

Complaint

109 F.T.C.

IN THE MATTER OF

C & D ELECTRONICS, INC., ET AL.

CONSENT ORDER IN REGARD TO ALLEGED VIOLATION OF SEC. 5 OF THE
FEDERAL TRADE COMMISSION ACT*Docket C-3212. Complaint, March 6, 1987—Decision, March 6, 1987*

This consent order prohibits, among other things, a Jenison, Mich. manufacturer and marketer of cable television decoders from selling or distributing the decoders to any unauthorized purchasers and requires respondents to cease representing that: (1) consumers can lawfully own or use decoders; (2) the use of decoders is legal without authorization from a cable company; or (3) ownership or use of a cable decoder is similar to the ownership or use of a telephone. The consent order also requires respondents to make an affirmative disclosure with the sale of any of their cable television decoders.

Appearances

For the Commission: *Alan E. Krause.*

For the respondents: *G.R. McIneney*, Grand Rapids, MI.

COMPLAINT

The Federal Trade Commission, having reason to believe that respondents C&D Electronics, Inc., a corporation, and David Barwacz and Larry Bostelaar, individually and as officers of the corporation, have violated the provisions of Section 5(a) of the Federal Trade Commission Act, and it appearing to the Commission that a proceeding by it in respect thereof would be in the public interest, hereby issues its complaint and alleges that:

PARAGRAPH 1. Respondent C&D Electronics, Inc., is a Michigan Corporation with its principal place of business located at 2026 Chicago Avenue, Jenison, Michigan 49428.

PAR. 2. Respondent Larry Bostelaar is an individual residing at 7920 Ronson, Jenison, Michigan 49428. He is a stockholder, officer and director of C&D Electronics, Inc. Individually or in concert with others, he formulated, directed and controlled the acts and practices of respondent C&D Electronics, Inc., including the acts and practices alleged in this complaint.

PAR. 3. Respondent David Barwacz is an individual residing at 2532 Northborough Court, NE, Grand Rapids, Michigan 49505. He is a stockholder, officer and director of C&D Electronics, Inc. Individually

or in concert with others, he formulated, directed and controlled the acts and practices of respondent C&D Electronics, Inc., including the acts and practices alleged in this complaint. [2]

PAR. 4. Respondents at the times mentioned in this complaint maintained a substantial course of business, including the acts or practices hereinafter set forth, in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act.

PAR. 5. Respondents have been engaged in the manufacturing, advertising, distributing and selling of cable television decoders, descramblers, converter-decoders, and converter-descramblers which were capable of decoding or descrambling certain television signals transmitted by cable to subscribers of various cable television systems throughout the United States.

PAR. 6. Cable system operators provide decoders, descramblers, converter-decoders or converter-descramblers to their subscribers as part of the cable delivery system in order to determine and charge for the level of programming service used.

PAR. 7. Cable system operators routinely prohibit subscribers from attaching to their cable system any decoder, descrambler, converter-decoder, or converter-descrambler other than one provided by the cable system operator.

PAR. 8. Cable television decoders, descramblers, converter-decoders and converter-descramblers sold by respondents were designed and have been used to allow the unauthorized viewing of certain signals transmitted by cable television systems operating throughout the United States.

PAR. 9. The sales of respondents' cable television decoders, descramblers, converter-decoders and converter-descramblers have resulted in the loss to cable companies of potential or present cable service subscription revenues. As a result, legitimate cable subscribers pay higher prices for cable service or receive reduced services from the cable companies. In addition, municipalities granting the franchises to provide cable television service receive reduced franchise fees from the cable companies to the detriment of all consumers in the municipalities.

PAR. 10. Respondents' actions as described above have thus caused substantial and ongoing injury that is not outweighed by any countervailing benefits to consumers or competition and is not reasonably avoidable by consumers. [3]

PAR. 11. The acts and practices as herein alleged are to the prejudice and injury of the public and constituted unfair acts or practices in or affecting commerce in violation of Section 5(a) of the Federal Trade Commission Act.

Commissioner Azcuenaga was recorded as dissenting.

