
Negative Option Billing: Current Practice and Future Concerns: Case Study

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Abstract: Negative option billing is a business practice in which goods or services are provided automatically while the customer must either pay for the service or specifically decline it in advance of billing. With the growing popularity of e-commerce, there has also been a growth of instances where this practice has started with a limited-time free trial, followed by an automatic conversion to being subscribed for a service, with fees deducted automatically from customers' pre-arranged payment account until the customer specifically contacts the vendor to opt out. This study reviews the growth in negative option billing and related marketing practices in the last decade and describes government reactions to curb undesirable or deceptive versions of such practices in the North America and Asia Pacific areas in general. Recognizing their rapid diffusion on the Internet, questionable forms of such practices should be fully understood by marketing professionals, consumers, and government regulatory bodies.

Keywords: negative option billing; free-to-pay subscription conversion; automatic account renewal; consumer information; e-commerce; Asia Pacific.

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A Canadian professional ordered flowers online, using his Visa card, checking a 15% discount offer on his next order of flowers, which was associated with a one-month free trial of an online promotional service. After a month, US\$11.99 was deducted monthly from his credit card, with the entry beginning “TLG*LIVWEL” on the Visa statement. The professional mistook this charge as one his teenager had arranged for with his permission. From month to month, the item had the appearance of plausibility because, after conversion to Canadian dollars, the charge varied between CAD\$11 and \$13. It was some time before this unsuspecting customer questioned the charge. When he did, he found that he could not reach the 1-800 number he'd found on the Web from his home in Canada, nor was his Visa credit card provider able to find any further information than the same 1-800 number. This individual eventually arranged for 1-800-flowers.com to call the 1-800 number from within the U.S. and connect him. The customer service representative on the phone politely informed him that the company's records showed that he had been subscribed for 39 months, but that he had never once used any aspect of the company's services. The customer was then referred to LiveWell's "Proof of Enrollment Department." The manager at that department indicated that the individual had checked off a box on the webpage offer, next to various details of the offer, which included a clause indicating that the party checking the box would be charged US\$11.99 per month until the subscription was cancelled. The manager expressed sympathy, but the best that company policy could allow was to send a check, reimbursing US\$23.98, for the last two monthly payments. An appeal was possible but seemed unlikely to succeed.¹

This vignette provides a detailed example of negative options billing, which is defined as “a business practice in which goods or services are provided

¹ The contact with LiveWell.net occurred in 2011, and the initial signup had occurred in 2008. This vignette records an actual set of events that happened to the first author of this paper.

automatically, and the customer must either pay for the service or specifically decline it in advance of billing.”² Several related marketing practices, commonly deployed on the Internet in conjunction with negative options billing, are also illustrated: automatic free-to-pay conversion (free the first month with an automatic subscription in months thereafter); continuity of service (no break in billing or service, and no need for the customer to opt in to affirm that the customer is aware of and wants the services before billing starts); automatic renewal (at the end of each year, the default is to renew the subscription without the need for the customer to take any action); and data passing (handing-off) to third parties (the customer’s personal data, including address and credit card information, is passed to third parties who are different from the party whose website the customer is responding to).

The main objectives of this short case are to (1) illustrate common negative option billing and related practices; (2) summarize legal and regulatory actions to date that are designed to restrict such practices; (3) review the arguments for and against these practices; and (4) discuss various remedies that have not yet been fully implemented in most countries. Recognizing their rapid diffusion on the Internet, questionable forms of such practices should be recognized and understood by marketing professionals, consumers, and government regulatory bodies.

1 The practice of negative option billing

Over the last decade, public records show that consumers in North America and the Asia-Pacific, in general, have increasingly encountered the marketing practice of negative option billing.

1.1 *Negative option billing in North America*

From the Better Business Bureau and elsewhere on the Internet³, there are numerous reports in the U.S. and Canada of selling practices and related charges to consumers’ credit cards. According to a survey conducted by Visa, “29 percent of U.S. consumers said they have had unauthorized recurring charges on their credit or debit card each month as a result of an offer they accepted online.”⁴ And 35 million consumers have paid \$1.4 billion for marketing offers with a data pass to third parties, according to a 2009 U.S. Senate Commerce

² U.S. Federal Trade Commission – Cable Services Bureau, (1996), In the matter of ML Media Partners, L.P., trading as Multivision Cable TV: Appeal of local rate order of the Cable Telecommunications Joint Powers Agency, memorandum opinion and order, Article 10 (Adopted: August 5, 1996, Released: August 14, 1996).

