Contract Law Update

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FTC Releases Final Rule on Negative Option Practices in Consumer Contracts

On October 16, the Federal Trade Commission (FTC) issued its final rule on negative option marketing practices – arrangements where a company automatically charges a consumer for a product or service unless the consumer takes affirmative actions to reject or cancel the arrangement. The final rule, which applies to all consumer-facing negative option practices regardless of how the initial arrangement is entered into, is intended to prevent unfair and deceptive practices that harm consumers and create unfair competition for legitimate businesses.

Some of the final rule's provisions take effect 60 days after the rule is published in the Federal Register; others, as noted below, take effect 180 days after publication. The rule imposes several requirements on companies whose sales and marketing practices include negative options, such as free trials and automatic renewals, including:

- Prohibiting misrepresentation of any material fact while promoting or offering goods or services for sale using a negative option feature. Material terms include those likely to affect a consumer's choice of, or conduct regarding, goods or services, such as the deadline to prevent or stop a charge or for cancelling, the costs, and the purpose or efficacy of the underlying good or service.
- Requiring clear and conspicuous disclosure of all material terms prior to obtaining a consumer's billing information and charging the consumer. Material terms include that the consumer will be charged for the good or service or that the charges will increase after a trial period, the amount (or range) the consumer will be charged, the frequency of charges, the deadline to stop charges, and the information necessary to find the simple cancellation mechanism. Clear and conspicuous means that disclosures must be easily noticeable and easily understandable by ordinary consumers. (Effective 180 days after publication.)
- Requiring the consumer's express informed consent to the negative option feature before charging the consumer. Express informed consent means the consumer must take an affirmative action, such as inputting the last four digits of the account to be charged for telemarketing sales or, for written agreements, checking a box or signing a line specific to the negative option feature indicating their agreement to the negative option *separately* from any other portion of the transaction. (Effective 180 days after publication.)
- Requiring a simple mechanism enabling the consumer to cancel the negative option feature and immediately stop all recurring charges. The simple mechanism must be available in the same manner the consumer used to agree to the negative option feature, such as online, by phone, or in person. The company must also promptly confirm the cancellation to the consumer and provide a cancellation number or other proof of cancellation. (Effective 180 days after publication.)
- Requiring companies to obtain and maintain verification of each consumer's consent for three years after the initial transaction, unless the company can demonstrate that it has a technological process that makes it impossible for consumers to enroll without providing unambiguously affirmative consent. (Effective 180 days after publication.)

Relation to State Laws

Many states, including California, Colorado, Illinois, New York, Georgia, Virginia and Utah, have already promulgated laws regulating negative option contracts. The FTC rule will only supersede a state statute if there is an inconsistency, and only if the FTC rule is more protective. Where the state statute provides greater protections for consumers, it will not be considered inconsistent with the FTC rule.

Key Takeaways

The final rule represents an expansion of the FTC's authority and enforcement tools to address negative option marketing practices, which have been a persistent source of consumer complaints and litigation. The rule also provides clarity and consistency for companies that use negative option features. Companies that use or plan to use negative option features in their sales and marketing practices should consider the following actions:

- Review existing consumer-facing disclosures in marketing materials and contracts to ensure that the documents meet the FTC rule's requirements. Note, however, that some state laws specifically mandate what the disclosures must look like (with some states even legislating the font size and style!). Ensure the material terms highlighted by the FTC and applicable state laws are included in the disclosures.
- Critically assess the negative option cancellation process to ensure that it is simple to find and submit a cancellation – it needs to be as easy for a consumer to cancel as it was for them to sign up – and that the process at least meets the FTC rule's minimum requirements. Verify that there is a process to provide a consumer with confirmation of their cancelation.
- Review business processes and recordkeeping practices surrounding storage of consents and cancellations. If a company is going to rely on its business processes for capturing consent rather than maintaining each consent for at least three years, it should ensure that it has appropriate documentation showing unequivocal capture of consent for consumers to proceed through its processes.
- Evaluate the potential benefits and risks of using negative option features. While they can provide substantial benefits for companies and consumers, such as greater revenue predictability, customer loyalty, convenience, and cost savings, they can also pose significant risks of legal liability and reputational damage if they are not implemented and managed in a compliant manner.

FOR MORE INFORMATION

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