ROBB EVANS & ASSOCIATES LLC
Permanent Receiver of
Lucas Law Center and Future Financial Services, LLC., et al

Federal Trade Commission v. Lucaslawcenter "Incorporated", et al.
CASE No. SACV 09-0770 DOC (ANx)

Order Granting in Part and Denying in Part Motion for Summary Judgment and Granting Motion to Strike

Filed June 3, 2010

UNITED STATES DISTRICT COURT

FOR THE CENTRAL DISTRICT OF CALIFORNIA

FEDERAL TRADE COMMISSION , **Plaintiff,** **v.** **LUCASLAW CENTER "INCORPORATED," FUTURE FINAINCIAL SERVICES, LLC, PAUL JEFFREY LUCAS, CHRISTOPHER FRANCIS BETTS, and FRANK SULLIVAN,** **Defendants.**	**CASE NO. SACV 09-0770** DOC (ANx) **O R D E R GRANTING IN PART AND DENYING IN PART MOTION FOR SUMMARY JUDGMENT AND GRANTING MOTION TO STRIKE**

Before the Court is Plaintiff Federal Trade Commission's ("FTC") Motion for Summary Judgment against Defendants ("Motion for Summary Judgment") and Motion to Strike Defendants' Designation of Expert Witness ("Motion to Strike"). After considering the moving, opposing, and replying papers, as well as oral argument, the Court GRANTS IN PART AND DENIES IN PART the Motion for Summary Judgment and GRANTS the Motion to Strike.

I. BACKGROUND

A. Procedural Background

The FTC alleges that Defendants Lucaslawcenter "Incorporated", d/b/a Lucas Law Center ("LLC") and Future Financial Services, Inc. ("FFS"), through Defendants Paul Jeffrey Lucas ("Lucas"), Christopher Francis Betts ("Betts"), and Frank Sullivan ("Sullivan"), advertised, marketed, or sold mortgage loan modification services to consumers throughout the United States in violation of Section 5(a) of the FTC Act. Defendants often failed to obtain mortgage loan modifications, and in numerous instances, consumers who did not obtain modifications encountered difficulty in obtaining promised refunds or did not receive a refund at all.

On July 9, 2009, the Court granted the FTC's Application for a Temporary Restraining Order ("TRO") against Defendants, which included the appointment of a receiver, Robb Evans ("Receiver"). On July 24, 2009, the Court issued a Preliminary Injunction, which appointed Evans as the permanent receiver.

B. Undisputed Facts

1. Parties

Plaintiff, the FTC, is an independent agency of the United States Government created by statute. Plaintiff's Statement of Uncontroverted Facts ¶ 5. The FTC is charged with the enforcement of Section 5(a) of the Federal Trade Commission Act, 15 U.S.C. § 45(a) and is authorized to initiate proceedings in the federal district court to enjoin violation of the FTC Act and to secure equitable relief including restitution and disgorgement. *Id.* ¶¶ 6, 7.

Defendants maintained a substantial course of trade in or affecting commerce. *Id.* ¶ 11.

Defendant LLC is a California corporation incorporated on June 30, 2008, with its principal place of business at 64 Enterprise, Aliso Viejo, California. *Id.* ¶ 12. FFS also had its principal place of business at 65 Enterprise, Aliso Viejo, California. *Id.* ¶ 13. FFS provided the offices, staff, and facilities for LLC. *Id.* ¶¶ 14, 15. An agreement between LLC and FFS–the Agreement re Management Services[1]–provided that while LLC was responsible for the delivery

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[1] Defendant Betts signed the Agreement on behalf of FFS. *Id.* ¶ 20.

of legal services, it delegated much of the delivery of the services to non-attorneys employed by LLC or employed by FFS and subcontracted to LLC. *Id.* ¶ 17. The Agreement set forth that FFS employees were to represent themselves as "'being with LUCAS' office" and/or 'employees of the law firm,' or of similar job description" and that the FFS employees would be trained and supervised by FFS according to LLC's guidelines. *Id.* ¶¶ 18, 19. Only the Lucas Law Center name was provided to consumers. *Id.* ¶ 21.

From June 2008 through July 2009, the only legal services provided by LLC were mortgage loan modification and foreclosure avoidance services. *Id.* ¶ 24. The sole source of FFS' income was from payments made to it by LLC under the Agreement re Management Services. *Id.* ¶ 25. LLC's records show that it paid $4,332,500 in management fees from July 2, 2008 through July 10, 2009. *Id.* ¶ 26.