³ Retrieved from <http://hawaii.bbb.org/deceptive-online-marketing-negative-options/>; retrieved from <http://www.edmonton.bbb.org/article/bbb-media-release---us-judge-freezes-alberta-marketers-assets-29511>.

⁴ Retrieved from <http://corporate.visa.com/media/DMP-Fact-Sheet.pdf>; This source goes on to indicate that “This national survey of 1,000 U.S. adults was conducted online via a web survey host portal between September 8-14, 2009. Respondents were randomly solicited using a permission-based national web panel of tens of millions of American adults with e-mail addresses. Participants were screened to meet quotas that are reflective of the U.S. adult population according to the U.S. Census Bureau. This survey has a margin of error of ±3.1% at the 95% confidence interval.” Also see http://usa.visa.com/personal/security/learn-the-facts/deceptive-marketing.html?ep=v_sym_negativeoption.

Committee staff report.⁵ In fact, the company that billed the individual in the above vignette (or its parent company) has faced several legal actions associated with related practices, including the following:⁶

- On March 7, 2005, the company made a Settlement Agreement with the Office of the Attorney General of Florida. Florida Deceptive and Unfair Trade Practices Act, Chapter 501, Part II, Florida Statutes.⁷
- In July, 2005, the Attorneys General of Connecticut, California, and Maine brought a lawsuit against TLG/Affinion for allegedly deceiving consumers into enrolling in its clubs.⁸
- In December, 2006, Trilegiant/Affinion agreed to pay over \$8 million dollars to 17 states and their residents to settle allegations of deceptive selling practices.⁹
- In August of 2010, Affinion/Trilegiant settled a consumer fraud action brought by the Attorney General of the State of New York for \$8 million USD.¹⁰
- Other examples of related practices with other companies appear in an opinion made to the U.S. Federal Trade Commission by the Attorney General of Vermont on behalf of 20 U.S. states, including the following.¹¹
- A professional couple in Vermont paid over \$750.00 through a joint credit card payment plus \$49.95 monthly increments for a discount plan that neither of them authorized, wanted, or knew they had purchased. The periodic charge was small enough that the couple did not question the bill.
- An Oregon woman ordered what was advertised on the Internet as a "Free Trial Offer" of a teeth whitening product for only \$4.87 shipping and handling and ended up getting charged \$78.41 and enrolled in an auto-ship program.

⁵ "Aggressive Sales Tactics on the Internet and their Impact on American Consumers," staff report, Commerce Committee, U.S. Senate, November 19, 2009. Retrieved from <http://corporate.visa.com/media-center/press-releases/press1011.jsp>.

⁶ Retrieved from http://en.wikipedia.org/wiki/Affinion_Group; Affinion is the parent of Trilegiant, according to this article, and LiveWell.net is a service (and website) offered by Trilegiant (retrieved from <http://www.livewell.net/>). The facts in the four paragraphs that follow were also obtained from this Wikipedia article.

⁷ State of Florida, Office of the Attorney General. "AG Case # L01-3-1484", retrieved from http://www.myfloridalegal.com/Trilegiant_Settlement.pdf.

⁸ CT Attorney General Lawsuit. Connecticut Attorney General's Office, (2005, July 12); retrieved from <http://www.ct.gov/ag/cwp/view.asp?id=A=1949&O=296406>; "CA Attorney General Lawsuit article." Connecticut Attorney General's Office, (2005, July 12); retrieved from <http://ag.ca.gov/newsalerts/release.php?id=1192&year=2005&month=7&PHPSESSID=c9b9f862bab5e75c7aa8b99b322b6587>.

⁹ Chase Bank, Trilegiant, Settle Negative Option Fraud Charges. Retrieved from http://www.consumeraffairs.com/news04/2006/12/trilegiant_chase.html.

¹⁰ Office of the Attorney General of New York, (2010, August 18), Cuomo obtains \$10 million in settlements with companies that tricked consumers into signing up for discount clubs with hidden fees. Retrieved from http://www.ag.ny.gov/media_center/2010/aug/aug18a_10.html.

