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FRAUDS AND DECEPTIONS AFFECTING THE ELDERLY

INVESTIGATIONS, FINDINGS, AND RECOMMENDATIONS: 1964

A REPORT

OF THE

SUBCOMMITTEE ON FRAUDS AND MISREPRESENTATIONS AFFECTING THE ELDERLY

TO THE

SPECIAL COMMITTEE ON AGING

UNITED STATES SENATE

JANUARY 31, 1965

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LETTER OF TRANSMITTAL

U.S. SENATE,
January 31, 1965.

Hon. GEORGE A. SMATHERS,
Chairman, Special Committee on Aging,
U.S. Senate.

DEAR MR. CHAIRMAN: I have the honor of transmitting a report which summarizes the findings of the Subcommittee on Frauds and Misrepresentations Affecting the Elderly. These findings and recommendations are based on hearings conducted in San Francisco and in Washington during 1964. The subcommittee also draws from the facts gathered by the full Committee on Aging during 3 days of hearings that, in 1963, led to the establishment of this subcommittee.

Witnesses at subcommittee hearings this year gave testimony on varied subjects, but one theme persisted throughout: as the number of elderly increases every year, so does the number of schemes intended to defraud that group of Americans.

We on the subcommittee have gathered much information, and we have begun to develop general suggestions for corrective action. In some cases, we have specific proposals.

We believe that this report will be of help to those who are concerned about the elderly, and consumer protection for all age groups.

The subcommittee wishes to acknowledge the invaluable help given throughout 1964 by the Federal Trade Commission, the Food and Drug Administration, the Office of the Chief Postal Inspector, and many individual postal inspectors and other officials who gave assistance, the National Better Business Bureau, the American Medical Association, the American Cancer Society, the Arthritis and Rheumatism Foundation (now the Arthritis Foundation), and the many witnesses who gave so much of their time to prepare testimony for our hearings.

HARRISON A. WILLIAMS,
Chairman, Subcommittee on Frauds and Misrepresentations Affecting the Elderly.

FOREWORD

On every hand we hear reports that the number of persons past 65 in this country is increasing at a rising rate every year.

To all Americans, this trend should be a source of pride, the rich fruition of accelerated medical and social progress. To many observers, however, the trend is a worrisome indicator of the work that must yet be done to prepare for population changes of unprecedented magnitude.

The Subcommittee on Frauds and Misrepresentations Affecting the Elderly has a special concern about the steadily increasing numbers of elderly.

In the course of 1 year we have gathered voluminous evidence which cogently demonstrates that our older citizens have become a clearly defined market—not only for reputable businessmen with new and valuable services and products for the elderly—but also to those who are looking for a vast new market to victimize.

To the unscrupulous, the retirement age group has several new and irresistible attractions.

Buying power is one. Elderly Americans, about 18 million in all, have an annual income of about $37 billion. It comes in the form of social security payments, pension plans, returns from savings and investments, and part-time or full-time employment.

Even though much of this income is fairly certain, it is pitifully inadequate in the vast majority of individual cases. This very inadequacy makes the yearning for security all the more desperate, and the elderly attempt to make slim resources cover all retirement contingencies including adequate shelter, care of multiplying ailments, and some semblance of protection against financial crises.

Anxiety is thus a weapon for those who cheat the elderly, and so is the very complexity of the modern marketplace. On every side, the elderly—and all other consumers—are confronted with claims made for products that can be evaluated accurately only by experts.

How can a retired person, for example, really understand claims made for a food supplement unless he happens to be a trained dietitian or a physician? How can he be sure that he has an adequate understanding of health insurance policy unless he has guidance from a trained, reliable expert? Now that it is possible to buy land by mail on the installment plan, who can be sure that he knows what he is buying unless he sees it?

The ready answer to these questions, when a consumer is dealing with a reputable seller, is that the seller will give him honest information in advertising or in personal sales presentations. But the unscrupulous seller is not bound by the same ethical standards. He takes advantage of complexity to cause confusion. He also takes advantage of a vague impression on the part of the consumer that—somehow, in some way—some level of government is protecting him against dishonesty and misinformation.

The subcommittee has no desire to add needless legislation to the lawbooks; neither do we propose to ignore obvious gaps in our present regulatory structure. The subcommittee also realizes that education, public and private, can often be more effective than regulatory action. In the following pages, the subcommittee makes recommendations that attempt to give at least as much attention to education as to law enforcement.

The subcommittee also believes that it has a responsibility to present facts that should be brought to the attention of all age groups. at future hearings, we will do all in our power to provide information that will help end abuses against a group of Americans who deserve our respect, our understanding, and our realization that their experience will soon be ours.

HARRISON A. WILLIAMS, *Chairman.*

INDEX TO MAJOR FINDINGS AND RECOMMENDATIONS

Conclusions presented in this report are based on the following subcommittee hearings:

Health frauds and quackery, San Francisco, Calif., January 13, 1964.

Health frauds and quackery, Washington, D.C., March 9 and 10, 1964.

Health frauds and quackery (eye care), Washington, D.C., April 6, 1964.

Deceptive or misleading methods in health insurance sales, Washington, D.C., May 4, 1964.

Interstate mail order land sales, Washington, D.C., May 18, 19, and 20, 1964.

Pre-need burial service, Washington, D.C., May 19, 1964.

The subcommittee also has referred to transcripts of hearings ("Frauds and Quackery Affecting the Older Citizen") conducted by the Senate Special Committee on Aging on January 15, 16, and 17, 1963.

Thus far the subcommittee has taken 1,128 pages of testimony, in addition to the 516 pages of testimony and exhibits taken by the committee in 1963. Major points from these transcripts are summarized in this report in the following way:

PART ONE

HEALTH FRAUDS AND QUACKERY

INTRODUCTION

THE ELDERLY—"MAIN TARGET FOR EXTENSIVE EXPLOITATION"

Americans are now paying the greatest price they have ever paid for worthless nostrums, ineffectual and potentially dangerous devices, treatments given by unqualified practitioners, food fads and unneeded diet supplements, and other alluring products or services that make misleading promises of cure or end to pain.

It is incredible that a wealthy nation, priding itself on its enlightenment and its thirst for progress, should pay such a heavy penalty for ignorance or lack of adequate enforcement.

And it is shameful that the elderly of the United States are now clearly the major victims of the highly organized, high-pressure techniques of the modern day medicine man. But this is clearly the case, and it was verified as woeful fact by witnesses who addressed the subcommittee.

California—Major programs, major concern

To begin its survey of health frauds and quackery, the subcommittee heard its first witnesses in California. This State was chosen, not only because of its relatively large number of retired persons, but also because the State agencies are waging a comprehensive counterattack on the cheaters.

Even though the dangers are recognized, however, witnesses readily testified that they foresaw even greater enforcement difficulties ahead.

> We are convinced [said Dr. Hamlet C. Pulley, Assistant Director of the California State Department of Health] that quackery exists in California to a degree substantially detrimental to the health and welfare of its citizens.
>
> A greater than usual number of referrals and complaints were received last year from consumers, civic organizations, voluntary health organizations, and other interested persons. These, coupled with our own observations, lead us to conclude that quackery is extensive in California and appears to be increasing.[1]

The same witness gave a poignant statistical picture of the vulnerability of the aged to salesmen of false hope:

> Eight percent of California's 17 million people are 65 years of age or older. In southern California this percentage may be higher, approximately 10 percent.
>
> Three-quarters of these have some type of chronic condition, cancer, rheumatoid arthritis, heart disease or other chronic disability.

[1] See p. 30, "Hearings on Health Frauds and Quackery," Subcommittee on Frauds and Misrepresentations Affecting the Elderly, 1964.

> It is this senior citizen with chronic ailments, approximately one-half million, that is the most sharply affected by the activities of the medical confidence man.
>
> It is this class that becomes the main target for extensive exploitation.[2]

An assistant district attorney for Los Angeles County, confirmed this conclusion. He said his records of quack prosecutions showed that 7 out of 10 victims are over the age of 60.[3]

Example after example was given in California to prove, in the words of a spokesman for the attorney general of California, that—

> * * * the snake oil medicine man has exchanged his stock for food supplements, and has rephrased his pitch in 20th century language. He has added to his stock electronic devices with curious dials. He can cure and prevent cancer, cardiac conditions, chronic disturbances of the gastrointestinal tract, dermatoses, rheumatism, improper blood pressure, nervousness, and anemia.[4]

Similar conclusions were reached during 3 days of hearings in Washington, D.C., by witnesses describing quackery as a national problem.

*The national scene: "Fraudulent schemes * * * on the increase"*

Asked whether fraudulent schemes are on the increase, the Chief Postal Inspector of the United States gave a definite affirmative. He also gave reasons for the increasing complexity of medical fraud cases:

> Although postal inspectors still occasionally encounter medical quackery items involving electric belts, buzzers, bell ringing, and even black magic potions guaranteed to cure all manner of disease, today's frauds are generally more sophisticated. Promoters do not so often promise outright cures for serious diseases but offer preparations to "aid" in curing various conditions which the American consumer finds undesirable, such as baldness, obesity, and so forth.
>
> Treatments are offered by mail for every conceivable condition, including cancer, diabetes, prostate trouble, asthma, arthritis, heart diseases, and impotency, to name but a few. Such schemes continue to be a source of great concern since the victims are frequently induced to attempt self-diagnosis and treatment, meanwhile deferring proper attention.[5]

Mrs. Esther Peterson, Chairman of the President's Committee on Consumer Interests, described the vulnerability of the elderly, not as sheer gullibility, but as the result of several causes: [6]

> In my capacity as Special Assistant to the President for Consumer Affairs, I am concerned, of course, with the myriad problems facing consumers of all ages and conditions.
>
> Yet, I confess willingly to a special concern for our aged, whose capacity to resolve many of their problems independently is considerably less than that of our younger citizen-consumers.

[2] P. 30, op. cit.
[3] P. 79, op. cit.
[4] P. 5, op. cit.
[5] P. 283, op. cit.
[6] P. 166, op. cit.

The aging men and women in our society are becoming increasingly a more significant percentage of our total population. As their numbers increase, so also will the incidence of fraud and quackery increase. For these people, removed—as many of them are—from the mainstream of daily business activity, cut off from the stimulation of regular "back fence" exchanges with neighbors, become in their loneliness evermore susceptible to the blandishments of facile hucksters.

I receive daily in my office scores of letters from older people all over the country. The range of subject matter with which these people are concerned is broad and varied, but there has been a heavy emphasis on health frauds and quackery.

Many of the writers have despaired long since of any redress of their grievances; they want simply to share their disappointment, their sense of loss, with someone, with anyone who will offer a bit of understanding. I am tremendously impressed with this dread of loneliness that seems to run through so many of the letters and interviews with people as I run around the country.

Others of them, confident still that frauds and quacks will somehow be searched out and restrained, plead with the eloquence of age for the Government to take some kind of action against those who would victimize the weak and the innocent.

Other testimony yielded a multitude of "horrible examples" that helped lead the subcommittee to the following findings and recommendations:

MAJOR FINDINGS

FINDING NO. 1

A substantial trade in worthless devices exists in the United States, and profits to some of the manufacturers are now in the millions of dollars

These devices are often used by phony practitioners to impress victims with "up-to-date" methods or "secret" treatments. One highly mobile pitchman, using and selling a machine that did little more than give colonic enemas to victims of major diseases, made an estimated $2½ million before conviction on a mail fraud charge. (See recommendation No. 1.)

FINDING NO. 2

Federal regulatory agencies are waging a continuing war against misleading claims made by dishonest or confused manufacturers of "health foods" and "food supplement products." This war has become highly technical and at times almost esoteric

Food and Drug Commissioner George P. Larrick described one battle in this war when he told the subcommittee about a "landmark decision" handed down by the U.S. district court in Trenton, N.J., on January 24, 1964:[7]

> In this action some 900 packages of Vitasafe capsules and over 3.7 million pieces of printed material (labeling, as de-

[7] P. 176, op. cit.

> fined by the statute), designed to promote the sale of the products were seized. The Vitasafe formulas were mixtures of numerous ingredients promoted for the treatment of many health conditions for which they are not effective. The label of this Vitasafe package bears the innocuous statements: "Food Supplement—For Dietary Purposes Only," "Average Dosage for Adults: One CF capsule daily," and a statement of "Ingredients in Each Capsule," of which 16 of the 25 listed ingredients are marked "Minimum Daily Requirement Not Yet Established" or "Need in Human Nutrition Has Not Been Established." This information is misinterpreted by accompanying circulars.

The FDA had to call in an expert witness to argue that the elderly actually believed they could buy some measure of rejuvenation when they bought the compound, and that they were influenced by such advertising claims as: "Important Message for Men and Women over 40," and "Our Fights Have Turned to Kisses."

Dr. Godfrey M. Hochbaum, Chief of the Behavioral Science Section of the U.S. Public Health Service, was the FDA witness. He told the court that such claims definitely have their effect upon elderly consumers: [8]

> * * * I believe that this kind of material would arouse the interest of many people who suffer from real or imaginary complaints, these vague variety of complaints such as tiredness, nervousness, real or imaginary, sexual impotence, marital problems, and so forth, because many of these people with little education who are very naive cannot identify the causes of their difficulties, and because they cannot * * * they look for some magic formula, something that will change their lives and satisfy all their needs and remove their frustrations, so they turn to something like this with the real hope that this would provide a solution to their problems. And everything in here is in the form that would appeal to exactly this kind of people, attract these kinds of readers.

Some idea of the magnitude of victimization was given by FDA Commissioner Larrick. He gave a case study of Nutri-Bio, which was recommended by its manufacturers as the answer to practically all health problems—anemia, arthritis, cancer, diabetes, frigidity, heart trouble, infections, nervousness, and so on:

> The Nutri-Bio promotion [according to the Commissioner] was a classic example of food faddism gone wild. It would take several pages to list all the false claims and representations. Mushroom promotion methods had built it up to the point where more than 75,000 full- and part-time sales agents were selling Nutri-Bio at $24 per package for a 6-month supply for one person * * * Nutri-Bio agents in the Chicago area alone turned in for destruction about 50 tons of literature. We invite you to compare this with the efforts of Government and voluntary health agencies to disseminate reliable nutrition information.[9]

[8] P. 176, op. cit.
[9] P. 201, op. cit.

In spite of individually successful enforcement efforts, the lure of riches in a lucrative field has great attraction for the unscrupulous. Great care and study is being given to the preparation of advertising schemes that stay, if at all possible, within the letter of the law while making every effort to circumvent the purposes of the law.

Heartfelt pleas were made by several witnesses for educational programs that would at least give consumers facts they must have to make wise decisions, and other witnesses made it clear that the consumer does not have all the protection he thinks that Federal agencies give to him.

FINDING NO. 3

Despite diligent attempts by enforcement agencies to keep informed about quackery operations and antiquackery crackdowns, the advantage seems to be on the side of the unscrupulous.

The quack has mobility and usually he has the advantage of secrecy, even on the part of his victims, as the following exchange indicates:

> Senator NEUBERGER. You [the state of California] do have adequate laws * * * Where is the gap that allows all this to flow through the community? Is it enforcement?
>
> Mr. JAMES [Charles A. James, assistant attorney general of California]. Well, we believe that the timelag between the discovery of the fraud as it is being practiced, and the putting of enforcement into actual gear, involves one problem. Many times enforcement agencies do not discover the frauds that are being practiced, and I think part of this is due to the reluctance of the people to disclose the fact that they have been deceived.[10]

If a quack becomes rich, he has additional advantages: funds for long legal battles, and skilled advice in finding ways to circumvent the intent of the law. Two witnesses, both members of college staffs, suggested to the subcommittee that academicians and other experts sometimes hesitate to speak out against food faddists because they do not have the funds to pay for an extended lawsuit.

> We find ourselves talking in generalities while the food faddist comes out and says, if you do this you will be cured, and I, in generalities, avoid the issue [said Dr. Dena C. Cederquist, chairman of the Foods Nutrition Department at Michigan State University].[11]

FINDING NO. 4

Complexity of modern life and modern medicine give the quack considerable opportunity to sow confusion

Ever hopeful of a shortcut to cure, patients have a predisposition to those who will save them from the costly rigors of orthodox treatment.

The subcommittee heard, for example, testimony describing a worthless product said to be "better than most plastic surgery."

[10] P. 8, op. cit.
[11] P. 309, op. cit.

The witness was Mrs. Virginia Nelson of the San Francisco Better Business Bureau.[12]

> Questionable business practices are worked in transactions involving the young and others at all ages, including the elderly. To be specific, in 1957, Age-less Cosmetics promoted the sale by mail of two cosmetic products which were represented to "banish wrinkles," and were subsequently cited for mail fraud.
>
> The fraud order was vacated in 1958 when Age-less Cosmetics signed an affidavit of discontinuance with the Post Office Department on May 4, 1959, Post Office Docket No. 1–100.
>
> On January 14, 1962, the better business bureau noted an advertisement in the feature section of a local newspaper for what appeared to be the same product, now under the name of Age-Wise Cosmetics.
>
> The bureau sent a clipping of the advertisement with a letter to the San Francisco postal authorities. During the months which followed, the bureau received requests for information about the product from better business bureaus and individuals throughout the United States, as the advertisement was appearing nationally, using such phrases as "Young throats for old * * * amazing clinical pad * * * better than most plastic surgery * * *."
>
> In December 1962, the Post Office Department held another hearing to determine the authenticity of the subject's written statements on its products in the form of printed matter going through the mails. At this hearing, representatives from the U.S. Food and Drug Administration were quoted by media as stating that subjects' cosmetics "didn't do a thing to alleviate wrinkles, sagging, or other signs of aging."
>
> On November 21, 1963, the judicial officer, Post Office Department, issued fraud order No. 63–190 requiring that all mail addressed to the firm or its proprietress be halted at the post office and return to sender marked "fraudulent."

The American Dental Association has estimated that the public pays more than $20 million each year to unqualified persons who operate contrary to State dental laws. The following excerpt from an association statement indicates that consumer attitudes contribute to the success of these practitioners: [13]

> The elderly are a prime target of dental "quacks" who operate independently of the dentist and in violation of the law. A survey conducted by the American Dental Association reported in 1961 that 78.3 percent of our citizens past the age of 60 wear dentures or bridges. Nearly two-thirds of the over-65 age group have either a complete upper or lower denture. Of those in the 20-to-29 age group, only 22.4 percent wore either dentures or bridges and only 10.1 had complete upper or lower dentures.

[12] P. 101, op. cit.
[13] Pp. 325–326, op. cit.

> The survey reported some significant results with respect to the cost of dentures and proved how effective the illegal operators have been in fooling the public. Those respondents to the survey who had obtained complete upper or complete lower dentures during the preceding 12 months were asked to indicate the cost of the dentures. The average (mean) cost of complete upper dentures obtained from dentists was $104.21, compared to $82.50 for those obtained from the "quacks." The averages for complete lower dentures were $100 from dentists and $71.88 from "quacks." Thus, for an illusory saving of a very few dollars, these people were subjecting themselves to nonprofessional care and risking injury to their oral health.
>
> Participants in the survey were asked where they intended to go for dentures, if necessary, in the future. *Of the persons over age 60 surveyed, 9.4 percent indicated they would go to a dental "quack" or that had no answer to this question. Of the persons over age 65, 6.2 percent indicated that they had had their denture repaired by a "quack" within the preceding 12 months.* Persons over age 65 were asked to indicate whether or not they agreed with the statement that a person could get satisfactory "false teeth" directly from a dental laboratory technician or other unlicensed persons. *A startling 12.1 percent agreed with that erroneous statement.* [Emphasis added.]

Arthritis offers special opportunities to the unscrupulous. Twelve million Americans have some form of arthritis; and, as one witness testified: [14]

> If we fall for the phony, and sooner or later most of us do, it is because the pains of arthritis are something that you just can't describe because nobody knows why it comes or how or when it goes.

The same witness, Mrs. J. P. Bramer of San Francisco, recounted her experiences with unorthodox practitioners during her private investigations in and near California. Among the treatments recommended to her: alfalfa tea and the plunging of hands into hot and cold water; sun lamps: "one woman told me that she gets a successful treatment by calling Dr. F. on the phone;" salves and a box containing "numerous little bottles with lavender caps" over which a little transparent crystal ball was swung.

Mrs. Bramer also made a comment often expressed by arthritis victims: [15]

> There must be an exchange list of arthritic victims because if you get on one list you receive material advertising all manner of devices, items such as vibrators, whirlpool baths, salves, uranium mitts, and things of that sort.

Mr. Jerry Walsh, special educational consultant to the Arthritis and Rheumatism Foundation, testified before the Subcommittee on Aging in 1963. Fellow arthritis sufferers, within 3 weeks after his appearance, sent him 4,137 letters recommending 231 products ranging in price from $2 to more than $200,[16] including many "cures" or

[14] P. 124, op. cit.
[15] P. 127, op. cit.
[16] P. 220, op. cit.

"lasting remedies" that aroused the skepticism of Mr. Walsh and the foundation medical experts.

Dr. John Calabro, associate professor of medicine and director of the Arthritis Clinics of Seton Hall and the Jersey City Medical Center, Jersey City, N.J., offered information on "the often difficult task of protecting the arthritis sufferer" [17]

> In a study of 100 patients (60 percent of these were over the age of 45) in our own arthritis clinics, a clinic affiliated with a school of medicine, *60 percent continued to try such remedies as alfalfa seed, liniments, cod liver oil, sea brine, etc., even while under treatment.* [Emphasis added.]
>
> The patients did not mention these experiments to the attending physician because they said they had not been asked directly by the doctor.
>
> Twenty-eight percent reported incidents prior to treatment at the clinic in which they felt physicians were in too big a hurry, did not know anything about arthritis, or said there was nothing that could be done about it.
>
> These attitudes need to be changed and a responsibility of the physician in changing them is paramount.

Perfectly healthy persons can make themselves victims of quack products, as indicated in this testimony from Mrs. Helen Nelson, consumer counsel to Gov. Edmund G. Brown, of California: [18]

> We have the case of the woman who with her husband had worked long, hard years building their restaurant business in which she served as hostess-manager. Conscious of the premium our society places on youth and beauty, her fear that an aging appearance would be detrimental to the family enterprise made her vulnerable to and then victim of luring advertisements for face lifting without surgery. The carbolic acid that was applied to her face when she succumbed to the lure disfigured her horribly and forever. She sued, of course. But it was a futile effort. The practitioner had moved and created a new corporation across the State line.

FINDING NO. 5

WHAT IS THE COST OF QUACKERY?

One billion dollars was mentioned most often as the annual cost of quackery in the United States today

Under questioning during hearings and in subcommittee inquiries, enforcement officials and representatives of private groups admitted that this was only a rough estimate. The following major subtotals, however, have been suggested:[19]

> $500 million for vitamin and "health food" quackery.
> $250 million for arthritic quackery.
> $100 million for ineffective drugs and devices for reducing.

[17] P. 222, op. cit.
[18] P. 119, op. cit.
[19] By FDA Commissioner George P. Larrick, speaking at the 1961 National Congress on Medical Quackery (proceedings, p. 13). Mr. Larrick used the billion-dollar figure but emphasized that all such figures are estimates.

But, like the witness who compared the extent of quackery to an iceberg—probably most of it is under the surface—the subcommittee must admit that no precise determination can be made. As the subcommittee chairman put it: [20]

> Senator WILLIAMS. It seems to me that there are losses that go far beyond the original purchase price for the phoney treatment, the useless gadget, the inappropriate drug or pill. How can we measure the cost in terms of suffering, disappointment, and final despair? Do we really know how many Americans are quietly using therapy or products that give them neither cure nor the hope of cure? Can we be sure that we know the full extent of operations by questionable clinics and neighborhood practitioners?

It becomes even more difficult to estimate the amount of quackery that directly affects the elderly, but even at a 10-percent ratio of the billion-dollar figure, the amount is tragically significant. To combat this menace on the scale that it obviously requires, the subcommittee recommends the following:

RECOMMENDATIONS

RECOMMENDATION NO. 1

Premarket testing of therapeutic, diagnostic, and prosthetic devices should be required at the Federal level

As has already been noted, the subcommittee is concerned about a widespread traffic in devices purported to provide treatments or diagnoses to patients in need of competent professional care.

One of the strongest arguments for a more effective action against such devices was a summary of seizure actions taken by the Food and Drug Administration between January 1 and December 31, 1963. Among the devices seized were the following: [21]

An "Oxy-Gear oxygen inhalator kit" described as providing effective treatment for ailments including cardiac and asthmatic attack, lung conditions, and the effects of shock.

A battery-operated "wrinkle remover" that produced electrical impulses to the body through sponge applicators.