From June 2008 to July 7, 2009 Defendant Lucas' principal business address was 65 Enterprise, Aliso Viejo, California, the same address as LLC and FFS. *Id.* ¶¶ 28,29. Lucas previously held an "inactive" status with the State Bar of California but regained "active" status on June 6, 2008.[2] *Id.* ¶ 38. Lucas is the CEO, CFO, Secretary, and a Director of LLC. *Id.* ¶ 30. Lucas' name was prominently displayed in email correspondence with consumers and on the LLC websites, and was the only attorney listed on the websites. *Id.* ¶¶ 32, 33. Lucas signed LLC's refund checks, signed contracts with consumers, and discussed the status of loan modification applications with consumers. *Id.* ¶¶ 34, 35.

From June 2008 to July 7, 2009 Defendant Betts' principal business address was 65 Enterprise, Aliso Viejo, California. *Id.* ¶ 42. Betts owned and operated FFS. *Id.* ¶ 43. Betts is a signatory on an FFS bank account; was the registrant and administrative contact for one of the LLC websites; and his home address was the billing address for one of Defendants' toll-free telephone numbers. *Id.* ¶¶ 44-46. Betts told consumers that he was "at the top" of the LLC hierarchy, right under Lucas, and Lucas described Betts as his partner and hiring manager. *Id.*

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[2] Lucas was subsequently ordered involuntarily inactive by the State Bar of California on November 4, 2009. *Id.* ¶ 39.

¶¶ 47, 49.

Defendant Sullivan held an office, as opposed to a cubicle, at LLC. *Id.* ¶ 59. FFS paid Sullivan $154,535 from July 16, 2008 to July 9, 2009, and LLC paid Sullivan $10,635 between May 8, 2009 and July 10, 2009. *Id.* ¶¶ 57, 58. Sullivan handled consumer concerns, complaints, and requests for refunds from LLC, sometimes denying or only issuing partial refunds. *Id.* ¶¶ 65,66.

2. LLC Business Practices

LLC advertised through radio and on the internet and encouraged consumers to visit its websites[3] or call a toll-free telephone number. *Id.* ¶¶ 68 - 70. The websites and call center representatives emphasized the expertise of LLC as a law firm and represented that LLC used attorneys to negotiate for customers. *Id.* ¶¶ 74, 75, 93, 94. The websites claimed, "The [Lucas Law Center] working with their first class network of over 30 affiliated attorneys will help you save your home, and provide a financial solution that works for you, and your family." *Id.* ¶ 78. The websites and representatives also stated that they had an ability to contact individuals who make the decisions at the consumers' lenders and were familiar with them due to prior dealings. *Id.* ¶¶ 80-81, 83, 96. The websites also promised "a money back guarantee if we cannot get you a work out agreement with your lender(s) as long as no sale date has been set. *Id.* ¶ 84. Likewise, the call representatives assured consumers that they had nothing to lose because LLC would provide a full refund if it could not obtain the loan modification. *Id.* ¶ 102.

The call representatives at the tollfree number often claimed that LLC had a success rate of 90% or higher in obtaining modifications and achieved modifications "all the time." *Id.* ¶¶ 86, 87. LLC representatives frequently claimed that LLC would obtain reductions in principal, interest, and monthly mortgage payments for consumers, at times quoting specific, substantial reductions, such as a reduction of a principal balance by "a few hundred thousand." *Id.* ¶¶ 88 - 91. The representatives gave time frames in which the modification could be expected, usually three months or less. *Id.* ¶ 92.

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[3] www.LucasLawCenter.com and www.oclawoffices.us.

LLC typically quoted fees of between $2,000 and $3,995 for its loan modification services. *Id.* ¶ 98. The fee had to be paid in whole or in part before LLC would begin its loan modification services. *Id.* ¶ 100. LLC frequently did not send a copy of its written contract to consumers until after the fee was paid. *Id.* ¶ 101. The written contract stated a refund policy: "In the event that we ware unable to obtain any loan modification on your behalf, *and* you decide not to pursue the other foreclosure avoidance services offered, we will offer you a full refund." *Id.* ¶ 104.

