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IN THE DISTRICT COURT OF GEARY COUNTY, KANSAS
Division 01

STATE OF KANSAS, *ex rel.*
CARLA J. STOVALL, Attorney General

Plaintiff,

vs.

TOP SECRETS, INC., THOMAS M. MICHAELS, and
TOP SECRETS, INC., d/b/a SECRET SOURCE,

Defendants.

Case No. 00-C-176

Pursuant to K.S.A. Chapter 60

JOURNAL ENTRY OF CONSENT JUDGMENT

NOW on this 8th day of June, 2001, Plaintiff's Petition for Approval of Consent Judgment comes before the Court pursuant to K.S.A. §50-632(b). Plaintiff, the State of Kansas, *ex rel.* Carla J. Stovall, Attorney General, appears by and through James J. Welch, Assistant Attorney General. Defendants Top Secrets, Inc., Thomas M. Michaels, and Top Secrets, Inc., d/b/a Secret Source, appear by and through David P. Troup.

Whereupon, the parties advise the Court that they have stipulated and agree to the following matters:

1. Carla J. Stovall is the Attorney General of the State of Kansas.
2. The Attorney General's authority to bring this action is derived from the statutory and common law of the State of Kansas, and specifically, the Kansas Consumer Protection Act, K.S.A. §50-623, *et seq.*

3. Defendant Top Secrets, Inc. is a corporation organized under the laws of the state of Kansas. Defendant may be served with process by the Attorney General's Office via personal service, or certified mail to its registered agent (and President, C.E.O., and sole officer and shareholder), Thomas Michaels at the corporation's registered office, 839 North Eisenhower, Junction City, Kansas 66441.

4. Defendant Thomas M. Michaels is an individual and the President, C.E.O., and sole officer and shareholder of Top Secrets Inc. and Secret Source. Defendant Michaels may be served with process by personal service by the Attorney General's Office at his last known address, 701 McClure, Junction City, Kansas 66441, or wherever in Kansas he may be found.

5. Defendant Secret Source is a wholly-owned subsidiary of Top Secrets, Inc. and, as such, may be served with process in the same manner as Defendant Top Secrets, Inc.; moreover, by serving the corporation's registered agent, Thomas Michaels, at the corporation's registered office, 839 North Eisenhower, Junction City, Kansas 66441. Defendant Secret Source was, during times relevant hereto, a corporation organized under the laws of the state of Kansas as The Secret Source, Inc., which was incorporated on or about December 28, 1998 and forfeited on or about July 15, 2000.

6. Defendants are suppliers, as defined by K.S.A. §50-624(i), and have engaged in consumer transactions within the definition of K.S.A. §50-624(c) and (h), with consumers, as defined by K.S.A. §50-624(b).

7. Defendants admit the Court has personal and subject matter jurisdiction over the parties.

8. The Attorney General alleges Defendants are responsible for the acts of their agents and employees under the legal theory of *respondeat superior*.

9. Plaintiff alleges that Defendants promote the Top Secrets' program, which includes several packages consumers may purchase. These packages include a "wholesale benefits package," the source of which is The Shoppers Network at a cost of \$199.00; however,

the primary inducement for consumers to enter into the Top Secrets program is the unique money-making opportunity available. Consumers are told that they need make no direct sales, but simply to promote Top Secrets' toll-free telephone number. Once referred persons call that number, the referring consumers are promised that they will receive a commission when the referred person joins the Top Secrets' program.

10. Plaintiff alleges that Defendants have engaged in deceptive and unconscionable acts and practices in violation of the Kansas Consumer Protection Act. These violations include, but are not limited to:

- a. Defendants adopted, implemented and enforced in its distribution system policies whereby Defendants paid commission, bonuses, rebates, and other benefits to participants that were not based on the sale of Top Secrets products to verified end-user consumers. Consumers are induced into paying to join Defendants' program with the promise that the consumer will receive a future bonus for finding additional persons who are willing to join the program. This promise of future financial benefit is the linchpin of Defendants' program. Defendants have engaged in multiple deceptive acts by making representations knowingly or with reason to know that the consumer will receive a rebate, discount or other benefit as an inducement for entering into a consumer transaction in return for giving the supplier the names of prospective consumers or otherwise helping the supplier to enter into other consumer transactions, where receipt of the benefit is contingent on an event occurring after the consumer enters into the transaction. The promotion and implementation of such a referral sales scheme constitutes a deceptive act, in violation of K.S.A. §50-626(b)(1)(E).
- b. Defendants made representations of hypothetical examples or representations of past earnings, sales, profits or payments that a person will or should earn or receive, or has the reasonable expectancy of earning or receiving as a Top Secrets

participant; such statements included the representation that participants could earn as much as \$10,000 per month. Defendants are unable to substantiate the claim that any person has earned this, or a comparable amount. This is in violation of K.S.A. §50-626(b)(2), in that it constitutes the willful use of exaggeration, falsehood, innuendo, and ambiguity as to a material fact.

