UNITED STATES DISTRICT COURT FOR
THE SOUTHERN DISTRICT OF NEW YORK

FEDERAL TRADE COMMISSION, Plaintiff, v. BLUEHIPPO FUNDING, LLC, and BLUEHIPPO CAPITAL, LLC, Defendants.	Civil No. 08 CV 1819 (PAC)

PLAINTIFF'S MEMORANDUM IN SUPPORT OF ITS MOTION FOR ORDER TO SHOW CAUSE WHY CONTEMPT DEFENDANTS BLUEHIPPO FUNDING, LLC, BLUEHIPPO CAPITAL, LLC AND JOSEPH RENSIN SHOULD NOT BE HELD IN CONTEMPT FOR VIOLATING THE FINAL JUDGMENT AND ORDER OF PERMANENT INJUNCTION

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I. INTRODUCTION

Declaring "BlueHippo to the Rescue," defendants BlueHippo Funding, LLC, BlueHippo Capital, LLC (collectively, "BlueHippo") and their owner Joseph K. Rensin (together with BlueHippo, "Contempt Defendants") aggressively market BlueHippo as a company in the business of financing computers to credit-challenged consumers. In reality, BlueHippo is in no such business. In fact, in the year following entry of this Court's Stipulated Final Judgment and Order for a Permanent Injunction ("Order"), BlueHippo financed – at most – a single computer to the over 35,000 consumers who had contracted with BlueHippo in time to receive computers by year's end. Ironically, while BlueHippo failed to finance computers for these duped consumers – those same consumers financed BlueHippo with more than $15 million in payments. Contempt Defendants' not only lie about the nature of BlueHippo's business, but also about when and whether consumers would receive merchandise once consumers meet all of their onerous conditions.

Moreover, adding insult to injury, consumers desperate to get out of Contempt Defendants' money pit find that Blue Hippo's "store credit" refund policy contains onerous conditions that were not disclosed when they placed their orders. Contempt Defendant's failure to disclose these conditions to any of the company's more than 61,000 post-Order customers, who in total paid BlueHippo more than $21 million, also violates the Order. Finally, as in the underlying case, Contempt Defendants have again unlawfully conditioned the extension of credit on mandatory preauthorized transfers, which also violates the Order. *See* FTC 20 at Sections I and IV.[1]

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[1] The evidentiary documents referenced herein are attached as FTC Consolidated Exhibits in Support of Motion for Order to Show Cause and Motion to Modify and identified by

As a result of Contempt Defendants' contumacious actions, the Federal Trade Commission ("FTC") seeks civil contempt sanctions, including compensatory relief for consumers who have been harmed by their misrepresentations and failures to disclose. In addition, the Commission is concurrently filing a separate motion, pursuant to Federal Rule of Civil Procedure 60(b), to ban BlueHippo from offering financing in connection with the sale of goods or services, from selling consumer electronics products, and imposing stricter refund requirements, because the company has demonstrated that it simply cannot conduct such activities in a lawful manner.[2]

II. THE COMMISSION'S PRIOR ACTIONS AGAINST BLUEHIPPO

A. The Complaint Action

In its complaint that led to entry of the Order, the Commission alleged that BlueHippo violated Section 5 of the Federal Trade Commission Act ("FTC Act"), 15 U.S.C. § 45, by falsely representing that it would ship computers and other products to consumers within promised times and by failing to disclose to consumers that their installment payments were non-refundable. The Commission also alleged that BlueHippo violated the Mail Order Rule, 16 C.F.R. Part 435; the Truth in Lending Act ("TILA"), 15 U.S.C. §§ 1601-1666j; and the Electronic Fund Transfer Act ("EFTA"), 15 U.S.C. §§ 1693-1693r.

Exhibit Number FTC ___.

[2] *See generally* Plaintiff's Motion to Modify the Final Judgment and Order of Permanent Injunction. The FTC seeks modification of the Final Order pursuant to Rule 60(b) only as to BlueHippo, because Rensin was not named as a defendant in the underlying action. However, as discussed below, although not an original defendant, Rensin is subject to contempt sanctions because he had notice of the Final Order and acted in active concert and participation with BlueHippo. *See* Fed. R. Civ. P. 65(d).