In some instances, LLC representatives also instructed consumers to stop making payments on their mortgages, claiming that stopping payments would benefit the consumer. *Id.* ¶¶ 105, 106. LLC representatives would then instruct consumers to use the money for their mortgage payments to pay the fee to LLC. *Id.* ¶¶ 107, 108

After securing payment, LLC's representatives routinely avoided consumers' requests for updates and the consumers had no contact with the purported attorneys who were supposed to be negotiating with their lenders. *Id.* ¶¶ 111, 113, 115. Consumers were told that default notices or collections calls were "normal" or "routine" and should be ignored. *Id.* ¶ 121.

The Receiver was unable to locate any documentation of LLC having a network of over 30 affiliated attorneys or any lawyer other than Lucas working on a loan modification. *Id.* ¶¶ 116-117.

In numerous instances, LLC failed to obtain the promised loan modifications. *Id.* ¶ 123. Many consumers ultimately lost their homes or sought bankruptcy protection, incurring additional costs and expenses. *Id.* ¶ 131. LLC routinely denied consumers' initial requests for full refunds. *Id.* ¶¶ 132, 133. In some cases, promised refunds were never delivered or were only partially delivered. *Id.* ¶ 134.

As evidence in support of these facts, the FTC presented numerous statements from consumers through declarations, deposition testimony, complaint emails to LLC, state bar complaints, and Better Business Bureau complaints. The parties stipulated to approximately 70 of these uncontroverted facts, and Defendants asserted the Fifth Amendment to approximately

60 more facts.[4]

II. MOTION FOR SUMMARY JUDGMENT

A. Legal Standard

Summary judgment is proper if "the pleadings, the discovery and disclosure materials on file, and any affidavits show that there is no genuine issue as to any material fact and that the movant is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(c).

The Court must view the facts and draw inferences in the manner most favorable to the non-moving party. *United States v. Diebold, Inc.*, 369 U.S. 654, 655, 82 S. Ct. 993 (1962); *Chevron Corp. v. Pennzoil Co.*, 974 F.2d 1156, 1161 (9th Cir. 1992). The moving party bears the initial burden of demonstrating the absence of a genuine issue of material fact for trial, but it need not disprove the other party's case. *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 256, 106 S.Ct. 2505 (1986); *Celotex Corp. v. Catrett*, 477 U.S. 317, 323-25, 106 S.Ct. 2548 (1986). When the non-moving party bears the burden of proving the claim or defense, the moving party can meet its burden by pointing out that the non-moving party has failed to present any genuine issue of material fact. *Musick v. Burke*, 913 F.2d 1390, 1394 (9th Cir. 1990).

Once the moving party meets its burden, "an opposing party may not rely merely on allegations on denials or its own pleading; rather, its response must–by affidavits or as otherwise provided in this rule–set out specific facts showing a genuine issue for trial. If the opposing party does not so respond, summary judgment should, if appropriate, be entered against that party." Fed. R. Civ. P. 56(e)(2); *see also Anderson*, 477 U.S. at 248-49. Furthermore, a party cannot create a genuine issue of material fact simply by making assertions in its legal papers. There must be specific, admissible evidence identifying the basis for the dispute. *S.A. Empresa de Viacao Aerea Rio Grandense v. Walter Kidde & Co., Inc.*, 690 F.2d 1235, 1238 (9th Cir. 1980). The Supreme Court has held that "[t]he mere existence of a scintilla of evidence . . . will be insufficient; there must be evidence on which the jury could reasonably find for [the opposing

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[4] The Court draws an adverse inference from the parties' assertion of the Fifth Amendment privilege against self-incrimination, as it is entitled to do in civil cases. *Nationwide Life Ins. Co. v. Richards*, 541 F.3d 903, 911 (9th Cir. 2008).

party]." *Anderson*, 477 U.S. at 252.

B. Discussion

At the outset, the Court notes that much of Defendants' opposition to the statements of uncontroverted facts and conclusions of law focuses upon the fact that the FTC filed its Motion for Summary Judgment five working days before all responses must be filed, which defense counsel deems "harassing and burdensome." Opp. to Statement of Unconverted Facts & Conclusions of Law at 1. The FTC filed its Motion for Summary Judgment on April 26, 2010, after meeting and conferring with defense counsel on April 12, 2010. Mot. Not. at 4. Pursuant to Local Rules 6-1 and 7-9, the FTC may file its motion no later than twenty-eight days prior to the scheduled hearing–exactly as was done by the FTC in this case–and Defendants must file their opposition no later than twenty-one days prior to the scheduled hearing. In other words, the Local Rules contemplate exactly the filing sequence that was accomplished in this action, and it was not "harassing" for the FTC to use the process contemplated and directed by the Local Rules.