¹¹ These examples were retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/543809-00098.pdf>, pp. 4-5. Similar opinions were advanced by Colorado and Florida.

- A Maryland consumer reported ordering a "free" bottle of Resveratrol by the Internet and agreeing to pay shipping charges of \$3.95. After the consumer received the shipment, his account was charged \$87.13. The company reported to the consumer that because he did not cancel, he was charged full price.
- A Hawaii man reported that he signed up on the Internet for "free trial" samples of an acai berry supplement and authorized a nominal shipping charge. The company sent him a two-month supply and enrolled him in an auto-ship program. His credit card was charged \$79.90 once a month for three months until he noticed the charges.
- In 2003, an Iowa couple discovered what they believed to be an unauthorized charge on their MasterCard in the amount of \$89.95 for Simple Escapes. Indeed, they ultimately discovered that such charges stretched back to 1998, and totaled \$489.70.
- In 2003, another Iowa couple discovered a \$96.00 charge for "MWI Connections" on their AT&T MasterCard, and complained that the charge was unauthorized. They stated they had no idea what the charge was for until they contacted the company and were told it had to do with entertainment coupons.
- In 2005, an Iowa couple reviewed their bank statement and discovered that \$199.95 had been withdrawn on their debit card the previous month for something called "Essentials." As it turned out, the wife had placed a call to order an unrelated product in 2002, had agreed to join the Essentials program, and had subsequently been charged hundreds of dollars over the course of four years.

1.2 *Negative option billing in Asia*

Instances of negative option billing have similarly grown outside of North America. The Bank of China, for example, was recently reported to automatically charge customers for one-year of transaction-texting services after a free trial period.¹² Other banks in China used similar practices. According to a 2011 Customer Survey of Retail Banking in China, conducted by J.D. Power & Associates' Asian Pacific company, 50% of respondents claimed they were not notified when their banks began charging them for formerly free services. As a result, the overall customer satisfaction score for retail banking in China dropped from 693/1000 (in 2010) to 685/1000 (in 2011).

The Bank of China's Hong Kong branch has used similar practices when offering cellphone banking services: The amount of monthly charge after ending a promotional free period was not pre-specified, and consumers needed to contact the service provider to opt out.¹³ Similar marketing practices providing evidence of forms of negative option billing have also occurred in areas such as telecommunications, online video gaming, or insurance – where electronic commerce has been widely adopted in the Asian-Pacific.¹⁴

¹² Retrieved from <http://finance.sina.com.cn/money/bank/guangjiao/20110906/041810437866.shtml>.

¹³ Retrieved from http://www.three.com.hk/website/appmanager/three/home?_nfpb=true&_pageLabel=P400328951219906687968&lang=chi&pageid=39E001.

¹⁴ See, for example, the launching announcement from an online video game website in Taiwan; retrieved from <http://www.gamez.com.tw/thread-135237-1-1.html>.

2 Regulatory actions

Although marketing practices associated with negative option billing are common in both North America and the Asia-Pacific, much of the early legal effort to regulate negative option billing began in North America.

2.1 *Recent legal actions curbing negative option billing in North America*

Early regulation of negative option billing arose in Canada when cable television companies added new special services, including new specialty channels, for which customers were subsequently billed. Public outcry prompted the introduction of a private member's bill in the Canadian Parliament in 1996 to ban the practice, and the bill eventually was passed by the Canadian Parliament in 1999 (Bill C-276). This bill placed restrictions on cable television companies from charging customers for new, unrequested channel services, but it did not focus on Internet practices. The Province of Ontario followed with its own Consumer Protection Act in 2002, and this bill did apply curbs on certain online negative option billing practices (but it did not protect consumers from owing for goods or services that they had consciously or inadvertently agreed to receive).¹⁵

In the United States, general restrictions on deceptive practices (including negative option billing) date back to U.S. Federal Trade Commission (FTC) policies in place by the 1970s. Greater attention to specific restrictions limiting negative option billing and related practices emerged in 2000 in an FTC document summarizing customer guidelines, warnings, and legal remedies applicable to new Internet practices.¹⁶ At that time, FTC policy consisted mostly of the application of existing rules administered by the FTC Bureau of Consumer Protection. The FTC later invited submission of public comments until October 13, 2009, on further regulations under consideration to curb negative option plans.¹⁷ There was support for more restrictions from the American Association of Libraries; the Broward County Permitting, Licensing, and Consumer Production Division; the Attorney General of Florida; and the Attorney General of Colorado. The Attorney General of Vermont submitted an opinion enumerating several specific recommended regulations that were endorsed also by the Attorneys General of the States of Arkansas, Illinois, Kansas, Maine, Maryland, Massachusetts, Minnesota, Nevada, New Mexico,

¹⁵ Consumer Protection Act, 2002; Ontario Regulation 17/05; retrieved from http://www.e-laws.gov.on.ca/html/regs/english/elaws_regs_050017_e.htm.

