

It is ordered, That respondents Records, Inc., a corporation, and Cecil Steen, individually and as an officer of said corporation, shall, within sixty (60) days after service upon them of this order, file with the Commission a report in writing, setting forth in detail the manner and form in which they have complied with the order to cease and desist.

IN THE MATTER OF
ALLIED MERCHANDISING, INC., ET AL.

ORDER, ETC., IN REGARD TO THE ALLEGED VIOLATION OF THE
FEDERAL TRADE COMMISSION ACT

Docket 7399. Complaint, Feb. 6, 1959—Decision, Apr. 18, 1960

Order requiring cigarette vending machine distributors in University City, Mo., to cease making in advertising deceptive employment offers, exaggerated earnings claims, false assurances of assistance, and other misleading representations.

Mr. Brockman Horne for the Commission.

Mr. Morris A. Shenker, of St. Louis, Mo., for Allied Merchandising, Inc., Peter A. Krane, and William Dardick.

Mr. James J. Rankin, of St. Louis, Mo., for Vern F. Hawkins.

INITIAL DECISION BY WALTER R. JOHNSON, HEARING EXAMINER

In the complaint issued by the Commission on February 6, 1959, respondents are charged with the use of unfair and deceptive acts and practices and unfair methods of competition in commerce in violation of the provisions of the Federal Trade Commission Act, in connection with the sale of and distribution of vending machines, including cigarette vending machines. In due time, after answer, six days of hearings were held at St. Louis, Missouri, Wichita, Kansas, Denver, Colorado, Dallas, Texas, and Houston, Texas. At the hearing held in the last mentioned city on June 30, 1959, counsel supporting the complaint closed his case. On September 10, 1959, the respondents electing not to offer any evidence, an order was entered closing the record for the reception of evidence and further

directing that the parties may file proposed findings up to and including October 30, 1959. Proposed findings were submitted in support of the complaint but not on behalf of the respondents. The proposed findings are sustained by the evidence and are approved.

Respondent Allied Merchandising, Inc., is a corporation organized and existing under the laws of the State of Missouri, with its principal office and place of business at 7307 Olive Street Road, University City, Missouri. Respondent Peter A. Krane's address is the same as that of the corporate respondent. Respondent William Dardick's address is c/o Bernard J. Mellman, Esq., 408 Olive Street, St. Louis, Missouri. Respondent Vern F. Hawkins' address is c/o James J. Rankin, Esq., 706 Chestnut Street, St. Louis, Missouri. From September 26, 1957 to July 24, 1958, Krane was president, Dardick was vice president and Hawkins was secretary-treasurer of said corporation. During said period the three were the sole stockholders and directors of the corporation and, as such, formulated, directed and controlled the policies, acts and practices of said corporation. On July 24, 1958, Dardick and Hawkins resigned as officers and directors and sold their stock to Krane, and from that date to the present Krane has been the sole stockholder of said corporation and controlled its policies and acts. Each of the individual respondents has been active in making the representations and sales as alleged in the complaint.

Respondents Allied Merchandising, Inc. and Peter A. Krane are now, and for sometime last past have been, engaged in the business of selling and distributing machines used for the purpose of selling merchandise, including cigarette vending machines. Respondents William Dardick and Vern F. Hawkins were likewise engaged during the period that they served as officers and directors of said corporations.

Respondents have done business on a nation-wide scale and have caused their vending machines, when sold, to be shipped from the states of Iowa and Missouri to purchasers residing in other states of the United States and have maintained a course of trade in their vending machines in commerce, as "commerce" is defined in the Federal Trade Commission Act.

In the course and conduct of their business as aforesaid, the respondents have been, and now are, in substantial competition, in commerce, with corporations, firms and individuals engaged in the sale of vending machines.

The respondents' first step in a program of fraud and deceit is the placing of advertisements in newspapers published in the various

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states of the United States which supplies them with leads to prospective purchasers of their machines.