The Auto-Electronic Radioclast, model 20, which supposedly detected diseased organs. Put on display at the hearing, the device was actually nothing more than a wooden cabinet containing a combination of electronic circuits, pilot lights, and dials operated by a practitioner allegedly trained to interpret its mysteries.

The Magnetron, originally advertised as a sure cure for arthritis, prostate gland trouble, varicose veins, diabetes, failing heart, and tumors, was demonstrated at the Washington, D.C., hearing. Here is an excerpt from the testimony: [22]

> MAURICE KINSLOW. You will notice that when I take my hand off of here the light brightens. You cannot tell this, but I am getting a little shock out of it. It is just enough to

[20] See p. 2, "Hearings on Health Frauds and Quackery."
[21] P. 204 ff., op. cit.
[22] P. 190, op. cit.

make the unsuspecting, naive, or desperate person believe that he is getting some advantage from it.

The instructions indicate that you start using it for a minute, and increase up to 30 minutes a day, but you should not expect results in less than a few months, and possibly after you have used it for a year, you will have much better results.

The Micro-Dynameter: The Food and Drug Administration rounded up 1,200 of these devices in 1963, and most of them were taken from licensed practitioners. It was claimed that the Micro-Dynameter could diagnose all kinds of disease by measuring the minute electrical currents generated when metal attachments were applied to the skin of the patient. FDA scientists found, however, that the device merely measured the amount of perspiration on the skin.[23]

Many other devices were brought to the attention of the subcommittee. In California, where State law already requires premarket testing of devices, a witness gave a dramatic demonstration of an ozone generator which crackled and buzzed as it produced a mixture of oxide and nitrogen. Advertisements for the generator claimed that the machine would cure cancer, heart disease, sinus infections, ulcers, and diabetes, to name a few of the ailments listed. Actual laboratory tests, however, have shown that such gases have killed mice in laboratory experiments. Experts have informed the California Bureau of Public Health that the gases could damage the lungs of people who breathe them very long.[24]

A lucrative trade.—Devices are moneymakers for small-time tinkerers with mechanical ingenuity, and also for entrepreneurs with more elaborate plans.

The Magnetron, for example, was a very simple cabinet that cost about $20 to build. It sold for $197.50.[25]

The Micro-Dynameter was a more sophisticated product. Each one sold for $875, and it is estimated that the cost to patients—at $5 to $10 per treatment—could easily have been from $25 to $50 million, just from the 1,200 devices seized by the FDA in 1963.[26]

In California, the subcommittee received some evidence of an organized plan to accelerate ozone generator sales. This exchange occurred between the subcommittee chairman and Joseph F. Bottini, program supervisor of the State bureau of food and drug inspections:[27]

Senator WILLIAMS. Do you know how many were sold?

Mr. BOTTINI. Yes; we feel there were about $1.5 million worth sold.

Senator WILLIAMS. Nationwide?

Mr. BOTTINI. Statewide. The interesting thing about it was that it was called Calozone in California, Orozone in Oregon, and Nevozone in Nevada, and this avoided the interstate requirements. It was really an elaborate scheme. It generated a considerable amount of ozone.

[23] P. 197, op. cit.
[24] P. 41, op. cit.
[25] P. 174, op. cit.
[26] P. 197, op. cit.
[27] P. 41, op. cit.

Mr. Bottini estimated that it cost $24 to make the generator. It was sold for $154, plus tax. The assistant district attorney of Los Angeles County, Mr. John Miner, showed the subcommittee a device that used blood samples in a machine to effect "cures" of serious and minor ailments: [28]

> Now we laugh at this, or at least it is humorous to us, and we smile. This particular operator has records of treating over 35,000 people of whom some 20,000 are in the area of your special concern and perhaps over the age of 60.
>
> At least from the records we have, well over a half million dollars has been taken from these people by the use of this one machine. They are retailing now at $550 apiece.

Difficulties of enforcement.—California State witnesses said that it took 2 years to prepare the evidence needed to proceed against the Calazone generator, and the devices were sold throughout that period. The officials were hopeful that their new State law—requiring testing before marketing—would eliminate the need for investigations after the abuses had been committed.

FDA Commissioner Larrick described the National problem and proposed a solution: [29]

> Under present law a device may be sold with impunity until the Government is able to accumulate evidence to prove in court that the device is unsafe or will not do what is claimed in its labeling. * * * To carry through one of these cases by the Government is a terrifically expensive deal. We have to have expert physicists to take those machines all apart and measure every circuit. We have to have very skilled physicians who will go on the witness stand and testify that the device will not do any good. * * *

The Commissioner drew a parallel to another consumer protection law:

> The new device clearance system would operate in much the same manner as the new drug procedure now works. The sponsor of a new device would be required to furnish for the Government's evaluation and approval sound scientific evidence that the device is both safe and effective for its recommended uses before it can be marketed. This would enable the Government to give the consumer the protection he deserves by requiring uncleared devices to come off the market promptly.[30]

Prosthetic devices, a special problem.—Under the proposed new regulations, prosthetic devices would be subjected to the premarket testing. Surgeons and other medical specialists, in treating elderly people and other patients, frequently introduce into the body artificial hip joints, pins or nails used to repair fractured bones, and other forms of prostheses.

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[28] P. 80, op. cit.
[29] P. 180, op. cit.
[30] Both President Kennedy and President Johnson have requested enactment of such a law. Bills were introduced in the 88th Congress by Senator Lister Hill (S. 2580) and Representative Oren Harris (H.R. 6788).

Usually, such devices give much needed help to persons for whom little else could be done. The subcommittee, however, received direct evidence that some unsatisfactory products are sold in this highly specialized marketplace.

The FDA brought to the hearing room 20 hip nails, 1 bone plate, and several metal hip joints, and other devices removed by one orthopedic surgeon from elderly patients over a period of less than 2 years. One had broken; all had set up chemical reaction in the body, followed by infection. Twenty-three artificial eyes, of poor design, were also displayed.

The following exchange between the FDA witness and a subcommittee member pinpointed the problems faced by surgeons and patients under present law: [31]

> Senator YARBOROUGH. Now what protection does the surgeon have in introducing these pins into the human body? What protection has the surgeon got to know that the metals in these pins are the kind that have been made biologically inert and that they will not be hostile to human tissue?
>
> Dr. (Martin) DOBELLE. Actually he has no protection whatsoever. Unfortunately, we have a gaining tide of malpractice suits, but counsel and attorneys in general now are aware of the fact that the defective device, even though the physician is a prime target, actually is the fault and the responsibility of the manufacturer.
>
> Senator YARBOROUGH. You mean for the malpractice suit, the doctor takes one of these pins made from metals that are not tolerated by the human body and human tissue, a competent surgeon introduces one of these pins into the body, to pin a broken hip, it is hostile, and the surgeon gets a suit for malpractice. There is no law or rule or regulation about the manufacture of these devices, these pins, these bolts, these metal braces that are put in the human body. There is no protection for the surgeon there except his judgment of the manufacturer; is that right?

Dr. DOBELLE. That is correct, sir.

The FDA witnesses made it clear that most manufacturers maintain careful metallurgical control standards and that a committee formed by the manufacturers is "doing some heroic work in trying to get some real standards." But they emphatically said that only premarket testing would give the patient protection. Examining the prosthetic devices, one subcommittee member asked this question: [32]

> Senator KEATING. Are they [the defective devices] put out by what you would consider reputable manufacturers?
>
> Dr. DOBELLE. Yes, sir; some of these unfortunately are. I do not think the manufacturer sometimes is quite aware of what might have taken place because they do not subject these to proper biological research. I am sure this one was put out by a very reputable concern, and it is completely rusted inside, completely rusted here. You have dulling along the very areas to show where these excrescences have been cleaned over.

[31] P. 192, op. cit.
[32] P. 194, op. cit.

Too much control?—At a later hearing, some concern was voiced by the subcommittee chairman about the possiblity of overregulation under premarket testing procedures: [33]

> Senator WILLIAMS. The problem arises with thousands of noncomplicated therapeutic devices. As a matter of fact, the manufacturers of thousands of devices have expressed concern * * * the Band-Aid, for example—does this have to be tested before marketing? You see, the simple device presents a problem, does it not?
>
> Mr. WINTON B. RANKIN. Assistant Commissioner of FDA. Yes; it does. Some of the manufacturers have spoken with us through their associations about this particular question. Now the way that we propose in the bill to deal with that problem is to classify as a device requiring testing only those products that are not generally recognized as safe and effective by the experts, so that a surgeon's scalpel made of ordinary steel that will cut would not have to be tested. It would be recognized as safe. And eyeglass frames made of nonflammable plastic would not have to be tested. They are recognized as safe.

The subcommittee feels, however, that the particular question raised about the "simple device" should receive careful study and deliberation by appropriate congressional committees.

Summary.—The premarket testing of devices was strongly endorsed by President Kennedy and President Johnson in consumer messages of 1963 and 1964. At subcommittee hearings, the FDA witnesses gave strong arguments for such action. The bill was also endorsed by a spokesman for the National Better Business Bureau.[34] Early action on a bill, with full hearings for adequate consideration of all its ramifications, is recommended.

RECOMMENDATION NO. 2

A Federal Antiquackery Bureau should be established at the earliest possible date

Antiquackery enforcement efforts at the Federal level are now divided among at least three jurisdictions: the Food and Drug Administration (labeling), the Federal Trade Commission (advertising), and the Post Office (mail fraud statute). The President's Committee on Consumer Interests is also keenly concerned.

Officials in each of these executive divisions make organized, serious attempts to communicate and cooperate on enforcement actions and activities of suspects. At subcommittee hearings, Federal officials won much praise for vigorous action, cooperation with State and local officials, and for dedicated action despite manpower shortages and limited budgets.

There were, nevertheless, many convincing statements on the need for swifter action. Witnesses for the FTC, and for the Post Office, offered their own suggestions for improving their effectiveness. (See pp. 77–86.) Examples of lengthy regulatory actions abound in the testimony; some cases have taken years to conclude, and usually the

[33] P. 358, op. cit.
[34] P. 275, op. cit.

quack or the manufacturer of worthless products continues to make lucrative profits while these timetaking procedures are followed.

In addition, the subcommittee believes that a central Antiquckery Bureau, established in the Food and Drug Administration, would do much to speed action and communication among Federal agencies. It is realized that these agencies already have formal procedures for interdepartmental communication, but it is also realized that each of these agencies has many burdens and some shortages of personnel in key areas. Even though they are doing a conscientious job and a far-reaching one, the very dispersal of efforts limits the impact of those efforts on the public awareness and upon the activities of quacks.

The case for such an agency was strongly put to the subcommittee, not by a Federal official, but by John Miner, assistant district attorney for Los Angeles County. He made it quite clear that, in his opinion, local law-enforcement efforts could be assisted considerably bv a new agency:[35]

> The right hand rarely knows what the left hand does in the field of medical quackery. Look how many Federal agencies you are involved in. You have the Food and Drug people and Health, Education, and Welfare, and so forth. This is a problem that requires a coordination of all of these agencies.
>
> Each one does a splendid job but you have got to have some single agency of leadership and I suggest that in the Department of Health, Education, and Welfare under the Surgeon General is where it would seem to me to belong and I believe that a unit solely concerned with medical quackery should be set up under a qualified specialist in law and medicine and that he be given the legislative and financial tools necessary to do his job, that he start on it much in the same way that the cigarette situation was approved. * * *
>
> Senator NEUBERGER. * * * You mentioned a department of organization (such) as the Surgeon General's Committee on Smoking and Health to deal with this. I get a report every month from the Food and Drug Administration about cases and they cite the cases that they have investigated and the results and enforcement and seizures and so on.
>
> Would you go beyond that; is that not sufficient or effective?
>
> Mr. MINER. I know very well, having worked with the Federal Food and Drug people, that they are dedicated and they do a wonderful job in view of the limitations of the legislation that they work under.
>
> What I am saying is that medical quackery is, by definition, really a single entity. It is where someone with fraudulent intent is representing something, whatever it may be, as a way of being able to diagnose and cure disease, fraudulent intent being the identifying mark. We have a multiplicity of agencies to deal with the problem and somewhere and in some way the bringing together of those agencies, at least in the sense that they all know what they are doing, and they use their multiple weapons in a coordinated approach to the problem, is desirable and necessary.

[35] P. 82 ff., op. cit.

Take our own State, for example; I think the Federal Government would be in the same boat. Any advertisements, for instance, over the television is interstate. We have a couple of very aggravated situations as to fake healers in Los Angeles County.

The initial investigation was started by the State department of public health, but its agency in that respect is the bureau of food and drug and they are limited to something tangible, not just the spoken word alone, and they are questioning now whether they can send in their people and spend their time, investigative time and money, on this particular problem.

That may be, of course, a legislative thing to be cured. What I am getting at is this. Every agency does a good job, but you need coordination of these agencies under a single agency that sees to it that each of the aspects—because these quacks overlap, they overlap from food and drug to postal, and they might be violating both laws which involves the two different agencies and that sometimes leads to more confusion through which, sometimes, the quack escapes.

Mr. Miner, asked to submit his recommendation in more detail, made it clear that the new antiquackery unit would supplement and accelerate present activities, rather than replace them: [36]

LOCATION

It is recommended that the central Federal agency be placed in the Office of the Surgeon General, U.S. Public Health Department, Department of Health, Education, and Welfare, with a specialist in legal medicine at its head, with the rank of Assistant Surgeon General or equivalent. The agency may be designated as the Bureau on Medical Quackery.

INVESTIGATION

From the data supplied, as above proposed, evaluation can be made to determine what Federal, State, county, or municipal agency would be the most appropriate one to conduct an investigation of a particular reported matter. In some instances, of course, the staff of the proposed Bureau itself might be the most effective agency to undertake such investigation. In any case, however, the Bureau would set up a file on a reported matter and follow up on all processes until it is resolved.

ENFORCEMENT

Where the Bureau's own investigative efforts establish that a form of medical quackery is violative of Federal law, the case will be prepared by the staff for presentation to the proper office or the U.S. Attorney General for prosecution. In other instances where the investigation has been made by another Federal agency, the Bureau will serve as a clearing-

[36] P. 256 op. cit.

house for channeling the case to the proper prosecuting authority, and for providing expert assistance in readying the matter for judicial and/or administrative proceedings.

EDUCATION

From its place as the central Federal agency on quackery, the Bureau would be able to provide information to the news media and to publish material, to inform and educate the public to the dangers of medical quackery. At present, this is done on a piecemeal basis without the compilation and coordination to make such educational activity as effective as it could be.

ASSISTANCE TO STATE AND LOCAL GOVERNMENT

It should be conceded that it lies within the province of local rather than Federal Government to deal with the bulk of medical quackery problems. For the most part, however, little is being done on the local level to prosecute or control a "billion-dollar racket" which unlawfully takes the lives of thousands. As one local prosecutor who has at least done something in this field, I believe I am qualified to say that local government would welcome having its attention called to a quackery situation within its jurisdiction, and receive gratefully any expert advice on how to deal with it.

Mr. Miner also noted that Senator Neuberger expressed some concern earlier in the hearing about a $50,000 annual budget for the California cancer control program, a program that involves the establishment of laboratory facilities to analyze substances offered as cancer cures. In Mr. Miner's opinion, $50,000 "was not even a starting point." He also noted that he is the only chief of a medical legal section in any prosecuting agency in the entire United States. He urged that considerably more attention be given to medicolegal law enforcement at the local level.

A proposal for a Federal coordinating agency also received strong support from Dr. Roald N. Grant, director of professional education, American Cancer Society. He said that such an agency could be helpful not only to public enforcement bodies, but also to private organizations, such as the cancer society, that maintain their own extensive antiquackery files and programs: [37]

It seems to me it would be desirable to establish a special division of the Federal Government, possibly in one of its agencies such as the Public Health Service, to deal with the entire problem of worthless remedies for illness and fraudulent activities of charlatans.

In the health field, such an agency could concern itself with collecting data and coordinating control efforts at the national level and in cooperation with the States and private health agencies.

Now this agency, by taking the initiative in efforts to control this problem, could make a very strong impact in diminishing the fraudulent practices in this country.

[37] P. 334 op. cit.

FDA Commissioner George P. Larrick described the suggestion as "splendid" but also said:[38]

> Actually, the year before last, when we went before the Appropriations Committee, we got $300,000 to be used to hire an outside public consultant group to make a comprehensive study of the relationship between the State and Federal laws in these broad areas, including foods, drugs, and therapeutic devices. We hired the Public Administration Service of Chicago, and they are presently making a very comprehensive study and will come up with recommendations of that sort, plus suggesting means of coordinating, preventing overlapping, and improving relationships between the Federal and the State Government in the whole area of consumer protection in our field.

Subsequent inquiries by the subcommittee staff, however, uncovered no such specific recommendation or specific area of study in the survey which is to be released early in 1965.

Summary.—Enough evidence was presented to the subcommittee to indicate that quackery—described often as a billion dollar menace to the people of the United States—warrants greater Federal attention to support existing Federal, State, and private efforts to combat quackery and disseminate information about this threat. Legislative action should be taken at the earliest possible time to establish the central bureau described by Mr. Miner.

Recommendation No. 3

Educational efforts should receive at least as much attention at the Federal level as enforcement efforts; the subcommittee calls for five immediate steps toward that end: A pilot program to demonstrate effective Federal-State-local-private information efforts, a broad research study on consumer attitudes, and implementation of agricultural extension services and college extension programs wherever appropriate, evaluation of government publications, and increased use of consumer education programs in Federally assisted housing programs for the elderly.

Again and again during the hearings, witnesses called for greater efforts to warn the consumer adequately against quackery.

The subcommittee agrees that educational programs are meritorious, but it wishes to point out that vague generalities about the need for information will not be effective against subtle, energetic, and unscrupulous quacks and merchandisers of phony products and cures.

Fortunately, the subcommittee received specific, constructive suggestions for action that would give Federal agencies a vital, but not dominant role to play in this effort. They are described below:

A. A pilot program to mobilize public and private information programs against quackery at a local level

The subcommittee asked Dr. Harold J. Cornacchia, chairman of the Department of Health and Education at San Francisco State College, to describe his efforts to alert the public to the dangers of

[38] P. 191 op. cit.

quackery. Dr. Cornacchia explained his methods by first asking for "an expanded and improved ongoing program of health education that emphasizes consumer health." To Dr. Cornacchia, consumer health is an area of concentration in the broad field of health education which "includes quackery and health frauds but is broader in scope and also refers to health fads, superstitions, health advertising, the selection of medical and dental services, health insurance, health budgeting, health laws, health products, self-medication, health organizations, and agencies protecting the consumer, and reliable sources of health information."

Dr. Cornacchia has already given consumer health education courses to 500 teachers, school nurses, and school administrators to improve health education programs in elementary and secondary schools. He had the full cooperation of the Federal Food and Drug Administration, the California State Department of Health, the Federal Trade Commission, and such private local organizations as the Arthritis and Rheumatism Chapter of Northern California.

To take information programs more directly to the public, however, Dr. Cornacchia made the following proposal to the subcommittee: [39]

> A regional center to establish a pilot program that would attempt to coordinate and prepare a cooperative attack by the professional, voluntary, and governmental health organizations and agencies on the suggestions outlined should be started. The complexity of the problem facing this subcommittee is such that an organizational pattern different from any that now exists which uses the combined efforts of the community resources is necessary to provide new dimensions and greater emphasis on consumer health in the community. Such a pattern is in the early stages of developing in the San Francisco Bay area. Representatives from the California State Department of Public Health, the San Francisco, Contra Costa and Marin County Health Departments, the San Jose City Health Department, the University of California Medical School, Stanford University Medical School, San Francisco State College, and others have been convening for the purpose of establishing a health information, education, and exhibit program. The problem of medical quackery and health frauds for the elderly, or consumer health, could well be an area of emphasis and development by this center. If the Federal Government deemed it advisable and useful to appropriate funds to help initiate such a program, the center's first effort might be devoted to the problem being explored by this subcommittee.

The subcommittee agrees that such a project would be helpful, not only to the elderly, but to all consumers who will eventually become elderly. It also believes that a positive approach of this kind will be helpful not only to combat quackery, but to build generally better lives.[40]

[39] P. 116 op. cit.

[40] Subsequent inquiry by the subcommittee staff indicates that the Surgeon General has broad authority under 42 U.S.C. 203, 246(C), and 241 to establish such a program. He has a broad mandate to promote coordination of * * * demonstrations and studies relative to the * * * diagnosis, treatment, control, and prevention of physical impairments of men.

B. Federal research programs should be used in every way possible to help determine consumer attitudes on key questions related to quackery

It became apparent during the hearings that quackery persists in this Nation because of puzzling consumer attitudes, even when facts are readily available. A thoughtful analysis of the situation was given by Dr. W. Edward Naugler, Northern California Chapter, Arthritis and Rheumatism Foundation: [41]

> Our recommendation at this time is that in inquiry be made into several questions which it is now appropriate to ask. The medical service organizations should pool their efforts and set up a study group composed of physicians, behavioral scientists, attorneys, newspapermen, and experts in advertising to study in depth this problem and the problems which the following questions define:
>
> (1) What are the factors underlying the tendency of many persons to rely on self-diagnosis and self-treatment?
>
> (2) What is the net effect of the advertising of medications and health foods for specific complaints? Does such advertising contribute to the tendency for self-treatment?
>
> (3) What is the real effect of magazine and newspaper articles on medical subjects? The physician wants an informed public but do these articles produce the effect generally hoped for?
>
> (4) What are the most effective methods of enabling the public to find the best kind of medical care available in the community?
>
> These could be amplified, of course, into many categories.

The subcommittee recommends that the National Institute of Mental Health give appropriate assistance it can to such a "study group" if it be organized. Until such an effort is launched, it is recommended that the National Institute of Mental Health consider the possibility of launching one or more surveys in cooperation with the President's Committee on Consumer Interests.

C. Federal extension programs should be used whenever possible to give specific information of value to consumers of all ages

An example of the versatility of Federal extension programs was given Dr. George M. Briggs, professor of nutrition, Department of Nutritional Sciences, of the University of California: [42]

> I welcome this opportunity to describe a highly successful course of nutrition education which the university gave as an experiment in the spring of 1963 primarily for health food store operators, and to give my views on a positive approach to the education of health food store operators. * * *
>
> The course, "The Nutrients in Our Food," presented as a special evening course X–106, over a 6-week period—April 25 to June 6, 1963—for one unit of credit, was administered by the university extension division. It was developed and sponsored by the department of nutritional sciences in cooperation with the family and consumer sciences program

[41] P. 90, op. cit.
[42] Pp. 108–109.

of the agricultural extension service, and the Division of Nutrition, School of Public Health, University of California, Berkeley. The faculty consisted of myself as coordinator and 14 leading and distinguished nutritionists and biochemists in the university and the bay area. The program consisted of six Thursday evening lectures for 2½ hours on such subjects as the nutrients of our foods, vitamins, amino acids, minerals, carbohydrates, polyunsaturated fats, cholesterol, chemical additives, toxins in our foods, nutrition and disease relationships, nutrition history, special dietary foods and their composition, food labeling information, a discussion of "who is a nutrition authority?", nutrition of infants, children, adults, and older people, and sources of nutrition information and misinformation.

We used as our textbook the excellent U.S. Department of Agricultural Yearbook for 1959 on food. Each evening session consisted of two to four lectures by different persons, plus a half-hour panel discussion with the "experts" answering and discussing questions from the floor. We developed as strong a program as possible so that there would be no question at any time by members of the audience as to who were authorities. In other words, we "led through strength."

The program proved to be highly successful as well as popular. We enrolled 140 persons—each of whom paid a $30 registration fee—and had to turn down more who could not be accepted because of the capacity of the meeting room. Two examinations were required for the 80 persons taking the course for credit—the rest were auditors. Attendance and interest kept up very well throughout the series. * * *

To me, this was an excellent example of how food quackery can be attacked by a strong, positive program of nutrition education. I am of the opinion that operators of legitimate health food stores—or dietary food stores, as I would rather call them—have as much interest in combating food quackery and as much right to be in business, and to receive special education, as do owners of any other stores where food items are sold—say a grocery store, drugstore, liquor store, or department store—as long as the products sold are not misrepresented, are properly labeled, and are legal in all other respects. They stay in business only as long as customers come to their stores and make purchases, and as long as they offer for sale what the customer wants and what he usually cannot obtain at the corner supermarket. They specialize in such widely diverse items as special dietary foods—low-sodium foods, low-sugar foods, allergy-free foods, et cetera—unusual breads and grains, rare fruits and nuts, foods raised without pesticides or without inorganic fertilizers, a wide variety of types of honey, nutrition books, and many different types of vitamins, mineral, and protein supplements available on a nonprescription basis.

