STATE OF SOUTH CAROLINA	)	BEFORE THE ADMINISTRATOR
	)	SOUTH CAROLINA DEPARTMENT
COUNTY OF RICHLAND	)	OF CONSUMER AFFAIRS
THE SOUTH CAROLINA DEPARTMENT OF CONSUMER AFFAIRS,	)	DOCKET NO. 0234
PETITIONER,	)	
	)	**ORDER**
VS.	)	
LHQ, INC., D/B/A LADIES HEALTHQUEST AND JOHN C. LUCAS & MARIA C. LUCAS, INDIVIDUALLY,	)	
RESPONDENTS.	)	

STATEMENT OF THE CASE

This matter came before me on Petition of the Staff alleging *inter alia* that the Respondents had failed to refund monies and/or cancel membership agreements of affected consumers after Respondents' Lexington location of Ladies HealthQuest had closed without notice; whether Respondents' bond should be assessed to compensate the affected consumers; whether Respondents' remaining location in St Andrews should be allowed to continue operation; and whether Respondents should be assessed an administrative fine.

The Petitioner represented by its attorney Helen Fennell presented its case on September 26, 2002. The Respondents were represented at the hearing by Henry McKellar, Esq.

A second hearing was scheduled for October 10, 2002, for the Respondents's case. At this hearing the respective parties, above, mutually agreed to continue negotiations to settle some issues

in this case, including but not limited to, refunds and cancellations, in lieu of the Respondents preceding with their case. A Preliminary Order was issued on October 14, 2002, retaining Philip S. Porter former Administrator as the designated hearing officer should a final hearing be necessary. A final hearing was held on January 8, 2003. The Respondents did not attend the final hearing.

This matter was commenced pursuant to a Notice of Hearing and Petition served on Respondents on or about August 20, 2002 (Exhibit 1). The Petition alleges that Respondent Ladies HealthQuest ("LHQ") and John C. and Maria C. Lucas individually as owners of LHQ had engaged in false, fraudulent or deceptive conduct in continuing to solicit and sell two year paid in full memberships up to the closure of its business in Lexington. Petitioner alleged further that the Lexington location of LHQ had in fact closed, resulting in consumer complaints from individuals no longer able to take advantage of health club services they had paid for. The Petitioner further alleged that LHQ was covered by a special deposit bond, MB003006682 issued by the Cumberland Casualty Company in the amount of twenty five thousand ($25,000.00) dollars to reimburse consumers who might have claims and that the bond should be assessed to reimburse those consumers. The hearing on September 26, 2002 was attended by Ms. Sylvia Beaver and her counsel, Paul D. deHolczer of the law firm of Moses Koon & Brackett, PC (who attended in the absence of Wm. Bert Brannon). Ms. Beaver, as was explained by counsel, was the owner of the mall property at which the Lexington location had operated. At the time, she was attempting to make a health center available there under the name Carolina Girls Health and Fitness Clubs, LLC ("Carolina Girls"). To further complicate this matter, it appears that an out of state acceptance company, Affiliated Acceptance Corporation ("AAC") was at the time of the hearing, and for all appearances is still taking draft payments from some of the members of LHQ (Exhibits 14, 15). Petitioner argued throughout both hearings that the

installment contracts were in the nature of personal services contracts, and thus consumers could not be compelled to continue the drafts or have them diverted to a third party. In the hearing on January 8, 2003, Mr. Brannon, without arguing the legal point, stated that Carolina Girls had been allowing former LHQ prepaid customers to workout at its facilities without charge as a service to the community, and if that practice is to continue, the viability of the ongoing health club Carolina Girls will to some extent depend on cash flow from the drafts being paid through Affiliated Acceptance Corporation.

FINDINGS OF FACT

Based on evidence presented by staff at the hearing, I make the following findings of fact:

1.) Respondents were originally served with the Notice of Hearing by Certified Mail and regular mail on or about August 20, 2002. (Exhibit 1).