¹⁶ Federal Trade Commission Bureau of Consumer Protection, (September 2000), Advertising and marketing on the Internet: Rules of the road" (published by the FTC). This states that "The Negative Option Rule applies to sellers of subscription plans who ship merchandise like books or compact discs to consumers who have agreed in advance to become subscribers. The Rule requires ads to clearly and conspicuously disclose material information about the terms of the plan. Further, once consumers agree to enroll, the company must notify them before shipping to allow them to decline the merchandise. Even if an automatic shipment or continuity program doesn't fall within the specifics of the Rule, companies should be careful to clearly disclose the terms and conditions of the plan before billing consumers or charging their credit cards." (p. 9)

¹⁷ See public comments under: # 307; FTC File No. P064202; 16 C.F.R. Part 425: Trade regulation rule concerning the use of prenotification negative option plans: Advance notice of proposed rulemaking: Reopening the record for the submission of public comments until October 13, 2009. Retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/index.shtm>.

Ohio, Oregon, Tennessee, West Virginia, and (shortly thereafter) Connecticut, Delaware, Louisiana, Mississippi, and New Jersey.

In 2010, the “Restore Online Shoppers’ Confidence Act” was passed by the U.S. Congress and signed into law.¹⁸ The law serves to “stop the practice of handing off data to third parties without the consumers’ consent or knowledge. According to the law, all third party sellers must now obtain any billing information directly from the consumer, and with said consumer having complete knowledge that there is no affiliation between the first transaction and the current third party offer.”¹⁹ This law provided effective new restrictions on passing data to third parties. Regarding negative option billing, the law did not go as far as the petition submitted on behalf of 20 U.S. States by the Attorney General of Vermont.

More recently, enforcement of the previous policies and new laws has been stepped up, including some cooperation between U.S. and Canadian regulators. On May 17, 2011, the FTC brought an enforcement action against Jesse Williams of Alberta, Canada and ten companies he controls for using online tactics associated with products offering a “free trial.”²⁰ On Sept. 13, 2011, an injunction was issued by a Seattle Court to curtail the practices of these companies involving free trials and negative option billing and to freeze the assets of the related parties.²¹

2.2 *Recent legal actions regarding negative option billing in China*

The Law of the People’s Republic of China on Protection of Consumer Rights and Interests²² is currently the main legal reference in China when it comes to consumer disputes regarding company practices, such as un-notified, free-to-pay conversion, auto renewal, automatic fee adjustment, and so forth. Under Article 8 of the law, “Consumers shall enjoy the right to obtain true information of the commodities they purchase and use or the services they receive,” a condition

¹⁸ Retrieved from <http://www.govtrack.us/congress/bill.xpd?bill=s111-3386>.

¹⁹ Retrieved from <http://www.kellylawblog.com/2011/01/old-and-notbusted-ftc-regulation-new-hotness-restore-online-shoppers-confidence-act>. This article goes on to state [Sec. 3] that “The Act prohibits third party vendors from charging a consumer for a membership fee or offer without directly receiving financial information from the customer unless: the third party vendor has clearly disclosed all of the information regarding the sale; completely described the goods and services being purchased by the consumer from the third party vendor; identified themselves as not affiliated with the vendor the customer was initially transacting with; completely identified all of the costs associated with the third party purchase. The third party vendor must also obtain the customer’s full credit card or banking account information directly from the customer and require the customer to perform an affirmative action (clicking on a box to agree) prior to completing the sale.” The bill can be downloaded at <http://www.ftc.gov/ogc/stat3/online-shoppers-enrolled.pdf>. Other provisions reinforce past restrictions on “Negative Option Marketing on the Internet [Sec.4]”, including [Sec.4] “(1) providing text that clearly and conspicuously discloses all material terms of the transaction before obtaining the consumer’s billing information; (2) obtains a consumer’s express informed consent before charging the consumer’s credit card, debit card, bank account, or other financial account for products or services through such transaction; and (3) provides simple mechanisms for a consumer to stop recurring charges from being placed on the consumer’s credit card, debit card, bank account, or other financial account.”