No matter what laws are passed against food quacks—and I'm as much against food quacks as anyone—legitimate dietary foods are going to be sold in one type of store or another as long as there is a demand for them and as long as

a small percentage of our population have special dietary needs. One cannot legislate against the "medicine man" any more than against immorality. In my opinion it is far better to educate the sellers of these products so that they become more responsible for what they sell, and to educate the consumer—the uninformed, the aged, the poor—so that they can buy wisely, if they need to buy these special foods at all. The great majority of persons have no need for special dietary foods.[42]

D. Government publications to warn the elderly and others against quackery should be evaluated

Early in 1964, the subcommittee staff began to collect information on publications issued by Federal agencies to warn the elderly and others against the dangers of quackery and other consumer frauds and misrepresentations. The survey is still incomplete, and no general conclusions can yet be made. The subcommittee intends to continue the survey in 1965.

Though many witnesses noted that such publications are issued, there was no widespread feeling that they are distributed adequately and that they attract the attention of those at whom they are aimed. Misgivings about the publications were voiced trenchantly by Dr. Irving Ladimer, vice president and Director of the Food, Drug, and Cosmetic Division, National Better Business Bureau, Inc.:[43]

I do not discount the very laudable work of many Government agencies, professional societies, voluntary health organizations, consumer and business groups in issuing books and pamphlets, but I wonder how well they reach people for whom they are intended and how effectively they are used.

I know this committee is compiling a bibliography of Government publications for the elderly and suspect that the total may well be over a thousand, covering health, clothing, housing, employment, business opportunities, insurance, and many other subjects.

But I would urge that the compilation project be extended to cover not only the number of booklets distributed but, at least in a few fields, the impact or change effected. Is a free or inexpensive brochure really helpful in improving buying habits, spending patterns, using equipment, keeping house, and, most important, avoiding health hazards and raising living standards? If not, perhaps other methods may be preferable.

Should we not, for example, teach how to get reliable information from responsible sources? Should we not instruct the various workers—doctors, nurses, social service personnel, guidance specialists, and other caretakers, how to help people help themselves in their communities?

Similar misgivings were expressed in 1964 during four regional conferences by the President's Committee on Consumer Interests. The subcommittee hopes to coordinate its specialized studies with a more general survey now under consideration by the committee.

[42] Pp. 108–109.
[43] P. 273.

The subcommittee also notes that the National Health Council, in cooperation with the American Medical Association, the National Better Business Bureau, the American Cancer Society, the Arthritis Foundation, and several governmental agencies, has conducted two meetings during 1964 in order to coordinate activities against quackery in medicine. At the March 9 hearing (p. 232), a representative of the AMA said that one of the major purposes of the effort would be to improve educational programs to local units of these organizations. Thus, the possibility exists that publications of private organizations may be given serious study to determine effectiveness and methods for improvement.

E. Increased use should be made of consumer education programs in federally assisted housing for the elderly

As has already been noted, agricultural extension services can be employed effectively to educate specialized groups about the dangers of quackery. (See pp. 19–21.) The Department of Agriculture also maintains cooperative service extension programs with low-income families in public housing. These programs have taken many forms, including the establishment of clubs to discuss homemaker problems.

In addition, the Public Housing Administration has statutory authority to provide housing and "necessary appurtenances" to tenants. In many cases, the Administration has authorized establishment of community space in public housing for tenant activities and has encouraged meetings on varying problems of mutural concern.

The subcommittee recommends that Department and Administration officials confer and report on additional steps that could be taken to provide consumer education demonstration projects of special value to elderly tenants.

Recommendation No. 4

Possible detrimental effects of the sale of spectacles through the mail should be the subject of a study by the Public Health Service; and the "corporate practice of optometry" in the District of Columbia should receive study by appropriate congressional committees

Under present law, it is permissible to advertise nonprescription eyeglasses through the mail if the advertising does not violate these Federal Trade Commission standards: [44]

> Rule 2—False advertising of nonprescription magnifying spectacles: It is an unfair trade practice for any industry member to publish, or cause to be published, any advertisement or sales presentation relating to nonprescription magnifying spectacles (sometimes referred to as readymade spectacles) which represent, directly or by implication, that the spectacles so offered will correct, or are capable of correcting, defects in vision of persons, unless it is clearly and conspicuously disclosed in the advertisement or sales presentation that the correction of defects in vision by such spectacles is limited to persons approximately 40 years of age and older who do not have astigmatism or diseases of the eye and who require only simple magnifying or reducing lenses; or to publish or cause to be published any advertise-

[44] P. 380, op. cit.

ment or sales presentation which has the capacity and tendency or effect of deceiving purchasers or prospective purchasers in any other material respect.

Highly critical statements about this policy were made before the subcommittee by witnesses who said that, in effect, the regulations encourage self-diagnosis by individuals. If they decide that they qualify for these glasses, they may wear them.

Dr. V. Eugene McCrary, vice president of the American Optometric Association, gave this summary of the situation:[45]

> The danger involved herein springs from the tendency on the part of many people to self-diagnose their problem and think to themselves: "All I need is a pair of readymade magnifying glasses." We feel that if a person insists on playing Russian roulette with his vision, he should at least realize the risks he is taking. The mere printing of a sign or ad, "Not for those folks under 40 or those with astigmatism or eye diseases," may salve a few troubled consciences, but does very little to remedy the problem.
>
> Statistics tell us that over 90 percent of the total population has some amount of measurable astigmatism, with about 65 percent requiring correction, and which these glazed goods lenses cannot correct. Statistics also tell us that from 2 to 4 percent of the population has some form of eye disease, and that there is a much higher incidence percentagewise for those over 40 and this incidence increases in frequency with the aging process. How can a person tell all by himself whether he has an eye disease which may eventually visually cripple or blind him if he must depend entirely upon his own observations? Commonsense tells us that few dime store or department store salesmen will require proof of age before selling a cheap pair of glazed goods lenses to a person.

Another reason for subcommittee concern was given by Dr. E. C. Nurock, O.D., chairman of the Advisory Law Committee, International Association of Boards of Examiners in Optometry:[46]

> A study made by an impartial organization disclosed that in more than 80 percent of the people there was a difference in the two eyes. Since readymade glasses have both lenses of the same strength of focus they could cause more discomfort and strain than without them. Age is only one factor in determining the prescription necessary for a patient and, in fact, is of very little importance. The sellers of glasses by mail seem to use age as the only basis for determining the lenses to be prescribed.
>
> The sale of readymade glasses to an uninformed and gullible public is an evil which all professional and lay organizations in the eye health and vision care fields agree should be completely eliminated without delay. The specious argument that these glasses cannot harm one's vision or that poor people will be deprived of reading glasses is simply not true.

[45] P. 380, op. cit.
[46] P. 478, op. cit.

> Vision problems, ocular and general disease, unfortunately increase with added years and are most prevalent among those who are most inclined to purchase readymade or so-called "grandmother" glasses. A great number of conditions, both ocular and general, can cause a decrease in vision. These causes can only be discovered by a professional examination. Some conditions can cause total loss of sight or even loss of life if not discovered in their early stages. Delay in seeking professional care and false reassurance caused by a possible increase in vision by using these magnifying spectacles is sufficient cause to eliminate their sale to protect an unwary public. Vision care is not a costly item by any standards and is well within the financial resources of virtually everyone. As professional men, we have great concern for persons in financial need, and it is incumbent upon us to provide eye care regardless of a person's ability to pay for our services.[46]

A further statement was given by the National Society for the Prevention of Blindness, Inc.: [47]

> It may be of concern to the committee to know that the prevalence of blindness in the age group 40 to 64 is 237.5 per 100,000 of the population; this figure increases to 1,098 per 100,000 of the population in the 65-and-over age group. These data indicate the urgent need for protecting senior citizens from the influence of information directed to encouraging self-diagnosis and treatment through the use of home remedies; and the purchase of spectacles, contact lenses, and other visual aids without examination by a qualified practitioner.
>
> Attention should be called to the need to emphasize the warnings on the possible deleterious effects on eye conditions of some drugs sold over the counter. Older people should be urged to carefully read labels and informational material packaged with drugs sold over the counter.[47]

To provide conclusive answers on possible detrimental effects of the mail-order sale of spectacles, the subcommittee recommends the Bureau of Medical Services, in the Public Health Service, undertake a study as soon as possible in order to present findings to Congress.

The subcommittee also received a number of statements condemning the "corporate practice of optometry." Dr. Maurice G. Poster, chairman of the Contact Lens Committee of the American Optometric Association, addressed himself to the fitting of contact lenses: [48]

> Aside from the question of competence, a person who depends for his livelihood on the sale of merchandise is unlikely to have the time or inclination to give the patient the attention which is required to instruct and supervise the patient.
>
> In all 50 States and the District of Columbia, only optometrists and physicians are licensed to prescribe contact lenses. *In actual practice, however, unlicensed and untrained*

[46] P. 478, op. cit.
[47] P. 515, op. cit.
[48] Pp. 415–416, op. cit.

and unsupervised laymen are fitting contact lenses for a staggering number of patients. We think this constitutes a health hazard to the public. [Emphasis added.]

William P. MacCracken, Jr., counsel for the American Optometric Association, gave additional commentary on the point: [49]

> In several States, corporate practice has been barred by judicial decision due to the fact that optometry is a profession and, as such, could not be practiced by a corporation. Several of our prominent chainstore merchandise establishments have what they call optical departments and employ a physician or optometrist to examine the eyes of their customers. One of them has as many as 80 outlets and each month they rate them on the volume of business transacted by the optical department. The manager, in his optical letter, uses such statements as:
>
> "Hail the champ. It's No. 1060. This fine operation repeated its stellar performance—and [the past year] found them ranking No. 1 again. Our congratulations to this fine optical department and its guiding light."
>
> The concluding part of this letter, after stating that the preceding year "was a good optical sales year" went on to say "all of you are to be congratulated. I salute you."
>
> This is all right for merchandising, but it has no place in any profession, and particularly one dealing with the sense of sight, the importance of which cannot be overemphasized.

Although, as indicated by Mr. McCracken, several States have acted [50] to restrict or ban "corporate practice" the optometry law of the District of Columbia was described as "lax" by one witness [51] and "antiquated" by another.[52]

Additional inquiry by the subcommittee reveals that the last congressional action in this field within the District dates back to 1924. Testimony taken by this subcommittee suggests that new merchandising methods have occurred since that action, and it is recommended

[49] P. 487, op. cit.

[50] The following summary was submitted to the subcommittee by the American Optometric Association, p. 479, op. cit.

Legal digest information—51 State boards of optometry

	Yes	No
1. Corporate practice prohibited by law	40	11
2. Space leased in mercantile establishment, prohibited by law	20	31
3. Readymade glasses prohibited by law	7	44
4. Minimum examinations required by law	21	30
5. Contact lenses included in law	26	25
6. Advertising prohibited by law	29	22
7. Professional card advertising permitted by law	40	11
8. Price advertising prohibited by law	35	16
9. Physicians and surgeons exemption	50	1
10. National board acceptable	24	27
11. Can grant reciprocity	34	17
12. Power to make rules and regulations	48	3
13. Can retain legal counsel	32	19
14. Attorney General used as counsel	42	9

[51] Dr. Nurock, p. 465, op. cit.

[52] Dr. McCrary, p. 402, op. cit.

that the Senate District of Columbia Committee examine the adequacy of present District laws on—

(*a*) widespread fixed-price advertising for regular glasses and contact lenses;

(*b*) sale of over-the-counter, nonprescription glasses;

(*c*) possible need for greater authority to the District Commissioners for regulation of "the corporate practice of optometry."

PART 2

INTERSTATE MAIL ORDER LAND SALES

INTRODUCTION

Until recent years, comparatively few Americans dreamed of retiring in distant States on land they had never seen. Approximately a decade ago, however, a mail order land sale boom began. Buyers were urged to make small payments—usually $10 down and $10 a month—for sites hundreds and even thousands of miles away. To many individuals near or past retirement age, the bright advertising brochures seemed to offer solid reason to believe that security, good climate, and a new way of life could be found on faraway sites in communities not yet built.

As 1962 neared its end, however, some purchasers, many enforcement officials, and a number of journalists began to find flaws in the boom. They tried to alert would-be purchasers to be on the watch for overly optimistic promoters and for outright fraud. Complaints and confusion increased; Federal agencies stepped up their surveillance.

Concerned about the potential impact of mail order land sales on the elderly, the U.S. Senate Special Committee on Aging devoted some attention to the industry in January 1963 during 3 days of general hearings on frauds and the elderly. Even in this preliminary study, the committee received considerable evidence of widespread sharp practices and misleading sales techniques. It was agreed at the hearings that the study of mail order land sales should continue. When a Subcommittee on Frauds and Misrepresentations Affecting the Elderly was established later in 1963, it was expressly instructed to investigate and report in more detail than possible at the earlier hearings.

Since that time, subcommittee staff field trips have been made to seven States. Witnesses representing nine States testified at hearings on May 18, 19, and 20, 1964.

MAJOR FINDINGS

FINDING NO. 1

Even at an early stage of growth, the mail-order land sales industry has already attracted many hundreds of millions of dollars from investors; it has great potential for increased service to the public as the demand for new homesites continues to mount

One of the major goals of the subcommittee was to arrive at some estimate of the magnitude of the industry. Difficulties in arriving at that estimate were summed up at the hearing by Gerald J. McBride, president of the National Association of License Law Officials: [1]

> A total estimate, for the entire United States, will take some time to compile, for there is no accurate source at the

[1] "Interstate Mail Order Land Sales," hearings before Subcommittee on Frauds and Misrepresentations Affecting the Elderly, May 18, 19, 20, 1964, p. 3.

present time. This is a difficult project, since the great bulk of these transactions are as yet unrecorded except in the records of the subdividers. The cumulative total of contracts on which purchasers are still paying must be enormous.

In spite of the difficulties in arriving at a total, there is good reason to believe that many hundreds of millions of dollars have already been invested.[2] Testimony revealed the following:

(*a*) Mr. McBride, basing his estimates on statements of other officials and claims of subdividers, said that the sales mark reached at least $500 million last year in Florida alone.[3] According to one recent newspaper estimate,[4] about 800,000 acres are selling on the installment plan.

(*b*) California public reports for the past 5 fiscal years have listed 677,590 acres in 861,778 lots.[5]

(*c*) Occasional clues are provided when enforcement action reveals the extent of operations for individual subdividers. H. B. Montague, Chief Inspector of the Post Office, told the subcommittee: [6]

> Our records show that in the seven cases where we have had convictions, the take was about $800,000; that in the cases we have under indictment, those cases that have not yet been to trial, the take was in the neighborhood of probably $4 million. Therefore, in these 20 cases, from actual figures that the inspectors compiled as a result of their investigations, there was a take of about $5 million.

(This estimate covers only 20 cases of 358 Post Office land fraud investigations that had been authorized by May 20, 1964.)

(*d*) There can be no doubt that the industry has already bought up large holdings in many parts of the Nation. One Florida witness said that 38 square miles of land has been bought up in Volusia County alone. He added:

> "They are usually able to get 512 acre-and-a-quarter tracts to 1 square mile, so 38 square miles adds up to 19,456 lots or investment parcels. That is just in 1 county, and there are 67 counties in Florida." [7]

Another witness, Reporter Robert A. Caro of Newsday, described another major land sale area: [8]

> I don't think any verbal description can prepare anyone for the sight of a vast desert valley in Mohave County, Ariz., perhaps 60 miles long and 20 miles wide.
>
> "When you top a mountain rise and come into the valley, you can see the entire valley. There is not a sign of human habitation, except every few miles there are signs saying, "This is Shangri La Rancheros" or "Heavenly Acres." Then you go into the county courthouse and ask the county clerk,

[2] Many studies of mail-order land sales have given $700 million as the annual approximate volume of sales. Mr. McBride, at the 1964 hearing, described this as a pretty good estimate, but emphasized that, for the reasons given above, more precise estimates cannot be offered at this time.
[3] P. 3, op. cit.
[4] Miami Herald, Apr. 19, 1964, article by Haines Colbert, cited on p. 213, op. cit.
[5] P. 3, op. cit.
[6] P. 238, op. cit.
[7] P. 151, op. cit.
[8] P. 89, op. cit.

"Are people out there really buying that land?" And he laughs and shows you the deeds, with thousands and tens of thousands of names of people in New York, New Jersey, and Illinois, paying their $10 or $20 a month on that same land that you just walked off of.

A few figures might give a better picture than I can of the scope I am talking about. In that single Arizona county, Mohave, there were, as of last July, 335 separate developments, some with thousands of lots being sold through the mail to residents of the Northern States.[8]

(*e*) Some idea of profits—when the subdivider is unscrupulous—was given by W. Dan Bell, president and general manager, Denver Area Better Business Bureau: [9]

> The promoter may have realized between $750,000 and $1 million in scrubland in 18 months of operation. We estimate that the total of wildcat promotions in Colorado during this period (1954–62) would approximate $5 million in sales.[9]

MANY REPUTABLE FIRMS AT WORK

Although the subcommittee was primarily concerned with promoters who deliberately cheat their victims, it recognizes that the mail-order land sales industry already has performed major service for many individual buyers. One developer, for example, told the subcommittee that his corporation devoted 5 years of research and approximately $16 million in the planning and construction of its first retirement community. Substantial, reputable developers are making comprehensive efforts to provide livable retirement environment for the elderly and others who buy through the mail.

The subcommittee also recognizes that increasing population pressures, and the ever-growing mobility of all citizens, will increase the demand for the opening of new, and sometimes marginal, land for development. Well-managed mail sales can make a considerable contribution to such development.

Recognition of the present and potential usefulness was given by the subcommittee chairman on March 19: [10]

> Senator WILLIAMS. It should be made clear here that the industry has already accomplished fine results in many parts of the Nation. Thousands of retired persons are now living in well-planned communities built on once-marginal land, or on lots deep in the desert, and even on land that was once jungle or swamp. We will hear from witnesses who will tell us just how much has been accomplished.
>
> In summary, the high standards of the many should not be endangered or clouded by the actions of the minority. With the objective of presenting a balanced picture of the accomplishments and the dangers, this subcommittee now begins this inquiry.

[9] P. 13, op. cit.
[10] P. 2, op. cit.

FINDING NO. 2

Enforcement action and publicity have hit hard at blatant schemes to defraud or mislead the buyer, but more subtle sales techniques are now at work; in some cases, where outright fraud may be difficult or impossible to prove, sales literature may nevertheless give the buyer a grossly distorted impression of the land he buys

Until public attention was drawn to them, many early promoters committed blatant excesses in ignorance or defiance of the Federal postal fraud statute.

They sold land they did not own. They offered "free lots" at State fairs or in lotteries and required the "winners" to pay so-called closing costs that were not actually required by local law. Some relied upon totally inaccurate advertising to sell their products. Two men who sold land in Idaho, for example, were convicted for making fraudulent representations as to streets and water and sewerage systems. Indictments were handed down against other developers charged with advertising that water and other amenities existed on their desert acreage when in fact there were none.[11]

Transgressions of these early promoters received careful attention from the Postal Inspector's Office.[12] Some idea of the extent of the land investigative program can be gathered from this summary of action between July 1, 1962, and the subcommittee hearing in May:

Land fraud investigations authorized	358
Cases closed	165
Cases currently under investigation	193
Cases presented to U.S. attorneys	35
Cases in which indictments returned	22
Number of defendants indicted	60
Cases in which convictions obtained	7
Number of defendants convicted	13
Cases wherein indictments are outstanding [13]	15

Each mail fraud case took months of painstaking investigation and preparation. And each (as explained in sec. V) was made more difficult by the "intent to defraud" provision of the mail fraud statute. The threat of 5-year sentences and fines up to $1,000 under that statute, however, undoubtedly inhibited those who had hoped to continue questionable mail order land promotions.

Notwithstanding the salutary effect of the mail fraud statute and new State laws, the subcommittee has become concerned about other practices that do not fall within the strictly defined jurisdiction of mail fraud investigators. Slippery language and omission of important facts can, in the opinion of the subcommittee, cause almost total misunderstanding and confusion.

Tricks of the trade.—A concise summary of present techniques was given by Alton W. Van Horn, then commissioner and now president of the New Jersey Real Estate Commission. Mr. Van Horn, who has conducted on-site investigations for the commission in many States to compare advertising copy with on-the-spot realities, told the subcommittee:[14]

[11] An analysis of Federal mail fraud actions on p. 242 of the transcript shows that the "free lot" frauds had resulted in the majority of convictions and indictments.
[12] State legislatures also contributed to the retrenchment of shady promoters. (See next section.)
[13] P. 234, op. cit.
[14] P. 248, op. cit.

The difference between the impression created by the promotional material and the true fact is of the greatest concern.

Artists' conceptions not labeled as such and alleged or suggestedly nearby—but actually quite distant—scenes are routinely used, instead of on-site or accurately labeled photos.

What pass to the uninformed as maps are too frequently prepared with shocking disregard to scale and proportion. Recreational areas, water bodies, and places where shopping, schools, and other facilities might be available, are pictured much closer than they are.

Distances tend to be indicated as "minutes away" instead of hours (at legal speeds) or in miles over travelable roads. One illustration was where you would have had to drive 68 miles in 45 minutes which is a little beyond the driving capability of most people.

The fact that flash floods, windstorms, sandstorms, temperature extremes and other weather phenomena affect some areas is not usually revealed; nor are such things as water depth (and cost to reach it), and the absence of vital services.

Another factor is the contract often used. The small down payment makes it easy to take. The long term postpones the day of discovery (of just what one has purchased). This is like a long-delayed fuse on a potentially explosive situation.

Quite general is the nonacceleration clause which prevents taking of title and delivery of deed before it meshes with the developer's convenience or his ability to release his mortgage or get subdivision approval. Some would take the money and give a certificate of ownership because they can't deliver a recordable deed.

The matter of a firm declaration of exactly what improvements will be installed—and when—is omitted more often than not and seems a very painful area even for discussion.

The usual money refund and transfer guarantee are far more useful to the promoter than to the investor or the retiree. They lull one into thinking it must be safe but, on close scrutiny, the money is returnable only on inspection and often only at the property, rather than at the point of sale. The exercise of the switch privilege—in order to reduce by many miles the distance between your lot and the nearest human abode, a water source or powerline—may add to or multiply your cost.

The guarantees are sometimes amusing. One even makes the generous guarantee that the "full 1-acre rancho" embraces 43,560 square feet, a little like guaranteeing the foot to be 12 inches.

Speaking of the fine print—a new twist is the back-of-contract pale gray, fine print. The things the developer wants read are in bold black, before you sign. Other things are on the reverse in pale gray. It often takes strong light, real diligence, and optimum visual acuity to penetrate that verbiage.

Mr. Van Horn also gave the subcommittee a step-by-step account of a field trip he made to a subdivision in a Southwestern State late in 1963. He described the sales promotion as "middle of the road" and by no means "exaggerated, extreme, or bad."

Nevertheless, the New Jersey Real Estate Commission denied permission to sell the land inspected by Mr. Van Horn because, in his words, the advertising "leaves significant facts unrevealed and would tend to create in the mind of a typical and reasonable reader an impression substantially at variance with the facts observed at and in the vicinity of the premises."

Some of the reasons for the commission's action given by Mr. Van Horn at the hearing:

1. Little or no indication was given of the true nature of the land that is being sold—the arroyos, the washes, the gullies. Photographs show the developed area—which includes a clubhouse, swimming pool, and model houses—and give absolutely no idea of the nature of the undeveloped area now being marketed.

2. The fact that the elevation reaches 6,100 feet was nowhere made plain. "That is a little like living at the summit of Mount Washington, give or take 280 feet," commented Mr. Van Horn.

3. Mr. Van Horn found much reason to question the glowing predictions of dramatic increases in land value in the area.

4. Buyers are offered an "exchange privilege," but Mr. Van Horn questioned whether they clearly understood the terms. He explained that some of land sold is 10 or more miles away from the small area that already has piped water, piped gas, power, and telephone lines.

"A prospective buyer," said Mr. Van Horn, "would have no way of knowing whether he was buying 9 or 10 miles removed from such an area or whether he was buying adjacent to such an area.

"Neither is there any indication given that the price is some $900 higher in the area where the utilities are available. This is according to the manager, who quoted figures of $995 and $1,895, respectively." [15]

5. Mr. Van Horn also concluded that the average buyer almost certainly would be overwhelmed by the sheer bulk of promotional material provided by the seller in the course of trying to conclude the sale, including brochures and contradicting facts given in other material. "We should have something which strips the problem to its essentials rather than a flowery prospectus type of thing where the true facts may be buried in it," said Mr. Van Horn.