2.) Respondents are a physical fitness facility engaged in offering physical fitness services as defined in *S.C. Code Ann.* §§ 44-79-20. They held Certificates of Authority to do business as a physical fitness provider from May 21, 2002 to December 30, 2002. (Exhibits 4, 5, 6, 13 and Testimony of Morris, Owens, Wilson, Love, Nance, Dorman). They held Certificates of Authority to do business as a physical fitness provider from May 21, 2002 to December 30, 2002 for locations at 929 North Lake Drive, Lexington and 75 93 St. Andrews Road, Irmo, S. C. (Exhibit 4).

3.) The record shows convincingly that LHQ was a company with financial trouble as well as one with ongoing compliance problems. (Testimony of Morris, Owens, Wilson , Love, Nance and Dorman; Exhibits 3, 8 -13). It closed its doors in Lexington temporarily from approximately January through March of 2002, and was served with ejectment papers for nonpayment of rent July 23, 2002.

(Exhibits 12 and 13). By the time of the January 8, 2003 hearing, a writ of ejectment had been filed for its Irmo location. (Exhibit 19).

4.) As a result of Respondents' default, as many as nine hundred customers were left unable to use services they had paid for or were paying for. (Testimony of Morris). Certain of them sought damages from the Magistrate's Court. (Exhibits 8 and 9). Others were either paid in full or were continuing to be drafted through AAC. (Exhibits 14 and 15). The total number of persons in each category is not clear in the record.

CONCLUSIONS OF LAW

Based on evidence presented by Petitioner at the hearing, I make the following conclusions of law:

1.) The Department has jurisdiction over this matter pursuant to the South Carolina Physical Fitness Services Act, *S.C. Code Ann.* § 44-79-10, *et seq*. (Supp. 2001).

2.) Respondents were timely and properly served with the Notice of Hearing in this matter, pursuant to *S.C. Code Ann*. §1-23-320(a) (Supp. 2001).

3.) Respondents have violated the Physical Fitness Services Act in, but not necessarily limited to the following particulars:

a.) By contracting to provide physical fitness services for a term longer than twenty four months, in violation of Section 44-79-40 by use of time extensions and "free" offers. (Exhibit 3).

b.) By engaging in false, fraudulent or deceptive conduct in dealings with consumers by selling cash memberships up to the time Respondents' closed the Lexington location, in violation of Section 44-79-80 (8). (Exhibit 7).

c.) By failing to maintain its two locations for which it had a Certificate of Authority for the use of individuals to whom it sold memberships, and refund unearned portions of the prepaid customers. (Exhibits 4-13, Testimony of Morris, Owens, Wilson, Nance and Dorman). While this is not technically a violation of any express prohibition of the Physical Fitness Services Act, this failure is the prerequisite for accessing the bond in *S. C. Code Ann*. § 44-79-80.

IT IS THEREFORE ORDERED, that Respondents, its agents, assigns or successors in interest:

(1) Cease and desist from soliciting or negotiating with the public contracts or memberships to a physical fitness service business that exceed twenty four months in length, whether by way of gift certificates, "free" offers or any other scheme or device whatever, purporting to allow the consumers membership or contract to exceed twenty four months in duration;

(2) Cease and desist from offering, negotiating or soliciting physical fitness services of any description to the public;

(3) Provide copies of membership contracts for the Irmo and the Lexington locations for the last three years to Petitioner;

IT IS FURTHER ORDERED that:

(1.) Respondents' bond, # MB003006682 issued by Cumberland Casualty Company be assessed in the full amount of twenty-five thousand ($25,000.00) dollars and that the Cumberland Casualty Company be so notified by copy of this Order;

(2.) The Department hold monies from said bond for a period of two years until the Department can determine whether additional, yet unknown consumers may have been affected during the term of the Bond;

(3.) That the Respondents pay an administrative fine of fifteen hundred ($1,500.00) dollars for violating the Physical Fitness Services Act as set forth above. Should the bond be insufficient to pay the claims of customers of the Respondents as set forth below, the bond will be exhausted in paying the claims of customers.