Furthermore, Defendants did not present the Court with any admissible evidence controverting the facts presented by the FTC.[5] Instead, they rely upon legal argument and the argument that the FTC has not met its initial burden in proving its case.

The FTC brings its claims pursuant to the FTC Act. Section 5(a) of the FTC Act, 15 U.S.C. § 45(a), prohibits "unfair or deceptive acts and practices in or affecting commerce." Defendants argue that the FTC is so vague that it is unconstitutional. *See* Defs.' Opp. at 3. However, the Ninth Circuit has issued many opinions interpreting the Section 5(a) requirements, and the Act is not impermissibly vague. The general principles for determining whether advertising is deceptive, as set forth by the Ninth Circuit, are that: "an act or practice [is] deceptive if, first, there is a representation, omission, or practice that, second, is likely to mislead

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[5] Defendants attach a list of modifications supposedly achieved by LLC in their opposition. This competing "evidence" is properly rejected as lacking foundation and authentication. Plaintiff's Evidentiary Objection to this Exhibit, Dkt. 160, is hereby SUSTAINED.

consumers acting reasonably under the circumstances, and third, the representation, omission, or practice is material." *FTC v. Pantron I Corp.*, 33 F.3d 1088, 1095 (9th Cir. 1994). In evaluating whether a defendant's claims were deceptive or misleading, the Court must examine the net impression of the representations as a whole. *See FTC v. Gill*, 265 F.3d 944, 956 (9th Cir. 2001); *FTC v. Tashman*, 318 F.3d 1273, 1283 (11th Cir. 2003) ("Representations violate Section 5 if the FTC proves that, based on a common sense net impression of the representations as a whole, the representations are likely to mislead reasonable consumers to their detriment"). A representation is considered material if it "involves information that is important to consumers and, hence, [is] likely to affect their choice of, or conduct regarding a product." *FTC v. Cyberspace.com, LLC* 453 F.3d 1196, 1201(9th Cir. 2006).

The FTC need not prove that each of LLC's consumers relied upon the defendants' misrepresentations. "A presumption of actual reliance arises once the Commission has proved that the defendant made material misrepresentations, that they were widely disseminated, and that consumers purchased the defendant's product." *FTC v. Figgie Intern., Inc.*, 994 F.2d 595 (9th Cir. 1993).

i. Count I

In Count I, the FTC alleges that Defendants violated Section 5 of the FTC Act by falsely representing that they would obtain mortgage loan modification services for consumers in all, or virtually all, circumstances. Compl. ¶ 30. In oral argument, the FTC clarified that Count I is not based on the claim that LLC represented a certain global success rate to consumers; instead, it is based on the claim that LLC promised each individual consumer that they would get a loan modification and that the modification would be successful.

The FTC provided uncontroverted evidence that sales pitches by LLC call representatives often claimed either a high success rate in obtaining modifications or a high likelihood of achieving a modification in a particular case. U.F. ¶ 85; *see* Marino Depo. at 16:16-20 (representative stated LLC had a "pretty good batting average"); Montgomery Depo. at 12:19-21 (representative stated "there was a ninety-eight percent chance that they were going to be able to get me a loan modification that I could afford"); Jeremy Decl. ¶ 9 (representative stated it was

"highly likely" that loan modification would be achieved); Kranzberg Decl. ¶ 4 (representative stated Countrywide modifications were achieved "all the time"); LaPoint Decl. ¶ 5 (representative stated that 90% of LLC's modification requests are approved by consumer's lender). Representatives often claimed that LLC had a success rate of 90% or higher in obtaining modifications. *See* U.F. ¶ 86; Montgomery Depo. at 12:19-21; Lapoint Decl. ¶ 5; Utley Decl. ¶ 6; McPeek Decl. Att. 11 at 143; Att. 43 at 116-117. Defendants have not presented any evidence challenging that these statements were made. These representations were widely disseminated by call representatives in inducing a confidence level in LLC by the individual consumers. However, the Court is concerned that the evidence presented in summary judgment does not support a finding that the practice was uniform; in other words, call representatives uniformly made statements to induce a high level of confidence by consumers, but those statements ranged from guaranteeing success, to stating that there was a high likelihood of success, to stating the high global success rating and allowing customers to infer that their modification would be successful as well.