DECISION AND ORDER

The Federal Trade Commission having initiated an investigation of certain acts and practices of the respondents named in the caption hereof, and the respondents having been furnished thereafter with a copy of a draft of complaint which the Chicago Regional Office proposed to present to the Commission for its consideration and which, if issued by the Commission, would charge respondents with violation of the Federal Trade Commission Act; and

The respondents, their attorney, and counsel for the Commission having thereafter executed an agreement containing a consent order, an admission by the respondents of all the jurisdictional facts set forth in the aforesaid draft of complaint, a statement that the signing of said agreement is for settlement purposes only and does not constitute an admission by respondents that the law has been violated as alleged in such complaint, and waivers and other provisions as required by the Commission's Rules; and [2]

The Commission having thereafter considered the matter and having determined that it has reason to believe that the respondents have violated the said Act, and that complaint should issue stating its charges in that respect, and having thereupon accepted the executed consent agreement and placed such agreement on the public record for a period of sixty (60) days, now in further conformity with the procedure prescribed in Section 2.34 of its Rules, the Commission hereby issues its complaint, makes the following jurisdictional findings and enters the following order:

1. Respondent C&D Electronics, Inc. is a corporation organized, existing and doing business under and by virtue of the laws of the State of Michigan, with its office and principal place of business located at 2026 Chicago Avenue, Jenison, Michigan 49428.

Respondents David Barwacz and Larry Bostelaar are officers of said corporation. They formulate, direct and control the policies, acts and practices of said corporation and their address is the same as that of said corporation.

2. The Federal Trade Commission has jurisdiction of the subject matter of this proceeding and of the respondents, and the proceeding is in the public interest.

ORDER

For purposes of this order, the following definitions are applicable:

"Authorized person(s)" shall mean any person that is a cable operator or a cable system operator, operating a cable system, as defined

herein, pursuant to a franchise issued by a cable franchising authority, or any person manufacturing or distributing cable television decoders, descramblers converter-decoders, or converter-descramblers pursuant to a contract, agreement, license or other arrangement with a cable operator or a cable system operator to provide, furnish or supply such products to a cable system.

"*Cable operator*" or "*cable system operator*" shall mean any person, partnership, or corporation that provides cable service over a cable system or that, directly or through one or more affiliates, owns a significant interest in any cable system or who otherwise controls or is responsible for, through any arrangement, the management and operation of a cable system. [3]

"*Cable system*" shall mean a facility or combination of facilities, constructed or operated pursuant to a franchise, that consists of a set of closed transmission paths and associated signal generation, reception and control equipment and that is designed to provide cable service to multiple subscribers within a community or a satellite master antenna system (SMATV), that serves subscribers in one or more multiple unit dwellings under common ownership, control or management.

"*Franchise*" shall mean an initial authorization or renewal thereof, issued by a franchising authority, whether designated as a franchise, permit, license, resolution, contract, certificate, agreement or otherwise, which authorizes the construction or operation of facilities designed to provide cable service.

"*Franchising authority*" shall mean any state, political subdivision, or agency thereof, or any governmental entity empowered by Federal, State or local law to grant a franchise.

I.

It is ordered, That respondents C&D Electronics, Inc., a corporation, its successors and assigns, and its officers, and David Barwacz and Larry Bostelaar, individually and as officers of the corporation, and respondents' agents, representatives and employees, directly or through any corporation, subsidiary, division or other device, in connection with the manufacture, advertising, offering for sale, sale or distribution in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, of any cable television decoder, descrambler, converter-decoder or converter-descrambler that may be used for the decoding, descrambling, and/or intercepting in any manner whatsoever of all or any part of any cable television transmission do forthwith cease and desist from selling or distributing, any such product to any person that is not an authorized person hereunder.

II.

It is further ordered, That respondents C&D Electronics, Inc., its successors and assigns, and its officers, and David Barwacz and Larry Bostelaar, individually and as officers of the corporation, and respondents' agents, representatives and employees, directly or through any corporation, subsidiary, [4] division or other device, in connection with the manufacture, advertising, offering for sale, sale, or distribution in or affecting commerce, as "commerce" is defined in the Federal Trade Commission Act, of any cable television decoder, descrambler, converter-decoder or converter-descrambler that may be used for the decoding, descrambling, and/or intercepting in any manner whatsoever of all or any part of any cable television transmission, do forthwith cease and desist from representing, directly or by implication that:

1. Any consumer may lawfully own or use such a product.
2. The ownership and use of any such product is the same as or similar to the ownership or use of telephone equipment.
3. Any consumer may lawfully use any such product without first obtaining authorization from a cable company and paying the required fees.

III.