²⁰ Retrieved from <http://www.ftc.gov/opa/2011/05/jessewillms.shtm>.

²¹ Retrieved from <http://www.edmonton.bbb.org/article/bbb-media-release---us-judge-freezes-alberta-marketers-assets-29511>.

²² Retrieved from <http://www.lawinfochina.com/display.aspx?lib=law&id=6137>.

that negative option billing is commonly argued not to satisfy.²³ Nevertheless, the majority of consumers in China still feel that they are not well protected from negative option billing practices. For example, in spite of the issuance of the Commercial Banking Services Pricing Rules in 2003, there are still recent reports from consumers in China that some banks are charging for previously free services without pre-notification.²⁴

3 The pros and cons for negative option billing

Exhibit 1 summarizes supportive and critical views about negative option billing and related online practices. Well-argued examples of both views can be found in submissions made in response to the United States Federal Trade Commission's (FTC) request for public comment on the "Use of Pre-notification Negative Option Plans" (until October 13, 2009). The first three columns of the table in this exhibit contain supportive views from the Promotion Marketing Association, while the fourth column represents opposing views enumerated by the Attorney General of Vermont, writing on behalf of the Attorneys General of 20 U.S. states.²⁵

3.1 Arguments for negative option billing

In essence, the main argument for allowing negative option billing and related policies (free-to-pay conversion, automatic renewal, and data passing to third parties) holds that these policies make commerce more efficient and flexible for the seller and buyer. In principle, if rational parties voluntarily enter a contractual agreement, they should be better off thereby (or at least not worse off) – provided that the parties are fully informed of the terms of the contract before they make the agreement. Along these lines, the Promotional Marketing Association argues (in their 2009 opinion) that "the FTC already has all the enforcement tools necessary to address false and deceptive offers with advance consent features, including Section 5 of the Federal Trade Commission Act, the Electronic Fund Transfer Act, the Negative Option Rule, the Telemarketing Sales Rule, and the Unordered Merchandise Rule." In 2010, as if in answer to this, the U.S. federal government enacted the "Restore Online Shoppers' Confidence Act." This Act provided further tools for the enforcement authorities (the FTC and the Attorney Generals of the states of the U.S.) to assure that e-commerce websites provide full information about contract terms, so that consumers are able to provide fully informed consent. This act requires, in part, that any online agreement should "provide text that clearly and conspicuously discloses all material terms of the transaction before obtaining the consumer's billing information" (and provides remedies and enforcement provisions).²⁶ With this greater guarantee of informed consent, this law would seem to strengthen the Promotional Marketing Association argument that negative option billing and related policies make commerce more efficient and flexible for the seller and buyer.

²³ Retrieved from <http://www.55148.net/UI/LegalConsultDetail.aspx?rowId=d2d79df4-7445-48c8-bf67-51e06af87b67>.

²⁴ Retrieved from <http://315gd.ccn.com.cn/HotNews/Print.asp?ArticleID=21181>.

²⁵ Retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/543809-00097.pdf>; retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/543809-00098.pdf>.

²⁶ Bill S.3386, Section 4 (1); retrieved from <http://www.ftc.gov/ogc/stat3/online-shoppers-enrolled.pdf>.