These representations qualify as material, as a consumer is likely to consider a high success rate at achieving modifications as a crucial criteria for choosing a loan modification service, particularly given the high stakes that homeowner consumers may be facing–foreclosure–if they are not able to obtain a modification. However, in determining whether a misrepresentation is likely to mislead consumers acting reasonably under the circumstances, the Court "examine the net impression of the representations as a whole." *Gill*, 265 F.3d at 956. In Count II, the FTC alleges that Defendants' sales pitches also stated that LLC provided a money back guarantee. The very existence of a refund guarantee in the sales pitch recognizes the possibility that an attempt by LLC to achieve a modification would be unsuccessful. Therefore, the representations left a net impression that LLC's ability to achieve a modification was highly probable but not absolutely certain. A reasonable consumer, taking a promise that the modification would be successful in the context of an express promise for a refund if the modification was not successful, would understand that there was a chance that the modification would not be successful.

The evidence provided in support of Count I fails to meet its burden in demonstrating that LLC was engaged in a deceptive practice of promising consumers that their loan modifications would be successful and fails to establish, that the representations were likely to mislead consumers acting reasonably under the circumstances. Because the FTC failed to provide sufficient evidence showing that the misrepresentation at issue was likely to mislead consumers, the Motion for Summary Judgment is DENIED as to Count I.

ii. Count II

In Count II, the FTC alleges that Defendants represented that they would give full refunds to consumers if Defendants fail to obtain a modification of their loan. Compl. ¶ 33. The FTC provided uncontroverted evidence that these representations frequently were made to consumers by the call representatives. The evidence of these representations was presented in the form of emails, depositions, and declarations of consumers. *See* UF ¶ 103; Pl.'s Exh. 97 (email from consumer stating that LLC promised full refund if there was no modification); Adkins Depo. at 16:18-20 (LLC promised to refund consumer's money if modification was not achieved); Cox Depo. at 20:5-11 (same); Lee Depo. at 14:8-14; Marino Depo. at 20:10-11, 17-21; Gearhart Decl. ¶ 7; Jeremy Decl. ¶ 11; Quintana Decl. ¶ 8; McPeek Decl. Att. 10, 11. Defendants have not provided any evidence challenging that these statements were made, but generally assert that the testimony of a few consumers is insufficient to show a deceptive practice. The Court finds that the evidence presented by the FTC was sufficient to meet their burden.

Defendants also argue that the refund promise was not unqualified but subject to limitations set forth in the contract. The standard contract stated, "In the event that we ware unable to obtain any loan modification on your behalf, *and* you decide not to pursue the other foreclosure avoidance services offered, we will offer you a full refund." UF ¶ 104; Pl.'s Exh. 232 at ¶ 4A.[6] However, the FTC provided evidence that in many instances, the contract was not even provided until after payment of the fee had been made. UF ¶ 101; Marino Depo. at 19:14-

[6] Defendants imply that the FTC was attempting to obfuscate the terms of the contract by not providing it as evidence. However, the FTC did provide an example retainer agreement to the Court. *See* Exh. 232.

21, 21:2-7; Jeremy Decl. ¶¶ 13-14; Keylon Decl. ¶ 8; Quick Decl. ¶¶ 12-13; Gearhart Decl. ¶ 8. In any case, "each representation must stand on its own merit, even if other representations contain accurate, non-deceptive information." *Gill*, 71 F. Supp. 2d at 1044. Because the refund representations were made by sales representatives on the telephone in the initial sales pitch, and the qualification to that refund was made in a later-received contract, the argument is not persuasive. *See FTC v. Connelly*, No. SACV 06-701 DOC (RNBx), 2006 WL 6267337, at *10 (C.D. Cal. Dec. 20, 2006) ("disclaimers are particularly inadequate when they appear in a different context that the claims they purport to repudiate").

Like the representations regarding the high success rate, representations regarding the refund were widely disseminated through a common practice of call representatives in the initial sales call. In addition, the representations were disseminated through the contract. The representation that consumers would receive a full refund is certainly material, as it minimizes the risk associated by paying a $2,000-$3,995 upfront fee. Consumers are more likely to make a multi-thousand dollar purchase when they believe that the money will be fully refunded if the loan modification service they purchase is not successful.

