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State Attorneys General Seek to Clarify the Negative Option Marketing Regulatory Scheme

BY [ANNA ANTONOVA](#)/ ON JANUARY 29, 2020



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Everyone loves a free trial... until you are caught in a perpetual billing cycle of paying for goods or services that you did not know you ordered.

Regulators call it negative option marketing.^[1] Advertisers refer to it as “advanced consent arrangements.”^[2] According to the Federal Trade Commission (FTC), it is a “common form of marketing where the absence of affirmative consumer action constitutes assent to be charged for goods or services.”^[3] Negative option marketing is once again under scrutiny by the FTC and state Attorneys General. Marketers, advertisers and businesses in all industries should stay abreast of the legal developments to remain compliant with a growing number of regulations that may affect the way they engage with their consumers.

Future expansion of current negative option laws is likely. The current legal framework does not adequately protect consumers and is increasingly confusing for marketers to comply with. Both consumer and business interests will welcome greater consistency and clarity.

FTC classifies negative option marketing into four categories: prenotification plans^[4] (e.g. book-of-the-month-club), continuity plans^[5] (e.g., bottled water delivery), automatic renewals^[6] (e.g., a magazine subscriptions) and trial conversion plans.^[7] Prenotification plans are the only category of negative option marketing currently covered by the FTC's Negative Option Rule, which requires sellers to "clearly and conspicuously disclose their plan's material terms before consumers subscribe"^[8] and enumerates seven material terms.^[9]

Current Regulatory Scheme Governing Negative Option Marketing

In its October 2019 Advance Notice of Proposed Rulemaking, the FTC solicited public comments about the Negative Option Rule and the existing "patchwork" of other laws and regulations that govern negative option marketing.^[10] In addition to the Negative Option Rule, the FTC's arsenal of enforcement tools includes Restore Online Shoppers' Confidence Act (ROSCA),^[11] which is designed to address issues with negative option marketing on the internet, and the Telemarketing Sales Rule (TSR),^[12] which prohibits deceptive acts over the telephone. The Postal Reorganization Act^[13] and the Electronic Fund Transfer Act (EFTA)^[14] also apply to negative option marketing in certain contexts. Finally, Section 5(a) of the FTC Act makes unfair or deceptive acts or practices in or affecting commerce unlawful^[15] and is relied upon for conduct that is not squarely within one of the other laws.

The Negative Option Rule, substantively unchanged since it was first promulgated in 1973, was last under FTC review in 2014.^[16] ROSCA and the TSR have recently been enacted and promised to address abuses in negative option marketing.^[17] The Commission decided to observe the effect of these laws before amending the Negative Option Rule.^[18] Five years later, the problems persist that the Commission was seeking to address.^[19] Accordingly, the FTC is once again surveying its regulation of the practice.

Growth of the Subscription Economy

According to one study, sales of online subscriptions increased by over 100% each year between 2012 and 2017, with sales reaching \$2.7 billion by 2017.^[20] 46% of the consumers surveyed reported subscribing to media streaming services such as Hulu, Netflix or Spotify.^[21] Across the various types of subscriptions (products and services), the median number of subscriptions an active subscriber holds was two, but almost 35% have three or more.^[22] Revenues from U.S. music digital streaming services reached \$8.6 billion in 2018, and the number of paid subscriptions in the U.S. alone is expected to reach nearly 115 million by 2025.^[23]

Corresponding to the rapidly growing subscription sector is an escalation in consumer complaints. Better Business Bureau (BBB) reports that it received 36,986 complaints pertaining to free trial marketing alone between 2015 and 2017.^[24] In the same time period, FBI's Internet Crime Complaint Center (IC3) received 6,151 complaints about free trial offers, with losses of \$15.2 million.^[25] Truth in Advertising, Inc. (TINA) suggests this growth of consumer dissatisfaction with negative option marketing is "likely exacerbated, in part, by increasing rates of digitization: without a physical item, like a book, arriving in the mail, or paying by writing a check, the only indication a consumer may have of a long-forgotten, converted subscription is an ambiguously labeled, recurring charge on their credit card."^[26] This issue is especially important for providers of entertainment services such as music, video or game streaming because the subscription does not usually include a physical item to serve as a reminder.