Typical of said advertisements is one which appeared under the classified column "Business Opportunities" in the Wichita Eagle, a newspaper published in Wichita, Kansas:

WANTED

MALE OR FEMALE

FULL OR PART TIME

To service route of cigarette machines. No selling or soliciting. Route established for operator.

Must have:

1. Automobile
2. References
3. \$995 to \$1995 cash available for inventory

Write briefly about yourself and include phone number for personal interview. Eagle Box 528-B.

Under the classification of "Male-Female Help Wanted" the following appeared in "The Wyoming Eagle" of Cheyenne, Wyoming:

RELIABLE MAN OR WOMAN

FULL OR PART TIME

TO SERVICE ROUTE

of

CIGARETTE MACHINES

NO SELLING OR SOLICITING

ROUTE ESTABLISHED

FOR OPERATOR

INCOME STARTS

IMMEDIATELY

\$995 TO \$1,995 CASH

REQUIRED

Please don't waste our time unless you have the necessary capital and are sincerely interested in expanding—we finance expansion—if fully qualified and able to take over at once write briefly about yourself and include phone number for personal interview.

The ads give the impression that an offer of employment is being made for persons to service an established route and the only investment required is that needed to purchase an inventory.

Persons answering the advertisements receive from the corporate respondent a form letter of acknowledgment signed by "Charles Davis" which reads in part: "Due to the tremendous response to this advertisement, it will be about a week or ten days before our Regional Director will call on you." "Charles Davis" is a fictitious name used by respondents in such letters and in future dealing

with their clientele through correspondence and telephone calls. Several days after mailing the letter of acknowledgment, a representative of respondents' calls upon a prospect. The testimony of all of the fifteen purchaser witnesses which appeared before the hearing examiner reveals that the same pattern of deception was employed in making the sales. With one exception all the sales, about which the purchaser witnesses testified, were made by either Krane, Hawkins or Dardick, the individual respondents.

The representative displays to the prospect a number of credentials, at times including air-travel, diner's and gasoline credit cards, some sort of Dun & Bradstreet card, and cards indicating membership in a Better Business Bureau and in the National Association of Manufacturers. The prospect is given the impression that he is dealing with an honorable business man who is worthy of the confidence and respect of his fellow man. The prospect is maneuvered to the dining room or other large table on which photographs of, and literature about the machines is spread. He learns that respondents' offer is not one of employment to service an established vending machine route and that an investment other than for inventory is required. Respondent representative writes on a piece of paper a column of figures purporting to give the costs which will be incurred and the profits which will be realized by the prospect upon the purchase of machines. The figures do not take into account the gas and upkeep of automobiles used to service the machines, machine repair, license fees and loss and damage caused by burglaries.

The prospects are told the profits on ten machines costing approximately \$2,000 will net from \$90 to \$100 per week; the figures are based on each machine selling fourteen cartons of cigarettes a week; not more than six hours per week of purchaser's time will be required to service such machines; respondents have made a survey, or will make a survey before machines are installed, of the surrounding area to determine profitable locations and they have trained men who went around and secured locations; that by the time purchasers' machines arrived locations would be picked out which would produce the promised profits and respondents' men would install the machines in such locations; respondents' representative would return after a period of time, usually ninety days, to check and determine whether or not purchasers' machines were producing the promised profits, and if a location proves unprofitable respondents will relocate machines; should the purchasers later become dissatisfied respondents will, upon request, resell them to others and they will get the full purchase price back; Allied requires a

purchaser to pay a royalty of two cents per carton on all cigarettes sold through the machines and such royalty is more important to Allied than the profit it might realize from the sale of cigarette machines; arrangements are made for the purchaser of cigarettes at better prices than the prospect can secure for himself; substantial amounts are paid by manufacturers of cigarettes for offering their brand for sale through the machines.