In order to show that this was a misrepresentation, *i.e.*, that LLC did not actually provide refunds when a modification was not achieved, the FTC provided extensive evidence from consumers that, after a loan modification was unsuccessful, LLC refused to provide full refunds to consumers. UF ¶ 132; *see, e.g.*, Pl.'s Exh. 96 (upon email request for full $3,000 refund for failure to modify a loan, LLC employee states, "Tell him to stuff it. LOL." and Lucas responds, "Agreed" with a smiley face emoticon), Pl.'s Exh. 97 (email from consumer stating, "[Sullivan] said I would not receive one red cent back, that he was done. And then he hung up on me."); Pl.'s Exh. 245 (state bar complaint alleging failure to provide refund); Pl.'s Exh. 247 (state bar complaint alleging Sullivan refused refund); Pl.'s Exh. 248 (state bar complaint alleging Sullivan told consumer he would never get his money back); Cox Depo. at 29:18-25 (only received 40% refund); Lee Depo. at 29:9-11 (no refund received); Montgomery Depo. at 20: 6-12 (Betts offered 20% refund and said there would be no refund if consumer continued to call him). To combat this evidence, Defendants argue that the Receiver reported that an excess of $998,000

was refunded to clients. Defs.' Opp. at 2. However, even if in some cases refunds were given, a promise that refunds were given in *all cases* where modifications were not achieved was clearly contrary to LLC's actual policy, and as such, a misrepresentation. The FTC need not show that every consumer was injured by the misrepresentation. *FTC v. Stefanchik*, 559 F.3d 924 (9th Cir. 2009) (citing *FTC v. Amy Travel Service, Inc.*, 875 F.2d 564, 572 (7th Cir. 1989). In this case, that means that the FTC need not show that every customer demanded and was denied a full refund; likewise, the fact that some consumers successfully received refunds does not operate as a defense to FTC Act violations. *Amy Travel Service*, 875 F.2d at 572.

Plaintiff provided evidence, evidence which is uncontroverted and much of which is subject to an adverse inference due to Defendants' assertion of the Fifth Amendment, demonstrating that Plaintiff has shown the existence of a deceptive practice under Section 5(a) for Count II of the Complaint. Defendants have failed to provide any specific, admissible evidence identifying the basis for a factual dispute that would preclude issuance of summary judgment. *S.A. Empresa de Viacao Aerea Rio Grandense,* 690 F.2d at 1238. Defendants' Motion for Summary Judgment as to Count I is GRANTED.

iii. Joint and Several Liability

The FTC argues that the corporate and individual defendants should be held jointly and severally liable for the deceptive practices. For LLC and FFS, this argument is based on the theory that the defendants were operating as a common enterprise. When determining whether a common enterprise exists, courts look to factors including "common control, sharing of office space and officers, whether business is transacted through a 'maze of interrelated companies,' the commingling of corporate funds, unified advertising, and any other evidence revealing that no real distinction existed between the corporate defendants." *FTC v. Neovi, Inc.*, 598 S. Supp. 2d 1104, 1116 (S.D. Cal. 2008). Here, the FTC provided a large amount of evidence that LLC and FFS operated as a common enterprise. Defendants did not present any opposition. LLC and FFS shared a common office space. UF ¶¶ 12-15. They also shared common employees, as all LLC employees other than Lucas were FFS employees. *Id.* Betts, who was the owner of FFS, played a prominent role in managing LLC. *Id.* ¶¶ 45, 46. The advertising for loan modifications

services were all under the LLC name, and only Lucas Law Center name was provided to consumers. *Id.* ¶¶ 18, 21. The Management Agreement between the two companies even specified that FFS employees were to represent themselves as "'being with LUCAS' office" and/or 'employees of the law firm,' or of similar job description." *Id.* ¶¶ 18, 19. Only the Lucas Law Center name was provided to consumers. *Id.* ¶ 21. Moreover, from June 2008 through July 2009, the sole source of FFS' income was from payments made to it by LLC under the Agreement re Management Services. *Id.* ¶ 25. There was no real distinction between LLC and FFS, and the Court finds they functioned as a common enterprise.