Since FTC's last review of the Negative Option Rule, the Commission initiated more than 20 cases involving negative option plans. In 14 of the resolved FTC cases, victims lost \$1.3 billion.^[27] The actual losses are likely considerably higher, as less than 10% of fraud victims report their losses.^[28] State enforcement actions involving the practice have also increased.^[29] For example, since 2010, New York has reached 23 negative option settlements, obtaining over \$10 million in consumer restitution and over \$14 million in penalties, costs and fees.^[30] Multi-state investigations are also on the rise. Sirius XM Radio, Inc. reached a \$3.8 million settlement with 45 states and the District of Columbia following a multi-state investigation concerning its cancellation and renewal practices.^[31] Finally, more than 100 federal class actions have been filed since 2014 on behalf of consumers complaining about various negative option terms and conditions.^[32]

Perspectives on Regulation of Negative Option Marketing

State Attorneys General and consumer advocates are seeking an expansion of the regulation, citing a lack of consistency among the various laws and regulations. Many of the existing tools address separate commercial channels (internet, telephone, postal mail) and impose different standards. Particularly problematic for these advocates is the fact that the Negative Option Rule only applies to prenotification plans and does not cover some of the "rampant" "deceptive practices occurring in the marketplace" such as trial conversions.^[33] Another perceived weakness of the scheme is that ROSCA lacks specificity as to how informed consent should be obtained or how clear and conspicuous disclosures should be made.^[34] For example, proponents of increased regulation find ambiguous ROSCA's requirement for "a simple mechanism" for cancellation, which results in roadblocks when consumers attempt to effectuate a cancellation and obtain a refund.^[35]

The proposal of a coalition of 23 state Attorneys General calls for an implementation of separate informed consent after completion of a free trial, before charging for goods or services.^[36] According to this proposal, consumers enrolled in negative option plans should

receive mandatory periodic notices that disclose the timing, amount, and method by which the seller bills the consumer for the renewal, and that includes a convenient method to cancel.^[37] The coalition advocates for a simple cancellation process by which consumers may cancel their memberships using the same method they used to enroll in a program.^[38] Finally, the state Attorneys General promote issuance of refunds for charges after the free trial has ended to consumers who are unwittingly enrolled in negative option plans.^[39]

Businesses are divided on this issue. Some businesses believe that the current framework adequately meets consumer protection goals while striking the right balance of deterring bad conduct and empowering businesses to provide innovative marketing arrangements to consumers.^[40] The Association of National Advertisers (ANA), the Entertainment Software Association (ESA) and the Internet Association (IA) do not perceive a discernible gap in regulatory coverage because Section 5 of the FTC Act authorizes the FTC and state Attorneys General to bring lawsuits against businesses engaging in unfair or deceptive acts or practices to deter conduct that does not fall within the purview of ROSCA, the TSR, or the Negative Option Rule.^[41]

The ANA argues that extending the scope of the Rule would not prevent bad and dishonest actors from behaving unfairly or deceptively in the marketplace, but likely would adversely impact consumers and legitimate marketers by burdening them with extended regulation.^[42] The ANA states that these negative option plans provide substantial benefits to both consumers and businesses, allowing consumers to enjoy the convenience and certainty of uninterrupted service, lower prices or opportunities to try new and unfamiliar products.^[43] Sellers, on the other hand, can increase revenue through savings generated by the ability to effectively manage inventory and avoid renewal costs.^[44] Furthermore, given the popularity of the subscription models, consumers are willing and sophisticated participants^[45] who are familiar with various negative option plans and embrace their benefits.^[46]

These commentators are concerned that new regulations would impose standardization that would be unworkable across all industries, media, and technology.^[47] For example, the ESA argues that the multi-media environment of games makes subscription enrollment and management possible through various account management features across devices and platforms that offer different user experiences.^[48] They believe that the regulatory framework should (and currently does) provide clear standards, but allow for sufficient flexibility to adapt the law to the evolving technology and marketing innovations.