It is further ordered, That respondents shall, for a period of five years after the date this order becomes final, maintain and upon request make available to the Federal Trade Commission for inspection and copying copies of:

1. All sales invoices showing sales of any cable television decoder, descrambler, converter-decoder or converter-descrambler with the invoices showing the name of the person or persons, to whom the sale was made, along with their address(es) and the quantity of such products sold to such person(s).
2. Documents verifying that for each such sale the buyer was an authorized person hereunder. [5]

IV.

It is further ordered, That respondents shall, in connection with the sale of any cable television decoder, descrambler, converter-decoder or converter-descrambler that may be used for the decoding, descrambling, and/or intercepting in any manner whatsoever of all or any

part of any cable television transmission, disclose clearly and conspicuously in writing to the buyer the following statement:

"The possession and use of cable TV equipment on any cable TV system without specific authorization from a cable company and the payment of required fees is strictly prohibited in most states. C&D sells its products only to authorized persons."

V.

It is further ordered, That respondents shall forthwith distribute a copy of this order to each of its agents, representatives and employees having advertising, marketing, sales or corporate policy responsibilities with respect to the subject matter of this order and secure from each such person a signed statement acknowledging receipt of a copy of the order.

VI.

It is further ordered, That respondents notify the Commission at least thirty (30) days prior to any proposed change in the corporate respondent such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change in the corporation which may affect compliance obligations arising out of the order.

VII.

It is further ordered, That respondents David Barwacz and Larry Bostelaar shall, for a period of five (5) years after the date of service of this order, notify the Commission of the discontinuance of their present employment and of their affiliation with any new business or employment, involving the manufacture, advertising, sale, offering for sale or [6] distribution in commerce of any cable television equipment or accessories, or of their affiliation with any new business or employment in which their duties or responsibilities would involve the manufacture, advertising, sale, offering for sale or distribution of cable television equipment or accessories, with each such notice to include respondent's new business address and a statement as to the nature of the new business or employment, as well as a description of their duties and responsibilities.

VIII.

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

DISSENTING STATEMENT OF COMMISSIONER MARY L. AZCUENAGA

I dissent from the Commission's decision to accept the consent agreement with C&D Electronics and its principals. Although this case may technically meet the criteria for application of an unfairness theory under Section 5 of the FTC Act, it is different from the usual case in which the Commission seeks to halt some form of seller behavior that creates or unfairly takes advantage of obstacles to fully informed decisions by consumers.

In this case, the product is a decoder, a device for obtaining access to cable programming. C&D allegedly acted unfairly by selling decoders to consumers who used them to obtain cable programming without paying for it, resulting in lost revenues for cable companies, higher cable prices for consumers and reduced franchise fees for municipalities. The order attempts to deal with the alleged unfairness by prohibiting C&D from selling decoders to unauthorized users.

The alleged injury, however, stems not from any overreaching by C&D but rather from the voluntary use of pirate decoders by consumers. What the order is really trying to stop—or, given C&D's size relative to the rest of the industry, to inhibit to some degree—is not the unlawful behavior of the seller of the product but rather the unlawful behavior of the consumers who purchase the product. This may be a laudable goal, but it is not the sort of accomplishment this agency was set up to achieve. By accepting this order, the Commission embarks on a course of social engineering that brings a radical new meaning to the concept of consumer protection.

No doubt consumers engage in a good deal of behavior, lawful or unlawful, that is costly to society. Some consumers litter our parks and highways, but the expense of cleaning up is not a basis for action by the Commission to restrict the sale of soft drink bottles and fast foods. Although federal or state lawmakers properly may attempt to restrict such behavior, I know of no mandate for the Federal Trade Commission to regulate undesirable behavior of individual citizens not involved in trade.

To address the problem of unauthorized cable TV decoders, Congress enacted the Cable Communications Policy Act of 1984, 47 U.S.C. Section 553, which exposes the users and sellers of pirate decoders to

substantial criminal penalties and civil liability. A number of state law restrictions also exist. In addition, the cable industry is developing technology to block pirate decoders. It seems to me that this agency should use its increasingly scarce resources to monitor unfair methods of competition and unfair or deceptive acts and practices by those who are engaged in trade and should leave the policing of the unauthorized use of decoders by consumers to the cable industry and to the Department of Justice.