Mr. Van Horn was careful to say that some of the conditions he observed may have changed after his trip. The subcommittee is also careful to note other States have approved the subdivision in question. But the subcommittee also believes that Mr. Van Horn's testimony raises significant doubts about the ability of a layman to evaluate, with any degree of accuracy, much of the advertising literature given to him by mail order land companies. The subcommittee also finds much to applaud in this statement by Mr. Van Horn: [16]

> New Jersey's regulatory philosophy is that a New Jersey resident should be able to buy anything, regardless of its

[15] Owners of the land in question, invited to testify, did not send a representative. In a statement later admitted into the record, an official of the corporation took sharp issue, among other things, with Mr. Van Horn's interpretation of the exchange privilege. The corporation statement begins on p. 338 of the transcript. Additional commentary by Mr. Van Horn on the exchange privilege and other matters begins on p. 350.

[16] P. 249, op. cit.

nature or value, provided he isn't being substantially misinformed or left materially uninformed.

INVESTMENT ACREAGE

A fairly new trend in mail order land sales was described at the hearing by Mr. McBride: [17]

> Now we find that stress is being placed either on holding the land as an investment for resale later at a profit or buying it now, so that when retirement age is reached the land will be paid for and ready for occupation.

Unlike those who claim that their subdivisions are idyllic and well endowed with modern conveniences, the investment acreage merchandiser usually specifically says that the land is undeveloped without any public facilities at all. He may also suggest, however, that the value of the land is almost certain to go up, perhaps to two or three times the original investment. He will also probably point out that Miami Beach and Los Angeles once were regarded as poor investment risks, but that fortunes have been made from wise real estate purchases on land once regarded as absolutely unpromising.

The subcommittee agrees that astute, or even lucky, buyers can make substantial profits by speculating in real estate. The subcommittee believes that nothing should interfere with the right of a buyer to make a purchase, no matter how risky it may seem at the time of purchase. But the subcommittee also believes that omission or distortion of facts, even under these circumstances, can lead a purchaser to make a transaction far more unfavorable than he may realize.

This attitude was expressed emphatically by Mr. John R. Hoffman, vice president of the National Better Business Bureau. He said: [18]

> We tell the public inquiring on "investment offers" that the purchase of undeveloped acreage is a highly speculative proposition depending for success on many factors that are difficult to estimate even when one is completely familiar with a given area. We urge a thorough personal investigation and a decision on facts developed, after personal inspection.

Many convincing reasons for such caution were expressed at the hearing. Mr. James Greenwood, a realtor and appraiser in Daytona Beach, gave this description of the typical operator: [19]

> How does an investment acreage promotion work? Well, a promoter buys a large tract of cheap land, often swampy. Usually he transfers the title to a related corporation to gain a tax advantage. Then he carves up the property into acre-and-a-quarter parcels, the smallest permitted under most plat laws.
>
> Then they have beautiful, enticing brochures printed and start running advertisements in various newspapers, magazines, company organs, et cetera. U.S. servicemen, especially those overseas, have been a favorite target of the

[17] P. 4, op. cit.
[18] P. 285, op. cit.
[19] Pp. 151-152, op. cit.

swamp merchants. The acre-and-a-quarter tracts are sold in installment contracts. No deed is recorded until the contract is paid off. Most contracts stipulate that the property reverts to the seller if the buyer misses one or two payments, and the seller is not required to notify the buyer that he is delinquent.

Many, but not all, contracts carry interest on the unpaid balance, usually 5 or 6 percent. Many of these lots are sold over and over again, year after year, as buyers stop their monthly payments for any number of reasons—they die, come upon hard times, come down and see the land, et cetera.

Few of the promoters make any improvements in the land although some will dig a small drainage ditch, give it a high sounding name such as the "Grand Canal," put in a road or two, bulldoze the swamps that can be seen from the main road, if indeed there is a main road. This is called window dressing and it enables the unscrupulous operator to tell his prospects that he is "improving" the property. Actually, if no real improvements are planned, he is required by the installment land sales board to say so in all of his advertising material, but it usually appears in the small print.

Usually, easements, not roads, are provided to each lot to give the owners legal access. Most lots are sold in metes and bounds, although some tracts are platted. It would cost most owners more to have their lot surveyed than they paid for it.

No surveys are furnished buyers other than a rough draft of approximately where their property may be located in a given area.

Several years ago I spent almost 2 days, using a slow plane and a four-wheel-drive, radio-equipped jeep, to try to locate a certain parcel in a development called University Highlands, being sold by a corporation named Firstamerica Corp., located approximately 10 miles west of Daytona Beach in a dismal swamp.

After 2 days of some of the roughest riding, we had to give up, as it was impossible to penetrate deep enough into the swamp to a point which we had spotted from the air.

Incidentally, this parcel was sold to a woman from Syracuse, N.Y., who had intended to use it as a homesite for a trailer house. Needless to say, it could never have been used for this purpose.

As a real estate broker and appraiser conversant with land sales as they affect Florida, I strongly urge that at least some form of Federal regulation be brought to bear upon the unscrupulous operators now enjoying Federal immunity.

The business editor of a Florida newspaper, gave the subcommittee other examples: [20]

A firm, forbidden by law to sell its tracts as homesites because of the lack of improvements had—at the time of the hearings—erected a model home on a highway about a half mile north of the property they were selling. A letter sent out by the owners of the property

[20] P. 134 ff.

mentioned that the model home had been built on the property. The implication was that other homes could be built, even though the subdivision law clearly forbade it.

Photographs showed tracts under water deep in cypress. The witness, Mr. Morton Paulson, said that U.S. soil conservation district records show that one-third of the land in the subdivision is solid cypress swamp.

At another "investment acreage" subdivision, owners are selling land even though they've been told that the property may be condemned as a water resource. If this takes place, buyers will be paid its appraised value at that time, and will have no opportunity at all for "doubling" or "tripling" profits. Highway builders working in another part of the property ran into a muck pocket that was more than a mile long and 20 to 25 feet deep.

Sales literature for still another development says:

> A system of graded roads makes every section readily accessible.

Mr. Paulson commented:

> The average real estate buyer probably doesn't realize it, but a section takes in 1 square mile of land; so any given tract * * * could be as much as a full mile away from the road.

An article by Mr. Haines Colbert in the Miami Herald of April 22, 1963, told the story about a woman who once asked how much it would cost to survey her small land purchase in eastern Collier County. She was told that it would cost $20,000, because the greater part of the area around it had never been surveyed—the nearest point previously surveyed was 20 miles away. The land in question was described by Collier County Engineer W. Harmon Turner as "flat, mostly covered by water in the wet season, and the water drains off very slowly. There are large marshes which are wet most of the time." [21]

[21] The upshot of this incident was described in a story by Mr. Paulson in the June 7, 1964, issue of the Daytona News-Journal:

"HOW'S BUSINESS?

"CHEERING NEWS FOR LOT BUYER: SURVEY WON'T COST $20,000

"(By Mort Paulson, Business News Editor)

"The Florida Installment Land Sales Board had good news (of sorts) last week for the Miami Beach woman who dropped the telephone in shock when told how much it would cost to survey her small tract of land in eastern Collier County.

"The survey won't cost $20,000 after all. The price will be no more than $125, and possibly as little as $50.

"It was the Miami Herald which first revealed in April how the unidentified woman called engineer W. R. Wilson in Naples for an estimate. He quoted the $20,000 figure to stake out her lot because, he said, he would have to go 21 miles from the nearest previously surveyed point, lay out a township of 36 square miles, reduce that to sections of 1 square mile and then find the boundaries of the woman's property. None of the land in the area has ever been surveyed.

"The story, which might be amusing if it weren't rather pathetic, was retold in testimony last month before a U.S. Senate subcommittee investigating land frauds. When John W. McWhirter, executive director of the Installment Land Sales Board, heard it, he got in touch with a Miami land surveying firm and sold it on the idea of doing a mass survey of property in Collier County.

"Within about 30 days, E. R. Brownell & Associates will start charting the thousands of small tracts in ranges 33 and 34 which were sold by mail for $10 down, $10 a month. Owners who want their lots marked off with flagging pipes and drawn up in certified sketches will be charged $50 for 2½ acres, $90 for 5 acres, and $125 for 10 acres.

"The program is expected to take 18 months to complete.

"So the lady in Miami Beach can rest easier. Now all she has to worry about is draining her property, clearing it, putting in streets, and being able to sell it to somebody who wants to live in the wilds of Collier County."

Perhaps the most pointed criticism of investment acreage sales techniques was made in a statement submitted to the subcommittee by Herbert E. Wenig, assistant attorney general, State of California: [22]

> I wish to emphasize at this point; even if there is full disclosure, the sale of undeveloped lots in a premature and remote subdivision for use as homesites or for investment is inherently fraudulent. Once the promoter sells the lots, the scattered ownership and diverse wishes of lot owners make concerted self-help most difficult. All the risks of creating a livable homesite by the development of an adequate water supply and the installation of streets, sewers, and other utilities rest upon the individual buyers. The problem is accentuated by the remoteness of the subdivision.

Telephone "boiler rooms".—As regulatory surveillance of claims made in printed advertisements increases, some subdividers are apparently resorting to intensive telephone sales operations. The most direct evidence on this point came from Mr. Paulson: [23]

> Now if you'll bear with me for just 5 more minutes, I would like to discuss one other sales approach that certain land dealers are making more and more use of. That's the long-distance telephone.
>
> Since the State of Florida began cracking down, and censoring out many of the wild claims made in printed brochures, many of the investment acreage companies have set up long-distance boiler rooms; that is, rooms full of telephone pitchmen.
>
> The companies subscribe to wide area telephone service, or WATS service, and can make unlimited numbers of long-distance calls at flat monthly rates.
>
> This is a very expensive way to sell, but it obviously pays off. It costs $2,475 a month for one WATS telephone on which calls can be made to any place in the continental United States.
>
> For proportionally less money, the companies can get phones covering limited sections of the country.
>
> I can't tell you how many companies are using this service, but I was told by a telephone company official that there are at least six in the Miami area alone. Some of them have several phones.
>
> This same official said their monthly phone bills would "knock your hat off."
>
> We know that one company, Firstamerica, has used as many as six WATS phones at one time, four nationwide and two limited. That means they spent somewhere around $14,000 a month for telephones alone.

[22] P. 25, op. cit.
[23] P. 145, op. cit.

Here's something else—a reproduction of a help-wanted ad which appeared a couple of months ago in the Miami Herald. It says telephone acreage salesmen make up to $25,000 a year.

At one point in the hearing it became apparent that there is basis for Federal action against false claims made during such sales talks even on the telephone: [24]

Senator WILLIAMS. You know another way these operators are doing business these days, some of the swamp merchants—we had some very good testimony on this yesterday, too—are using the telephone, long-distance telephone calls.

Mr. MONTAGUE. Yes, sir.

Senator WILLIAMS. You don't reach the operator who is dealing with interstate commerce through the telephone.

Mr. MONTAGUE. Yes; we could, Senator, because usually a telephone call of this kind would cause the use of the mails as it could cause the receiver of the telephone call to send an order through the mail or something of that kind so the mails would be brought into the picture.

Senator WILLIAMS. Yes; I see your point. Because one of the staff members at my request took a newspaper ad for one of these developers in Florida. She was getting a call a day and sometimes two. She received at least six or seven calls. Mr. Paulson from Florida yesterday stated that he did that, too. He said that the pitch got better all the time.

And then a fellow called and said, "We just learned that the power company is going to run a powerline down there." This was old news indeed. The company 2 years before had said that they were going to do it but didn't say when. Then he fixed a deadline but even after the 24-hour deadline had passed he still got calls from the salesman.

FINDING NO. 3

State regulations grow more complex and diversified as the industry grows

As mail order land sales have become a multimillion-dollar business, the various States in which large-scale developments are located or in which there is a heavy volume of mail order sales have attempted to protect their citizens from fraudulent or misleading sales.

[24] P. 246, op. cit.

By 1964, at least 20 States had some form of law regulating the sale of out-of-State land development.[25]

The most common regulatory technique is "full disclosure." The developer is required to submit detailed data as to the condition of the land he proposes to sell to the State real estate commission or department before he is permitted to sell within the State and his property may be inspected by agents of the State board. New Jersey has such a law, which has recently been broadened to provide for the preparation of a public report by the real estate commission on each development. A copy of this report must be furnished by the seller to a prospective buyer.

The principle behind the "full disclosure" laws is a sound one. The buyer is provided an objective yardstick by which he can judge the financial soundness of the developer, and the actual state of the development where he intends to buy land. Hopefully, the buyer will

[25] The following summary was offered by Mr. McBride (p. 8, op. cit.).

Name	Have law	Type
Alabama	No	
Alaska	No	
Arizona	Yes	Full disclosure.
Arkansas	No	
British Columbia	Yes	Full disclosure and permit system.
California	Yes	Full disclosure and fair, just, and equitable theory.
Colorado	Yes	Licensing statute—developer must be certified.
Connecticut	No	
Delaware		(No reply.)
Florida	Yes	Installment land sales act.
Georgia	No	
Hawaii	Yes	Full disclosure.
Idaho	No	
Illinois	No	
Indiana	No	
Iowa	No	
Kansas	No	Securities Act provision.
Kentucky	No	
Louisiana	No	
Maine	Yes	Administered by security division on fair, just, and equitable theory.
Maryland	No	
Massachusetts	No	
Michigan	No	Statement of policy requested.
Minnesota	Yes	Full disclosure.
Mississippi	No	
Missouri	No	
Montana	Yes	Inquiry information.
Nebraska	Yes	Permit system.
Nevada	No	
New Hampshire	No	
New Jersey	Yes	Full disclosure.
New Mexico	Yes	Do.
New York	Yes	Do.
North Carolina	Yes	Ordinance approved plan.
North Dakota	No	
Ohio	Yes	Security, fair, just, and equitable theory.
Oklahoma		(No reply.)
Ontario	Yes	Full disclosure.
Oregon	Yes	Full disclosure and permit system.
Pennsylvania		(No reply.)
Rhode Island	No	
South Carolina	No	
South Dakota	No	
Tennessee	Yes	Security division.
Texas	No	
Utah	Yes	Full disclosure and permit system.
Vermont	Yes	Securities commission regulation.
Virginia	No	Local control.
Washington	No	
West Virginia	Yes	Securities commission regulation.
Wisconsin	Yes	Fair, just, and equitable theory.
Wyoming	No	

study the statistics and often cryptic language of a public report on a land development with the same interest that he reads the glossy brochure of the salesman.

Five States which do not have laws specifically directed at interstate land sales regulate these sales under State statutes governing the sale of securities.

Several States, notably California, carry the "full disclosure" method one step further and apply the "fair, just, and equitable" test to interstate land sales. Under California law, the California real estate commissioner not only investigates out-of-State land developments and issues a public report on them, he also determines that the offering price is fair, just, and equitable.

The testimony of many State officials demonstrated the conscientious and determined efforts the States themselves are making to eliminate the worst abuses in interstate land sales. However, it is certain that operating through the mails, land developers are at work in every State. Although many States may give some measure of protection to their citizens, there is still ample territory in which the unscrupulous developer may operate without effective regulation.

Your subcommittee hopes that other States will adopt adequate laws for the regulation of interstate land sales. The National Association of License Law Officials has been actively studying a model State law requiring full disclosure by developers and issuance of a public report. At its annual meeting in 1964, the National Conference of Commissioners on Uniform States Laws appointed a special committee to draft uniform legislation on interstate land sales for enactment by the States. The work of these two influential organizations should give added impetus to the passage of adequate laws by States which do not now have them. Your subcommittee believes that regulation of interstate land sales by each of the 50 States would be a strong deterrent to the operations of fly-by-night land developers and would encourage public confidence in those honest developers who make up the majority of this industry.

FINDING NO. 4

Local authorities are giving more consideration to potentially undesirable land use patterns that can follow in the wake of mail-order land sales promotions

The subcommittee, attempting to determine whether elderly purchasers can run grave risks in purchasing land described as having great profit potential, received testimony suggesting that some holdings have little potential for any development at all. Scattered ownership and other complications, said several witnesses, can cloud the future of land that might otherwise be eminently suitable for other use.

Mr. Keith Koske, executive secretary of the Colorado Real Estate Commission, described the consequences of large-scale land sales without adequate control at the local level: [26]

> I realize that the primary purpose of this subcommittee is to investigate methods to protect the aging purchaser. However, personal injury is not the only injury created by the unscrupulous subdivider. There is also an injury to the

[26] P. 71, op. cit.

State wherein the land is located, and there is also an injury which will fall upon our posterity. The orderly development of land is necessary to provide a continuous economic stability. Rural counties of Colorado have found some of their land to be so irresponsibly subdivided that tax assessment and collections are made difficult and costly. A county treasurer may have registered, as the owner of the land, a foreign corporation which has no intention of paying taxes. If a new owner of a lot has recorded his interest, the county treasurer may be compelled to spend $3 preparing a tax bill of 50 cents to be mailed to a resident of New York or Hawaii. Land is the tax base of the rural county for the support of its schools and other services. The tax base may be altered or made smaller.

Migration to such an undeveloped subdivision causes other problems. The only development that occurs may be a shack town created by the individual purchasers. Their development of the land is limited by their own individual financial resources. Oftentimes a health problem results, and the State or county may forbid further development. The land is abandoned by the purchasers, and it reverts back to the county for nonpayment of taxes. This cycle may repeat itself.

The reputable subdivider may wish to begin a proper development of the same land. He may find a renewal problem. Or he may find it necessary to begin an action to quit title, but this may not be successful. Assembly of lands is difficult because of the many owners scattered all over the United States and Canada. The assembly of the land may even be impossible. Orderly development of the land may be stopped, or delayed, or be made far more costly than it should be.

These are all injuries which are suffered not by the individual purchasers but by the residents of the State and community wherein the land lies; and, they are injuries which will also fall on our children.

Much the same situation was described by Mr. Robert Doyle, planning director of the East-Central Florida Regional Planning Council: [27]

As to what, if anything, the irresponsible mail-order developer does to "improve" the land for residential use, I'd like to describe one promotional effort that took place in our region a few years ago.

The original people are now bankrupt. The property was redistributed and a reputable developer has since tried to reassemble this property and do something with it. This is what he found when he tried to do something with it.

In this case, no sewer or water provisions of any kind were ever installed to serve the property in question; nor were any areas set aside for school, recreation, or other public purposes. Although drainage of a sort was attempted, it was

[27] Pp. 156–157, op. cit.

largely ineffective, according to the developing group, because it was laid out in the gridiron pattern.

Other than the entrance proper, what passed for roads were "constructed" as follows: First, a narrow right-of-way was bulldozed through the palmetto underbrush in the prescribed gridiron fashion.

Next, small ditches were dug on either side of these "pathways" such that continuous, parallel furrows of earth were created. These furrows were then flattened to give the appearance of freshly graded streets—especially if photographed or reviewed from the air.

The promoters of this "development" eventually went bankrupt, but not before scores of lots were sold sight unseen through mail and television advertising methods to persons of modest means who were located, for the most part, in certain Midwestern States. I am happy to say that the county wherein this operation took place has since instituted controls which should prevent a recurrence in future years.

In California, according to Assistant Attorney General Wenig, the excesses of other decades are having their effects today: [28]

> California has witnessed a series of land promotions—indeed, some people think that the promotion never stops. A national magazine article, "The Boom of the Eighties," describes the land promotions of that decade in our State—the promises, projections, and the resulting ghost towns. Even today, 75 years later, when population pressures and suburbanization are beginning to reach some of the ghost town areas, it is difficult to develop the tax-deeded acreage because of scattered ownership of the lots which were sold. California's response to the recurrent speculation and improvident premature land subdivision was the enactment of its subdivision law requiring a public report fully disclosing all pertinent facts to a prospective purchaser and a concomitant subdivision map act enabling counties and cities to enforce local ordinances calling for the installation of improvements prior to sale.

Mr. Caro warned that the greatest impact of the mail-order land sales of the 1950's and 1960's is yet to come: [29]

> This is not a problem of the present. None of the big problems posed by the mail-order real estate boom is hitting us right now. But the boom contains a built-in time bomb. As you know, this land is being sold off on installment contracts, and these contracts are generally being paid off over 9 or 10 years. Since the boom only reached large-scale proportions relatively recently, these contracts won't begin to mature for a while yet.
>
> Until they do, experience has shown the majority of the individuals paying off on their contracts won't go down to see their land. At that time, those purchasers who bought

[28] P. 24, op. cit.
[29] P. 93, op. cit.

land in completely worthless desert or swamp promotions will realize that they have been gypped.

Keith Barnard, former president of the Chicago Better Business Bureau, says that when this happens "it will be the great national scandal of the 1960's." I agree. But I would also like to go a little further.

I submit to you that the bigger problem, in terms of its total implications, is what is going to happen to the tens of thousands of elderly couples who do move from the cities and suburbs of the North to partially developed "retirement cities" in undeveloped counties of Florida and the Southwest. Without industries to provide them jobs to eke out their social security and pension checks, without adequate municipal services, hospitals, or adequate funds for welfare, what is to become of them?

What of the whole concept of herding together large numbers of elderly persons, an idea now being frowned upon by many leading gerontologists, as you know.

We don't know the answers to these questions. But the questions are starting to loom ever larger. To me, anyway, they seem frightening. This is a national problem, and it should be handled on a national basis by Federal regulation.

Industry witnesses, in letters and in testimony, made it quite clear that entire communities have already been built through mail order sales. But they also made the point that such efforts required adequate financial resources and years of careful preparation. The subcommittee is concerned, not about such commendable projects, but about those who sell land with the vague suggestion that it can ultimately become part of a bustling community when, in fact, major obstacles have been put in the pathway of such development.

Only local action can effectively cope with the local problems. But how is a buyer to know whether such action has been taken, unless the seller is honest enough to tell him or unless some form of legal standard requires the seller to do so?

FINDING NO. 5

Industrywide self-regulation is a commendable goal, but it is slow in coming

Soon after the first news reports about mail-order land sale problems began to appear in 1961 and 1962, many subdividers and developers began to promulgate codes of ethics for private application by members. Others spoke of more extensive self-regulatory efforts.

The National Better Business Bureau, which also distributes a code of ethics, attempted to stir more direct action.

Mr. John R. Hoffman, testifying for the NBBB at the hearing, described the results: [30]

Senator WILLIAMS. Thank you very much, Mr. Hoffman. Did you sponsor a meeting of the industry last year?

Mr. HOFFMAN. Yes; we had a meeting last December in Scottsdale, Ariz., near Phoenix wherein the bulk of the industry was invited to attend the meeting to implement a

[30] P. 285, op. cit.

program of self-regulation. We proposed a 10-point program to the entire industry, an example of which I have here, which we would have implemented.

Regrettably that program has not been put into effect.

Senator WILLIAMS. You wouldn't have been able to gather or to bring to the meeting the worst of these operators, would you? They wouldn't come out, would they?

Mr. HOFFMAN. We had nearly a hundred representatives there representing both the good and the bad. Some I would characterize as highly promotional operators. Others were definitely responsible developers who had a community to show. They were, I am afraid, in the minority of that group.

Senator WILLIAMS. What were the lines of discussion in this industry group?

Mr. HOFFMAN. We presented, as I say, this 10-point program of what we proposed to do about the problem. We had many questions and an open meeting after our various presentations and answered many questions.

There seemed to be some enthusiasm among a number of the industry people there. And then there was a closed industry meeting thereafter wherein the question of raising of funds to implement a program was discussed. It was decided that an effort would be made and we were given assurances that the funds would be raised to implement the program, but this has not happened.

Senator WILLIAMS. If we wait for effective self-regulation I imagine we will be waiting a long, long time, won't we?

Mr. HOFFMAN. It is conspicuous by its absence at the present time.

Statewide associations are at work. A representative for the League of Arizona Developers gave a summary of the league's progress thus far: [31]

Senator WILLIAMS. Could you describe the League of Arizona Developers, what the membership is, and what part of the total industry you represent?

Mr. BERTOCH. In dollar figures, Senator?

Senator WILLIAMS. No, developers.

Mr. BERTOCH. We have at this time approximately 25 active members. We have five or six associate members. I don't have the list of the membership at this time. I could prepare one and have it forwarded to the committee. This is a group, again, which is a young group, but we think we have some of the people in industry who are interested in this movement. We feel that we are going to increase our membership this year and the following years, and become a stronger voice.

Senator WILLIAMS. What is your estimate of the number of developers that there are in Arizona, those eligible for your membership?

Mr. BERTOCH. That almost requires a definition of "developer," Senator.

