated. Similar legislation was introduced in the House by Congressman Bob Eckhardt of Texas with whom I have worked closely.

The bill was designed to reverse the effects of *Snyder v. Harris* and, in addition, to broaden the basis for federal jurisdiction over consumer fraud. By doing so, it would afford the liberal machinery of federal Rule 23 for joinder of all persons in like situations involving deception, fraud or other illegal overreaching of consumers.

In July, the Senate Subcommittee on Improvements in Judicial Machinery, of which I am chairman, held hearings to consider the merits of this legislation. Each of the witnesses—including Virginia Knauer, Special Assistant to the President for Consumer Affairs; Ralph Nader, the "consumer watchdog"; and Bess Myerson Grant, Commissioner of the Department of Consumer Affairs for the City of New York—called for increased consumer access to the broad class action

rule available in the federal courts.

In her testimony, Mrs. Knauer presented a somewhat different approach than S. 1980, suggesting legislation to permit consumer class action suits for the broad range of practices condemned as "unfair or deceptive" under the Federal Trade Commission Act. After close study of Mrs. Knauer's testimony and in depth discussion between Mrs. Knauer's staff and our own, I introduced S. 3092 combining Mrs. Knauer's complimentary proposal with that contained in S. 1980; Congressman Eckhardt introduced the same bill in the House of Representatives.

Basically, S. 3092 makes unlawful and subject to class suits, acts in defraud of consumers that affect commerce, without regard to the amount in controversy.

An act in defraud of consumers is defined as including two distinct things: (1) an unfair or deceptive act or practice as condemned in section 5(a) Federal Trade Commission Act, and (2) an act that gives rise to a civil action by a consumer or consumers under state, statutory or decisional law for the benefit of consumers. Diversity of citizenship is not required. Federal jurisdiction is premised upon the commerce power.

Such a suit in federal court would apply the laws of the state in exactly the same manner that the federal courts apply such law in a diversity of citizenship cases. Thus, the court in any suit would be dealing with a definite body of law in a manner in which it is accustomed to deal with such law.

Perhaps the most significant provision of S. 3092 is section 4(d) which governs the award of attorneys fees. If an action has been successful, the attorney will receive an award of a reasonable fee, based on the value of his services to the class. A 10% guideline is set, subject to adjustment. The guideline has received some criticism and will certainly be subjected to further study.

I have become increasingly convinced that the private bar is the untapped reservoir of consumer power. S. 3092 is designed to insure the ready availability of competent well-compensated counsel. By doing so, it guarantees a major increase in legal muscle for the consumer.

Significantly, that muscle will be in the form of private legal actions, the traditional method of effectively redressing grievances in this country. The bill does not require the creation of any new agencies with the accompanying bureaucratic expenses. It depends only on existing legal processes.

The bill has therefore been attacked as "an ambulance chasing" bill, which, in my opinion, is slandering the bar, casting disrepute on our legal system, and bringing no credit upon the critics.

Unfortunately that attack and other pressures have induced the Administration to retreat from the strong proposal originally advocated by Mrs. Knauer. The bill that the President finally sent to Congress on October 30 offered a sorry substitute for meaningful consumer class action protection: a private remedy that is not self-starting but must be triggered by successful determination of a government suit.

Not only will this make for excessive delay, but it leaves to a government agency rather than an injured party the power to determine which consumers are to be protected. Moreover, even the government suits would be limited to a series of defined forms of fraud, forms that unscrupulous merchants can change as rapidly as the legislation can be enacted. The Administration's proposal will not provide the American public with meaningful protection. S. 3092 will.

It is my hope that a perfected version of the Consumer Class Action Protection Act will be enacted and will operate to provide the consumer with the meaningful remedy that has too long been denied him. The time has come to redress the imbalance of commercial power that puts the consumer at the mercy of the overreaching merchant. □

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1. See *Kellogg Bridge Co. v. Hamilton*, 110 U.S. 108, 116 (1884).