(4.) Should the bond be sufficient to pay the claims of customers and the above referenced fine, any overage is to be returned to the Cumberland Casualty Company.

Additional matters are worth noting here. It appears that some of the relief requested by Petitioner has become moot. Inasmuch as the Certificate of Authority has expired, and Respondents have not renewed their Certificate, revocation or suspension of the Certificate is unnecessary. Petitioner also argued that in this case the physical fitness contracts of the customers were in the nature of personal service contracts not susceptible to being assigned to a third party and remain binding on the physical fitness customer. I so find based on the cases cited in Petitioner's memorandum of law. I note further, as pointed out in the memorandum, that the Respondent's own contract contained a cancellation and transferability clause that prohibits the membership from being transferred. Moreover, it appears in the record there was more than one period of substantial breach of Respondent's obligation to provide physical fitness services even if I concluded that the duty to perform the contracts were otherwise freely assignable.

Nevertheless, Mr. Brannon stated that Carolina Girls has been operating a working physical fitness facility at the former LHQ location in Lexington since early September, allowing former LHQ paid in full members to work out without charge for the balance of the term of their LHQ contract. He said Carolina Girls had operated without receiving any payments from any former LHQ monthly draft customers even those who were working out at Carolina Girls. He also said Carolina Girls would endeavor to maintain a working physical fitness facility through the month of January, 2003 at the Irmo location of Respondent. He further stated that the feasibility of maintaining the center or centers to a large extent hinged on whether the new center, Carolina Girls could continue to use the cash flow from drafts continuing to go through AAC. This statement was unsworn, but I give it credibility coming from an officer of the court. While recognizing that personal services contracts are not freely assignable should the customer object, simple mathematics of this case show that if customers depend solely on

the bond for relief, and if there are claims from as many as nine hundred members, the maximum the bond would pay per person would a little over twenty seven dollars, when many have prepaid in the range of six hundred to seven hundred dollars. Clearly, if there is an alternate method that would do more good for more people, it should be explored.

It appears that Carolina Girls was open for business and accepting Respondent's members as of no later than early September 2002. (Testimony of Dorman). Certain of the customers have already complained to the Department or the magistrate. Some have apparently determined that use of the Carolina Girls facility is their best option. Notwithstanding that the contracts are not assignable, it is reasonable to assume that customers not happy with the current situation will complain to Carolina Girls or the Department or to the courts, and that those using the Carolina Girls facilities currently are not in a position to complain of a loss other than during the time periods in which neither facility was open.

For the guidance of the Petitioner and Carolina Girls, any customer wishing to cancel the AAC draft may do so and will be dealt with as they file a complaint, either to the Department or Carolina Girls. The Department will also query the Better Business Bureau within two weeks from the signing of this Order, and if complaints are made to the BBB, they will be eligible for the same treatment. Cancellation will be deemed effective as of the time of the filing of the complaint, and the customer will be told that the Carolina Girls/AAC will cancel their draft as of that time. If a lawsuit has been filed within the next sixty days, or there are customers who have previously requested the draft be stopped and the request has not yet been honored, the refunds must be made from the time of the complaint, unless the customer continued to use Carolina Girls services after the compliant. If the customer continued to use Carolina Girls services after making a complaint, Carolina Girls will either convince

the member to sign a new contract with Carolina Girls, or honor the request to cancel from a time no later than two weeks after this Order is final.

Carolina Girls is free to approach former members of Respondent and seek to have them sign new contracts with Carolina Girls. The Department will forbear asserting any liability on the part of Ms. Beaver or Carolina Girls with respect to any electronic drafts which may have been forwarded to it by AAC during periods that Carolina Girls was open for business and honoring Respondents' memberships, except as specifically set forth above. The Department will not object to the release of escrowed electronic drafts to Carolina Girls for those former members of Respondents who sign new contracts with Carolina Girls. The Department will not object to the release of escrowed electronic drafts from former members of Respondents who have not complained to the Department. Such former members will be eligible for claims against the bond, but refunds will not be made for any time periods in which Respondents or Carolina Girls were open for business at the location the customer had contracted with. There are also an unknown number of former LHQ electronic or monthly draft customers whose accounts were delinquent or in collections at the time the LHQ facilities ceased operating. Mr. Brannon stated that Carolina Girls has no interest in such accounts as they do not involve customers who are current or actively working out.

