11-374

IN THE UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

FEDERAL TRADE COMMISSION,
Plaintiff-Appellant

v.

BLUEHIPPO FUNDING, LLC; BLUEHIPPO CAPITAL, LLC;
and JOSEPH K. RENSIN
Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF NEW YORK

REPLY BRIEF FOR APPELLANT FEDERAL TRADE COMMISSION

OF COUNSEL:

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RULES AND REGULATIONS

INTRODUCTION

hundreds or even thousands of dollars, BlueHippo failed to tell them that they would need to pay additional fees to redeem their store credit, and that they could not use any of the money they had already paid BlueHippo to cover these undisclosed fees. Not surprisingly, 89% of BlueHippo's customers never received anything in exchange for the millions of dollars they paid BlueHippo.

The Federal Trade Commission ("FTC" or "Commission") seeks to make whole those customers who were harmed by BlueHippo's contempt. The Commission showed that the appropriate compensatory sanction was $14 million. Nothing in Rensin's brief rebuts that showing.[1]

ARGUMENT

AS A RESULT OF BLUEHIPPO'S CONTEMPT, ITS CUSTOMERS WHO

[1] The relevant district court's decisions were rendered by the Hon. Paul A. Crotty in unreported opinions, *see* Local Rule 28.1(b), and appear in the Special Appendix at (SA.1-12), (SA. 14-16) and in the Appendix at (A.995-1006), (A.1015-17).

Br. at 24-29.[2] This argument misstates the nature of the issues on appeal, and therefore the standard of review.

Civil contempt sanctions are reviewed under an abuse of discretion standard.[3] *FTC v. Kuykendall*, 371 F.3d 745, 763 (10th Cir. 2004); *United States v. Chusid*, 372 F.3d 113, 117 (2d Cir. 2004). Under that standard, issues of fact are reviewed for clear error, but issues of law are reviewed *de novo*. *See Southern New England Tel. Co. v. Global NAPs Inc.*, 624 F.3d 123, 144-45 (2d Cir. 2010).

The issues before this Court are sole

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[2] As explained in the Brief for Appellant Federal Trade Commission ("FTC Br."), although Rensin was not named as a defendant in the Consent Order, the district court properly held him liable for BlueHippo's contumacious conduct. *See* FTC Br. at 15. Rensin, who owned BlueHippo and was its Chief Executive Officer, Rensin Br. at 3, has not challenged this holding.

[3] Rensin argues that the district court should have employed a clear and convincing evidence standard of review with respect to the factual issues related to the appropriate compensatory sanction. Rensin Br. at 25 n.5. This argument has no relevance to the standard of review on appeal.

[4] Rensin provides no support for the proposition that *de novo* review of legal errors is appropriate only where the appellant is the defendant in a civil contempt action and the issue involves whether the sanctions are punitive. *See* Rensin Br. at

compensatory sanction resulting from BlueHippo's civil contempt, the district court made two legal errors. First, it ignored the law establishing a legal presumption of consumer reliance and injury where consumers are deceived by material misrepresentations that are widely disseminated (as BlueHippo's misrepresentations were). *See, e.g., Kuykendall*, 371 F.3d at 765. Second, the court was required by law, but failed, to award a compensatory sanction even after the Commission established that consumers were harmed by BlueHippo's contumacious conduct. *See Vuitton*, 592 F.2d at 130 (once it has been shown that contumacious conduct caused damages, the court must award a compensatory sanction). Thus, cases cited by Rensin applying the clear error standard, *see* Rensin Br. at 25-27, are irrelevant, and the legal issues before the Court should be reviewed *de novo*.[5]

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27. Regardless of which party is the appellant, this Court reviews legal issues *de novo*, including the methodology applied by the district court in assessing contempt sanctions. *See, e.g., Vuitton et Fils, S.A. v. Carousel Handbags*, 592 F.2d 126, 130 (2d Cir. 1979) (on appeal by plaintiff, reviewing award of contempt damages *de novo* and reversing, finding legal error in failure to award compensatory damages in amount proven by plaintiffs).

[5] Even were this Court to review the district court's decision under the clear error standard, it should find such error here. As shown in the FTC's principal brief, the district court based its decision to refuse a compensatory sanction on its mistaken belief that the Commission had "conceded" that it had failed to provide any evidence of consumer injury. D.76 at 10-11 (A.1004-05). But even Rensin

2. BlueHippo's Failure to Disclose was Material – Not "Minor" or "Secondary" – Because It Affected the Decision by Its Customers to Pay Any Money to BlueHippo

BlueHippo enticed consumers with very poor credit to enter into a transaction in which they could purchase a computer, but only if they could fulfill particularly stringent payment requirements. If the consumer failed to make the required payments (which most of them failed to do), the only way they could get anything for the money they paid BlueHippo was to use store credit, *i.e.*, to make a purchase for an item from BlueHippo's store credit online store. Yet, in violation of the Consent Order, BlueHippo failed to disclose to consumers all the terms and conditions that increased the cost of redeeming that store credit.