B. The Compliance Monitoring Contempt Actions

BlueHippo repeatedly violated the compliance monitoring provisions of the Order. First, BlueHippo failed to provide a compliance report "setting forth in detail the manner and form in which Defendants have complied and are complying with [the] Order" as required under Section X.[4] Originally due in October 2008, by April 9, 2009, BlueHippo still had failed to provide this required report, despite the FTC's repeated requests and BlueHippo's repeated assurances that it would do so. Second, BlueHippo failed to produce information or produced inadequate responses to requests issued by the FTC on January 29, 2009 and failed to respond to written demands for reports and documents issued by the FTC on March 9, 2009. Accordingly, on April 9, 2009, the FTC filed a motion to show cause why BlueHippo should not be held in contempt for failing to provide the required information. *See* Motion to Show Cause (Docket No. 3).

On April 16, 2009, this Court found BlueHippo in contempt and ordered the company to produce a compliance report and to produce certain documents. *See* FTC 24. Specifically, the Court ordered BlueHippo to pay $2,500 per day until it provided a compliance report. *Id.* at 2, ¶ B. BlueHippo provided the report five days later resulting in a total sanction of $12,500. The Court imposed an additional daily sanction of $5,000 per day commencing May 1, 2009 for BlueHippo's continued failure to provide responsive information to the FTC's requests. *Id.* at 2, ¶ C. The Court fined BlueHippo $20,000 before it provided sufficient information to convince the court to lift the sanction.

By late June 2009, BlueHippo still had failed to provide certain information dating back to the FTC's January and March requests, and also failed to provide any information in response

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[4] BlueHippo also had failed to verify the accuracy of the consumer database it was required to produce to the Commission so that redress could be effectuated.

to a request issued on May 29, 2009. As a result, on June 23, 2009, the FTC brought a second contempt action. The Court once again found that BlueHippo's failures were unjustified and ordered BlueHippo to produce additional information or face further coercive sanctions. FTC 25 at 2, ¶ D.

III. PARTIES TO THE CURRENT ACTION: CONTEMPT DEFENDANTS

A. BlueHippo Capital, LLC and BlueHippo Funding, LLC

Contempt Defendant BlueHippo Capital, LLC is a Virginia corporation wholly owned by Contempt Defendant BlueHippo Funding, LLC. *See* FTC 26. Contempt Defendant BlueHippo Funding, LLC is a Maryland corporation wholly owned by Contempt Defendant Joseph K. Rensin. *See id.* The BlueHippo companies are located in Baltimore, Maryland and market computers and other electronics to consumers Funding[(broufasted ogrow is8.7(ers)]2J1 finan foputers2ies 4re l

IV. CONTEMPT DEFENDANTS' VIOLATIVE BUSINESS PRACTICES

Contempt Defendants aggressively advertise BlueHippo as a company in the business of financing computers for credit-challenged consumers. However, this representation is patently false. Indeed, in the year following entry of the Order, Contempt Defendants financed – at most – only one computer[5] for more than 35,000 customers.[6] Contempt Defendants only began to provide financed computers to some of its customers after the FTC intensified its scrutiny of BlueHippo by bringing its first contempt action. Contempt Defendants compound the harm caused by BlueHippo's failure to finance computers by failing to disclose fully the onerous conditions of its store credit refund policy, thereby rigging their refund policy to avoid giving anything back to consumers lured into BlueHippo's money pit.

A. Contempt Defendants Aggressively Market BlueHippo as a Company That Is in the Business of Financing Computers.

Contempt Defendants repeatedly and aggressively tout BlueHippo as a company in the business of "financing" computers. To that end, they widely disseminate advertisements, including in major metropolitan newspapers, on television, on the internet, and through direct mail, emphasizing that what they do is finance computers for credit-challenged consumers:

C "BlueHippo finances thousands of computers to people with past credit

[5] As noted below, BlueHippo appears to have erred when it shipped this single customer a computer. *See* fn.16, *infra*.

[6] All figures cited in this Memorandum are derived from BlueHippo's responses to FTC Requests for Information 3, 6, and 18, as summarized in the Fed. R. Evid. 1006 summary prepared by Erez Yoeli, Ph.D. *See* FTC 21. The correspondence between the FTC and BlueHippo relating to these requests for information and associated responses are provided as FTC 22A - 22G.