[31] P. 84, op. cit.

Senator WILLIAMS. The subdivider. Is that another way of expressing it?

Mr. BERTOCH. Our group has subdividers selling Arizona property to Arizona people in Arizona, and it also has people who have Arizona property who are marketing in other States. So when it comes to Arizona subdividers, as such, marketing in Arizona, we have a representative group of that level of operation. When it comes to those who are marketing Arizona property in other areas, we then have a representative group there. We do not have an organization at this time that represents all the people in the business.

FINDING NO. 6

There is some discontent within the industry about the complexity of some State regulations and the wide differences that exist from State to State

Mr. Carl Bertoch, chairman of the Rules and Regulation Committee of the League of Arizona Developers, gave this description of the situation:[32]

> Some of us in the industry are beginning to feel that no longer are we in an area without sufficient regulation as it may have appeared here a year and a half ago, but we are now rapidly becoming overburdened by a prolixity of regulations which lack uniformity and represent divergent philosophies.

Though not asking for Federal regulation, Mr. Bertoch was expressing a complaint heard frequently from developers. A similar, but more detailed, comment was given in a statement submitted to the subcommittee by James H. R. Cromwell, chairman of the board, American Realty & Petroleum Corp., which is selling land at three large development projects, two in Florida and one in New Mexico.

Mr. Cromwell stated:[33]

> Instead of one Federal registration, as is proper with interstate commerce, we have separate registrations in each of the States with increasingly high legal and other costs. Instead of one inspection of the property, to this point we have had to bring various State inspectors on 15 separate trips from the various States. We have had to pay over $10,000 in expenses for these trips, over $5,000 just in the many States' filing fees and well over $50,000 in legal fees for various lawyers in the many States to handle the complicated State registrations for us. All of this on one property alone. These are certainly unnecessary costs.
>
> Gentlemen, I would think interstate land sales are truly interstate commerce, to be regulated only at the Federal level.
>
> But let us remember that the present State laws are doing an excellent job of policing, and additional Federal legislation on top of the present State laws would be unnecessary and wasteful. However, I do believe that one Federal agency to replace the presently existing State agencies would be far

[32] P. 77, op. cit.
[33] P. 346, op. cit.

more preferable and far more economical, for Government, for the consumer, and for the businessmen. If it is possible to replace the separate State regulation with one overall, interstate Federal law, then we are all for it. To leave as is the present individual State laws and add an additional Federal bureau would be, we feel, unnecessary.

RECOMMENDATIONS

RECOMMENDATION NO. 1

The subcommittee believes Federal regulation of an essentially interstate problem is necessary. Such regulation would take into account the efforts of the States, and would not supplant, but complement, existing State legislation

A number of approaches to the solution of this problem have been suggested. Among them are strengthened postal fraud statutes (see sec. V) broadening the advertising provisions of the Federal Trade Act, or requiring registration of interstate land sales with the Securities and Exchange Commission.

Your subcommittee believes that the most practical and effective method of Federal regulation would be to require a Federal "full disclosure" statute administered by the Securities and Exchange Commission.

1. *The subcommittee recommends legislation which would require registration of the sales of land in a subdivision with the SEC whenever the mails or instrumentalities of interstate commerce are used to sell the land or, in appropriate cases, to offer or advertise the land.*—Such a bill should provide minimally that registration would be accomplished by filing an application including information as to (*a*) the topography of the subdivision and existing streets and roads, water and general condition of the development, (*b*) condition of the title, and (*c*) condition of sewage disposal facilities and existing public utilities.

Additionally, if the subdivision were mortgaged or otherwise subject to a "blanket encumbrance," the registration statement should show that a purchaser could obtain title free and clear of this encumbrance or that his investment would be protected by an escrow arrangement, a trust agreement, or a bond.

Based on the information in the registration application and appropriate investigation, the SEC would prepare a public report on the development. Such a report would have to be shown to a prospective buyer prior to entering any sales agreement.

In addition, individual salesmen of such subdivision would be required to register with SEC.

It should be emphasized that such a law would apply only to the sale of undeveloped land in interstate commerce. The sale of improved land on which there is a dwelling would be exempted from its provisions.

Your subcommittee believes that the SEC is the appropriate agency to administer such a law for several reasons. The procedure for the registration of proposed land sales, and the preparation of a public report is analogous to regulations now applied to offerings of new securities. Also the SEC has the regional offices and the trained

personnel to administer the provisions of the bill, albeit with some expansion. In addition, such a law would complement and encourage appropriate State action. If compliance with an adequate State "full disclosure" law were deemed to meet SEC standards, a developer would merely have to file duplicate copies of appropriate State registration applications with the SEC. In this manner, the SEC will administer the law in cooperation with the various States. However, the major responsibility for its administration should remain with the SEC until the States enact adequate legislation themselves. Federal legislation would merely serve, as it properly should, to fill the gap now left by the absence of proper legislation in every State.

2. *The subcommittee also believes that congressional attention should be given the following suggestion by Herbert Wenig, assistant attorney general of California.*[34]—I suggest a statute which would make it a crime to use interstate commerce to sell out-of-State land in a State contrary to the laws of that State. One precedent is the statute which makes it a Federal offense to transport liquor into a State contrary to State law. Such a statute would protect States like California which have adequate laws to protect land purchasers, but which have great difficulties in enforcing these laws against the out-of-State seller. Injunctive relief in the Federal courts should be made available either in the district where the seller resides, or where the sales are taking place.[35]

[34] The subcommittee has already had preliminary discussions with the National Conference of Commissioners on Uniform State Laws in order to determine whether State and potential Federal regulatory action can be coordinated to avoid needless duplication and confusion.

[35] P. 27, op. cit.

PART 3

DECEPTIVE OR MISLEADING METHODS IN HEALTH INSURANCE SALES

INTRODUCTION

Health insurance received the attention of two subcommittees of the Senate Special Committee on Aging in 1964.

In April, the Subcommittee on Health of the Elderly took testimony that later yielded these major findings: [1]

> Private health insurance is unable to provide the large majority of our 18 million older Americans with adequate hospital protection at reasonable premium cost * * *
>
> Only 9 million of the Nation's elderly held hospital insurance policies of any kind at the end of 1962. The other half—predominantly the very old, those in poor health, the unemployed, and those with the lowest incomes—were without hospital insurance of any kind * * *
>
> * * * The elderly who now hold private health insurance are having great difficulty keeping even an inadequate level of protection. They find themselves squeezed between higher premiums and shrinking benefits, as hospital and medical costs continue to climb.
>
> * * * As a result, increasing numbers of our older people are confronted with financial catastrophe brought on by illness.

These Health Subcommittee findings lend special urgency to facts gathered by this subcommittee on May 4 during a hearing on deceptive or misleading methods used to sell health insurance to the elderly. The reasons for that urgency are expressed in the first of the following major findings of the Subcommittee on Frauds and the Elderly.

MAJOR FINDINGS

Economic pressures on older Americans are causing many to turn to mail-order health insurance offered by marginal companies which distort or omit facts in order to suggest that the policy gives more protection than it really does

At the very outset of the hearing, the subcommittee chairman made it clear that the subcommittee was concerned only with the dubious policies offered by a small part of the insurance industry: [2]

> Senator WILLIAMS. This subcommittee recognizes that the majority of mail-order firms and other health insurance companies are honestly interested in giving value to their

[1] "Blue Cross and Private Health Insurance Coverage of Older Americans," a report by the Subcommittee on Health of the Elderly, U.S. Senate Special Committee on Aging, July 1964, p. 1 ff.

[2] "Deceptive or Misleading Methods in Health Insurance Sales," May 4, 1964, p. 1.

customers. It is for the protection of these reputable companies, as well as for the benefit of the buying public, that this subcommittee is conducting this hearing.

The National Association of Insurance Commissioners asserted that the field of concern to the subcommittee is "less than 1 percent of the total health insurance market in the United States." The NAIC estimated that the total premium volume of health insurance issued by direct-mail insurers during 1963 was $44.3 million.[3] This sum, small in comparison to the $6.4 billion premium volume of the overall health insurance industry, is nevertheless a significant figure to large numbers of policy holders who pay comparatively small monthly premiums for protection against financial and personal tragedy at time of great need.

To the subcommittee it has become apparent that such protection, with dismaying frequency, exists only in the mind of the purchaser and not in the print of the policy, as this evidence from the hearing transcript will attest:

1. *Federal Trade Commission investigations are on the upswing.*

James McI. Henderson, General Counsel of the Federal Trade Commission, informed the subcommittee that "as the new type of insurance is now becoming popular, more complaints are coming to us."[4] He also said that the FTC, for reasons to be explained later, "has been virtually out of this area up until quite recently," but he also gave this picture of the scope of present FTC actions, as compared to the total industry:[5]

Senator FONG. Mr. Henderson, in your Commission, how many orders of cease and desist have you issued against insurance companies who have fraudulent health insurance representations?

Mr. HENDERSON. Senator, I believe we have issued either orders or assurances to discontinue in a total of approximately 15 cases.

Senator FONG. And of these 15 cases, how many companies are involved?

MR. HENDERSON. There would be 15 companies.

Senator FONG. And there are approximately 200 companies in the field?

Mr. HENDERSON. That is my understanding, Senator. I have no personal knowledge of that.

Senator FONG. Are you working on many cases now?

Mr. HENDERSON. We have 11 investigations actively under investigation at this time. * * *

Senator FONG. Do these 11 complaints that you are working on involve the same 15 companies?

Mr. HENDERSON. No; these are new companies, additions—I do not mean new; they are new complaints, not necessarily new companies.

Senator FONG. You have approximately 26 complaints on 26 various companies?

Mr. HENDERSON. Right, sir.

Senator FONG. Thank you.

[3] P. 159, op. cit.
[4] P. 22, op. cit.
[5] P. 22, op. cit.

2. *Elderly citizens have become highly prized markets for the sale of mail order health insurance policies and for more direct sales approaches.*

Testimony to this effect came from several sources. Mr. Sherwood Colburn, former insurance commissioner of Michigan, gave the most succinct summary of reasons: [6]

> Why is the older American such an irresistible target for these unscrupulous promoters?
>
> 1. Most of the avenues to the better commercial insurers are blocked to the elderly. Extraordinarily high annual premiums, benefit limitations, and in many instances the inability on the part of the older person to meet the minimum physical requirements effectively serve as barriers to the better insurance policies.
>
> 2. Coupled with this is the fact that older people often have poor medical histories and are subject to a variety of chronic illnesses which necessitate expensive care on a recurrent basis.
>
> 3. The desperate need for insurance protection born from the two factors previously mentioned, along with their reduced incomes, force the aged to seek and embrace almost any insurance policy offered. Even those who have sacrificed to retain fairly decent policies are lured by the siren song of claims hailing "low cost, no exam, comprehensive hospital and medical coverage, no ifs, ands, or buts, no limitations * * * all for pennies a day." In many instances this come-on is gilded with the phrase: "Only 25 cents for the first month." And far too often these people tragically abandon higher cost, but most certainly higher benefit protection.
>
> In Michigan, there are some 650,000 citizens over the age of 65. And, for example, the average annual income of an older person in that State, living alone or with nonrelatives, is only $1,010.
>
> These problems which I have outlined are not peculiar to nor unique to Michigan. I dare say they occur in every State in the Union. This is a serious national problem, and one that has occupied the attention of the National Association of Insurance Commissioners since 1888. Many proposals have been made to the NAIC to curb the harmful practices of such insurers in order to protect all citizens in every State, but all too few proposals have been implemented.

Mr. Colburn also gave an example of more direct methods used by one "salesman": [7]

> There is no doubt that the elderly person has a specific problem when it comes to health insurance. I have one case in mind that I call the Saginaw case. I had accepted an engagement in 1963 to address the Saginaw Association of Life Underwriters in Saginaw, Mich. Two members of the Michigan department, enforcement division, were accompanying me on this trip, and we determined that we would take two or three files with us, so that in the event we had some spare time, we could do a little fieldwork.

[6] Pp. 108-109, op. cit.
[7] P. 112, op. cit.

We went to one home and here we found a retired couple. He was 74 years of age. He had been approached by a Borax operator and was sold on dropping his Blue Cross-Blue Shield. He was convinced by this "sharpie" that he was getting more for less.

Now this man had a history of diabetes and had suffered a stroke. He told the agent of this past medical history. The new policy was still issued. Several months later, the insured had a leg amputated as a result of his diabetes condition. Within 1 month he had a second stroke. Bills from these two claims totaled over $3,500. Both claims were rejected by the X company. The reasons were twofold, preexisting conditions and that he had withheld important medical information from the company. We contacted the agent. He was no longer in the business. We corresponded with the company. We had no reaction from this company other than the fact that there were no claims. We called an officer of the company into our office. In the middle of our negotiations with this company to settle this claim, the insured passed away. We were finally able to get his widow $2,000 which actually reflected what Blue Cross-Blue Shield would have paid under their policy.

Senator WILLIAMS. Who paid that?

Mr. COLBURN. The company that originally denied the claims. We told them, sir, that in our opinion their actions and activities made our department question just how much longer the citizens of Michigan could have faith and confidence in their company. Now they did pay the claim. But certainly an insurance department cannot sit back and take on these activities daily.

Representative James Cameron, of California, commenting on a California health service plan that had cost its victims millions of dollars before being put out of business by State action, also noted: [8]

Mr. James [Charles A. James, assistant attorney general of California] referred to the fact that in Western's case a great many of the people appeared to be elderly, which they deduced from extraneous information. It was my finding over several years in California that the bulk of the employed people of the State of California—and I would assume this would apply throughout the Nation—are covered by some type of group plan through their employment; generally these tend to be extremely well regulated. There are obvious exceptions. Generally they tend to be very good.

What happens, though, a person terminates from employment, he is no longer involved in a group that can qualify for group benefits, he then becomes the prey of people such as Western, and I have seen this repeated time and time and time again, and, of course, I think that the import of what the FTC said this morning is very important; but, it limits itself, as I understand it, to insurance, and I think that you are going to see as your investigation develops that there is another area here which Mr. James was talking about, that

[8] P. 80, op. cit.

> of service plans, in which I carefully talked in terms of benefits rather than in terms of insurance, because these service plan groups are the ones that are easily formed, subject to very little regulation in any of the States, and are in a position to make a very attractive offering that is basically fraudulent in its inception.[9]

Earlier, Representative Cameron had made a connection between rising health costs and new methods of selling health services.[10]

> It is becoming patently obvious to the public that each year the cost of medical care as measured in the Consumer Price Index rises faster than any other item—and there is a direct correlation between this inflationary spiral and the funds that are bilked from a well-meaning and defenseless public in the name of health benefits.

The most direct testimony on sales of health insurance to elderly Americans came from Mr. Loren Hicks, 73-year-old president of the North Broward Senior Citizens Club, Inc., and treasurer, Florida State Council for Senior Citizens, of Pompano Beach, Fla.: [11]

> The only available insurance to give decent protection is priced out of reach of most senior citizens. The cost of these policies involves an outlay of from $500 to $600 for a retired aged couple. This sum constitutes about one-thirds of their average income. I consider myself to be a little better off than the average retiree. My income from social security, plus company pension, is less than $170 per month. I am lucky in that the health insurance I carry is a company-matched policy. But it pays only $10 per day for hospital room and board, plus very limited benefits. However, this is all I can afford due to the heavy medical and drug bills for my wife, who is now in the Pompano Beach Hospital.
>
> Once again I shall have to draw from my life savings for this purpose as I did 2 years ago when I spent a week at Holy Cross Hospital. It is true that I have a modest amount of savings, but did I work and save only to use this money for doctor, hospital, and drug bills. It was saved in order that we might supplement our meager income, so that by careful management we might live in some semblance of decency.
>
> We senior citizens are not only at the mercy of fly-by-night insurance companies, who advertise through the newspapers and by mail, but we are also being victimized by slick insurance salesmen whose verbal statements do not coincide with the fine print of their companies' policies. Are these companies in no way responsible when they discover that certain of their salesmen have been consistently guilty of misrepresentation?
>
> I offer for your inspection the policy of Beneficial Standard Life Insurance Co. of Los Angeles, Calif., together with the

[9] The NAIC, asked to give more information on State regulation of health service plans said, "most States" have regulation of some kind (p. 160, op. cit.).
[10] P. 70, op. cit.
[11] P. 141, op. cit.

complaint of possible high-pressure sales representation by their agent.

The same kind of complaint, with the same company, comes from Mr. Albert Ross of 2916 NE. 24th Avenue, Lighthouse Point, Fla., on policy No. 1–802–506–852.

In both instances, the agent stated that only preexisting conditions of 5 years previous would be considered. Yet the company takes a lifetime record of exclusion.

Another operation in this county was the selling of Broward 65 policies by one Henry Mathes. The underwriter of this insurance was the Great Atlantic Life Insurance Co. of Miami, Fla. I ask, why was this man approved by Great Atlantic with no investigation whatever, since he could not obtain a license to do business in the State of Florida? He is now under indictment by the grand jury for alleged malfeasance of operation. This person is one of scores who have personally visited me in an endeavor to infiltrate my senior citizen club. I have been offered the sum of $200 for the mailing list of our members by an insurance agent.

Kenneth Williamson, associate director of the American Hospital Association, also had direct evidence for the subcommittee: [12]

> The association and its members are, of course, keenly aware of the results of the public's purchase of inadequate health insurance protection. Any substantial inadequacies in insurance benefits become obvious in the payment of hospital bills. If the holder of the insurance policy believes, as they sometimes do, that the insurance was a great deal better than it really is, then their displeasure and even anger may be taken out on the hospital. Thus, the public image of the hospital is not helped.
>
> Hospitals have also been much concerned with the total amount of the premium dollar paid, which is returned to the participants in the form of benefits. There still appears to be a substantial amount of health insurance being sold which returns an inadequate amount in the form of benefits. As hospitals look at this situation, it appears that their services are being used and sold so as to result in inordinately large profits to insurance companies rather than in the payment of hospital services. Here again the end result is hardship to the individual and difficulties for hospitals in the collection of hospital bills. The situation, of course, often is worse where it exists in relation to aged persons because of their limited income and other factors pertaining particularly to the spot.
>
> It is our general observation that as voluntary health insurance has grown it has improved markedly with greater benefits and an increased percentage of the premium dollar being spent for benefits. Group policies are generally found to be superior and the difficulties arise in connection with individual policies. As health insurance for the aged has become a matter of particular public concern in recent years, it may well be that there has been some overly aggressive

[12] P. 145, op. cit.

selling. Apparently, too, some of this newer insurance contains stipulations which are not well understood by elderly purchasers and which clearly would limit the value of the insurance. The American Hospital Association has not made any detailed studies of this overall situation. We do receive general reports which indicate the sort of problems I have mentioned.

FINDING NO. 2

Wide opportunities for deception or confusion exist in sales of health insurance policies, and buyers are usually dependent upon the good faith of the seller for accurate interpretation of provisions

The Federal Trade Commission announced at the subcommittee hearing that it was about to print its guides for the mail-order insurance industry. These guides, Mr. McI. Henderson explained, "have no probative effect but are intended to clarify for the mail-order industry the laws on deception which may apply to their practices."

The guides are also a compendium of deceptive methods that can occur when a layman buys a policy.

Guide 1 states the law on general deception:

> No advertisement shall be used which because of words, phrases, statements, or illustrations, therein or information omitted therefrom has the capacity and tendency to mislead or deceive purchasers or prospective purchasers, irrespective of whether a policy advertised is made available to an insured prior to the consummation of the sale, or an offer is made of a premium refund if a purchaser is not satisfied. Words or phrases which are misleading or deceptive because the meaning thereof is not clear, or is clear only to persons familiar with insurance terminology, shall not be used.

Summarizing other potential dangers as expressed in the guides, Mr. McI. Henderson said: [13]

> Certain specific deceptions may occur in the advertising and sale of mail-order insurance. Each of them is related to the general deception in the manner of its operation; that is, misstatement, by concealment, by specialized language which may mislead, or by a statement of the truth in such a manner as to give a false impression. Here are some of the means of deception:
>
> An advertisement which fails to disclose:
>
> 1. Exceptions, reductions, or limitations of the policy;
> 2. A waiting, elimination, probationary, or similar period before the policy becomes effective and benefits become payable;
> 3. That benefits are payable only on the occurrence of certain conditions, and what those conditions are;
> 4. The effect preexisting conditions of health may have on insurance coverage;
> 5. The age limitations within the policy when the policy is applicable only to a certain age group;

[13] Pp. 4–5, op. cit.

6. All terms affecting renewability, cancelability, or termination, or which directly misrepresent such matters;

7. That a combination of policies is involved when the advertisement refers to various benefits which are contained in more than one policy;

8. That total benefits are allocable among family members and not payable in total on the death of one member, when such is the fact.

An advertisement which represents:

9. That the health of the insured is not a factor affecting insurability or payment of benefits, when such is not the fact;

10. That no medical examination is required when medical examination before payment of benefits is or may be required;

11. Truthfully, that no medical examination is required when there is no disclosure of the limitations which the insurer places on his liability under the policy so issued;

12. Testimonials, appraisals, or analyses of policies which are not genuine, or do not represent the current opinions of the author, or an advertisement which does not accurately describe the facts or reflect the current practice of the insurer;

13. Statistics such as time within which claims are paid, dollar amounts paid, number of claims paid or persons insured under a particular policy, or other statistics, which do not accurately reflect all the relevant facts on which the statistics are based,

14. That claim settlements are liberal or generous beyond the terms of the policy.

An advertisement which:

15. Uses words which indicate broader coverage than the policy affords;

16. Uses words which imply greater benefits than the policy affords, such as "up to" and "as high as" when perhaps only one benefit is equal to the maximum figure;

17. Implies that the policy provides additional benefits for certain illnesses, when such is not a fact;

18. Misleads or may mislead purchasers concerning the insurer's assets, financial ability, relative position in the insurance industry, or any other material fact.

It is not intended that the committee should believe the foregoing list is a complete catalog of the deceptions which are, or may be, currently used in unscrupulous insurance advertising and mail-order insurance. However, the list is indicative of the type which may be used. Other misrepresentations, if they fail to meet the standards of the Guide on General Deception, are likewise violations of the Federal Trade Commission Act.

Representative Cameron gave examples of techniques he has observed in direct sales of policies: [14]

> Hundreds of times I have seen persons drop plans that provided far superior benefits to those being sold by a suede-shoe operator with a fancy pitch. They drop these plans

[14] P. 70, op. cit.

because they mistakenly believe the salesman and they have no objective means to evaluate the relative benefits of the two programs.

Typically, persons will purchase a plan and pay more for it if it provides 90 days hospitalization, at $20 a day, and for a maximum total of $1,800, over a plan that provides 30 days hospitalization at $40 a day, for a maximum total of $1,200.

The second plan is far superior as to hospitalization if one considers that the average hospital stay varies from 5 to 7 days and costs per day vary from $30 to $65 depending upon the area of the country.

Also, the average individual tends to prefer indemnity-type benefits as opposed to service plan benefits, without realizing that in the typical cash indemnity program which we normally refer to as insurance, the company pays not more than 50 cents in benefits for each dollar collected in premiums; whereas, the typical service plan—such as Blue Cross—pays benefits well in excess of 90 cents of each dollar collected.

At present, I believe it takes too sophisticated a buyer of health benefits to overcome the purveyor's policy of caveat emptor.

I have long contended that the insurance and service plan trade associations in the health and accident field are destroying their industry by this policy of "let the buyer beware."

Mr. Colburn drew from his former experience as Michigan Insurance Commissioner to add these examples of other direct-sales techniques: [15]

One of the most widespread, persistent, tragic, and almost uncontrollable problems which has confronted the Michigan Department of Insurance for all too many years has been the high-powered sales pitches designed to sell completely inadequate and totally misrepresented health insurance policies to the elderly.

These irresponsible huckster approaches have taken the forms of:

1. Wholesale mail-order solicitation which emanates from insurers who are not licensed nor authorized to conduct their business in the State;

2. Intensive and dramatic newspaper advertising by these same unlicensed insurers; and

3. The employment of specially trained one-shot interview "con" artists whose object is to "hit and run." While representing but a small segment of the licensed insurance carriers, these "gangs" descend upon preselected target communities—often rural—as well as other areas with a preponderance of older residents. Their bag of tricks includes completely fraudulent comparisons of their policy with that which may be presently held. Far too often, past medical history is completely ignored or glossed over by the unscrupulous agent in completing the insurance application to the

[15] P. 109, op. cit.

later distress of the individual who thought he was purchasing coverage. * * *

Another problem just as serious as unlicensed direct mail-order and newspaper advertising are these "gangs," of whom I have previously referred to, who represent a very small segment of the licensed insurance community. They can keep an entire insurance department busy keeping up with their activities.