If the prospect decides to purchase machines, he signs a printed document entitled "Purchase and Sales Agreement," to which the representative of the respondent adds his signature, in the company of witnesses, subject to acceptance by the company. The purchaser is required to make a down payment which must be a bank draft, certified check, express or post office money order. Almost immediately the corporate respondent, over the signature of "Charles Davis," dispatches a letter to the purchaser accepting his order. The letter states that the machines are ready to be shipped and upon receipt of the balance due they will be shipped. The purchaser then remits the balance and receives another letter stating that his order has been forwarded to "the factory" or "our factory" for shipment, and further stating that Allied will try to have its location man in the purchaser's area at the same time the machines arrive "so you may be set up in business quickly." In due course the machines arrive, usually a small seven-column machine of inferior construction, each column providing room for no more than two cartons (20 packs) of cigarettes. However, the location man is never present when the machines arrive. The purchaser waits for the location man to show up, in the meantime telephoning and writing Allied's office in University City, Missouri, to find out why he is not on hand. Finally, the location man arrives and the purchaser learns from him that no survey has been made by Allied to determine profitable locations. One of the witnesses testified that when she asked the location man, who was having difficulty finding locations for her machines, about placing the machines according to the survey, she received this reply: "That's a lot of malarkey. They don't survey it. They put the ad in the paper, they sell the machines and then it's up to me to find a place to put them." In some instances the location man will go by himself, and at times the purchaser will accompany him, to solicit and obtain locations in which to install the machines. In other instances the location man will find locations for and install only some of the machines and leave it to the purchaser to find locations and to install the others. The attitude of the location man, who is paid by Allied \$10 for each machine installed, is reflected by the following incident.

The owner of the establishment where a machine was being installed told the location man: "There is no sense putting a machine in here, we don't have any traffic," and the location man said, "I don't care, all I want to do is hang these machines and give her a location and get out of Cheyenne and on back to Denver."

Sometimes the location man gives to the purchaser the name of a wholesaler from whom cigarettes may be bought, but in no instance was it shown that such wholesaler offered the purchaser a better price than what he could have secured for himself. Many times the purchaser is not furnished the name of any wholesaler.

Upon the departure of the location man, the purchaser fills his machines with cigarettes. As time passes he finds that nowhere near the promised sales are being made. Instead of sales of fourteen cartons per week per machine, the machines in some cases make no sales at all. Sales of as little as one-half carton per week are not unusual. None of the locations secured for the fifteen purchaser witnesses sold as many cigarettes as promised and, in fact, none sold more than six cartons per week. Sales of four or more cartons were unusual. Contrary to the representation of the individual who sold the machines, neither he nor any other representative of respondents calls again to find out how a purchaser is succeeding in the operation of his machines. When purchasers contact Allied stating that locations secured by it are not making satisfactory sales and requesting that the machines be relocated they get little satisfaction. Illustrative is the situation where a purchaser, after telephoning Allied several times, received a letter reading: "At the present time, we have no planned itinerary for your area. However, just as soon as possible, which we believe will be in the near future, I will dispatch a location man to your area for the purpose of locating your machines. In the meantime, realizing that the task of relocating machines might be a hard one for a woman, if you can obtain the help of some other person capable of doing this job, I will be happy to defray your costs to the amount of Six Dollars (\$6.00) per machine." The purchaser later called again and "Mr. Davis" told her that Allied's obligation to her was completed. In another instance, when the purchaser requested the relocation of his machines and asked when Krane was coming back, he received as reply from "Charles Davis" that Krane was away on business and his return was indefinite. "As has happened occasionally in the past," "Davis" continued, "some machines need to be relocated. Insofar as the success of this business depends on the ingenuity and active interest of the individual, I am suggesting that you take a more interested and positive approach toward your business."

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In the end the purchaser has to relocate his machines and where this is done he usually find the new location produces little, if any, better sales. In no case do they provide the volume represented by respondents.