[7] The cited advertisements are intended as examples of the violative advertisements disseminated by Contempt Defendants during the period between April 10, 2008 and December 10, 2008 and are not intended to be a complete index of those advertisements. BlueHippo advertisements that ran during this time period and that make representations concerning BlueHippo's financing program have been attached at FTC 29-37.

[8] As stated, BlueHippo does not actually manufacture the computers its customers order, nor does it maintain an inventory of computers; instead, in those rare instances in which it

BlueHippo's advertising, including its website, provides toll-free telephone numbers for interested consumers to call. When they do, BlueHippo telemarketers read from scripts touting their business providing financed computers to consumers:

- "But, after only 13 consecutive layaway payments, we can finance your balance and ship your computer directly to your home." FTC 40 at FTC041309/BH00009;

- "Now, because we don't check your credit, all we ask is that you build a short credit history with us by making a small down payment ... and then pay just 9 short weeks worth of layaway payments. Then we finance, order and ship your computer directly to your home." FTC 39 at FTC021209/BH00005;[9]

- "After you've paid your initial payment and a minimum of 13 consecutive layaway payments, we will send you an offer to finance your balance." FTC 40 at FTC041309/BH00029; *see also* FTC 39 at FTC021209/BH00026 (offering financing after 9 consecutive payments).

In addition, during these calls, Contempt Defendants' telemarketers explain to consumers the steps they must take to obtain a computer. Specifically, consumers must pay an activation fee (generally $99) and then make weekly payments of approximately $35 or bi-weekly payments of approximately $70 for a year.[10] *See, e.g.*, FTC 39 at FTC021209/BH00007; *id.* at FTC021209/BH00025; FTC 40 at FTC041309/BH00009; *id.* at FTC041309/BH00028. However, telemarketers emphasize that if a consumer makes thirteen consecutive payments and completes and returns a financing agreement and other paperwork, Contempt Defendants will

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Dell.

[9] The minimum number of consecutive payments Contempt Defendants require to qualify for financing varies based on the promotion BlueHippo is running at the time, but generally ranges from 9 to 13 consecutive payments.

[10] The amount of consumers' payments and the number of payments required varies depending upon Contempt Defendants' promotions and the particular products selected by consumers. Pursuant to these payment arrangements, the few consumers who manage to pay in full, on average, pay BlueHippo over $1,950.00 per computer. *See* FTC 21 at ¶ 21.

the Order.

To determine how many computers Contempt Defendants actually financed in the year following entry of the Order,[13] the FTC considered the 36,090 computer orders consumers placed during the eight-month period between April 10, 2008 (the day after entry of the Order) and December 10, 2008. The FTC considered the computer orders during this eight-month period, rather than throughout the entire year, to ensure that BlueHippo could have financed each order within a year (*i.e.*, by April 8, 2009), pursuant to its financing criteria, taking into account the maximum 17 weeks (a maximum of 13 weeks of consecutive payments plus 4 weeks for shipping and handling) that BlueHippo required to provide a financed computer.[14]

During the period, 35,698 consumers, having been told that BlueHippo is in the business of financing computers, ordered 36,090 computers from Contempt Defendants. *See* FTC 21 at 20.[15] However, Contempt Defendants financed at most a single computer[16] out of these 36,090

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[13] This one-year period was not chosen randomly. Rather it coincides almost exactly with the filing of the FTC's first contempt motion on April 9, 2009. As discussed further below, this contempt action, along with subsequent FTC enforcement inquiries, spurred BlueHippo to break with its normal post-Order business practices and finally finance some computers for consumers in June 2009.

[14] In other words, in order to receive a financed computer within a year after entry of the Order, a consumer would have to order no later than December 10, 2008.

[15] It appears that 392 of these customers placed more than one computer order with BlueHippo. FTC 21 at ¶ 20.