Exhibit 1 Benefits and pitfalls of negative option billing practices

<i>Program</i>	<i>Structure</i>	<i>Benefit</i>	<i>Pitfalls</i>
Free trial; Free-to-pay conversion	The consumer is allowed to try the seller's product or service for free during a specified time period, and can cancel during the trial period without any obligation to pay for the product or service or to continue in the program.	The consumer is able to actually sample the product or service for a specified period of time before incurring any purchase obligation.	Trial of an unwanted offering might be tied to obtaining another desired offering for free or at a discount. The need to opt out may be a surprise to the consumer because of lack of sufficient emphasis in the offering communication.
Continuity	The consumer consents in advance to receive goods or services in the future on a periodic basis and is billed or charged each time the goods or services are provided.	The consumer knows in advance exactly what will be in each future shipment, because the contents of that shipment are selected by the consumers. • The consumer can generally cancel future shipments at any time without any further obligation. • The consumer can be confident that he or she will have a sufficient supply of the product for as long as the consumer wishes to continue using the product.	The consumer consent may be unintentional and induced by manipulative promotional layout. • Cancellation can consume time and phone/mail charges, which costs much be borne by the consumer.
Automatic renewal	The consumer agrees that the seller may automatically renew and/or bill the consumer's membership, subscription, or participation in a plan at the end of each term unless the consumer cancels.	The consumer is ensured that he or she will have uninterrupted delivery of a particular product or service for as long as the consumer wishes to keep receiving the goods or services.	If the consumer does not want a service and waits more than a month, one month will be billed. If the service is intangible, the consumer may not even realize he or she has "subscribed" and will pay for multiple months without using the service.

The first three columns appeared in comments to the Federal Trade Commission, submitted by the Promotion Marketing Association, Inc. (PMA), in response to the FTC's request for public comments as part of its systematic review of the Trade Regulation Rule concerning "Use of Prenotification Negative Option Plans" ("Negative Option Rule" or "Rule"). See 74 Fed. Reg. 22720 (May 14, 2009). Retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/543809-00097.pdf>, pp. 5-6. The fourth column summarizes points from the opinion of the Attorney General of Vermont. Retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/543809-00098.pdf>.

Additional arguments favouring negative option billing and related practices are enumerated in the opinion from the Promotional Marketing Association, which points out that such programs:²⁷

- allow for simple, convenient, and continuous access to goods and services that the consumer can stop at any time with no further obligation, assuming the consumer has met any applicable minimum purchase requirements;
- enable the consumer to try a product for free or at a reduced cost for a specified period of time, reducing the risk for uncertain buyers;
- reduce the number of notices the consumer receives and allows the consumer to enjoy uninterrupted service without expending time and effort to renew the service or subscription;
- expose consumers to goods and services that are tailored to their interests and to which they may not have been exposed; and
- provide convenience and receive lower prices in exchange for agreeing to participate in an advance consent marketing plan.

And for sellers, advance consent marketing programs:²⁸

- reduce marketing, operational, and transaction costs through simplifying the renewal process;
- enable sellers to build long-term relationships with consumers;
- allow sellers to more efficiently stock inventory and avoid costs associated with renewals; and
- empower lesser known businesses to better compete against better known competitors by offering consumer-friendly terms for their products and services.

3.2 *Arguments against negative option billing*

The main argument against allowing negative option billing and related policies concerns the limits to consumers' attention relative to reasonable expectations for expending cognitive effort in the context. This argument builds on results from the consumer behavior literature,²⁹ which suggest that because of inevitable limits to human attention, people typically act as "cognitive misers," rationing their cognitive effort to the most effective uses. Recognizing cognitive limitations, if an agreement is lengthy in context, cognitively taxing, or presented on a screen containing several visual or verbal elements competing for

²⁷ Edward M. Kabak, (2009, October 12), Before the Federal Trade Commission: In the matter of prenotification negative option rule review, Matter No: PO64202; Comments submitted by the Promotion Marketing Association. Retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/543809-00097.pdf>, pp. 6–7.

²⁸ Retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/543809-00097.pdf>, p.7.

²⁹ A good reference for interested readers is Alba, Hutchinson, and Lynch, (1991), Memory and decision making, in *Handbook of Consumer Behavior*, 1–49. Edgewood Cliffs, NJ: Prentice Hall.

attention, fully informed consent about all contract terms may be an unreasonable expectation.

It is instructive to make an analogy between offline and online shopping. When making a \$30 purchase in a store, no reasonable person would expect to have to spend five to ten minutes reading contract terms in a check-out line. But when ordering the same product online, a consumer might now encounter several paragraphs of contract terms within which some sort of negative option billing practice exists. This analogy suggests that it is unreasonable to impose such cognitive costs on purchasers for relatively small items.

Similarly, when paying for a meal in a restaurant, it would be unexpected (and unreasonable) for there to be a clause next to the signature subscribing the signer to a restaurant magazine. Is it reasonable for web pages that are selling inexpensive items to include terms that commit the consumer to something much larger, or for a longer duration, than the original purchase? One can argue that it is unreasonable to expect consumers to absorb complex information (about unexpected longer-term commitments) on what otherwise appears to be a small simple purchase.