Finally, most of the purchasers abandon any attempt at operating the machines. Some request Allied to repurchase or resell their machines, but the typical reply they receive from Allied is that its obligation to purchaser has been fulfilled or that the purchaser should insert an advertisement in his local newspaper to sell his machines. In a few instances the purchasers have prevailed upon Allied to repurchase the machines at about 50 percent of the purchase price. Some purchasers do not request Allied to repurchase or resell their machines feeling, in light of the experience already had with Allied, that such a request would be a waste of time.

One of the witnesses who had purchased ten machines for \$2,190, decided not to install them. He had been told by men in his town, who had cigarette machines, that the seven-column machines delivered to him were only suitable for poor locations and he would not make much out of them. He communicated with Allied by letter and telephone requesting a refund of the purchase price. Allied offered to remit \$1,100 by check upon receipt of the unused machines. The witness testified as to the reason why he rejected the offer: "Well, I wanted them to send \$1,100 down here to be paid to me on receipt of the machines, but they wouldn't do that. They said I would have to prepay them up there and if they were all right, then they would send me the money. I just figured that was taking too much of a chance. So I didn't send them." The purchaser finally disposed of the machines for about \$700.

A few of the purchaser witnesses have continued to keep their machines in operation, and in such instances at a slight profit or at a loss. Some purchasers experienced costly burglaries of their machines in which not only were money and cigarettes stolen but machines were damaged. Purchasers found that they were required to pay license fees on their machines. Only a few of the purchasers secured advertising allowances or subsidies, and those who did found it was insubstantial in amount.

The purchaser witnesses were persons with comparatively little means who wanted to supplement their incomes; two were widows, one trying to support herself and a small son on social security income and the other elderly, disabled and unemployed; two were retired individuals; one was a telephone operator recently displaced by the dial system and whose husband was totally disabled; one was an elderly part-time night watchman who could not do

hard work; one was an elderly man who had just sold his business; one was an elderly foreigner out of a job; one was a disabled and unemployed workman and one was the wife of an aircraft worker who wanted to earn more for their three children. Each of them bought from respondents from five to twenty-five machines at a cost running from \$995 to \$5,392.50.

All of the purchasers were without experience in operating vending machines and considering the competitive situation and the type of machines sold and delivered to them by the respondents, there was little likelihood that they would have any success.

Three experienced operators of cigarette vending machines testified in this case, and the following facts were developed: Competition between experienced operators for profitable locations is fierce; securing good locations depends to a good extent upon the experience of an operator in giving good service and upon personal contacts; a 10-carton-a-week location is quite difficult for even an experienced operator to secure; a new operator entering the market is at a distinct disadvantage in securing profitable locations; a major location is one which sells 20 cartons per week, a good location is one which sells 10 cartons a week, and a poor location is one which sells less than ten; an industrial location, such as a manufacturing plant or other establishment which does not attract customer traffic, is rated by the number of persons employed. A rule of thumb followed is that one pack of cigarettes will be sold each week for each employee; a commercial location is rated by the amount of customer traffic, either on foot or on wheels, which the location generates; restaurants and taverns are considered to be good locations, as well as supper clubs; all-night service stations are good, while those which close are not; the more profitable locations demand good-looking machines of the low console type which sit on the floor and which offer a wide variety of brands. Beginning in about 1957, the number of brands of cigarettes offered for sale increased greatly. This caused smaller machines, 6 to 9 columns, to become obsolete. There are about 40 brands of cigarettes on the market today, but experienced operators usually limit themselves to carrying about 20 brands. The minimum size machine which experienced operators have been buying since prior to 1957 is 14-column. Machines range up to 30-column in size; although experienced operators do operate some 7 and 9-column machines, they do so only because such machines have remained in their inventory for several years and operators have no way to profitably dispose of them. Said machines are located along routes of larger machines or placed along the side of a larger machine so that little

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expense is incurred in servicing them; it would be almost impossible for a man to make a net profit from the operation of only 7-column machines.

It is found that the charges alleged in the complaint have been established by the evidence.