2. Quoted in Magnuson, *The Dark Side of the Market Place*, 59 (1968).

3. For example the Uniform Consumer Credit Code (Rev. Final Draft, 1968), a comprehensive effort to revise state regulation of loans, credit sales, and leases was introduced in a number of state legislatures in 1969 and enacted in Utah.

4. *Hearings on S. 1980 Before the Subcom. on Improvements in Judicial Machinery of the Senate Com. on the Judiciary, 91st Cong., 1st Sess.*

5. *The Washington Post*, September 11, 1969, at A2, Col. 1-2.

6. *Consumer Bulletin* at 26 (April 1965).

7. 24 F.T.C. 1413-14 (1936).

8. *Consumer Bulletin* at 25-26 (April 1965).

9. See 55 F.T.C. 55 (1958).

10. *Id.* at 91, *aff'd*, 295 F. 2d. 302 (7th Cir. 1961).

11. In Re Holland Furnace Co., 241 F. 2d. 548 (7th Cir.), *cert. den*, 381 U.S. 924 (1965).

12. See Dixon, *Federal State Cooperatives to Combat Unfair Trade Practices*, 30 State Gov't 37 (1966); Mendell, *N.Y. Bureau of Consumer Frauds and Protection*, 11 N.Y.L.J. 603 (1965); O'Connell, *Consumer Protection in the State of Washington*, 39 State Gov't 230 (1966); Rice, *Remedies, Enforcement Procedures and the Quality of Consumer Transaction Problems*, 48 B.U.L. Rev. 559 (1968).

13. See Dole, *Consumer Class Actions under Recent Consumer Credit Legislation*, 44 N.Y.U.L. Rev. 80 (1969); Staars, *The Consumer Class Action*, 49 B.U.L. Rev. 211 (1969).

14. E.g., *Holland Furnace Co. v. Robson*, 157 Colo. 378, 402 P. 2d. 628 (1965).

15. E.g., *Holland Furnace Co. v. Korth*, 43 Wash. 2d. 618, 262 P. 2d. 772 (1953).

16. See *Dolgow v. Anderson*, 43 F.R.D. 472, 485-88 (E.D.N.Y. 1968); Dole, *Consumer Class Actions Under the Uniform Deceptive Trade Practices Act*, 1968, Duke L.J. 1101, 1103.

17. Daar v. Yellow Cab Co., 63 Cal Rptr. 724, 433 P. 2d. 732 (1967).

18. *Id.* at 746; accord, *Eisen v. Carlisle & Jacquelin*, 391 F. 2d. 555, 563 (2d. Cir. 1968).

19. *Holstein v. Montgomery Ward & Co.*, No. 68, CH 275 (Ill. Cir. Ct., Cook County, 1969).

20. *Holstein v. Montgomery Ward & Co.* at 27.

21. E.g., *Society Milion Athena, Inc. v. National Bank of Greece*, 281 N.Y. 282, 22 N.E. 2d. 374 (1939); *Brenner v. Title Guarantee & Trust Co.*, 276 N.Y. 230, 11 N.E. 2d. 890 (1937).

22. E.g., *Gaynor v. Rockefeller*, 15 N.Y. 2d. 120, 204 N.E. 2d. 627, 256 N.Y.S. 2d. 584 (1965).

23. *Hall v. Coburn Corp.*, 160 N.Y.L.J., No. 28, at 2 (Sup. Ct. Bronx County, 1968), *aff'd mem.* (1st Dept. 1969), appeal pending.

24. 246 Mass. 259, 140 N.E. 795 (1923).

25. *Id.* at 797.

26. Ch. 690, 814, 1969 Acts, Commonwealth of Massachusetts, amending Ch 93A, General Laws of Massachusetts.

27. 394 U.S. 332 (1969).

28. See Donelan, *Prerequisites to a Class Action Under New Rule 23*, 10 B.C.L. Rev. 527 (1969); Kaplan, *Continuing Work of the Civil Committee: 1966 Amendments of the Federal Rules of Civil Procedure I*, 81 Harv. L. Rev. 356, 375-400, 414-16 (1967).

29. *The Class Action—A Symposium*, 10 B.C. Ind & Com. L. Rev., Spring (1969).