Indeed, Rensin concedes that BlueHippo's failure to disclose critical information about its store credit policy was "material" to consumers' decisions to enter into a contract with BlueHippo. Rensin Br. at 29. Paradoxically, however, he asserts that these material conditions were of "minor" or "secondary"

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admits that there was no such concession by the Commission regarding the failure to disclose claim. *See* Rensin Br. at 54-55. Further, Rensin admits that BlueHippo's failure to disclose was material, Rensin Br. at 29, and such a material omission affected consumers' decisions to enter into the transaction in the first place. The court thus committed clear error in refusing to recognize record evidence of consumer harm, which, as shown below, Rensin failed to rebut.

importance to consumers. *Id.*[6] However, as the district court correctly recognized, "materiality" is defined under both the Consent Order and case law as "likely to affect a person's choice of, or conduct regarding, goods or services." *See* D.76 at 6 (A.1000); D.2 at 3 (A.35); *FTC v. Cyberspace.com, LLC*, 453 F.3d 1196, 1201 (9th Cir. 2006); *Kraft, Inc. v. FTC*, 970 F.2d 311, 322 (7th Cir. 1992); *FTC v. Five-Star Auto Club, Inc.*, 97 F. Supp. 2d 502, 529 (S.D.N.Y. 2000). Disclosures that affect a consumer's decision to purchase goods or services are not "minor" or "secondary."

The district court specifically held that BlueHippo violated the Consent Order by failing to disclose three material conditions of its store credit refund

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[6] Rensin also claims that BlueHippo's failure to disclose the terms of its store credit policy was only a secondary part of the Commission's case. *See* Rensin Br. at 29-32. In fact, however, BlueHippo's failure to disclose has been central to the Commission's contempt allegations from the beginning of these proceedings. The claim was referenced throughout its legal brief in support of the contempt motion (D.43 at 1, 13-15, 20-21, 24), in its reply brief (D.57 at 6-7, 10), and in its expert's declaration (Def. Ex. NN ¶¶ 2-5) (A.698) (quantifying damages). Indeed, the Commission highlighted the failure to disclose claim in the very beginning of the legal brief supporting the contempt motion: "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." D.43 at 1.

[7] More specifically, the court found that BlueHippo failed to disclose that: (1) consumers would need to pay additional amounts for shipping and handling fees and taxes before they could receive any store credit merchandise; (2) money already paid did not cover these additional expenses (*i.e.*, consumers would have to pay those amounts by cash, check or money order); and (3) consumers could order only one item at a time and would have to pay these additional expenses for each item ordered using their store credit (the

customers could obtain any benefit for the payments they made to BlueHippo, it was crucial that BlueHippo disclose all the material terms of its store credit policy before the customer paid anything. Further, this is what the Consent Order required. D.2 at 4 (A.36).

F.2d 595, 605-06 (9th Cir. 1993); *FTC v. Security Rare Coin*, 931 F.2d 1312, 1316 (8th Cir. 1991); *see also FTC v. Bronson Partners, LLC.*, No. 10-0878-cv, 2011 WL 3629718 at *6 (2d Cir. Aug. 19, 2011).

Once the FTC establishes reliance, and, hence, injury, it need only demonstrate a "reasonable approximation" of damages. *See FTC v. Verity Int'l, Ltd.*, 443 F.3d 48, 67 (2d Cir. 2006); *Trudeau*, 579 F.3d at 772-73; *Kuykendall*, 371 F.3d at 764; *New York State Nat'l Org. for Women v. Terry*, 886 F.2d 1339, 1353-54 (2d Cir. 1989). In this context, the FTC meets this burden by showing defendants' gross receipts. *Bronson Partners*, 2011 WL 3629718 at *6 (the baseline for calculating a defendant's unjust gains equaled its gross sales generated through widely disseminated deceptive advertising); *Kuykendall*, 371 F.3d at 764-66; *McGregor*, 206 F.3d at 1387-88; *Figgie* 994 F.2d at 605-06. The burden then shifts to the defendant to show that the FTC's calculation is inaccurate. *Bronson Partners*, 2011 WL 3629718 at *6; *Verity*, 443 F.3d at 67; *Kuykendall*, 371 F.3d at 766; *FTC v. Febre*, 128 F.3d 530, 535 (7th Cir. 1999).[11] Contrary to

[11] Rensin's assertion that without a liquidated damages provision in the Consent Order no damages are cognizable, *see* Rensin Br. at 39-41, ignores that district courts have the inherent authority to award civil contempt sanctions to fully compensate an injured party. *See, e.g.*, *McComb v. Jacksonville Paper Co.*, 336 U.S. 187, 193 (1949); *Kuykendall*, 371 F.3d at 765.