SEPARATE STATEMENT OF CHAIRMAN DANIEL OLIVER

After extensive consideration and reflection I have concluded that the consent agreement in this matter should be provisionally accepted. This case fits the analytic framework that we have established for our "unfairness" jurisdiction, and the facts present justify Commission action. There is reason to believe that the practices of C&D Electronics have resulted in substantial consumer injury that is not offset by any legitimate countervailing benefits to consumers or competition and that the resultant consumer injury was not reasonably avoidable.¹

CONSUMER INJURY

The cost of stolen cable services is initially borne by the cable companies, the premium cable services, and the municipalities that grant cable franchises. There is little doubt, however, that most or all of those costs are passed along to honest cable service subscribers in the form of higher prices.

Such activities can result in actual and substantial consumer injury, far greater than that challenged in many of our other cases. In many of our deception and competition cases, for example, we rely in large part on presumptions about the likely adverse effects on consumers. And like our other competition and [2] consumer protection actions, this injury takes place in the context of a commercial transaction.

Moreover, consumer injury can provide a basis for Commission action even when there is no direct contact between the respondent and the ultimate consumer. Our concerns in halting conduct that results in unjustified harm to the public is not limited to injury incurred by the direct purchasers of products. An example of this is the Commission's consent agreement in *Phillip Morris, Inc.*, 82 FTC 16

¹ I am wholly unable to fathom concerns that we are engaging in some form of social engineering by accepting this consent agreement. In this case there is no attempt to substitute our views for those of an informed public. Congress, it should be noted, has already passed legislation prohibiting the type of conduct alleged here.

(1973), where the company had distributed free samples of razor blades that the Commission alleged were a safety hazard because they could come into the hands of small children or injure others who had not purchased a product.

The consumer injury at issue here is similar to that in our competition cases, where our purpose is ultimately to prevent restraints on trade that would result in consumer injury in the form of increased prices. In *FTC v. Indiana Federation of Dentists*, 106 S.Ct. 2009 (1986) the Court found that the concerted action taken by the dentists was:

likely enough to disrupt the proper functioning of the price-setting mechanism of the market that it may be condemned even absent proof that it resulted in higher prices or, as here, the purchase of higher priced services, than would occur in its absence.

Id. at 2019. Such price increases injure consumers who cease purchasing or turn to a less satisfactory substitute (i.e., who then have no direct contact with the respondent) as well as those who continue to purchase at higher prices. The injury alleged [3] here is more direct than in many of those cases, and I am aware of no compelling reason for treating the situations differently.

In addition, in a case of this sort injury to consumers may go well beyond a simple increase in prices; the activity here may provide disincentives that will result in services not being available to consumers at all. There is little or no reason for businesses to establish cable services, or expand and improve existing ones, unless sufficient revenue can be generated to warrant expenditures. Widespread or unchecked free riding could discourage ventures that would offer such services or could result in raising the prices for cable subscriptions in existing networks beyond optimal levels. Thus such action could not only result in present injury, but also could undermine the competitive process that encourages innovation or maintenance of such facilities and thereby increase the risks of collateral consumer injury of a different type.

COUNTERVAILING BENEFITS TO CONSUMERS OR COMPETITION

I am unable to identify any collateral benefits to consumers or competition that are likely to offset the conduct alleged here. Significant free riding on services paid for by others can hardly be considered a benefit that offsets the resultant costs imposed on honest cable subscribers. [4]

AVOIDABILITY OF THE INJURY

This aspect of our unfairness jurisdiction involves an inquiry into whether market forces provide an adequate disincentive for conduct injurious to consumers.² In many of our cases there is a defect in the information available to consumers in making purchase decisions that they cannot easily protect themselves from.³

However, we have also recognized that unfairness may be involved in situations where there is no informational problem—for example, where a clearly defined right cannot be enforced effectively by private actions.⁴ In my view, it was this rationale that supported our finding of liability in *Orkin Exterminating*, Docket 9176, (December 15, 1986). In that case, like this one, there was a firmly established (and rational) [5] legal standard governing the conduct, the consumer injury alleged was substantial and readily identifiable, and the injury resulted from commercial transactions within our jurisdiction and expertise.⁵