They descend on all areas, particularly those with a high percentage of elderly people, and conveniently leave out past medical history in the application forms. In some instances they hear of past medical history from the elderly applicant. However, they do not put it into the application. In other instances, they do not even bother to ask. They automatically write "No, no, no, no," or they might say, to somebody, "Well, a little ulcer condition such as the one you are talking about has no bearing on our company's underwriting attitude."

I have always violently opposed what I call postclaim underwriting. They start underwriting these insurance contracts at the time of the loss. The underwriting should take place when the application is submitted to that company. In a memo from my staff I quote:

"We have found that the limitations with respect to preexisting conditions are a continuing problem, insofar as claim settlements are concerned, primarily because the insureds are not aware of the restrictions imposed upon them by preexisting limitations."

At that time, I wanted to place a large overprint on the policy explaining preexisting conditions and limitations. Furthermore, I wanted a statement signed by the insured upon delivery of that policy to the point that he understood that preexisting conditions could conceivably interfere with a claim settlement. Once a person has this full knowledge, then I think we have a fair and equitable situation between the insured, the agent, and the company.

We further determined that another solution would be to block out the medical history questions in the application. I feel that the medical history portion of every single health and accident insurance application should be answered in the handwriting of the applicant with each answer initialed. In that way, we would be able to avoid some of the activities of the unscrupulous insurance agent.

Still other difficulties were recounted in a statement by Jack Owen, executive vice president and director of the New Jersey Hospital Association: [16]

> The New Jersey Hospital Association is interested in this hearing since deceptive or fraudulent claims by small insurance companies not only cause hardship to the individuals purchasing such insurance but create financial problems for our member institutions and cast suspicion on legitimate insurance carriers.

[16] P. 147, op. cit.

A quick review of our member institutions revealed problems with seven carriers at the present time. Three of these companies are located in New Jersey, one in Michigan, one in Massachusetts, one in New York, and one in Delaware.

One of the New Jersey carriers has a name similar to a large reputable insurance company and to uninitiated or poorly educated, the resemblance of names causes confusion. To cite a specific example, Mr. Doe was recently hospitalized in one of our member institutions, he informed the admitting desk that he had insurance in one of the large insurance companies for complete hospitalization, and had paid the premiums for the past 2 years. Scrutiny of the policy revealed it was not purchased from a large insurance company but from a small company with a like name and, further, the patient had been paying for a disability policy which paid $15 per week. The patient's bill for hospitalization was $603 for which the insurance paid $27.

In another instance, a patient had been paying $124 a year in premiums to a small company for "complete" hospitalization. After being hospitalized, the insurance carrier was contacted but refused to respond to either the hospital or the patient. In this case, the patient's family eventually settled the hospital bill without ever hearing from the insurance carrier.

In still another case, one of our member institutions filed a claim in November of 1963 which has still not been acknowledged. Repeated letters to the address of the insurance carrier have been returned and phone calls have gone unaswered although premiums can still be paid to the address.

These are specific examples for which names can be supplied and facts supported.

The subcommittee recognizes that, as explained in the next finding, Federal regulation is limited to the mail-order health insurance industry and, only, to a part of that. Nevertheless, the subcommittee also believes that it has a responsibility to give as much public notice as it can to practices that fall within the jurisdiction of State regulatory agencies. Despite intensive enforcement efforts, and educational campaigns at the State level, consumer confusion on the subject apparently is widespread.

Finding No. 4

Federal jurisdiction is limited to one special area of mail-order insurance: State insurance agencies regulate all other insurance. There is good reason to believe, however, that interstate mail-order health insurance causes special problems for State agencies and for consumers

Aware that the Federal Trade Commission conducts investigations into certain deceptive practices related to health insurance, the average buyer may believe that he is thus assured of Federal regulation of all such sales.

This layman's viewpoint, however, is far from the fact. The actual situation was described by Mr. McI. Henderson in his opening statement: [17]

> It would be less than candid to overstate to the committee the limits of the Commission's jurisdiction in insurance matters. The Commission to a great extent relies upon the aid of the National Association of Insurance Commissioners and the cooperation of State authorities for adequate regulation of mail-order insurance advertising.
>
> This reliance is important not only because it is good Government, but the McCarran-Ferguson Act of 1945, as amended in 1947, makes the business of insurance subject to the provisions of the Federal Trade Commission Act, and other antitrust acts to the extent such business is not subject to State regulation. Cases involving the limits of our jurisdiction have in a practical sense marked out the area of mail-order insurance. The Commission is able to act when the State into which a mail-order solicitation is sent has not licensed the soliciting company, and no agent of the company for the service of process and property on which judgment can be executed may be found within the State. This is the case of *Travelers Health Association* v. *F.T.C.*, on remand at 298 F. 2d 820, 824. The test is whether the State is able in fact, to regulate the insurance business of the company.

He later gave additional information: [18]

> Senator WILLIAMS. When you discover a misrepresentation within the terms that you have just discussed, can you move in in any case or only in some cases to stop the deception?
>
> Mr. HENDERSON. In a very limited number of cases, Senator, can we move in. That is only in those cases where it is a mail-order operation which is not effectively regulated by the State into which the mail-order advertisement is sent.
>
> Senator WILLIAMS. Are there large gaps where a State has not regulated? Certainly the State has the authority to regulate any company disseminating advertising material from its jurisdiction, does it not?
>
> Mr. HENDERSON. Oh, yes.
>
> To answer your question, we have 11 investigations going at the present time to ascertain our jurisdiction to prevent alleged deception in the sale of insurance where we believe that the States do not have the capacity to effectively regulate these companies.
>
> The illustration that is a good one is the *Travelers* case where this company was licensed to do business in only 2 of the 50 States, but it was advertising in all 50 of the States, so that 48 States had no way of effectively controlling the mail flow into its own bailiwick.

[17] P. 7, op. cit.
[18] P. 16, op. cit.

Senator WILLIAMS. But the other two States would have the jurisdiction to control the outflow from their borders; is that right?

Mr. HENDERSON. Not the outflow of mail; I doubt it, Senator. Because this is a Federal function, and I doubt that a State could say you cannot send mail out of the State. It would have to be at the other end, at the recipient's end where to the company, the State can say you must come in here and take a license and you must have an agency for service at that point and then it can also say this is fraudulent advertising.

Senator WILLIAMS. Then there are large gaps and in these gaps you have authority to deal with misrepresentations?

Mr. HENDERSON. Yes, sir.

Senator WILLIAMS. What is the method used to stop it?

Mr. HENDERSON. Depending on the abuse and on the past history of the company. If this seems to be an inadvertent type of thing, the company may have fallen into by an overzealous advertising manager, we may ask them to give us assurances of discontinuances of the practice. This is simply an assurance that they will abandon this particular practice and will abide by the guides. If this is a company which is noted for its predatory practices, its fraudulent representations, we would probably file a formal complaint against it and either insist on a consent order to try the case and enter an order of the Commission which would forbid it from continuing these practices.

That order is litigated, but a consent order would be enforcible by the courts as well.

The FTC procedure, however, is timetaking. (See sec. V.) What is more serious in the long run, the FTC cannot even enter the picture until after the public has been deceived. State insurance commissioners and others concerned about the problem have frequently asserted within recent years that predatory mail-order companies deliberately take advantage of the regulatory gaps in the mail-order health insurance industry.

Complaints from States.—As noted in the statement by the National Association of Insurance Commissioners, "several commissioners have issued warnings against dealing with unlicensed companies."[19]

The warnings, always prompted by the advertising and sales of out-of-State companies, take many forms, including the following:

BEWARE OF BOOTLEG INSURANCE

Oklahomans are being warned by Joe B. Hunt, State insurance commissioner, that they should not buy insurance from unlicensed companies that are bootlegging business into the State of Oklahoma through the mails and through various advertising media.

These unlicensed companies do not pay premium taxes and fees to the State of Oklahoma nor have their policy forms been approved by the Oklahoma insurance commissioner.

[19] P. 92, op. cit.

Oklahomans purchasing insurance from unlicensed companies do not have the benefit and protection of the Oklahoma Insurance Code afforded to them through licensed insurance companies.

Oklahomans should buy their insurance from local hometown agents who sell through duly licensed companies.

When in doubt, write or contact Joe B. Hunt, State Insurance Commissioner, Will Rogers Memorial Office Building, Oklahoma City, Okla.

New York Insurance Department Issues Warning: Physicians Mutual Is Unlicensed Insurer

Superintendent of Insurance Henry Root Stern, Jr., today warned New York State residents of the risks involved in purchasing insurance offered by the Physicians Mutual Insurance Co. of Omaha.

The warning was issued as the State insurance department received inquiries arising from widespread mail-order solicitation of New York State residents by the company, which is not licensed to do business in this State.

The unauthorized company's mailed literature gives the misleading impression that its veterans' benefit health insurance policy is Government guaranteed and comparable to low-cost national service life (GI) insurance. Physicians Mutual also has been offering by mail a "40-plus" health insurance plan.

Mr. Stern pointed out that since the company is not licensed in New York, its financial condition, policy provisions, rates, and dealings with policyholders are not subject to examination by the insurance department. In addition, the department would not be able to assist policyholders in any dispute arising out of a claim under the policy. Thus, New Yorkers dealing with such unauthorized insurers lose the benefits provided for their protection by the laws of this State.

"Licensed companies must comply with specified financial requirements, must file annual reports of their financial condition, and are subject to thorough examination by the department concerning all phases of their operations, including claims handling," a department statement points out. "The department passes upon premium rates and provisions of many types of insurance policies" of licensed companies.

Policyholders frequently have difficulties in obtaining satisfactory settlements of claims against unlicensed insurers. In the case of licensed insurers, State law empowers the insurance department to see to their fair treatment of policyholders and settlement of claims in accordance with contract terms.

A similar warning against dealing with Physicians Mutual has been issued to New Jersey residents by Charles R. Howell, New Jersey commissioner of banking and insurance.

INSURANCE DEPARTMENT WARNS PUBLIC AGAINST TIME LIFE OF SAN ANTONIO

Superintendent of Insurance Henry Root Stern, Jr., today cautioned New York State residents against the risks involved in purchasing insurance from companies not authorized to do business in this State.

This warning was issued as a result of the continued advertising in this State, via newspapers, radio stations, and magazines by Time Life Insurance Co. of San Antonio, Tex., an unauthorized insurer. That company has been soliciting mail orders from New York residents for an accident and hospital policy offering benefits of $1,000 per month for hospitalization resulting from accidental injury. * * *

The National Association of Insurance Companies listed several methods that could be used to deal with an offender after a purchaser asserts that he has been cheated by an out-of-State company.[20] Such action, however, is usually corrective rather than preventive.

Similar commentary was given in a National Underwriters editorial submitted by Mr. Colburn:[21]

UNLICENSED INSURERS

Protecting the public against the dishonest or dubious insurer must be one of the least-relished jobs of a State insurance department. In the first place, most people are unaware of this function of their State insurance authorities. The national activities of the Pure Food and Drug Administration in safeguarding the consumer are well known, but the corresponding insurance protection by the States is less publicized. In the second place, insurance has so thoroughly sold itself to the public by its high standard of performance that the unscrupulous are able to trade upon a tremendous fund of goodwill. Furthermore, many reputable insurance companies use direct-mail promotion extensively, and the shady operator can slip his in with the rest; some of the unlicensed insurers with bucketshop operations have impressive-sounding names. And a nonlicensed insurer who operates by mail is not necessarily fraudulent, only likely to be an unwise choice for the buyer.

WARN THE PEOPLE

About all the insurance departments can do when the shaky nonlicensed insurer floods several States with advertising and direct-mail promotion is to warn the people of their States against doing business with a company from which it may be difficult to collect in case of a claim. Hampering such a company legally is as difficult as trying to collect water in a net.

The best protection for the policyholder is to continue to deal with an agent he can trust. Fortunately for the public,

[20] P. 93, op. cit.
[21] P. 113, op. cit.

most buyers of insurance do just that. Furthermore, the agent or broker should be prepared to furnish information about insurers his clients may ask about. He should be ready to tell whether the company is licensed in the State and something about its financial stability. In some cases this information is not in standard books of reference, and this omission is the most damning fact that can be ascertained about any except a very new company. Confidence in the informed agent will help protect the policyholder more than any other single factor.

An even more urgent appeal was made by the New York State Association of Life Underwriters on April 6, 1964, when they submitted a letter in support of a bill to prohibit advertising on behalf of unauthorized insurers: [22]

Hon. Sol Neil Corbin,
Executive Chamber, State Capitol,
Albany, N.Y.

Dear Mr. Corbin: We are an association of 5,600 career life insurance men and women who are licensed by the New York State Insurance Department to sell authorized insurance policies. We would like to state our reasons why we support this bill.

THE NEED

The New York insurance law is inadequate to cope with solicitation of insurance on New York State residents by unauthorized insurance companies. Insurance is solicited and sold to our citizens in many ways—by mail, by television, by radio, by magazines, and newspapers, as well as by individuals. Only the last is controlled by the present insurance law. Attempts to limit solicitation of unauthorized insurance by advertising media have failed under existing law.

We have given thought to ways other than "limiting solicitations" as a means of curtailing the sale of policies not approved under New York law. We raised the question whether unauthorized insurers are subject to New York State premium taxes because they are "doing business" here. This inquiry was aborted because "doing business" in insurance is related to where the policy is issued or contracted for; and the New York advertising agencies that handle the requests for insurance contend they relay the application and, therefore, are not "doing business."

Likewise, the attempt to bring unauthorized insurers under control by the Federal Trade Commission "misleading advertising" regulations has not been helpful. The New York State Superintendent of Insurance, Thomas Thacher, in a personal interview on this problem with officers of the New York State Association of Life Underwriters in early 1963 expressed the hope that a resolution he was working on for adoption by the National Association of Insurance Com-

[22] Submitted by Mr. Colburn, p. 123, op. cit.

missioners would bring the matter under control. This, too, did not materialize in the way expected; but a substitute effort was made by a joint press release distributed by the Federal Trade Commission and the president of the National Association of Insurance Commissioners on November 6, 1963 (copy attached). The advertisements by nonadmitted companies in local newspapers and radio stations continue in New York State. * * *

It has become apparent that the question of unlicensed, out-of-State health insurance companies remains a largely unanswered one despite the concern of the State insurance commissioners, the clear-cut jurisdiction of the FTC, and the action individual States have taken in passing corrective legislation.

RECOMMENDATIONS

Recommendation No. 1

Your subcommittee strongly recommends passage of Federal sanctions against the use of any instrumentalities of interstate or foreign commerce by any insurance company or agent to sell or advertise for sale health insurance where such sales and advertising would be in violation of the regulatory statutes of the State in which the sale or advertisement is made.

(a) To secure enforcement of this statute, Federal district courts shall have original jurisdiction over civil actions brought by State licensing authorities to obtain temporary or permanent injunctive relief after a showing of probable cause that the statute has been violated.

Care should be taken to expressly provide for the continued existence and validity of all State remedies for enforcement of their own regulatory statutes to ensure that the Federal injunctive remedy is merely supplementary and by no means exclusive.

(b) Violation of such statute shall be punishable by fine and/or imprisonment.

Recommendation No. 2

Your subcommittee recommends that all possible efforts be made by the Federal Trade Commission, the National Association of Insurance Commissioners, and State insurance licensing authorities to secure voluntary industrywide compliance with the Commission's recently completed Guides for the Mail Order Insurance Industry. The subcommittee wishes to maintain continued liaison and communication with these groups in order to keep fully appraised of how successful they are in obtaining adherence to the guides.

Recommendation No. 3

The Housing and Home Finance Agency should, before Federal funds are approved for projects, give sufficient consideration to safeguards against deception in the advertising or sale of health benefits and other services offered in conjunction with these projects.

Retirement communities, usually restricted to persons 45 to 50 years and older, are completed or contemplated in many parts of the

Nation. California alone has 350 such communities.[23] The "condominium" concept, which permits residents to buy and take title to individual units in multiunit buildings, has been employed in some of these projects, occasionally with assistance from the Federal Housing Administration.

Mr. Robert Peacock, secretary-director of the New Jersey Real Estate Commission, gave a detailed report to the subcommittee on the commission's concern about advertising for one such condominium project.[24] Originally, said Mr. Peacock, the brochures "indicated that the development was offering phenomenal bargains on medical plan rates." The commission and the State Division of Aging questioned the accuracy of these claims. The commission conducted hearings and conferences that led to adjustments satisfactory to the commission.

Mr. Peacock emphasized that the commission would have been powerless to act if it were not for the fact that the owner is also the holder of a real estate broker's license and therefore under commission jurisdiction. He added:

> From our observation of the entire matter, this is not the most serious inadvertence—but neither is it to be taken lightly. The inaccurate and misleading aspects place it within a somewhat indefinable gray area.

His comments led to a colloquy between the subcommittee chairman and a witness, Representative James Cameron of California: [25]

> Senator WILLIAMS. The condominium concept was accepted nationally for FHA in 1961, and I gather it is springing up as the means of creating homes for elderly in many parts of the country.
>
> Certainly one of the attractions of a retirement community for those who are promoting it is to provide within the area medical facilities. Therefore, I would think it is incumbent upon those of us in Government to not be the handmaiden, with our condominium concept in the housing bill, of misrepresentation and illusory promises.
>
> Yes?
>
> Mr. CAMERON. Mr. Chairman, on that very point, we in California have many condominium projects that are financed under FHA—I can think of several that presently

[23] The California situation was described at another hearing ("Interstate Mail Order Land Sales," p. 26, May 18, 1964), in a statement by Assistant Attorney General Herbert Wenig:

"As Commissioner (Milton G.) Gordon stated, there are nearly 350 of these retirement villages or adult communities in California alone. When your subcommittee (Subcommittee on Housing for the Elderly) was in California recently, under the chairmanship of Senator Frank Moss, it heard some of the problems concerning these subdivisions. They may be listed as follows:

"1. The increased cost of health and medical plans after the sale of the community interest or the negotiation of a long lease.
"2. Inadequate funding of clinical care.
"3. Inequitable management control by the promoter, including excessive management fees.
"4. Inadequate financing for projected recreational facilities such as swimming pools, golf courses, etc.
"5. Inadequate funding of repair and maintenance costs.
"6. Excessive amounts of prepaid rent.
"7. Management control or developer control of community development.
"8. Inequitable charges for funeral and burial expense.
"9. Inadequate supervision of medical plans by State authorities.

"One word of caution, however: retirement subdivisions and senior citizens villages are fulfilling the needs of many of our senior citizens by offering them a healthful, productive, and convivial life during the twilight years. In California, as well as other States, responsible developers are building this type of retirement facility in a manner not requiring regulation. *However, when the demand is high and funds are readily available through the sale of businesses and homes by persons going into retirement, or through Government aid, there are attractive opportunities for the fraudulent as well as the inefficient developer.*" [Emphasis added.]

[24] P. 77 ff., op. cit.

[25] P. 81, op. cit.

have occupancy in excess of 10,000; and many more that are under construction. And it occurred to me that possibly this is an area that through the FHA, the Federal Home and Housing Agency, they should be taking a very serious look at. In one particular unit that I am familiar with, the plan with regard to medical benefits was sold not dissimilar to that that Mr. Peacock described. Subsequently, it was found it was not an insured group at all, but rather it was a closed panel medical group that was being set up within the condominium project and there were no hospital benefits available under the program.

Senator WILLIAMS. Well, I would think that where the development has FHA guarantees, there ought to be, even presently existing authority for FHA, to evaluate it——

Mr. CAMERON. Apparently it is my understanding, sir, that this has been outside the purview of the FHA to date with respect to the medical benefits sold. They are concerned in financing and providing the other facilities, but the medical group facility is built by private funds, not financed, that is the clinic facilities built by private funds, by private finances, and is an ancillary benefit to the project, though this tends to be the one that is promoted and is foremost in the minds of the purchasers of the property.

A different view was expressed by another subcommittee member in the following exchange: [26]

Senator FONG. I think with the FHA benefits for the condominium buildings, you are going to run far afield, because as far as I know, the condominium idea is purchasing a lot in space, and the FHA comes in only to take care of the mortgage to insure that the man who buys it is able to pay; if he is not able to pay, then the man who lends the money will be paid. Then the agreement made with the individual is that he pays for that unit that he purchases.

Senator WILLIAMS. But the whole deal lacks integrity if something is costing a lot of money and the services are not being provided. This puts a taint on FHA, I would think, if they are, through their guarantee, making it possible for the promoters to do something wrong.

Senator FONG. The promoters could enter into any kind of agreement with the people who are selling services in town, like the dentist or the garage man, the repairman; and if the condominium purchaser wants to enter into an agreement like that, he could enter it. That is why I feel it is going to be very difficult for the FHA to really enter into this phase of the frauds on the elderly which we are now considering.

All aspects of the question should receive full consideration in the near future. As a first step, the subcommittee recommends an HHFA evaluation for the purposes given above.

[26] P. 82, op. cit.

PART 4

PRENEED BURIAL SERVICE

Testimony by two witnesses on May 19 gave the subcommittee its first evidence of abuses fostered by the growth of preneed burial service plans. According to facts presented at that time, well-organized sales efforts—some using IBM cards for mail payments or even telephone "boilerroom" tactics—are now operating across State lines. Their usual goal is to persuade buyers, especially the elderly, that burial services should be contracted far in advance of death as a hedge against inflation and as a guarantee that costs of burial have been provided.

Though many preneed plans are conservative and sound,[1] the attention of the subcommittee was drawn to the activities of promoters who apparently promised far more than actually provided in the contract terms. Another major concern is the proliferation of preneed plans that keep no trust or escrow funds in States where sales are made, even though they make elaborate efforts to suggest that such protection is given.

Informative as the initial testimony was, the subcommittee realizes that the subject is deserving of far more study to determine whether Federal action is necessary or feasible.

Only a summary of testimony will be given in this report.

SUMMARY OF TESTIMONY

New Mexico: New law tested.—Seven years ago, the State of New Mexico adopted a law requiring preneed plans to be the transaction of the insurance business and "requiring that they be regulated by the superintendent of insurance for the protection of the public in the same manner as the business of life insurance."[2]

Compliance with this law has been far from extensive. New Mexico Special Assistant Attorney General Richard Carpenter gave the subcommittee this estimate of the situation:[3]

> The Supreme Court of Illinois has stated:
> "In the long interval between full receipt of the purchase price and contract performance, the opportunities for fraud

[1] The attitude of the National Selected Morticians, a national association of funeral directors, was summed up in these paragraphs in a letter to the subcommittee chairman from W. M. Krieger, managing director of the organization:

"Honest preneed or prearrangement planning can and does serve a useful purpose to the elderly and the public at large. Funeral arrangements made in advance of death generally are unaccompanied by factors of stress which make arm's-length dealing more difficult. The purchaser is able to give effect to his own preferences and to select with care the type of funeral service which meets his budgetary and other requirements. Lawyers and trust officers, as well as funeral directors, can render the public, as well as the elderly, invaluable counseling service in matters of this kind.

"It is my belief that preneed or prearrangement planning, whether it is effected by will, contract, or otherwise provides the public and particularly the elderly a greater measure of protection against the unethical funeral director or cemetery operator who exploits the bereaved. It is important, however, especially in the case of so-called preneed trusts, that there should be wholly adequate procedures to safeguard deposited funds; that in all instances the purchaser should receive precisely what he believed he was buying; that receipt of full value by him should not be made dependent upon his place of residence at the time of death; and that fraudulent and deceptive promotional and selling methods should be effectively prevented."

[2] "Preneed Burial Service," hearing before the Subcommittee on Frauds and Misrepresentations Affecting the Elderly, May 19, 1964, p. 2.

[3] P. 3, op. cit.

are great and risk of insolvency, with consequent inability to perform, apparent."

These dire predictions have, unfortunately, often become fact in New Mexico. The sales are in the hundreds of thousands of dollars and contract purchasers are at the mercy of the selling groups to perform at a time of grief. None of the nonprofessional groups selling preneed in our State have complied with the above statutory regulation, despite vigorous attempts by our superintendent of insurance and office of the attorney general to enforce the law.

The sellers of these preneed plans use the type of hard-sell tactics so vividly shown in recent issues of national magazines. Our State is very much concerned that these vendors, usually based outside of New Mexico's territorial jurisdiction, have sole, unregulated control of vast sums of our citizens' money.

Mr. Carpenter described a 3-year struggle between the State attorney general's office, and the largest vendor of preneed sales, a Denver, Colo., firm operating under the corporate name of Consolidated Industries, Inc., and headed by Mr. Dallas J. Dhority. The following summarizes the course of the legal action and the reasons for it:[4]

The sales are made door to door and are upon the installment basis. The purchaser signs a promissory note, is given a packet of IBM cards and envelopes and is requested to mail his payment directly to Consolidated Industries in Denver.