[12] Although Rensin acknowledges that this Court's decision in *Verity* did not discuss the presumption of reliance, he suggests that *Verity* somehow bars the

precedent involving the FTC Act or contempt proceedings barring or even limiting the FTC from applying the presumption of reliance to meet its burden of showing consumer injury.

Instead, Rensin asserts that, even if it is presumed that consumers relied on BlueHippo's failure to disclose the terms of its store credit refund policy, the Commission must additionally show that consumers were injured as a result of that reliance. Rensin Br. at 46-51. This argument fails. Indeed, in every FTC case cited by Rensin that addressed the issue, Rensin Br. at 48-49, the court held that where the deception or omission was material and widespread, the presumption of reliance applied, and the amount that consumers paid, *i.e.*, the defendant's gross receipts (less any refunds), constituted the consumer injury. *See, e.g.*, *Kuykendall*, 371 F.3d at 764, 766; *McGregor*, 206 F.3d at 1387-88; *Figgie*, 994 F.2d at 605-06. Those courts logically determined that every consumers' decision to purchase the product was tainted by defendants' material deception or omission. The consumer injury – the purchase of the product without complete and accurate information – automatically follows from the reliance. In such cases, consumers to whom defendants made material deceptive statements are entitled to full refunds. *See, e.g.*, *McGregor*, 206 F.3d at 1388-89 (all payments should be returned to customers even if they received a useful product, because "the seller's

misrepresentations tainted the consumer's purchasing decisions."); *Figgie*, 994 F.2d at 606 ("The fraud in the selling, not the value of the thing sold, is what entitles consumers in this case to full refunds or to refunds for each [product] that is not useful to them.").

Here, the district court found that, when BlueHippo sold computers, it failed to disclose material terms of its store credit policy to each and every customer. D.76 at 8 (A.1002). Thus, as in *Figgie* and *McGregor*, the appropriate measure of relief is a full refund (*i.e.*, the total amount paid by consumers). Rensin simply ignores the direct nature of the consumer injury here: since BlueHippo's failure to disclose the material terms of its store credit policy tainted the purchasing decision of every person who entered into a transaction with BlueHippo, consumer loss is equal to the full amount paid by every customer who received nothing in return.

Rensin also argues that *Figgie* requires proof that the false statements "actually caused the homeowner to purchase an unwanted product" – in other words, that *Figgie* requires a showing of individual reliance. *See* Rensin Br. at 47-48. Rensin has misread *Figgie*. In fact, *Figgie* held that "proof of individual reliance by each purchasing customer is not needed." 994 F.2d at 605; *see also Trudeau*, 579 F.3d at 773 n.15 (in calculating injury "the FTC is not required to prove individual consumer dissatisfaction because 'it would be virtually impossible

for the FTC to offer such proof, and to require it would thwart and frustrate the public purposes of FTC action'") (citations omitted); *Kuykendall*, 371 F.3d at 765 (no need to provide individual consumer injury in contempt, and holding that "[i]n cases of pervasive, persistent contempt, the use of gross receipts simply allows courts to assure those injured receive full compensation").

Rensin relies instead on *Figgie*'s response to a speculative argument: even though Figgie used deception to sell heat detectors, thereby entitling consumers to full refunds, there might be some consumers who, even after learning that their heat detectors were not as effective as smoke detectors, might nonetheless want to

reliance discussed in private securities law cases. Rensin Br. at 46-47. In those cases, private plaintiffs were required to prove "loss causation" as an element of a violation of the antifraud provisions of Section 10(b) of the Securities and Exchange Act, *i.e.*, that each plaintiff suffered economic loss as a result of a material misrepresentation or omission made in connection with the purchase or sale of a security. *See, e.g., Erica P. John Fund, Inc. v. Halliburton Co.*, 131 S.Ct. 2179, 2185 (2011) (noting "elements in a private securities fraud claim"). Private plaintiffs are required to prove reliance and loss causation to ensure that they have standing to enforce the securities antifraud laws. *SEC v. Rana Research, Inc.*, 8 F.3d 1358, 1364 (9th Cir. 1993). Rensin, however, ignores that in public law enforcement actions brought by the SEC to enforce Section 10(b) – the parallel to an FTC action to enforce the FTC Act – the government is not required to prove either investor reliance on a misrepresentation or "loss causation." *See, e.g., Rana Research*, 8 F.3d at 1363-64; *SEC v. North Am. Research & Dev. Corp.*, 424 F.2d 63, 84 (2d Cir. 1970); *SEC v. Credit Bancorp, Ltd.*, 195 F. Supp. 2d 475, 490-91 (S.D.N.Y. 2002).[13] Thus, cases involving private rights of action under the