The individual defendants face joint and several liability for both the monetary and injunctive relief. *FTC v. Cyberspace.com, LLC*, 453 F.3d 1196, 1202 (9th Cir. 2006); *FTC v. Am. Standard Credit Sys., Inc.*, 874 F. Supp. 1080, 1087 (C.D. Cal. 1994). For injunctive relief, individuals may be held liable when the individual defendants either (1) directly participated in the deceptive practices or (2) had authority to control them. *Am. Standard Credit Syst.*, 874 F. Supp. at 1087. Authority to control "can be evidenced by active involvement in business affairs and the making of corporate policy, including assuming the duties of a corporate officer." *Id.* at 1089. Here, Lucas was the CEO, CFO, Secretary, and a director of LLC. As the head of LLC and only lawyer employed by LLC, which had a purported business model of negotiating modifications through lawyers, Lucas clearly had the authority to control the deceptive practices. Betts owned and operated, and was an officer of, FFS. Betts was intimately involved with LLC's operations, acting as a manager of LLC. Betts clearly had the authority to control FFS' involvement in the deceptive practices, making such decisions as entering into and signing the Management Agreement between FFS and LLC. Sullivan is the only employee warranting a more parsing evaluation. Defendants argue that Sullivan was not an owner of any named defendant and was merely an employee. Defs.' Opp. at 3. The FTC argues that while Sullivan was not formally an officer of either of the companies, his authority to control LLC is demonstrated by the fact that he handled consumer concerns, complaints, and refund requests and decided whether to issue refunds. Certainly his participation in the refund request process demonstrates that he participated in the deceptive practices. Sullivan was on the receiving end

of numerous refund request complaints that were based on the fact that the consumers claimed they had been promised refunds if the loans were not modified. When Sullivan refused to grant refunds, he did so knowing that the earlier statements regarding refunds were misrepresentations. Therefore, all three individuals have met the requirements for individual liability for injunctive relief.

For monetary relief, individuals may be held liable when they had knowledge of the deceptive practices. *Am. Standard Credit Sys.*, 874 F. Supp. at 1089. Knowledge can be shown by actual knowledge of material misrepresentations, reckless indifference to the truth or falsity of the misrepresentations, or an awareness of a high probability of fraud along with an intentional avoidance of the truth. *Id.* Lucas, Betts, and Sullivan were so involved with the day-to-day activities of LLC, a small company, that one cannot plausibly argue that they did not know of the misrepresentations, or at the very least, were aware of a high probability of fraud. If nothing else, the large number of complaints on file and received through email alerted them to the deceptive practices and any ignorance was due to intentional avoidance. Therefore, all three should be held liable for monetary relief.

iv. Permanent Injunction, Monetary Relief, and Ancillary Relief

Section 13(b) of the FTC Act, 15 U.S.C. § 53(b), empowers this Court to grant equitable relief to halt and redress violations of the FTC Act. Under Section 13(b), Congress also gave the Court the authority to grant "any ancillary relief necessary to accomplish complete justice." *FTC v. H. N. Singer, Inc.*, 668 F.2d 1107, 1113 (9th Cir. 1982). Defendants have provided no opposition to the issuance of an injunction and ancillary relief. The Court finds an injunction necessary because there is a "cognizable danger of recurrent violation." *U.S. V. W.T. Grant Co.*, 345 U.S. 629, 633, 73 S.Ct. 894 (1953); *FTC v. Gill*, 71 F. Supp. 2d 1030, 1047 (C.D. Cal. 1999). The fraud perpetrated here was ongoing over an extended period of time, done with awareness, and targeted at a particularly vulnerable segment of the population. The Court has reviewed the restrictions set forth in the proposed permanent injunction against Defendants and finds them to be both appropriate and sufficiently narrowly tailored. The non-monetary ancillary relief is appropriate as well.

Section 13(b) also encompasses the award of monetary relief through restitution or disgorgement. *FTC v. Pantron I Corp.*, 33 F.3d 1088, 1102 (9th Cir. 1994). As to the measure of monetary relief, the FTC "must show that its calculations reasonably approximated the amount of customers' net losses, and then the burden shifts to the defendants to show that those figures were inaccurate. *FTC v. Febre*, 128 F.3d 530, 535 (7th Cir. 1997); *FTC v. Medicor, LLC*, 217 F. Supp. 2d 1048, 1057-58 (C.D. Cal. 2002). The Receiver has determined that Defendants received $7,118,509.40 from their consumers during the loan modification scam. UF ¶ 141. Defendants refunded $998,308.97, resulting in net sales of $6,120,200.43. *Id.* ¶¶ 140, 141.