Once the funds leave New Mexico, our authorities can offer only minimum protection and we have no concrete knowledge of how the funds are disposed of once they leave our territorial limits. Preliminary investigation has uncovered only minimal assets in New Mexico, under whatever corporate names this group deigns to use at a given moment.

No matter what corporate name is used upon the written contractual instruments, the term "escrow plan" usually accompanies the "sales pitch." Preliminary investigation has uncovered a bank account with a small deposit which was entitled an "escrow account" but which was, in truth and in fact, a mere savings account under the signature of Mr. Dhority and an associate.

This group's written contracts purport only to furnish caskets. *The contracts' total purchase price has usually been $637.50 per plan, or what professional statistics show is approximately the regional average for complete funeral services, including the casket.* [Emphasis added.]

Evidence introduced in a trial on this matter tended to show that purchasers believed that these so-called casket contracts included complete funeral services, and it is no wonder that some purchasers believed the contracts provided for the furnishing of services in addition to the casket, in view of the customary practice of funeral directors to quote

[4] Pp. 3-4, op. cit.

only an integrated price for both the casket and accompanying professional services, which price is usually displayed upon the casket.

In October 1961, after numerous complaints and inquiries from purchasers of these preneed plans, the superintendent of insurance instituted injunctive proceedings against further sales until our statutory requirements were met and to require an accounting of all previous such insurance business.

The following month, a consent decree was entered by which the defendants—Mr. Dhority and his local corporate entities and employees—were required to render an accounting and were enjoined from certain acts in connection with such preneed funeral matters.

In September 1962, our attorney general, at the insistence of the superintendent of insurance, instituted contempt proceedings for violation of the consent decrees by a continued sales program based upon outright and unequivocal violation of New Mexico law.

Mr. Dhority, the president of Consolidated, Consolidated Industries, Inc., Our Chapel of Memories, and two New Mexico employees of the sales organization were adjudged in contempt and given partially suspended fines and suspended jail sentences.

On April 6 of this year, the Supreme Court of New Mexico affirmed the contempt judgment. State officials now will attempt to coerce compliance by enforcing the terms for suspension of part of the fines and jail sentences.

But, Senator, unfortunately, even this action has not begotten compliance. The Denver-based group continues to operate from its out-of-State base, in conflict with the statutes and public policy of the State of New Mexico and contrary to the best interests of the investing public.

Before leaving this foreign vending organization, let us relate what its president and chief stockholder, Mr Dhority, testified was *the cost of the casket delivered—hopefully, again—under their praying hands escrow division contract: $96.50.* [Emphasis added.]

Even if our elderly citizens believed they purchased merely caskets and not professional services, we were astounded at the margin of profit claimed by the vending group at the expense of elderly consumers, many of whom are on limited retirement incomes.[5]

Mr. Carpenter, describing what he called the abuses possible even under a regulated system, added, "We shudder to think what is happening in other States where preneed may be sold and where the

[5] Payment of a $6,000 fine was made by Consolidated Industries to the court clerk of the Santa Fe district court in July 1964 as payment of the contempt of court fine imposed in October 1962.

citizenry has not been alerted and regulatory laws have neither been enacted nor vigorously enforced."[6]

He also described the activities of the Memorial Management Association, Inc., of El Paso:[7]

> The records of our corporation commission indicate that this group is headed by Mr. Norman Anderson, of El Paso, Tex. Under its new name, the so-called Anderson group openly advertised in newspapers in Carlsbad, Clovis, and Tucumcari that it is selling complete funeral services, claiming that its instruments will be honored throughout the United States and Canada. As far as we know, the funds collected under these contracts are transported to Texas and kept without our jurisdiction. There are no substantial, or even insubstantial, assets left within our control.
>
> One of the several affidavits on file may illustrate to this subcommittee how this preneed operation served the public. On or about November 28, 1962, a Carlsbad married couple, with one adult son, and the husband working for the Potash Mines Transportation Co., was approached by a salesman for the Memorial Management Association and was told by the salesman that the funeral service agreement was good anyplace in the United States and Canada.
>
> The family entered into two contracts for $1,324 each, payable $29 monthly upon the express representation that the services covered could be performed by the funeral home of this family's choice.
>
> After becoming suspicious 6 months later, the family inquired whether the benefits would be available at the funeral establishment of their preference, but, after they had already paid in $145 on the two contracts, were told by a representative of the Memorial Management Association that another funeral home, not of their choice, would be used at contract price and asked if it would be worth $400 or $500 more for the family to use the establishment of their choice. This conduct resulted despite the express contrary representation of newspaper advertising and of the salesman.
>
> In truth and in fact, at the time the contracts were sold, the Anderson group had contracts with only three New

[6] The Association of Better Business Bureaus gives this summary of State laws:

"STATE LAWS FOR YOUR PROTECTION

"Twenty-two States, i.e., Arizona, Arkansas, Colorado, Idaho, Illinois, Indiana, Kansas, Maine, Michigan, Minnesota, Montana, New Jersey, New York, North Dakota, Ohio, Oregon, South Dakota, Tennessee, Texas, Utah, Virginia, and Wisconsin enacted laws since 1953 which require that whenever funeral merchandise or services are sold in advance of need all moneys paid in advance for such merchandise and services must be placed in trust by the individual or organization selling the preneed program.

"Under a Pennsylvania law, only licensed funeral directors are authorized to accept money for a preneed contract for professional funeral service. Pennsylvania funeral directors than must place 100 percent of such money in trust.

"A Georgia law demands that 85 percent of all such funds shall be so entrusted. In Iowa, the figure is 80 percent and in Florida 75 percent.

"Another Pennsylvania law requires that cemeteries and other persons selling merchandise and service on a prearranged basis for the interment of human remains place 70 percent of all money collected into a merchandise trust wherein a bank will act as trustee.

"In Florida, Washington, and Wyoming, the legislatures have placed all preneed funeral programs under the jurisdiction of the insurance departments of these States.

"An Oklahoma law prohibits funeral directors from soliciting funerals. The Nebraska law relating to funeral directors gives as one of the definitions of unprofessional conduct: 'Such applicant or licensee contracting with or performing any service for an individual, firm, or corporation engaged in the preneed solicitation or sale of funeral merchandise such as, but not limited to vaults, caskets, markers, and related merchandise or service.' "

[7] P. 5, op. cit.

Mexico funeral homes to furnish services, and these contracts have since been terminated.

Again, the personal story is rooted in the misrepresentation and fraud perpetrated upon real life citizens of New Mexico in the course of making the sale. But the larger picture must include the query of where all the moneys collected under these contracts have gone. Our State authorities do not know and our worries should become those of all the citizenry and of this subcommittee.

Mr. Carpenter also gave considerable detail on mail solicitation used in conjunction with "a virtual army of high-pressure salesmen" to sell preneed services in Roswell, N. Mex., and vicinity. Among his examples: [8]

Three examples will show how these discrepancies misled the public.

Case 1: Mr. and Mrs. X. of Ruidoso, N. Mex., each purchased a Mason contract for a total of $1,287.50, being represented that 75 percent of these payments were to be placed in escrow at a named bank and that credit life insurance was being purchased.

Mr. and Mrs. X are 73 and 66 years of age, respectively. Mr. and Mrs. X paid in $460 before becoming alarmed. Immediately before the hearings in February of this year, Mr. X became suspicious and talked to the vendor's then manager who told him the money was on deposit and insurance was carried upon the balance and that the money would be refunded upon request. Subsequent to the hearing, Mr. X requested a refund and was refused.

Case 2: After receiving letters through the mail, Mr. and Mrs. Y purchased two contracts under the representation that the approximately $1,300 paid in would be kept intact and invested until the time of need. Mr. and Mrs. Y were in their 70's and lived in Roswell upon retirement income from the Santa Fe Railway.

Case 3: Mr. and Mrs. Z of Roswell, N. Mex., each purchased a Mason contract. The salesman represented to them that each payment would be kept in a bank, that the profit to the vendor would be the interest on the amount deposited, and that credit life insurance would cover the unpaid balance. At the time of the above hearings, Mr. and Mrs. Z had paid in $420.

An "Effort To Capture Bodies of the Future": The second witness was W. Dan Bell, manager of the Rocky Mountain Better Business Bureau in Denver, Colo. He made it clear that the principle of preneed service is sound, but that difficulties arise quickly when it is employed: [9]

We feel that the idea of a person arranging their funeral now in theory is good. This means there is no emotion, you can select your price, you can make your arrangements, and this sort of thing. But in practice, we think it's terrible. We think that the present legal measures are not effective.

[8] P. 7, op. cit.
[9] P. 15, op. cit.

> Our law, in spite of it being a new law, is not controlling the situation. We feel that many of these people who have gone into the business, so to speak, will be out. They will have used this money, they will have dissipated it, and generally, the victims in this sort of thing are not people who will complain to the point of prosecuting, and so forth.

The new law to which Mr. Bell referred is a Colorado statute that requires 100 percent of preneed burial sales returns to be put into trust under the supervision of the State banking department. Describing the preneed burial sales as "an effort to capture bodies of the future," Mr. Bell said that 80 percent of the solicitation is directed at people between 60 and 70 years of age. He also gave these examples of current methods: [10]

> In Colorado, in the past year, there is an estimated $8 to $10 million in prearranged funeral contracts that have been sold. Of this money, much of it is sold on an installment contract, and it seems to be a little bit cloudy under the law as to whether it is necessary for the promoter, No. 1, to deposit the money until the contract has actually been paid out, and No. 2, if his contract calls for the sale of a casket or the providing of a funeral plan, whether he needs to put this money in trust on that portion which is applied to the sale of the casket, which he may write in as $300 or $400 for the casket alone.
>
> The methods of doing business vary in our State. We have some that advertise, as for instance, this advertisement that reads:
>
> "Do you qualify for these U.S. Government death benefits? U.S. Social Security, maximum, $255, United Memorial's answer to the ever-increasing cost of funeral services, the united plan. The preneed plan that costs $10."
>
> Now, their actual contract that they write up calls for the purchase of a casket, and a representation that the funeral service will be given by whatever mortuary they choose. They have what they call the endorsed mortuaries, who are any mortuary that they so desire to say, "You are endorsed."
>
> We had a complaint a couple of weeks ago, a party died who had bought one of these plans—an elderly man—from this company, and had designated a certain mortuary in the Denver area as the one to handle his services. When his relatives went to this mortuary, the mortuary refused to handle the service because the man had contracted under this plan, and the only amount of money that the mortuary would get would be the social security benefit that the man had coming.
>
> The mortuary did not have any prior agreement with this United Memorial Service to perform this service, and therefore, refused it. According to the complainants, they tried then several other mortuaries in town, and were turned down on all of them except finally they found a smaller mortuary who agreed to perform a $225 service.

[10] P. 13ff., op. cit.

So that this illustrates that a professional promoter in this field who does not have an assured place to which the service can be referred can sell a lot of contracts, but the people may not even get their funeral services that they paid for, or contracted for. * * *

Another operation that is of a similar character that is soliciting our elderly people comes from out of Kansas City, and it was initiated by two men who had been recently expelled from the livestock business. They had been caught shipping cattle, misrepresenting cattle, and the Department of Agriculture barred them from the livestock business, for I believe, a period of 10 years.

They apparently had a little money, so they started a company they called "American Mausoleum Service Co.," and this is another preneed promotion, in that they tied up with your friend, Mr. Dhority, in Denver, on a contract to build mausoleums on Mr. Dhority's cemeteries, and they immediately had a large sales crew go out and work through churches, and got some of the churches to give their lists of their members.

They did some advertising. They developed their sales leads, and they sold people crypts in mausoleums that have not yet been built, and there may be a question as to whether they ever will get built.

They also started a business of selling plastic caskets, which they claim had more merit than those being sold that were made of steel. This whole activity, at least again in our area, seems to be geared toward what Mr. Dhority told me, getting 100 percent of the death dollar. * * *

There is one other facet to this that we have noticed in the fast-buck operations. Under the law, again, if a holder of these contracts defaults, and doesn't pay it out, or if he moves from the State, the trustee need only return 75 percent of the money.

In other words, the trustee can hold 25 percent of the total contract price, so that it is to their advantage, actually, to discourage the complete payment of these contracts. If a person has a $600 contract and pays in $300, the promoter can then retain $200 (sic) of that, or 25 percent, and refund only $100 * * *.

Senator WILLIAMS. Have you had many direct complaints?

Mr. BELL. We say it is many for the type of business that it is. There aren't many people that want to revive the feeling that they have about a funeral, but we get complaints on, for instance, the techniques of solicitation.

We have one party who complains that she just recently went to a funeral. She noticed this man out at the cemetery, writing down license plate numbers, and about 3 days later, she gets a phone call, this counselor, wanting to come out and sell her a funeral service.

We have had complaints from people who object to the giving of trading stamps, if they will listen to the story on the funeral plan. We have people who call us and complain

about the telephone solicitation and that they get calls on this at 9:30 at night, and this sort of thing.

They have professional promoters, one in from California, another one from Kansas, that actually operate boilerrooms and promote these. The little fellows don't like this type of thing, but they are having to employ, and they are going together, because no one of the little guys can afford it, they are going together and forming organizations to do this, throughout the State.

Extent and other aspects.—Mr. Bell described preneed sales as a growing problem in Missouri, Kansas, and Colorado. He said: "It is creeping up into Wyoming, over into Utah, and unfortunately, there seem to be two bases for this operation, one out of Denver, and one out of Kansas City." [11]

Additional information was given in a statement submitted by Mr. Howard C. Raether, executive secretary, National Funeral Directors Association of the United States: [12]

> Testimony before your committee has dealt primarily with operations stemming from Colorado and Missouri. But the promotions and schemes are not limited to these States. They have been or are in most States west of the Mississippi. And as near saturation points are reached where the area has been productive, said promotions are moved into other States. Some of the groups cited in testimony presented before you have tried to establish themselves in States east of the Mississippi.
>
> In addition to plans emanating from Missouri and Colorado cities, there also are some based in Arizona, Nevada, and Texas. And while people of all age brackets are vulnerable to the misrepresentations of these plans, the elderly often are the most gullible while being least able to bear the losses and disappointments inherent in such schemes.

Another aspect of the prearrangement and prefinancing of funerals was discussed in a booklet distributed by the Association of Better Business Bureaus: [13]

> Sometimes, belief that a funeral has been fully prearranged and paid for can create a false sense of security in survivors. For example, a man in a Midwestern State prearranged and prepaid his funeral expenses. He died in a distant city while visiting a daughter who made the arrangements for the funeral of her father so that not only friends in his home city could pay their respects but also those at the place of his death. This made for two funeral services instead of one and called for the expenditure of additional funds. The man's widow was very distressed at the additional charges because she had been led to believe that her husband's funeral had been paid for. Such incidents are not uncommon. The United States is a mobile nation. More than 10 percent of our people die in communities other than those in which the funerals are conducted. The difficulties in making

[11] P. 13, op. cit.
[12] P. 20, op. cit.
[13] "Facts You Should Know—Questions You Should Ask About—The Prearrangement and Prefinancing of Funerals," Association of Better Business Bureaus, 405 Lexington Avenue, New York, N.Y.

funeral plans by prearrangement, not knowing where or when one will die, are obvious.

Mr. Carpenter added one more cautionary comment. He said he believes that the number of dishonored contracts may well increase: [14]

> Senator WILLIAMS. Have these companies been honoring their obligations, at least to the extent of the casket? Or have there been any defaults there?
>
> Mr. CARPENTER. Well, where we have a difficult time is finding out when they have honored it, because then we don't get the complaint. Of course, most of these people, at the present time, we anticipate honoring all these so-called casket contracts for 2 or 3 years in New Mexico, because they are still trying to sell them, and they will not be dishonoring their policies while at the same time they are still trying to foist them on the public.
>
> But what we are anticipating is somebody 60 or even 50 years old buying one, and we have to look forward to what's going to happen 30 years, or if they are lucky enough, even 40 or 45 years from now, but in the immediate future, we believe that they will perform them.

Summary: **Preliminary inquiry by the subcommittee has revealed actual and potential losses resulting from the sale of preneed burial services across State lines or through the mail. Often, victims are elderly persons who have sought to make certain that they themselves, rather than their survivors, will bear such costs. The threat of such losses, and the cruel nature of the deception, calls for broadened investigation by this subcommittee.**

[14] P. 16, op. cit.

PART 5

THE REGULATORY AGENCIES—PROBLEMS AND PROPOSALS

INTRODUCTION

Time and again during its investigations and hearings, the subcommittee received information about the mounting consumer protection responsibilities of the Federal Trade Commission, the Food and Drug Administration, and the U.S. Postal Inspection Service.

The final section of this report offers recommendations that would, in the opinion of the subcommittee, help agencies to act more effectively against many of the abuses discussed in this report, and against other practices employed by cheats to take advantage of every delay and deficiency in existing law.

Food and Drug Administration

Assigned a major role in the campaign against quackery and other sources of potential danger and loss to consumers, the Food and Drug Administration has undergone extensive reorganizational changes in recent years. It has also been given new regulatory responsibilities.

Two years ago, the FDA clearly recognized that it needed nationwide perspective on the impact of these changes and other new influences on its mission. The agency commissioned the Public Administration Service of Chicago to conduct a comprehensive survey of the relationships between State and Federal laws in broad areas of mutual interest, including regulation of foods, drugs, and therapeutic devices.

This survey, which was to be published early in 1965, is certain to give useful information of direct concern to the subcommittee, other congressional units, and public agencies, and private organizations concerned about quackery control and related efforts.

1. It is recommended, therefore, that this report receive careful attention in order to facilitate suggestions for coordinating and improving relationships between the Federal and State Governments in regulation of foods, drugs, and therapeutic devices.

2. It is further recommended that the study serve as the basis for determining whether States should be urged to enact uniform laws [1] on—

(a) Premarket testing of drugs for efficacy and safety, with technical assistance from the Federal level.

[1] Federal legislation in 1963 established new and effective methods of protecting the public against quack drugs. In individual States, however, premarket testing of drugs for efficacy as well as safety has not yet been established. This deficiency permits pockets of unregulated activity to continue within State lines. As a result, large-scale interstate promotion of products banned in interstate traffic continues.

Seven States—California, Nevada, Colorado, Kentucky, Maryland, North Dakota, and Pennsylvania—have established cancer control programs that require full evaluation of unproven cancer remedies before they can be sold. It is still too early to determine whether these laws are completely workable and protective, but it is obvious that similar protection should be given to those seeking help from other kinds of remedies.

A similar problem arises in connection with intrastate use of devices. The subcommittee has received testimony indicating that some practitioners deliberately make patients come to them for treatment in order to keep devices within States and free of Federal regulation.

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(b) Premarket testing of therapeutic, diagnostic, and prosthetic devices, with technical assistance from the Federal level.

THE U.S. POSTAL INSPECTION SERVICE

Mail fraud statutes enacted by Congress impose a duty upon the Postmaster General to prevent the Postal Establishment from being used in the perpetration of schemes to defraud the public. Some idea of the size of the task can be gathered from these statistics: In Fiscal year 1964, 119,092 complaints of alleged mail fraud were received; 8,769 investigations were completed; 709 arrests were effected; and 544 convictions obtained.

The postal fraud statute.—In 1963 and again in 1964, U.S. Chief Postal Inspector Henry B. Montague testified on the wide responsibilities given to the men who work in his Bureau. A point made clearly at each of his appearances is that limitations of the administrative fraud statute makes quick action against offenders difficult.

This exchange on March 10 concisely explains the situation: [2]

> Senator WILLIAMS. Prosecutions are made rather difficult, are they not, in mail fraud, because of the elements of proof that are necessary?
>
> Mr. MONTAGUE. Yes, sir, we have to prove beyond a reasonable doubt that there has been a scheme devised, that there is an intent to defraud.
>
> Senator WILL AMS. Do you have any suggestions to us how legislation might be changed to make it possible for you to reach more of these practitioners who are grossly misrepresenting and grossly overclaiming benefit from their product?
>
> Mr. MONTAGUE. As far as the criminal statute is concerned, Senator, we feel it is fair and equitable that we should have to prove that a scheme was devised, that there is intent. We do obtain voluntary discontinuances of many of these schemes, and the U.S. attorney sometimes decides not to prosecute as long as the operator has gone out of business.
>
> With regard to our formal administrative action cases, Mr. Wenchel (Adam G. Wenchel, Associate General Counsel) may have some comment on that.
>
> Mr. WENCHEL. As you know, there has been in the Department consideration of suggesting amendment to the administrative fraud order statute to eliminate the necessity of finding intent to defraud. However, the Department has not yet worked out all of the problems which are inherent in such an amendment, so we are not ready at this time to recommend to Congress that there be an amendment to that statute.
>
> Senator WILLIAMS. Senator Fong?
>
> Senator FONG. Mr. Montague, what is the difference between an administrative action as differentiating from a criminal prosecution?

[2] P. 285, hearings on health frauds and quackery.

Mr. MONTAGUE. In administrative action, Senator, the General Counsel would notify the operator that there is to be a hearing to decide whether or not the use of the mails should be barred to the operation, and the operator would have an opportunity to come in and be heard, with counsel. If the final determination is made that a fraud exists, then a fraud order would be issued against the operator; that is, any mail addressed to him under the name by which he is doing business would be stamped fraudulent and returned to him.

Under the criminal action, we present the findings to the U.S. attorney. If he decides there is evidence of a criminal violation, he presents it to the grand jury. If an indictment is returned then the operator has the opportunity to plead, and if he pleads not guilty, a trial ensues. Then we get either an acquittal or conviction.

Senator FONG. Most of the work of the Department is to get the fraudulent person to desist?

Mr. MONTAGUE. Yes, sir, we try to accomplish both, if possible. We attempt, if there is evidence, to get a voluntary desist and go ahead with the criminal action. If the person does not voluntarily desist, then we would recommend to the General Counsel that appropriate action be taken formally.

Additional perspective was given on May 20: [3]

Senator WILLIAMS. Have you developed any suggestions for the Congress as to ways the statutes could be improved, from your standpoint, to make your work more efficient?

Mr. MONTAGUE. Not so far as the criminal statute is concerned. We believe it is equitable, that we have to prove that there has been a scheme devised. With regard to the administrative procedures, I would ask Mr. Wenchel if he would address himself to that feature.

Mr. WENCHEL. The one feature in our administrative proceedings law, which is section 4005 of title 39, on which some attention has been focused is the requirement in that law that intent be established. There has been a considerable amount of discussion as to whether this law should not be so amended as to allow us to issue a fraud order on the basis of false advertising or false representations, even though we cannot establish that they were intentionally fraud.

This involves a great many considerations. We have been discussing this matter with the Department of Justice and other agencies, but we have not yet formulated any legislation to present to the Congress on that.

One other minor aspect. At present we have no subpena powers to use in our fraud order proceedings. There are provisions in the various bills which are under consideration now for amending the Administrative Procedure Act which would give us that subpena power which would be of some assistance to us in these fraud cases.[3]

[3] P. 241, hearings on Interstate Mail Order Land Sales.

There is a clear-cut need for action in this area. The subcommittee therefore recommends: [4]

Earliest possible passage of a postal fraud administrative statute that will remove difficulties caused by the "intent to defraud" language of the statute.

Demands on manpower.—Congress provided in 1964 for 25 additional inspectors to work on fraud investigations. Under questioning during the hearing on mail order land sales, however, Mr. Montague gave this picture of total demands on the Post Office investigators: [5]

> We have, in all, 1,028 inspectors to make all of our investigations. These investigations include inspections of post offices, thefts from the mails, robberies, holdups, obscenity, mail fraud, and all of the other responsibilities we have. We are able to devote the time of about 100 inspectors, that is about one-tenth of our force to this type of investigation throughout the country. That is: all frauds, not just land frauds, but all categories of frauds * * *.
>
> Each of our inspectors last year worked an average of about 54 hours per week. To handle this type of case, taking into consideration that we have all other types of fraud, medical frauds, vending machine cases, work-at-home schemes of all kinds, I would say that consistently we are probably not able to devote more than the time of 20 inspectors to this particular type of investigation (land frauds).

At an earlier hearing, Mr. Montague answered a question about the budget of the postal fraud program: [6]

> We have costed out the program and in total, that is considering all of our inspector manpower, clerical manpower, auditing manpower, the time that the General Counsel would devote to this, and the judicial officer, the cost comes to about $2.4 million per year.
>
> Last year fines imposed by the court were $125,000; court-ordered and voluntary restitutions were $1,995,000, for a total of $2,120,000. So this program comes within about a quarter of a million dollars of paying for itself, and this is without taking into consideration the huge sums saved the public by putting the swindlers out of business.