- c. Defendants do not explain to consumers the eventual economic and mathematical failure of such a pyramid system due to market saturation. Thus, consumers are unaware that those recruited last in the system will have little chance of finding additional investors. Defendants have willfully failed to state a material fact, and willfully concealed, suppressed or omitted a material fact by failing to explain market saturation and its impact on future earnings in oral and written representations of Defendants' sales referral scheme. Such failure constitutes a violation of K.S.A. § 50-626(b)(3).
- d. Defendants' transactions whereby referred-consumers were solicited by receiving a postcard which invited the consumer to call Defendants' toll-free number constitute door-to-door sales, as defined by K.S.A. §50-640(c)(1); however, Defendants failed to furnish consumers with completed notices of cancellation which comply with Kansas law. Such failure constitutes a violation of K.S.A. §50-640(b).
- e. The three-day right of cancellation which Defendants provided to all consumers (regardless of the classification of sale as a door-to-door sale, as defined by K.S.A. §50-640) included the disclosure that any cancellation properly made within the three days allotted would be subject to reduction by a 20% "restocking fee." This is in violation of K.S.A. §50-640(b)(6), in that it is a misrepresentation of a consumer's right to cancel, which, in a Kansas door-to-door sale, is absolute and unconditional. This is also in violation of K.S.A. §50-627(b)(7), in that it is

an unconscionable attempt to exclude, modify or otherwise limit the remedies provided by K.S.A. §50-640.

- f. Defendants used the names and addresses of each and every person who, after being referred, telephoned the defendants' toll-free telephone number, whether or not such persons entered into any transaction with Defendants, in order to generate income for Defendants, without disclosing to said persons the material fact that Defendants would be selling that information to other network-marketing companies. This is in violation of K.S.A. §50-626(b)(3), in that it is the willful failure to state a material fact, and the willful concealment, suppression or omission of a material fact.

- g. Defendants made willful use, in oral or written representations to consumers, of exaggeration, falsehood, innuendo and ambiguity as to material facts, in violation of K.S.A. §50-626(b)(2), in the promotion of the Top Secrets program, including but not limited to:
 - (1) The representation that products obtained through The Shoppers Network would be available to participating consumers at wholesale cost when, in fact, such products were available, in rare cases, at a discount of retail price and, more commonly, at prices comparable to those of merchants local to consumers;

 - (2) Defendants represented that they would refund a consumer's money if the consumer could substantiate an inability to save money using the Shoppers Network and that the consumer, after attempted promotion of Defendants' program, was unable to recoup the consumer's investment in the Top Secrets program, when such refunds, in actuality, were not made;

- (3) The representation that the consumer could obtain a refund from Defendants by calling a certain telephone number, which was a recorded message telling the consumer to call back another time and subsequently terminating the telephone call.
 - (4) The representation that the consumer could obtain a refund from Defendants by returning the merchandise received from Defendants in substantially the same condition as received, and subsequently refusing to accept delivery of packages so returned.
 - (5) The representation of the benefit of a free vacation as a part of the Shoppers Network without disclosing to the consumer that the "free vacation" (transportation not included) conditioned upon consumer's listening to a sales presentation for time-share properties.
- h. Defendants have represented that Top Secrets, Inc. is a member of the Better Business Bureau; however, Top Secrets, Inc. is not only not a member of the Better Business Bureau, but has several unsatisfied complaints with that agency. This is in violation of K.S.A. §50-626(b)(1)(B), in that it is a representation that Defendants had a sponsorship, approval, status, affiliation and connection that Defendants did not have.
- i. In many instances, Defendants are telemarketers, as defined by K.S.A. §50-671, in that Defendants, individually and through salespersons, initiate the sale with the intent to sell consumer goods or services by telephonic means or by postcard or other written notice sent through the mail in which the goods and services and all the material terms of the transaction, including price and any fees or handling, shipping or delivery charges, are not fully described and which requests that the

consumer contact the seller to initiate the transaction. Defendants accepted payment from consumers in transactions in which Defendants acted as telemarketers, as defined by K.S.A. §50-671 without obtaining a signed confirmation containing all elements required in such a confirmation by K.S.A. §50-672(b), in violation of K.S.A. §50-672(c).

j. Defendants, acting as telemarketers within the definition of K.S.A. §50-671, accepted payment from consumers without obtaining a signed confirmation complying with K.S.A. §50-672(b), refused to cancel consumer transactions for consumers so situated who requested cancellation in writing, in violation of K.S.A. §50-672(e).

k. Defendants have offered for sale certain CD-ROM 's when in fact no such CD-ROM's exist in violation of K.S.A. §50-626(b)(5)&(6).