[13] In such cases, the SEC may still obtain disgorgement of illegally obtained profits where it proves a securities law violation. *SEC v. Hasho*, 784 F. Supp. 1059, 1111 (S.D.N.Y. 1992).

[14] Rensin's effort to disconnect BlueHippo's store credit refund policy from the computers it sold is particularly hypocritical given the prominence with which

Resin has never disclosed those fees.

[18] The accuracy and completeness of

orders would have been identical. But Rensin provided no direct evidence of the amounts BlueHippo actually charged its customers. Nor does he provide any explanation of the circumstances under which BlueHippo would forgo charges for shipping, handling, or taxes.[19] Indeed, the only testimony regarding the extract from the spreadsheet on which Rensin bases this argument was that of the FTC's expert, Dr. Erez Yoeli, who disagreed that the existence of some items with an identical "total price" necessarily demonstrated that shipping, handling, and taxes were not charged for those items. *See* 02/09/10 Tr. (D.73) at 143-44, 150 (A.171, 173); 02/11/10 Tr. (D.74) at 180-187 (A.180-81).

In any event, the mere fact that 91 customers (or any group of customers) out of the more than 8,000 consumers who placed store credit orders may have been able to avoid charges for shipping, handling, and taxes does not advance Rensin's cause, *see* Rensin Br. at 15-17, because it does not show that BlueHippo either had or disclosed any relevant policy as to who could escape such charges.

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[19] Indeed, there are several reasons that explain why these consumers may have been charged the same total price and which included taxes, shipping and handling charges. First, these 91 consumers may have lived in the same state (or in states with identical sales tax rates). *See* 02/09/10 Tr. (D.74) at 143-44 (A.171) (FTC expert pointing out that no information about consumers' location is provided in data). Second, BlueHippo may have charged a flat fee for shipping and handling, as opposed to actual shipping rates. By not providing any evidence relating to the geographic location of the store credit consumers or the manner in which BlueHippo charged for shipping and handling, Rensin fails to prove that his preferred explanation – that no taxes, shipping and handling were charged – is true.

Perhaps under some conditions BlueHippo allowed some customers to escape those charges. But if there were such conditions, BlueHippo's failure to disclose them would also have clearly violated the Consent Order.[20] And, although BlueHippo's contumacious conduct may not have harmed the 91 customers who may not have paid the extra charges, this does not help all the others who were not so lucky.

Rensin's second attempt to show that the FTC's figures are inaccurate fares no better than his first. He argues that, if a customer never tried to take advantage

[20] The *only* record evidence reflecting BlueHippo's policy regarding store credit was a response by its counsel that "[s]tore credit cannot be used for taxes or shipping and handling (store credit amount is principal paid, so store credits can only be used for principal)." *See* FTC 22F at 6 (A.335). While Rensin tries to dismiss these admissions as statements of counsel and in some way inaccurate or incomplete, s*ee* Rensin Br. at 14-15, the statement was made in response to a request made by the FTC pursuant to the Consent Order that required complete and accurate responses under penalty of perjury. *See* D.2 at 17 (A.49). If any qualifications or exceptions existed to charging such taxes and fees, they should have been included in the company's response.

wanted to redeem their store credit, but were not able to do so as a result of the additional payments that were required. There is no basis for Rensin's conclusion that the consumers who actually placed orders using their store credit were the only consumers that wanted or tried to use the credit. Rensin Br. at 18, 53. Indeed, customers who were interested in redeeming their store credit would have logged in and, for the first time, learned about the added costs of using store credit. Presumably, many of these consumers would have been dissuaded from placing an order. *See* FTC Ex.22F at 6 (A.335). Rensin tries to blame the Commission for the weakness of his evidence in support of this argument. *See* Rensin Br. at 18. However, because Rensin is the party trying to rebut the presumption of reliance, it is *his* burden – not the FTC's – to come forward with such evidence. *Kuykendall*, 371 F.3d at 766; *Trudeau*, 579 F.3d at 773. In addition, at this stage, the risk of any uncertainty falls on the wrongdoer, BlueHippo, not on the FTC. *Verity*

[21] Rensin argues that the FTC's evidence to support its contempt claims changed during the hearing below. *See, e.g.*, Rensin Br. at 12 n.3, 30. In fact, to the extent that any figures changed, those figures related only to the business of financing claim, which is not at issue in this appeal.