[16] The shipment of this computer was most likely in error, rather than a computer that BlueHippo intended to finance. The consumer (whose scheduled bi-weekly payments were $61.32) only paid $185.32 towards a computer with a total sale price of $2,515.00 and never entered into a financing agreement. *See* FTC 21 at ¶ 27.

orders.[17] *Id.* at ¶ 27. Incredibly, Contempt Defendants received *at least* $15,182,479.64 from consumers for these 36,090 orders. *See* FTC 21 at ¶ 24.[18]

C. After the FTC's First Contempt Action, Contempt Defendants Begin to Ship More Computers.

After the FTC brought its first contempt action on April 9, 2009, Contempt Defendants, in an apparent effort to avoid further law enforcement action, considerably accelerated their shipment of computers to consumers. Between April 9, 2009 and July 24, 2009 (*i.e.*, the last date for which BlueHippo provided data), BlueHippo ordered 4,056 computers for the consumers who ordered during the eight-month period, with a staggering 3,756 orders placed in June and an additional 238 orders placed in July. *Id.* at ¶¶ 29, 31.[19] Significantly, in their rush to get computers out the door quickly, Contempt Defendants disregarded their own qualification criteria. Indeed, out of those 4,056 consumers for whom BlueHippo ordered computers during this spike, 2,594 did not even meet BlueHippo's financing qualification criteria – highlighting that their haphazard, litigation-driven efforts were not truly reflective of their business practices,

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[17] Out of these 36,090 consumer orders, 2,477 qualified for financing on or before March 11, 2009 (the last date for which a consumer could qualify and expect to receive a computer by April 9, 2009). *See* FTC 21 at ¶ 25. The number of orders that qualified was determined by identifying all orders for which consumers made a minimum number of 13 consecutive payments and returned financing contracts. *See* FTC 21 at ¶ 12. While BlueHippo did send computers to 13 out of these 2,477 consumers prior to April 9, 2009, it did so only after the consumers had paid for the computers in full. FTC 21 at ¶ 26. Thus, these 13 computers were not financed.

[18] These consumers may have paid BlueHippo as much as $3.5 million more, depending on whether the payment data provided by the company included for each of its customers the required "activation fee" of approximately $100.

[19] Astoundingly, Contempt Defendants ordered the vast majority of these computers from vendors during a 7-day period. Indeed, between June 16, 2009 and June 23, 2009, Contempt Defendants ordered 3,311 (over 81%) of the 4,056 computers it ordered during the entire spike. FTC 21 at ¶¶ 31-32.

[20] Moreover, Contempt Defendants' litigation-driven ordering spike demonstrates that20

[21] In total these consumers paid BlueHippo at least $21 million. FTC 21 at ¶ 16

[22] BlueHippo neither manufactures nor inventories the products it offers through the on-line store; rather, as with the computers it offers, it orders these products from third-parties. *See* FTC 22F at 6-7 and fn. 10, *supra*.

[23] It is ironic that consumers lured into paying BlueHippo on average more than $1950

actually paid the previously undisclosed, additional costs for shipping, handing, and taxes. However, BlueHippo ordered merchandise for only 750 of these consumers.[25] *Id.* at ¶ 43. Therefore, BlueHippo failed to provide merchandise to 2,704 (approximately 75%) of the consumers who met its burdensome, undisclosed store credit requirements. *Id.* at ¶ 44. Needless

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[25] BlueHippo has refused to provide us confirmation of shipment for these 750 orders, claiming they do not maintain such records. Thus, we cannot confirm that even these consumers actually received the merchandise they ordered using store credit.

[26] There is no question Contempt Defendants are bound by the Order. As a party to the underlying action, BlueHippo has notice of, and is, therefore, bound by the Order. *See SEC v. Current Fin. Servs., Inc.*, 798 F. Supp. 802, 806 n.11 (D.D.C. 1992). Further, as BlueHippo Funding's owner and former Chief Executive Officer who was involved in the company's day-

(1) that they were in the business of financing computers, (2) that consumers would receive a

consumers – accounting for essentially zero percent of its substantial revenues – is not in the business of financing that product.