Private actions may not be able to deter the type of conduct that C&D Electronics was charged with engaging in. First, most cable companies and municipalities do not have the technology to detect the use of these sorts of decoders, and thus have a difficult time determining the scope of the problem and the source of illegal decoder use.⁶ Thus most municipalities, even though deprived of revenue, have little incentive to take action. Cable companies are faced with the same difficulties. Moreover, they may have little incentive to fund litigation which will benefit competitors as much as, or perhaps more, than themselves. Even where a problem is identified and litigation ensues, the relief obtained frequently extends only to the geographic area of the complaining party. Neither trade associations nor the premium services themselves have mounted efforts to curtail such activities. As a result I believe that the consumer injury alleged to result from the actions of C&D Electronics is not reasonably avoidable. [6]

² The need for this inquiry is made explicit in the Commission's Policy Statement on Unfairness, and is incorporated into the analysis of whether injury is reasonably avoidable:

Normally we expect the marketplace to be self-correcting, and we rely on consumer choice—the ability of individual consumers to make their own private purchasing decisions without regulatory intervention—to govern the market.

Unfairness Statement at 7.

³ *Id.* "[W]e rely on consumer choice—the ability of individual consumers to make their own private purchasing decisions without regulatory intervention"

⁴ "In some senses any injury can be avoided—for example, by hiring independent experts to test all products in advance, or by private legal actions for damages—but these courses may be too expensive to be practicable for individual consumers to pursue." Unfairness Statement, n.19 at 7.

⁵ These considerations demonstrate why there is no role for the Commission in matters such as pollution or gun control.

⁶ Even if the technology to circumvent use of illicit decoders were available, however, the cost of implementing safeguards of that type would probably be imposed on consumers as well.

Statement

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CONCLUSION

Accepting this consent decree does not, to my mind, signal a broad foray into Commission enforcement of all property rights. In fact, I would suspect that situations like the one present here will come to our attention infrequently. When we do find substantial consumer injury in such situations, it is important that the conduct satisfy our criteria on unfairness, and it is particularly necessary that we be able to determine whether private actions are adequate to vindicate private rights. This process must, of necessity, result from case-by-case analysis based on the particular facts involved. I am satisfied that the consent agreement negotiated in this matter satisfies those standards, and I am therefore voting to accept it provisionally.

IN THE MATTER OF
ALLIED CORPORATION

MODIFYING ORDER IN REGARD TO ALLEGED VIOLATION OF THE FEDERAL
TRADE COMMISSION AND CLAYTON ACTS

Docket C-3109. Consent Order, May 17, 1983—Modifying Order, Mar. 18, 1987

The Federal Trade Commission has modified a 1983 consent order (101 F.T.C. 721) by requiring that, until 1993 and with certain exceptions, the successors to Allied must obtain prior FTC approval before acquiring any interests or assets of a high-purity acid maker.

ORDER REOPENING THE PROCEEDING AND
MODIFYING CEASE AND DESIST ORDER

On July 29, 1986, Allied Corporation ("Allied") filed a document entitled "Petition By Allied Corporation Pursuant to Section 5(b) of the FTCA and Rule 2.51 To Reopen and Terminate Paragraph III of the Consent Order Entered in Docket No. C-3109." The petition requests that the Commission reopen the order and terminate Paragraphs III and IV. In the alternative, Allied requests that the Commission relieve Allied of its compliance obligations under those paragraphs. Paragraph III prohibits Allied from acquiring for ten years without prior Commission approval "any assets of or any stock interest in any company engaged in the manufacture of high-purity acid in the United States * * *." Paragraph IV requires Allied to file annual reports respecting its compliance with Paragraph III. The preamble to the order defines "respondent" to mean "Allied Corporation, its subsidiaries, affiliates, divisions, successors, and assigns."

On September 19, 1985, Allied merged with The Signal Companies, Inc. ("Signal"). They formed a new parent corporation, Allied Signal Inc. ("Allied Signal"), with Allied becoming a wholly owned subsidiary of Allied-Signal. In December 1985, Allied-Signal restructured itself by forming a new corporation containing thirty-five former businesses of Allied or Signal. The new corporation was named The Henley Group, Inc. and included the entire high-purity acid business of Allied. On May 28, 1986, Allied-Signal spun-off Henley. Seventy percent of the equity of Henley was distributed to the shareholders of Allied-Signal as a stock dividend ("Distribution"). The remaining thirty percent was retained by Allied-Signal. The formation agreement between Allied-Signal and Henley dated February 26, 1986, included a schedule of enumerated liabilities which stated that Henley may be liable for the Commission's order in this matter. On Janu-