A more moderate business view shares much of these concerns regarding regulatory standardization but favors a more uniform framework. For example, Performance-Driven Marketing Institute (PDMI) finds compliance with the legal “patchwork” increasingly burdensome, especially for the small businesses and start-ups without a large legal team

monitor the shifting regulatory landscape.[\[49\]](#) In addition to the federal laws, this group is concerned about the growing number of state laws that regulate negative option billing.[\[50\]](#) Half of the states have enacted laws that specifically address negative option billing.[\[51\]](#) Recently, Mastercard and Visa established rules that govern negative option offers that apply to merchants accepting these methods of payment.[\[52\]](#)

These laws and rules vary significantly in scope, requirements, and category of products to which they apply,[\[53\]](#) making it difficult for businesses that operate in many states (as most online businesses do) to comply with all. Businesses either need to design different order pathways and disclosures for consumers in different states, or create one order experience that complies with the most restrictive law.[\[54\]](#) Some businesses and marketers would welcome federal preemption rather than having to comply with dozens of different rules.

Looking Ahead

Negative option billing is likely to continue to be the subject of investigations and lawsuits brought by state Attorneys General. In 2019, states' top legal officers have been increasingly active in regulation and enforcement of various aspects of marketing and advertising, often setting precedent and garnering record settlements.[\[55\]](#) As the Sirius XM settlement demonstrates[\[56\]](#), state Attorneys General have an appetite for regulating negative option marketing practices as well and have brought these actions individually and in multi-state coalitions.[\[57\]](#) A growing number of states are enacting laws that specifically govern this marketing practice that the state Attorneys General are tasked with enforcing, but most states' Unfair or Deceptive Acts and Practices (UDAP) laws can apply in the absence of specific negative option regulation.

State Attorneys General are well-positioned to hold businesses accountable for deceptive practices. Their subpoena power authorizes them to conduct discovery during an investigation and reach a settlement without ever filing a complaint.[\[58\]](#) Moreover, the precedent set by state Attorneys General can help shift best practices towards greater consumer protections.[\[59\]](#) FTC is more likely to embrace evolving consumer protection norms if they reflect existing best practices established by the states.[\[60\]](#) Because of their effectiveness in quickly obtaining restitution for their harmed citizens and their norm-setting influence over the FTC, state Attorneys General are likely to continue to bring actions surrounding negative option marketing.

Long-term, the FTC is likely to make some amends to the regulatory framework governing negative option marketing. In 2014, the Commission declined to expand or enhance the Negative Option Rule in the hopes that ROSCA and the TSR would adequately address existing issues.[\[61\]](#) The Commission stated that it would continue to monitor the marketplace and would consider whether changes in the marketplace warrant reevaluation.[\[62\]](#) Five years

later, the FTC believes that there is “prevalent, unabated consumer harm in the marketplace involving negative option marketing.”^[63]

Both marketers and consumers should welcome regulatory change in this area. Although the FTC is facing a challenging task in balancing the consumer interests with needs of evolving businesses, a sensible solution is achievable since both sides benefit from greater clarity and uniformity. A more uniform regulatory scheme will make compliance with the law easier, and improved consistency will clarify what conduct is required for compliance. A standard-based rule that covers all types of negative option marketing but allows flexibility to adapt to changing times is likely to satisfy both interests. FTC can support these standards with issuance of periodic guidelines to provide greater clarity to businesses, as well as by offering consumer education.

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^[1] Advanced Notice of Proposed Rulemaking; Request for Public Comment on the Rule Concerning the Use of Prenotification Negative Option Plans, 84 Fed. Reg. 52,393 (Oct. 2, 2019) [hereinafter FTC Notice].

^[2] Ass’n of Nat’l Advertisers, Comment Letter on the Rule Concerning the Use of Prenotification Negative Option Plans Review, 16 CFR part 425, Project No. P064202 (Dec. 2, 2019) [hereinafter ANA Comment Letter], <https://www.regulations.gov/document?D=FTC-2019-0082-0008>.

^[3] FTC Notice, *supra* note 1 at 52,394.

^[4] *Id.* (“[S]ellers send periodic notices offering goods to participating consumers and then send—and charge for—those goods only if the consumers take no action to decline the offer. The periodic announcements and shipments can continue indefinitely.”).

^[5] *Id.* (“In continuity plans, consumers agree in advance to receive periodic shipments of goods or provision of services . . . which they continue to receive until they cancel the agreement.”).

[6] *Id.* (“In automatic renewals, sellers . . . automatically renew consumers’ subscriptions when they expire and charge for them, unless consumers affirmatively cancel the subscriptions.”).