In other contexts, courts have found that where a company engages in an activity infrequently, accounting for an insubstantial portion of its total revenues, it is not "in the business of" that activity. *See, e.g., Bramblett v. Commissioner of Internal Revenue*, 960 F.2d 526 (5th Cir. 1992) (finding that entity was not "in the business of" selling land even though it made five sales of land in three years, netting over $7 million, because these sales were infrequent and insubstantial); *Byram v. United States*, 705 F.2d 1418 (5th Cir. 1983) (affirming district court finding that even when entity made 22 sales over three years, resulting in profits of $3.4 million, company was not in the business of selling land). Here, of course, because Contempt Defendants have financed computers for virtually none of their 35,698 customers, they have not financed computers on even an "infrequent" or "insubstantial" basis. Thus, contrary to their representations to consumers, for the year after entry of the Order, Contempt Defendants were not in the business of financing computers.[27]

Moreover, this misrepresentation was "material," or "likely to affect a person's choice of, or conduct regarding, goods or services." *See* FTC 20 at 3 (definition of "Material"). Put another way, if consumers knew that Contempt Defendants were lying when they said that they

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[27] Contempt Defendants are not saved by their belated efforts to finance computers to avoid law enforcement action. Indeed, courts have found that defendants' claims "of abandonment [are] rarely sustainable as a defense to a Commission complaint where, as here, the alleged discontinuance occurred '*only after the Commission's hand was on the respondent's shoulder*.'" *International Assoc. Of Conf. Interpreters*, 123 F.T.C. 465, 658 (1997), *quoting Zale Corp.*, 78 F.T.C. 1195, 1240 (1971) (emphasis added); *see also FTC v. Sage Seminars, Inc.*, 1995 WL 798938, *6 (N.D. Cal. Nov. 2, 1995) (where violative conduct ceases "after defendants learn that the FTC [has] commenced an investigation . . . cessation can hardly be considered 'voluntary'") (internal citations omitted) (attached).

action shipping spike, however, BlueHippo failed to order – let alone ship – the computers within the promised three to four weeks. In total, more than 1,400 consumers placed orders for computers with BlueHippo between the date of entry of the Order and December 10, 2008; met BlueHippo's financing conditions; and received a computer by July 24, 2009. FTC 21 at ¶ 34. *None* of those consumers, however, received their computer within the promised time frame. *Id.* at ¶ 35. Instead, they waited for their computers, on average, more than 26 weeks, or *six and a half months*, after qualifying. *Id.* at ¶ 37. Of course, BlueHippo also has violated this provision with respect to the additional 1,015 who met the conditions for financing during the period and still have not received a computer.

d. Contempt Defendants Misrepresent That Consumers Who Meet Certain Conditions to Use Store Credit Will Receive Merchandise.

Contempt Defendants also misrepresent that consumers that meet the onerous conditions precedent to using "store credit" to purchase merchandise at BlueHippo.com will actually receive that merchandise. Despite the burdensome nature of these conditions, since entry of the Order, 3,454 consumers qualified to buy merchandise using store credit. FTC 21 at ¶ 41. Yet, BlueHippo only ordered merchandise for 750 of these consumers, leaving 2,704 consumers without their merchandise. *Id.* at ¶ 43.

2. Contempt Defendants Fail to Disclose Three Material Conditions of Their Store Credit "Refund" Policy.

Section I.B of the Order expressly prohibits BlueHippo from making any representations about their "refund, cancellation, exchange or repurchase policy without disclosing clearly and conspicuously, prior to receiving any payment from customers[,] all material terms and conditions" of such policy. While Contempt Defendants' telemarketing sales scripts disclose that they offer "store credit" in lieu of cash refunds, they fail to disclose several material terms and conditions of their refund policy prior to receiving payment. Specifically, they fail to disclose that: 1) consumers may not apply their store credit to shipping, handling, and taxes; 2) consumers have to send in money orders to pay for these additional charges before BlueHippo will order their merchandise; and 3) consumers may only redeem their store credit for one item at a time and have to wait for the first item to be delivered before ordering a second.

As described above, the practical effect of Contempt Defendants' lack of disclosure is that consumers who have already been victimized by Contempt Defendants' misrepresentations concerning the nature of BlueHippo's business are required to give BlueHippo even more money before they can recover anything. Requiring consumers to advance additional money to Blue Hippo in the hope of getting *something* for the hundreds of dollars already paid certainly calls for a leap of faith from already-victimized consumers, especially when these conditions are only disclosed at the time consumers seek to redeem their store credit. Contempt Defendants intentionally compound consumers' Hobson's choice by forcing them to repeat the process for each item ordered in an obvious effort to rig the refund process in their favor. These are exactly the type of "material terms and conditions" concerning BlueHippo's refund policy that, as required by the Order, consumers should have been informed of *before* they started throwing their money down the drain.