11. Defendants deny the Plaintiff's allegations as set forth above and specifically deny that Defendants have engaged in any deceptive or unconscionable acts and practices or any violations of the Kansas Consumer Protection Act. Notwithstanding such denial, Defendants agree to refrain from and to be permanently enjoined from engaging in those acts and practices alleged to be deceptive or unconscionable in paragraph ten (10) of this Consent Judgment and to refrain from establishing, operating, promoting or participating in any pyramid promotion scheme. Defendants agree that engaging in such acts or similar acts, after the date of this Consent Judgment, shall constitute a violation of this Order.

12. The provisions of this Consent Judgment will be applicable to Defendants, and every employee, agent or representative of Defendants.

13. Defendants agree to be permanently enjoined from entering into, forming, organizing or reorganizing into any partnership, corporation, sole proprietorship or any other legal structures, for the purpose of avoiding compliance with the terms or this Consent Judgment.

14. Defendants agree to the judgment amount of \$20,000.00 in civil penalties, pursuant to K.S.A. §50-632.

15. The parties agree that the Court sequestered approximately \$40,000.00 of the defendants' funds on August 24, 2000 in Central National Bank (specifically, in accounts no. #4347145, held by Top Secrets, Inc.; #4347153, held by Top Secrets, Inc.; #4347161, held by Top Secrets, Inc.; #4347463, held by Top Secrets, Inc.; #4347927, held by Secret Source, Inc.; and #5956196, held by Thomas M. Michaels. Parties agree that Defendant have no interest in said funds and recognize that any issue as to the party(s) entitled to said funds exists solely between the Attorney General and the Trustee of the U.S. Bankruptcy Court.

16. Jurisdiction is retained by this Court for the purpose of enabling any of the parties to this Consent Judgment to apply to this Court at any time for such further orders and directions as may be necessary or appropriate for the modification of any of the provisions hereof, for the enforcement of compliance herewith, and for the punishment of violations thereof.

17. If any portion, provision, or part of this Consent Judgment is held to be invalid, unenforceable, or void for any reason whatsoever, that portion shall be severed from the remainder and shall not affect the validity or enforceability of the remaining provisions, portions or parts.

18. Compliance with this Consent Judgment does not relieve Defendants of any obligation imposed by applicable federal, state, or local law, nor shall the Attorney General be precluded from taking appropriate legal action to enforce civil or criminal statutes under her jurisdiction.

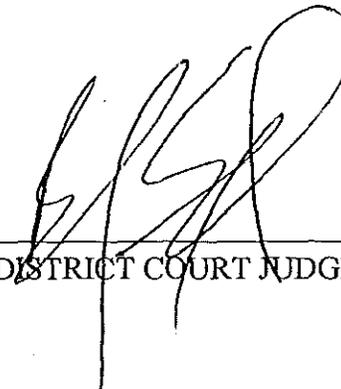
19. The parties understand that this Consent Judgment shall not be construed as an approval of or sanction by the Attorney General of the business practices of Defendants nor shall Defendants represent the decree as such an approval. The parties further understand that any failure by the State of Kansas or by the Attorney General to take any action in response to any information submitted pursuant to the Consent Judgment shall not be construed as an approval of or sanction of any representations, acts or practices indicated by such information, nor shall it preclude action thereon at a later date.

IT IS THEREFORE ORDERED, ADJUDGED AND DECREED that the stipulation and agreement of the parties contained herein are adopted and approved as the findings of fact and conclusions of law of the Court and any monies owed hereunder by Defendants immediately become a judgment upon filing.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that judgment is entered against Defendants in favor Plaintiff in the amount of \$ 20,000.00.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED that pursuant to the Kansas Consumer Protection Act, and the provisions of K.S.A. §50-632(b), the Court hereby approves the terms of the Consent Judgment and adopts the same as the order of the Court.

IT IS SO ORDERED.

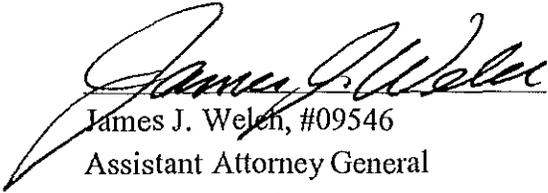

DISTRICT COURT JUDGE

Approved by:


Carla J. Stovall, #01433

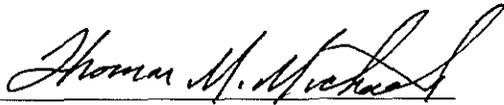
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