The subcommittee recommends that appropriate congressional committees consider the preliminary findings of this subcommittee and any other information that will be helpful in evaluating present budgets and manpower requirements of the postal fraud control program.

The Federal Trade Commission

Established a half century ago, the Federal Trade Commission was specifically created to deal with "unfair methods of competition" and other restraints on trade. To at least one authoritative analyst, the Commission's success in establishing jurisdiction over advertising was

[4] A bill (H.R. 7813) to this effect was introduced by Representative Morris K. Udall on July 29, 1963. A similar bill (H.R. 11141) was introduced in 1960. Another bill (S. 1563), introduced in 1963, would amend sec. 6(c) of the Administrative Procedure Act to grant subpena power to the Post Office Department.

[5] Pp. 237-238, May 20, 1964.

[6] P. 286, Mar. 10, 1964.

merely "a fortuitous byproduct" [7] of its more general duties; there was no direct basis for it in the enabling legislation.

However interpretations of the original law may vary, the Commission took an early interest in advertising.[8] Court rulings and a 1938 amendment of the law firmly established that the Commission had a clear-cut duty to monitor advertising and to act against advertisers who make false promises to buyers.

Fifty years after its founding, the Commission may now seem to have, in the eyes of the public, formidable punitive powers over those who deliberately make false statements in newspapers, magazines, and more recently on radio and television.

The Commission, however, does not mete out punishment; it merely attempts to end deception in advertising as quickly as possible without necessarily subjecting the violator to any penalty at all.

To accomplish this, the FTC employs procedures [9] that have been criticized before the subcommittee and elsewhere as cumbersome and time-taking. Commission Chairman Paul Rand Dixon, in fact, told the subcommittee that it now takes about 1 year for cases "to reach the Commission level" for issuance of a complaint.[10] This complaint gives the respondent an opportunity to consent to a cease-and-desist order without admitting any violation of the law. If the respondent

[7] Henderson, "The Federal Trade Commission," 1924, p. 339.

[8] In the 1916 FTC Annual Report, the Commission noted: "The Commission has gone further than this, however, and in some instances where these elements (restraint of trade or lessening of competition) did not appear, as in certain cases of misbranding and falsely advertising the character of goods where the public was particularly liable to be misled, the Commission has taken jurisdiction."

[9] The U.S. Government Manual for 1964 gives this description of the FTC procedures:

Legal casework: Cases before the Commission may originate through complaint by a consumer or a competitor; from Federal, State, or municipal agencies; or the Commission itself may initiate an investigation to determine possible violation of the laws administered by it. No formality is required in making application for complaint. A letter giving the facts in detail is sufficient, but it should be accompanied by all evidence in possession of the complaining party in support of the charges made. It is the policy of the Commission not to disclose the identity of any complainant.

"Upon receipt of an application for complaint, the Commission considers the essential jurisdictional elements before deciding whether it shall be docketed for investigation.

"On completion of an investigation, there may be a staff recommendation for (1) informal settlement of the case on respondent's assurance of discontinuance of the illegal practice, (2) issuance of a formal complaint, or (3) closing the case.

"If the Commission decides to issue a complaint, normally the party so concerned is served with notice of the Commission's intention in that respect and is furnished a copy of the intended complaint and order. The respondent then has the privilege of consenting to a cease-and-desist order without admitting any violation of law.

"If an agreement containing a consent order is not entered into, the Commission may thereafter issue its complaint.

"The case is heard by a hearing examiner who, after taking testimony at public hearings, issues an initial decision. This becomes the decision of the Commission at the end of 30 days unless the Commission decides to review the case, in which case the initial decision is sustained, modified, or reversed.

"Under the Federal Trade Commission Act, the Clayton Act, and the Wool, Fur, Textile, and Flammable Fabrics Acts, an order to cease and desist (and, in the case of the Clayton Act, an order to divest or rid) becomes final 60 days after date of service upon the respondent, unless within that period the respondent petitions an appropriate U.S. court of appeals to review the order. In case of review, the order of the Commission becomes final after affirmance by the court of appeals or by the Supreme Court of the United States, if taken to that court on certiorari. Violation of an order to cease and desist after it becomes final subjects the offender to suit by the Government in a U.S. district court for recovery of a civil penalty of not more than $5,000 for each violation. A respondent found guilty of violating a cease-and-desist order is liable up to $5,000 for each violation and, where violation continues, each day of its continuance is a separate offense.

"Under all these statutes the respondent may apply to a court of appeals for review of an order and the court has power to affirm, modify, or to set aside the order. Either party, on writ of certiorari, may apply to the Supreme Court for review of the action of the court of appeals.

"In addition to the regular proceeding by complaint and order to cease and desist, the Commission may bring suit in a U.S. district court to enjoin the dissemination of advertisements of food, drugs, cosmetics, and devices intended for use in the diagnosis, prevention, or treatment of disease, whenever it has reason to believe that such a proceeding would be in the public interest. These temporary injunctions remain in effect until an order to cease and desist is issued, or until the complaint is dismissed by the Commission or the order is set aside by the court on review.

"Further, the dissemination of a false advertisement of a food, drug, device, or cosmetic, where the use of the commodity advertised may be injurious to health or where there is intent to defraud or mislead, constitutes a misdemeanor; and conviction subjects the offender to a fine of not more than $5,000, or imprisonmemt of not more than 6 months, or both. Succeeding convictions may result in a fine of not more than $10,000, or imprisonment of not more than 1 year, or both. The statute provides that the Commission shall certify this type of case to the Attorney General for institution of appropriate court proceedings."

[10] P. 353, Hearings on "Health Frauds and the Elderly."

decides not to consent, he may—if he has the resources—delay final action for 2, 3, 4 years or even longer.[11]

It has been suggested on more than one occasion that some affluent advertisers deliberately take advantage of complex Commission procedures and court struggles in order to continue sales of misrepresented, but lucrative, products for as long as they possibly can.

A direct statement on this subject was given by Dr. Frederick J. Stare, chairman of the Department of Nutrition, School of Public Health, Harvard University, before the subcommittee. Dr. Stare discussed a complaint brought by the FTC against the advertising for a book he described as "filled with misstatements, with falsehoods, and with all kinds of errors and implications": [12]

> I don't know how long it has been available, my guess would be at least 5 years. Well, the Federal Trade Commission got after the publisher and asked if I would be a witness for them, and I said that I would be. This case was to come to trial four or five times, and then at the last minute it would be postponed.
>
> This past fall, I would say some time in November, just the day before it was to finally come to trial in New York, as usually happens, they throw in the sponge and say, "The Federal Trade Commission was right," and they quit. But in the meantime, they have had a few years to sell this book and get all this nonsense around to the American public. Also during this stalling they have time to write a similar book, giving the same old nonsense, bringing it up to date, and coming out with it about the time they throw in the sponge on the former book. This has happened—same author, same publisher, only a different title. So here they go again for a few years while the FTC prepares a new case.

FTC Chairman Dixon was asked about the situation when he appeared before the full committee in 1963. He replied: [13]

> You remember this: The mere fact that we start looking at something or we even serve a complaint, that advertising does not have to stop, if one keeps the case alive going through review to the Supreme Court. Until the Supreme Court stamps approval, and then our order becomes final, he has to stop, but until they stamp it approved and our order becomes final, the promoter can get himself about a 4-year period to reap a lot of money, sir, is what I am telling you.
>
> Senator MUSKIE. In other words, the regulatory lag.
>
> Mr. DIXON. This is correct, sir.
>
> Now what I am talking about, if this kind of a practice is going on, I think it is disgraceful—if on its face it is that phony, and we can show upon the record the irreparable

[11] One major case now before the Commission, for example, deals with two products advertised as effective against anemia and other deficiency ailments. The initial complaint, following a 3-year investigation, was issued on December 18, 1962. Prehearing conferences ended in March 1963, and hearings were conducted in 15 cities before the year ended. The FTC called 44 scientific witnesses, most of whom were experts in hematology. The Commission hearing examiner issued his initial decision by May 1964; final briefs were submitted in December: and the Commission is expected to announce its final decision in 1965. If the Commission decides adversely, the company may then go to the Federal district court or even ultimately to the U.S. Supreme Court.

[12] P. 288, op. cit.

[13] P. 287, "Frauds and Quackery Affecting the Older Citizen," hearings before the Special Committee on Aging, Jan. 15 16, 17, 1963.

harm and injury that will come to the public—that we can't enjoin that practice while we are trying it. You see the practice is that what is happening here is that we might say the runner here reaps the benefit. The public is not only the loser, but is going to lose while this goes on.

A few pages later, this was added:

Senator MUSKIE. Would you say that there is any truth to the suggestion that the promoters of these schemes and devices and plans rely upon the regulatory and judicial lag as a period when they can escape?

Mr. DIXON. Well, I wouldn't be surprised if they were not aware of it, and——

Senator MUSKIE. Sort of a predictable thing.

Mr. DIXON. I think they could nearly predict that if they wanted to pay a high-priced lawyer to file every motion that he can file, which any half-qualified lawyer can do, and they resolve to take every appeal that he can take, to engage in every legal shenanigan that a lawyer is capable of to get a complete judicial review, yes, he could keep one of these things alive for 2, 3, or 4 years, no matter how fast we do our job, sir.

SUGGESTIONS FOR IMPROVING PROCEDURES

Now at a critical point in its development, the FTC has, within recent years, implemented some administrative changes. The Chairman has also asked for the right to issue temporary injunctions without going through the courts [14] in order to prevent advertising from misleading large numbers of buyers before the abuses can be stopped by ordinary procedures. Mr. Dixon, however, acknowledged that a bill to this effect would be confronted with major obstacles in Congress.

Manpower: The Commission has asked within recent years for more funds and manpower to keep pace with its formidable workload, as this testimony from Mr. Dixon indicates: [15]

Senator MUSKIE. What can we do further to reduce this regulatory lag? Do we need more law, do you need more staff, or are we doing all we can with it?

Mr. DIXON. We need both, sir. We need both.

I think that if it should be the will of the Congress—because it must eventually be your decision as to whether we get this additional power or not—this additional power to issue cease-and-desist orders would certainly be helpful in eliminating some of the outrageous things that we see.

Then our ability to stay abreast of our load. I think now, sir, we are getting about 6,000 complaints a year—about 7,000, now, Mr. Wheelock reminds me—and we are not married to this mailbag; this just comes in. One complaint comes in and it may result in 200 cases, but these are coming.

[14] The Commission now may, under certain circumstances, ask Federal district courts for injunctions against advertising used for foods ,drugs, devices, and cosmetics. Chairman Dixon believes that this power should be broadened. His testimony on this point may be found on pp. 280-281 of the 1963 committee hearing transcript and on page 354 of the "Health Frauds and Quackery" hearing, Mar. 10, 1964.

[15] P. 288, 1963.

> We are a body of about 1,130 employees today, and we are required—really, our vista is the American free enterprise system, with only those narrow areas that have been whittled out for possible action by the true regulatory bodies.
>
> This is a tremendous undertaking. I would not say that we ought to have so many people that the town is crowded, but I think that we have a far way to go.
>
> Then you have got to discover some other procedure to keep these boys here in these agencies.
>
> I was looking at my rolls yesterday. I was told that in the last 5 months I had hired about 150, and had lost 148, so I am 2 ahead, sir.
>
> Now, you have done a good job on the salaries. This will help. But when I have lawyers, and I get them trained in 2 or 3 years, and then a law firm or a corporation comes in and gives them $25,000, I have trained them mighty fine boys.

Mr. Dixon, in testimony this year before a House Appropriations Subcommittee asked for a $13,270,000 budget for fiscal year 1965, an increase of $1,055,250 over fiscal 1964. Mr. Dixon said that additional funds could be used, for the most part, to help the Commission deal more adequately with questionable advertising of new drug and health products. He said:

> These include pain-relieving drugs of furiously competing speeds being sold at a $360 million rate; arthritis and rheumatism concoctions being sold to 12 million sufferers for "cure" or "quick relief"; a host of impressive claims for vegetable oils and margarine products as heart attack insurance; air filters and purifiers that will remove any germ that worries a buyer; and, of course, the nasal sprays, mouth washes, liniments, sirups and tablets that have conquered the common cold, or at least, its unpleasant features.

Congress appropriated $12,875,000 for fiscal 1965. The increase over fiscal 1964 was not enough to offset automatic and other pay increases, but departures from the staff enabled the Commission to keep its consumer protection programs at approximately the same level as in fiscal 1964.

RECOMMENDATION

Faced by complex and multiplying responsibilities, the Federal Trade Commission can look forward to an even heavier load as the advertising industry continues to grow. The estimate is frequently made that the volume of advertising, now at about $12.5 billion a year, will double by 1972.

In addition to becoming bigger, the industry will become more complicated as more products are offered. Advertising experts, testifying last year before another congressional subcommittee, said that supermarkets alone carry 7,000 to 8,000 different items on their shelves now. They expect the number to increase to 20,000 by 1970.

Existing difficulties are thus likely to be intensified by future growth unless adjustments in Commission procedures are made.

Much as the subcommittee sympathizes with the purposes of the temporary injunction power sought by the Commission, the subcommittee questions whether this and other proposed improvements would be more than patches on an old structure in need of thorough examination that will identify areas of strain or weakness.

In many ways, the FTC is in much the same situation that the Food and Drug Administration faced 10 years ago. The FDA had suffered several consecutive budget cuts necessitating the release of agency employees and a curtailment of agency enforcement programs, despite the outpouring of new and potentially troublesome products on the market. To many observers, it was apparent that the FDA had to undergo a searching reevaluation of its programs and purposes.

Early in March 1954, a spokesman for the Health, Education, and Welfare Department [16] asked the House Appropriations Committee for funds to create a Citizens Advisory Committee to assess the programs and policies of the FDA. Given these funds, the Secretary of Health, Education, and Welfare selected 14 advisory committee members, including representatives of the legal, judicial, pharmaceutical, medical, and scientific fields, representatives of labor and consumers; and representatives from industries regulated by FDA. The Committee, given a budget of $75,000, met in February 1955 and reported to the Secretary in June 1955.

Among the major findings of the first report were: a pressing need existed for staff, office space, and testing facilities; educational programs should be directed to consumers and industry; cooperative enforcement programs should be developed with the food, drug, and cosmetic industries; and more attention should be given to development of cooperative relationships with State and local agencies.

The report of the Second Citizens Advisory Committee on the Food and Drug Administration, issued in 1962, also made searching recommendations for more effective action by the agency.

The experience of the FDA and its Citizens Advisory Committee has caused some speculation about the desirability of a similar effort to assist the FTC.[17]

In the course of its hearings this year, the subcommittee did not specifically seek arguments for or against an FTC Citizens Advisory Committee. However, because the question strikes to the very heart of one of the basic issues before the subcommittee—losses sustained by the elderly because of deceptive advertising—the

[16] HEW was not functioning as a department when the Citizens Advisory Committee was established; food and drug regulation was administered in the Department of Labor, but HEW was established late in 1954.

[17] In "The Federal Trade Commission and False Advertising," Columbia Law Review, vol. 64, March 1964, Dr. Ira M. Millstein, chairman of the Subcommittee on Regulations Affecting Advertising of the Committee on the Federal Trade Commission, Antitrust Section, American Bar Association, made a strong recommendation for a Citizens Advisory Committee to the FTC. He argued that the Commission cannot hope to prosecute case by case every false advertiser in the United States—"such an approach to consumer protection in the field of false advertising is completely unrealistic."

He also made this assertion: "Recognizing that the Commission should have jurisdiction over all interstate advertising in order to avoid chaos by inconsistent interpretation, yet also recognizing that the Commission cannot conceivably enforce at the local level and should not proceed against essentially local advertising, one concludes that the only alternative is to encourage uniform State activity. The Commission should occupy a primus interpares role with respect to the State agencies, encouraging passage of needed legislation, offering advice and possibly assistance in litigation and the formulation of guides; becoming the focal point of coordination among State agencies to avoid inconsistencies; referring complaints of an essentially local nature to State agencies; and, in general, developing programs designed to urge and aid State agencies to adopt a rational but consistent approach to local advertising, thereby relieving the Commission of a host of essentially local matters."

subcommittee will seek more information in the course of hearings and investigations in 1965.

In addition, the subcommittee recommends that the Federal Trade Commission make its own analysis of the need for such a study, and that it seek the advice and opinions of industry, labor, consumer agencies and organizations, and experts on law.

PART SIX

MINORITY VIEWS OF SENATOR WINSTON L. PROUTY AND SENATOR HIRAM L. FONG

The human and financial loss resulting from quackery, misrepresentation, and other fraudulent practices has been fully developed in the subcommittee report.

Every reasonable approach aimed at elimination or reduction of the waste and suffering resulting from such practices should be pursued as expeditiously as possible. We should not permit our enthusiasm for correction of the evils, however, to carry us into ill-considered action which might create more serious problems than those we hope to solve.

From testimony produced at the subcommittee hearings, certain facts regarding the problem of frauds and misrepresentations affecting the elderly, and those of other ages as well, come through clearly:

1. The most effective deterrent to fraud and quackery is an informed people. High priority should be given, therefore, to expansion of public education in these areas.
2. As commodities and services, genuine or fake, are offered to the public, accurate information on them and what they will or will not do should be made available promptly.
3. A major part of the problem is produced by operators who completely disregard Federal and State law. Its correction requires, not necessarily new law, but improved law enforcement.
4. Improper practices and misrepresentations involve a very small percentage of the total business carried out in the areas studied; this constitutes a tribute to the integrity of law enforcement officials and the intelligence of American citizens, young and old; in the aggregate, however, its magnitude in dollars, and in the suffering and deprivation which it produces, calls for vigorous action.
5. Lines of attack on the problem, by government at all levels and by other elements in society, are many and varied. The complicated nature of the problem is shown by the fact that it still persists after years of vigorous effort and a multiplicity of laws and programs designed for its eradication.
6. There is no controversy regarding our national determination to war on quackery and frauds. There may be, indeed apparently are, however, differences of opinion as to the implements and battle plans which will most effectively produce the victory we all seek. The problem's very complexity demands that full use be made of all expert opinion, including differing points of view, and every pertinent fact. Only thus can we be assured that new lines of action are not only well motivated but sound and workable.

The subcommittee has accumulated a large store of facts about the problems confronted by individuals. It would appear, however, that more information is still needed.

Deficiencies in the data available are to the subcommittee all understandable. The limited time available to it has been used well. Nonetheless, serious information gaps do exist. Until they are filled, proposed cures for some parts of the problem cannot be evaluated intelligently.

In the field of mail-order health insurance, for example, answers to additional questions appear necessary to pinpointing more clearly the problem of whatever misrepresentation may exist.

In its findings with reference to mail-order health insurance, the majority report accepts the National Association of Insurance Commissioners estimate that—

> Less than 1 percent of the total health insurance market in the United States is attributable to direct mail companies

but ignores the June 18, 1964, letter on behalf of NAIC from its director, William R. Morris.

In this letter, responding to a series of questions from the subcommittee chairman, Mr. Morris observed in part:

> If the premium volume of Blue Cross, Blue Shield, and other hospital-medical plans were included, the $6,431,124,200 figure would be increased by over $3 billion, without an increase in the $44,326,096 figure (since such plans are not written on a direct-mail basis), thereby reducing the proportion from seven-tenths of 1 percent to below one-half of 1 percent.

It would appear further that accurate assessment of injury to older people through improper advertising of health insurance would require an additional fourfold inquiry.

(*a*) What part of the less than one-half of 1 percent resulted from improper advertising by direct-mail insurers?

(*b*) Of that part, what portion was issued to elderly persons?

(*c*) To what extent have existing statutes, particularly regarding the mails, been enforced?

(*d*) Are improper practices widespread geographically, or are they largely to be found in specific geographic areas?

According to some knowledgeable people in the field, there is no evidence to indicate that the answers to the foregoing questions demonstrate widespread misconduct of the part of direct-mail insurers. Even if half of direct-mail health insurance advertising were improper (which it is not), and even if half of the policies issued in response to such improper advertising were issued to elderly persions (which they were not), the problem would embrace less than one-eighth of 1 percent. Even if the percentage were this high, further efforts should be aimed as a rifle at that very small percentage.

Another illustration of de minimis non curat lex is provided by the testimony of Federal Trade Commission Counsel James McI. Henderson, that the FTC has had only 26 complaints including those now under investigation. In a nation where nearly 1,000 insurance companies and other organizations have provided voluntary health insurance to three-quarters of the entire population, those 26 complaints provide an inadequate basis for the conclusion that FTC investigations are on the upswing and a questionable foundation for the claim that further Federal regulation is needed.

It should be acknowledged that the limited time available to the subcommittee has made it impossible to delve thoroughly into all aspects of the problem, as it may occur in various fields of activity. It is important, however, that this type of information be obtained.

The majority report offers a number of specific recommendations for governmental action at both Federal and State levels. Some of these, or others which further study may develop, would probably deserve support after additional careful evaluation. Some, however, might create new problems and evils more serious than those they are designed to prevent.

Throughout the hearings, for example, both law-enforcement officials and subcommittee members have recognized the delicate balance necessary between enforcement powers and adequate safeguards for the innocently accused.

Likewise, while every effort should be made to protect the unwary from the unscrupulous, the processes designed for this purpose should not be permitted to destroy completely the individual American citizen's right to exercise his own judgment.

These and similar considerations, raised during the subcommittee hearings by both majority and minority members, demand that great care be used in evaluation of all remedies, including legislative, no matter how sincere is their motivation or glowing their apparent promise.

A single recommendation in the majority report may serve as an example. It is proposed that premarket testing of therapeutic, diagnostic, and prosthetic devices should be required at the Federal level.

Informal inquiry about this recommendation indicates that there are serious questions as to its efficacy and desirability. Doubt has been expressed that this would strike effectively at the truly fraudulent operation. Fears have been voiced that such a program would be so cumbersome that it could impede prompt delivery of new and needed legitimate procedures to those who are ill.

Proposed legislation already introduced to implement this type of program is so broad that no one knows how far it would thrust Federal control into the lives of American citizens and into American businesses which have some, but minor or indirect involvement, in matters of health devices.

These proposals, and the majority recommendation, equate drugs and devices, disregarding essential differences between the two.

Premarket testing inevitably delays delivery of devices to the patient. Delays in use of lifesaving devices, often tailored to individual requirements, might result in death for patients who otherwise might be saved.

Surgical devices, which would be covered by this proposal, afford an example.

That such fears should not be taken lightly is supported by the conclusions of the National Research Council at its May 22–23, 1964, workshop on "Testing and Evaluation of Surgical Devices."

In its as yet unpublished findings, the National Research Council concluded that:

> 1. Surgical devices probably cannot be considered for regulation in the same way as drugs can, since frequently they are tailored to the requirements of individual patients.

2. Surgery is still an art, though it is based on scientific principles. Therefore, each application of a device becomes a test in itself because of the vast number of variables involved, variables not only of source but of the user and the patient-consumer.

3. There is no adequate test animal which can be substituted for man in many areas, since mechanics and time factors are not always comparable between two different species.

4. It may be practical to set surgical device specifications for raw materials and fabrication from groups such as the F–4 Committee of ASTM. Great care must be exercised when specifications are extended beyond this point, however, since the surgeon is the best qualified individual to set standards in a given clinical application.

This reaction from such a distinguished scientific group clearly indicates the desirability of at least exploring alternatives to and modifications in the majority recommendation. Possibilities include legislation aimed at requiring:

(1) Registration of all manufacturers of devices.

(2) Manufacturers of devices to furnish annual catalogs of devices they market to the Food and Drug Administration, plus periodic notification of new devices.

(3) Development of specifications as to ingredients for use in broad classes of devices.

It should be reiterated that in singling out this one majority recommendation we are not limiting our appeal for comprehensive study to it alone. Other majority recommendations require equally careful review.

It should be further reiterated that, in the limited time available to it, the subcommittee could not possibly have entertained all opinions in these areas, or assessed all the facts. That it has assembled so much data is a tribute to its industry.

The fact remains, however, that all of the majority recommendations and findings should be given the benefit of further study.

There is no controversy regarding our national determination to war on quackery and frauds. There may be, indeed is, controversy regarding specifics as to how that inevitably long war should best be carried out.

Further use of all expert opinion, including those who differ, should be made.

We, therefore, recommend that this subcommittee or other appropriate committee of the Senate, should undertake comprehensive hearings on all of thse specific proposals. Effective measures may thus be perfected to meet the real needs we all recognize.

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