[7] *Id.* (“[I]n free-to-pay or nominal-fee-to-pay plans, consumers receive goods or services for free (or at a nominal fee) for a trial period. After the trial period, sellers automatically begin charging a fee (or higher fee) unless consumers affirmatively cancel or return the goods or services.”).

[8] Rule Concerning the Use of Prenotification Negative Option Plans, 16 C.F.R. pt. 425. [hereinafter Negative Option Rule].

[9] FTC Notice, *supra* note 1, at 52,394. (Enumerated material terms include: “(1) How subscribers must notify the seller if they do not wish to purchase the selection; (2) any minimum purchase obligations; (3) the subscribers’ right to cancel; (4) whether billing charges include postage and handling; (5) that subscribers have at least ten days to reject a selection; (6) that if any subscriber is not given ten days to reject a selection, the seller will credit the return of the selection and postage to return the selection, along with shipping and handling; and (7) the frequency with which announcements and forms will be sent.”).

[10] *Id.* at 52,396.

[11] 15 U.S.C. §§ 8401–8405.

[12] 16 C.F.R. pt. 310.

[13] 39 U.S.C. § 3009 (Also referred to as the Unordered Merchandise Statute).

[14] 15 U.S.C. §§ 1693–1693r.

[15] 15 U.S.C. § 45(a)(1).

[16] Pa. Office of Att’y Gen., Comment Letter, State Attorneys General Negative Option Rule (16 C.F.R. Part 425) (Project No. P064202); Advance Notice of Proposed Rulemaking: Request for Public Comment, 84 Fed. Reg. 52393-01, 2019 at 1 (Dec. 2, 2019) [hereinafter Att’y Gen. Comment Letter], <https://www.regulations.gov/document?D=FTC-2019-0082-0012>.

[17] *Id.* at 2.

[18] *Id.*

[19] *Id.*

[20] *Thinking Inside the Subscription Box: New Research on E-commerce Consumers*, McKinsey & Company (Feb. 2018) (Data only includes subscriptions for products),

<https://www.mckinsey.com/industries/technology-media-and-telecommunications/our-insights/thinking-inside-the-subscription-bo-new-research-on-ecommerce-consumers>.

[21] *Id.*

[22] *Id.*

[23] Digital Media Ass'n, Comment Letter on 16 CFR Part 425 — Negative Option Rule, Project No. P064202 (Dec. 2, 2019), <https://www.regulations.gov/document?D=FTC-2019-0082-0015>.

[24] Better Bus. Bureau, Subscription Traps and Deceptive Free Trials Scam Millions with Misleading Ads and Fake Celebrity Endorsements at 2 (Dec. 2018) [hereinafter BBB Report], https://www.bbb.org/globalassets/local-bbbs/st-louis-mo-142/st_louis_mo_142/studies/bbb-study-free-trial-offers-and-subscription-traps.pdf.

[25] *Id.*

[26] Truth in Advertising, Inc., Comment Letter, The FTC Should Update Its Negative Option Rule at 2, n.3 (Dec. 2, 2019) [hereinafter TINA Comment Letter], <https://www.regulations.gov/document?D=FTC-2019-0082-0014>.

[27] BBB Report, *supra* note 24.

[28] TINA Comment Letter, *supra* note 26, at 2.

[29] Att'y Gen. Comment Letter, *supra* note 16, at 3.

[30] *Id.*

[31] *Id.*

[32] TINA Comment Letter, *supra* note 26, at 2.

[33] Att'y Gen. Comment Letter, *supra* note 16, at 6-7.

[34] *Id.* at 2.

[35] *Id.*

[36] *Id.* at 8-9.

[37] *Id.* at 9.

[38] *Id.* at 10-11.

[39] *Id.* at 11.

[40] ANA Comment Letter, *supra* note 2, at 6.

[41] *Id.* at 5; See also Entm't Software Ass'n & Internet Ass'n, Comment Letter, 16 CFR Part 425 –Negative Option Rule, Project No. PO642 2, at 2 (Dec. 2, 2019) [hereinafter ESA Comment Letter], <https://www.regulations.gov/document?D=FTC-2019-0082-0011> (“Congress, the FTC, and the states have provided marketers with an abundance of laws, regulations, and case precedents to provide consumers with clear and conspicuous disclosures about the terms of a negative option offer, obtain affirmative consent to the offer, and provide an easy and simple means to cancel the arrangement.”).