3. Contempt Defendants Violate Section IV of the Order by Conditioning Credit on Mandatory Preauthorized Electronic Transfers.

Section IV of the Order prohibits "conditioning the extension of credit on mandatory preauthorized transfers, in violation of the EFTA and its implementing Regulation E." Under EFTA, "credit" is defined as the right "to incur debt and defer its payment." 12 C.F.R.

§ 205.2(f) (definitions applicable to Regulation E). Here, Contempt Defendants extend "credit" to consumers by offering to provide computers after only thirteen weeks of payments and "defer" payment of the balance. Further, EFTA defines "preauthorized electronic transfers" as "electronic fund transfer[s] authorized in advance to recur at substantially regular intervals." *Id.* at § 205.2(k). Contempt Defendants offer of credit is conditioned on mandatory "preauthorized electronic transfers" because their financing contracts require consumers to agree to weekly or bi-weekly electronic debit entries from consumers' checking accounts. Thus, Contempt Defendants' financing contracts extend credit conditioned on mandatory preauthorized transfers in violation of Section IV.

B. Contempt Defendants Have Not Diligently Attempted to Comply with the Order.

Contempt Defendants' misrepresentations and failures to disclose evidence affirmative misconduct and, thus, are wholly inconsistent with any attempt to comply diligently with the Order. *See Paramedics Electromedicina Comercial, Ltd.*, 369 F.3d at 655. Here, Contempt Defendants violate the core conduct provisions of the Order, by – first and foremost – misrepresenting what they do (*i.e.*

compliance where defendants persisted in unlawful conduct despite availability of lawful alternatives).

C. Contempt Defendants Should Pay Contempt Sanctions.

Courts may impose sanctions for civil contempt "either to coerce the contemnor into future compliance with the court's order or to compensate the complainant for losses resulting from the contemnor's past noncompliance." *Terry*, 886 F.2d at 1352-53 (citing *United States v. United Mine Workers*, 330 U.S. 258, 303-04 (1946)). In a civil contempt action, "[t]he measure of the court's power . . . is determined by the requirements of full remedial relief." *McComb v. Jacksonville Paper Co.*

BlueHippo not misrepresented the nature of its business in widespread nationwide advertising, these consumers would not have paid hundreds, if not thousands of dollars to BlueHippo. *See McGregor v. Chierico,* 206 F.3d 1378, 1388 (11th Cir. 2000) (widespread misrepresentations in violation of a court order create presumption that all customers relied on the misrepresentations); *FTC v. Trudeau*, 579 F.2d 754, 773, fn.15 (7th Cir. 2009).[28]

Second, all consumers who have placed orders with BlueHippo since entry of the Order have been harmed by Contempt Defendants' failure to disclose fully the onerous terms and conditions of the refund policy. Since entry of the Order at least 61,878 consumers placed orders with BlueHippo with the understanding that if they chose to cancel those orders they would be able to obtain merchandise using store credit, and paid over $21 million in the process. In violation of the Order, these consumers were not told of material, onerous conditions associated with receiving any kind of refund. Again, if consumers were aware that BlueHippo's store credit refund policy was rigged against them, they would not have ordered anything from BlueHippo. *See McGregor,* 206 F.3d at 1388; *Trudeau*, 579 F.2d at 773, n.15. As a result, all consumers who did not receive computers or store credit merchandise from BlueHippo should receive full refunds.[29]

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[28] Of course, the 1,015 consumers who failed to receive computers even after qualifying for financing would be included within this category of consumers.

[29] These consumers would include the 2,704 consumers who met the conditions to receive merchandise purchased using store credit but failed to receive their ordered products. In addition, the 750 consumers who received merchandise purchased using store credit were injured by Contempt Defendants' undisclosed requirement that those customers could not use their store credit to cover taxes, shipping, and handling, and should receive refunds of the additional monies they paid to BlueHippo to cover those costs.