In exchange for these terms, Carolina Girls and Ms. Beaver, though not a party to this action, will be a signatory to this Order and bound to its terms as a matter of contract. Carolina Girls will continue to honor Respondents' paid in full contracts, for the term of the contract, at any location for which it accepts electronic drafts initiated by Respondent's agreement or contract with AAC.

Regarding the Bond, I further rule that:

1.) The Bond will be assessed on a pro rata basis in descending order of priority below set forth. If the bond is found insufficient to fully cover all claims, it will be exhausted to pay each succeeding class before any money is provided to the next lower class:

a.) Pre-paid memberships written at or near (within forty-five days) of the time of Lexington closure or Irmo change of ownership;

b.) Pre-paid memberships written within a calendar year of Lexington closure or Irmo change of ownership;

c.) Lexington members who are eligible to be refunded for the three month period when the center closed and later reopened;

d.) Lexington members who are eligible to be refunded for the period between August and September when the center closed and had not yet reopened as Carolina Girls; and

e.) The fine above assessed for at least partial reimbursement to the Department for the expenses of this case.

f.) Should Carolina Girls close or refuse to honor prepaid memberships of Respondents during the term of membership, such Ladies HealthQuest members who have not yet complained will be put in the priority they would have been in a.) through d.) above had they complained.

2.) Notwithstanding, f.), above, should Carolina Girls close, it will be solely responsible to make refunds from its own posted bonded on any pre-paid contracts it has written initially or accepted through written reformation/rescission of a former Ladies HealthQuest member contract.

3.) The Department will hold the bond money for a period of two years should any money be available after current complaints are satisfied.

IT IS FURTHER ORDERED that no consumer is entitled to a refund from the bond for periods of time in excess of two years that Respondents may have contracted for in contravention of the

Physical Fitness Services Act, nor is Carolina Girls obligated to honor memberships Respondents may have written for period in excess of twenty four months. Likewise, no consumer is entitled to a refund from the bond who cannot show she complained to the Department, Carolina Girls, the Better Business Bureau or a court. Nevertheless, any customer who can show that she made a timely complaint but it has not yet been acted on, Carolina Girls will be required to refund moneys from the time the complaint was made if it was released by AAC to Carolina Girls.

Regarding those Ladies HealthQuest customers who have complained and whose complaints are unresolved or who have not already signed an agreement with Carolina Girls, the Staff will prepare a mailing informing these members a.) they can work out at Carolina Girls, or if they do not choose to go to Carolina Girls they will be put in a pool that is eligible for refunds, but that it is also already reasonably clear not all individuals will get full refunds, if any, b.) that even if they receive a refund, they will not receive it for six to eight months, and c.) that if they wish to go to Carolina Girls they should contact Carolina Girls within two weeks. A copy of the letter and a list of those Ladies HealthQuest customers to whom it is sent shall be provided to Carolina Girls to ensure that all parties are aware of the status of all complaints.

IT IS FURTHER ORDERED that Respondents and Ms. Beaver/Carolina Girls shall give reasonable access to their records for purposes of fully identifying customers and for proof of compliance with this Order. I retain jurisdiction for any further proceedings necessary to implement this Order and to supplement it with page citations should any party appeal and transcription from videotape be necessary.

IT IS SO ORDERED.

/s/
Philip S. Porter, Esq.
Designated Hearing Officer
South Carolina Department of
Consumer Affairs

_____, 2003
Columbia, South Carolina

/s/
Wm. Bert Brannon, Esq
Moses Koon & Brackett, PC
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Attorney for Carolina Girls Health and
Fitness Clubs, LLC

_____
Date

/s/
Helen Fennell, Esq.
Attorney for Petitioner
South Carolina Department
of Consumer Affairs

_____
Date