FTC's showing regarding the appropriate compensatory sanction because it focuses solely on post-purchase conduct. As explained above, BlueHippo's customers were harmed when they made payments to BlueHippo without receiving disclosures required by the Consent Order. The Consent Order prohibited BlueHippo from "[m]aking any representation about any refund * * * policy without disclosing clearly and conspicuously, ***prior to receiving any payment from customers*** all material terms and conditions of any refund * * * policy." D.2 at 4 (A.36) (emphasis added). This express language, consistent with FTC case law, recognizes that when, as here, consumers do not receive material cost information when deciding whether to pay for goods or services, they are injured *at the point of purchase*. *See, e.g.*, *McGregor*, 206 F.3d at 1387-88; *Figgie*, 994 F.2d at 606.

The gist of Rensin's second argument is that, because BlueHippo failed to make disclosures regarding its store credit policy, no consumer was injured unless that consumer actually attempted to seek store credit. *See* Rensin Br. at 41. But this would be like arguing in *Figgie* (where defendants made misrepresentations regarding the ability of its heat detectors to warn of house fires) that the only consumers who would be entitled to monetary relief were those whose houses burned down. But *Figgie* made clear that *all* the defendant's customers were injured at the point of purchase based on the deception and were entitled to full

refunds. 994 F.2d at 606. The mere fact that some customers may not have availed themselves of BlueHippo's store credit policy (assuming that Rensin had produced any adequate evidence as to the number of such consumers) in no way shows that these consumers were not deceived when they first agreed to make payments to BlueHippo. It is that deception that is the source of BlueHippo's contempt, and it is that deception that sets the measure of the compensatory sanction that it should pay.

Finally, what is equally telling is that Rensin failed to produce evidence of *even a single consumer* who would have agreed to pay BlueHippo anything had that consumer received full disclosure of BlueHippo's store credit refund conditions at the time of entering into the transaction. *See Kuykendall*, 371 F.3d at 766 (finding that, to rebut the FTC's reasonable approximation of harm based on gross receipts, "defendants might be able to show that some customers received full refunds of their payments or that others were wholly satisfied with their purchases and thus suffered no damages."). In contrast, the *only* evidence in the record regarding injury to consumers was from consumers who confirmed precisely what the law presumes (*i.e.*, had the store credit refund conditions been fully disclosed they would have elected not to go through with the transaction). *See* FTC Exs. 48D-H (A.490-503). Because Rensin completely failed to rebut the

Commission's showing with respect to the harm caused by BlueHippo's contempt, *i.e.*, $14 million, that is the amount that the district court should have awarded.

CONCLUSION

For the reasons set forth above and in the FTC's principal brief, this Court should reverse that portion of the district court's order denying the Commission compensatory sanctions for BlueHippo's civil contempt violation resulting from the material omission of its store credit refund policy and order compensatory sanctions in the amount of $14,062,627.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I certify that Plaintiff-Appellant Federal Trade Commission's ("FTC") Reply Brief complies with the type-volume limitation set forth in Fed. R. App. P. 32(a)(7)(B) because it contains 6520 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii), as counted by the Corel WordPerfect word processing program used to prepare the Reply Brief.

I further certify that the FTC's Reply Brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because the Reply Brief has been prepared in a proportionally spaced typeface in 14-point Times New Roman font.

/s/ *Michael D. Bergman*
Michael D. Bergman
Counsel for Appellant
Federal Trade Commission

CERTIFICATE OF FILING AND SERVICE

I hereby certify that, pursuant to Fed. R. App. P. 25(a) and Local Rule 25.1, on September 12, 2011, I electronically filed the foregoing Reply Brief for Appellant Federal Trade Commission with the Clerk of the Court of the United States Court of Appeals for the Second Circuit using the Court's Case Management/Electronic Case Filing (CM/ECF) system. I also certify that I will submit 6 paper copies of the Reply Brief consistent with Local Rule 31.1.

I further certify that, pursuant to Fed. R. App. P. 25(d) and Local Rule 25.1(h), on this date I served the foregoing Reply Brief by operation of the Court's CM/ECF system on all registered counsel of record in this case.

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