Upon the findings of fact hereinbefore made, it is concluded and found:

1. The Commission has jurisdiction over all of respondents' acts and practices as alleged in the complaint.

2. The individual respondents are liable in their individual capacities.

3. The use by respondents of the false, misleading and deceptive statements and representations hereinabove referred to has had, and now has, the capacity and tendency to mislead and deceive members of the purchasing public into the erroneous and mistaken belief that said statements and representations were and are true and to induce the purchase of substantial quantities of their machines used for the purpose of vending merchandise because of such erroneous and mistaken belief. As a result thereof, substantial trade in commerce has been, and is now being, unfairly diverted to respondents from their competitors and injury has been, and is now being, done to competition in commerce.

4. The aforesaid acts and practices of respondents were, and are, all to the prejudice and injury of the public and of respondents' competitors and constituted, and now constitute unfair and deceptive acts and practices and unfair methods of competition, in commerce, within the intent and meaning of the Federal Trade Commission Act.

Upon the foregoing findings of fact and conclusions of law, the following order is hereby entered:

ORDER

It is ordered, That respondents Allied Merchandising, Inc., a corporation, and its officers, Peter A. Krane, individually and as an officer of said corporation, and William Dardick and Vern F. Hawkins, individually, and respondents' agents, representatives and employees, directly or through any corporate or other device, in connection with the offering for sale, sale, or distribution of machines and other devices used for the purpose of vending merchandise, in commerce, as "commerce" is defined in the Federal Trade Commission Act, do forthwith cease and desist from representing directly or by implication:

1. That any offer is an offer of employment when, in fact, the real purpose is to obtain purchasers of their machines, or other devices.
2. That an established route of operating machines or other devices is offered for sale.
3. That the only investment required of a purchaser is that needed to purchase an inventory.
4. That the earnings or profits derived from the operation of their machines or other devices are any amounts in excess of those which have been, in fact, customarily earned by operators of their machines or other devices.
5. That surveys have been or will be made by respondents to determine locations which would prove profitable for the installation of such machines or other devices.
6. That profitable locations will be secured for a purchaser's machines or other devices.
7. That, should a location of a purchaser's machines or other devices prove to be unprofitable, said machines or other devices will be relocated by respondents.
8. That no selling or soliciting is required of the purchaser in the operation of such machines or other devices.
9. That respondents will resell or repurchase the machines or other devices sold by them in the event the purchaser becomes dissatisfied with the profit derived therefrom and requests them to do so; or will resell or repurchase said machines or other devices for any other reason, unless such is the fact.
10. That respondents make arrangements whereby the purchasers of their machines or other devices may buy merchandise at wholesale prices.

It is further ordered, That the complaint be and it is hereby dismissed as to William Dardick and Vern F. Hawkins in their capacity as officers of respondent Allied Merchandising, Inc.

DECISION OF THE COMMISSION AND ORDER TO FILE REPORT OF COMPLIANCE

The Commission having by its orders of March 2, 1960, and March 15, 1960, extended until further order the date on which the initial decision of the hearing examiner would become the decision of the Commission; and

The Commission having determined that said initial decision is not appropriate in all respects to dispose of this matter:

It is ordered, That the initial decision be, and it hereby is, modified (1) by striking the sentence appearing on page 4 of the initial decision which begins with the words "The ads * * *" and ends

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with the words "an inventory," and (2) by substituting in lieu thereof the following paragraph:

"Another advertisement used by respondents was headed 'Owner Must Sell Established Vending Machine Route.' Through use of the foregoing advertisements, the respondents have represented that an offer of employment is being made to service an established route, that an established cigarette vending machine route is offered for sale and that no soliciting or selling or investment other than for inventory will be required."

It is further ordered, That the initial decision, as herein modified, be, and it hereby is, adopted as the decision of the Commission.

It is further ordered, That the respondents shall, within sixty (60) days after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with the order to cease and desist.