The Receiver reviewed a subsection of the cases that Defendants claim resulted in successful modifications, and found that some of those cases (approximately 40) resulted in successful modifications. *See* Pl.'s Mot. at 22-23. The FTC argues that the revenue from those consumers should not be deducted from the monetary relief because the harm was in the misrepresentation when it was made, and the fact that a consumer later received a refund is irrelevant. In support of this argument, they cite *FTC v. Figgie Intern., Inc.*, in which the Ninth Circuit observed that deceptive advertising practices "tainted the customers' purchasing decisions" and "[t]he fraud in the selling, not the value of the thing sold, was what entitled consumers to full refunds." 994 F.2d 595, 606 (9th Cir. 1993). In *Figgie*, the court used the example of a rhinestone merchant to explain this proposition. The rhinestone merchant misrepresents that its rhinestones are actually diamonds. The court reasoned that the consumers still received something of value–a rhinestone–but that the value of the rhinestone should not be deducted from the recovery because the deception tainted the purchasing decision. If the customers had known that what they thought were diamonds were actually rhinestones, they may not have made the purchase at all.

The FTC argues that the same logic applies here. Even though some consumers may have received something of value–loan modifications–they were still induced to purchase the service through misrepresentations. This argument has particular force when looking both at the holding in *Figgie* and more generally at the purpose of disgorgement, which is not to

compensate victims of fraud but to deprive the wrongdoer of ill-gotten gains. *FTC v. Gem Merchandising Corp.*, 87 F.3d 466, 470 (11th Cir. 1996). LLC made misrepresentations to consumers about the availability of refunds, and those misrepresentations had the potential to result in the miscalculation of the risk of purchasing LLC's services by the consumer. If the consumer knew there was a risk of not receiving a refund when a modification was not successful, that could very well change the purchasing decision. The purchasing decision process was tainted, regardless of whether those consumers were eventually satisfied with their purchase. *See FTC v. Neovi, Inc.*, No. 06-CV-1952-JLS JMA, 2009 WL 56130 (S.D. Cal. Jan. 7, 2009), affirmed by --- F.3d ----, 2010 WL 1930229 (9th Cir. May 14, 2010) (in unfair business practices case under FTC Act, court awarded disgorgement of all revenue from checks created through unfair practices, both fraudulent and legitimate checks) . Even if LLC eventually delivered on its promise, it did so having secured the business of that consumer based on a misrepresentation, and as such, the payment for those services were ill-gotten.

Therefore, the Court finds that the FTC has provided a reasonable estimate of consumer harm of $6,120,200, which Defendants have failed to rebut.

III. MOTION TO STRIKE

A. Legal Standard

Federal Rule of Civil Procedure Rule 37(c)(1) states: "If a party fails to provide information or identify a witness as required by Rule 26(a) or 26(e), the party is not allowed to use that information or witness to supply evidence on a motion, at a hearing, or at a trial, unless the failure was substantially justified or is harmless." "Rule 37(c)(1) gives teeth to [the Rule 26(a) disclosure] requirements by forbidding the use at trial of any information required to be disclosed by Rule 26(a) that is not properly disclosed." *Yeti by Molly, Ltd. v. Deckers Outdoor Corp.*, 259 F.3d 1101, 1106 (9th Cir. 2001). Rule 37(c)(1) is recognized as a broadening of the sanctioning power and a rule that is "self-executing" and "automatic." *Id.* Two express exceptions to the sanction exist: "The information may be introduced if the parties' failure to disclose the required information is substantially justified or harmless." *Id.*

B. Discussion

Plaintiff states that under Fed. R. Civ. P. 26(a)(2)(C), Defendants were required to designate their expert witnesses and serve the experts' written reports ninety days before trial, which was April 14, 2010. The FTC objects to the expert disclosure of Martin D. Andelman, provided on April 14, 2010 on the basis that (1) the designation did not include a report prepared and signed by the proffered expert; (2) Martin Andelman does not qualify as an expert; and (3) the designation fails to provide any indication as to the nature and bases of the opinions to be offered by the expert. Mot. at 2.

Defendant failed to file any opposition to this motion. The Motion is GRANTED as unopposed and the expert designation is STRICKEN.

IV. DISPOSITION

For the foregoing reasons, the Motion for Summary Judgment is DENIED as to Count I; GRANTED as to Count II; GRANTED as to Joint and Several Liability; GRANTED as to the Injunctive and Ancillary Relief against all Defendants; and GRANTED as to the monetary relief against all Defendants. The Motion to Strike is GRANTED.

A separate final order as to the granted injunctive and ancillary relief shall be forthcoming and shall take effect as of the date an order is entered resolving all remaining claims in this action.

IT IS SO ORDERED.

DATED: June 3, 2010

David O. Carter

DAVID O. CARTER
United States District Judge