[42] ANA Comment Letter, *supra* note 2, at 5.

[43] *Id.* at 6; ESA Comment Letter, *supra* note 41, at 2.

[44] Wang, Sophia, *One Size Does Not Fit All: The Shortcomings of Current Negative Option Legislation*, 26 Cornell J. L. & Pub. Pol’y 197, at 200 (Fall 2016).

[45] ESA Comment Letter, *supra* note 41, at 2.

[46] Performance-Driven Marketing Institute, Comment Letter, Negative Option Rule (16 CFR part 425) (Project No. P064202) at 3 (Dec. 2, 2019) [hereinafter PDMI Comment Letter], <https://www.regulations.gov/document?D=FTC-2019-0082-0018>.

[47] ESA Comment Letter, *supra* note 41, at 2.

[48] *Id.* at 8.

[49] PDMI Comment Letter, *supra* note 46, at 4.

[50] *Id.*

[51] TINA Comment Letter, *supra* note 26, at 3.

[52] Paul Petta, *Free Trials Without The Hassle*, Mastercard: Beyond The Transaction (Jan. 16, 2019), <https://newsroom.mastercard.com/2019/01/16/free-trials-without-the-hassle/>; Visa Bus. News, Updated Policy for Subscription Merchants Offering Free Trials or Introductory Promotions (June 20, 2019), <https://usa.visa.com/dam/VCOM/global/support-legal/documents/subscription-merchants-visa-public.pdf>.

[53] TINA Comment Letter, *supra* note 26, at 3.

[54] PDMI Comment Letter, *supra* note 46, at 3.

[55] See e.g., Press Release, N.Y. State Office of the Att’y Gen., Attorney General James Announces Groundbreaking Settlement With Sellers Of Fake Followers And “Likes” On Social Media (Jan. 20, 2019) (announcing New York State’s settlement with Devumi LLC marked the first finding by a law enforcement agency that the sale of fake social media engagement constitutes illegal activity), <https://ag.ny.gov/press-release/2019/attorney-general-james-announces-groundbreaking-settlement-sellers-fake-followers>; Press Release, N.Y. State Office of the Att’y Gen., AG James: Google And Youtube To Pay Record Figure For Illegally Tracking And Collecting Personal Information From Children (Sept. 4, 2019) (announcing a \$170 record settlement between New York State, FTC, YouTube and Google over tracking and serving targeted advertisements to users watching videos directed to children under the age of 13 on YouTube, in violation of Children’s Online Privacy Protection Act), <https://ag.ny.gov/press-release/2019/ag-james-google-and-youtube-pay-record-figure-illegally-tracking-and-collecting>; Bob Christie, *Arizona Sues Juul, 2nd Vaping Firm; Cites Illegal Marketing*, AP News (Jan. 7, 2020) (reporting that the Attorneys general of Arizona, California, Illinois, New York, Minnesota, North Carolina and Washington D.C have filed lawsuits against Juul Labs alleging misleading advertising and marketing targeting youth), <https://apnews.com/089d8b5355e22bb1f56c9713fa23c4d3>; Robert Channick, *Illinois Sues E-cig Maker Juul for Allegedly Targeting Minors*, Chi. Trib. (Dec. 13, 2019), (reporting that Illinois has become the latest state to sue Juul for allegedly misleading advertising and marketing targeting youth) <https://www.chicagotribune.com/business/ct-biz-illinois-ag-sues-juul-20191212-wb3zu6wbqvgxabc7s3dj62gwq6m-story.html>

[56] Att’y Gen. Comment Letter, *supra* note 16, at 3.

[57] *Id.* at 3-4.

[58] Danielle Keats Citron, *The Privacy Policymaking of State Attorneys General*, 92 Notre Dame L. Rev. 747, 761 (2016).

[59] *Id.* at 794.

[60] *Id.* (“Attorneys general serve as ‘connected critics’ to the FTC, they may have a powerful bid for the FTC’s attention.”).

[61] Att’y Gen. Comment Letter, *supra* note 16, at 2.

[62] *Id.*

[63] FTC Notice, *supra* note 1, at 52,396.