Furthermore, the practice of a free trial, followed by a free-to-pay conversion (with negative option billings in place to keep the customer subscribed until he or she opts out) also preys on human cognitive limitations and proclivities. The free trial serves to quickly lower the mental hurdle of consumers to tentatively accept the initial promotional offer.³⁰ But afterward, the consumer must remember to unsubscribe before the first billing. Is it reasonable to set the default to charging a customer in the likely event that the consumer forgets to unsubscribe?

Additional arguments against negative option billing and related practices are enumerated by the Attorney General of Vermont (on behalf of the Attorneys General of 20 U.S. states) as follows:³¹

- The misleading character of negative options advertised as involving ‘free’ or ‘trial’ offers. The long-term impression created by this type of terminology is that consumers have no obligation to do anything, not that their silence after acceptance of the offer will open them to recurrent charges of unlimited duration.
- Consumers' lack of awareness as to the existence of ongoing periodic charges to their credit card or bank account, in connection with trial conversions. The reality is that many consumers do not scrutinize their account statements and thus can go for long periods of time without realizing that they are being charged. Modest charges, like \$19.95 per month, can "fly under the radar." This is particularly true with respect to bank account charges, the details of which, on an account statement, can be inscrutable to even well-educated consumers. [Again, this is a result of limits to attention.]
- The piling up of trial conversion charges over long periods of time, amounting to substantial amounts of money, even where consumers make little or no use of the goods or services offered. With no time cap on charges, consumers can incur hundreds of dollars worth of charges, or more.
- The difficulty faced by consumers in contacting the seller of the goods or services in order to cancel a trial conversion. There is no reason why a

³⁰ Chris Anderson, (2009), *Free: The future of a radical price*. Hyperion Publishing, New York, NY.

³¹ Retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/543809-00098.pdf>.

consumer who is bound by consent communicated in a particular way electronically, for example, should not be able to cancel in the same manner.

Another problem with negative option billing is that consumers may not be aware of underlying connections with third parties. As a result, the customers may place more trust in the seller than is warranted. And sometimes the product tie-ins confuse the issues. The customer may want one product, but another is tied in, and since the customer has no interest in the tied-in product or service, the customer skips over the details of the purchase of the tied-in product.

A final problem is that certain consumer groups may be in a disadvantageous position in terms of age, disability, or unfamiliarity with e-commerce. Individuals in these groups might be taken advantage of, not realizing what has happened upon signing up with the initial promotional/free offer. Recognizing this, the Canadian Market Association's Code of Ethics and Practice Standards³² makes explicit requirements, for marketing interactions directed to such disadvantaged consumer groups, that include the collection, transfer, and requests for personal information to have the default being opt-in consent as opposed to opt-out, which is implied by negative option billing.

In summary, proponents of negative option billing and related policies argue that these policies make commerce more efficient and flexible for the seller and buyer (especially given the existence of new government policy requiring clear and conspicuous disclosure by vendors of all material terms of contracts). In contrast to this, opponents of negative option billing argue that such practices take advantage of well-documented limits on human capabilities when engaging in the purchase process (including limitations on attention and cognitive effort, a low ability to fully account for or remember future costs, and an inability to quickly recognize whether an offer comes from a trusted website operator or from a third-party offer provider). Ultimately, the underlying issue concerns whether having a seller make explicit enumeration of all material contract terms implies that the buyer is giving fully informed consent. Perhaps fully informed consent should not assume unreasonably taxing human cognitive capabilities in the relevant online purchase context.

4 Remedies proposed in 2009

Writing on behalf of the Attorneys General of 20 U.S. states, the Attorney General of Vermont argues that only focusing on full disclosure, as had been previous FTC practice, is insufficient to solve this problem:

Much of the public discussion of the PNOR [Federal Trade Commission ("FTC") rule on Use of Prenotification Negative Option Plans, 16 C.F.R. Part 425] has focused on improving disclosure as a way of protecting consumers from being harmed by trial conversion negative option marketing. See, for example, FTC, *Negative options, a report by the staff of the ftc's division of enforcement* (Jan. 2009). However, in the context of free-to-pay conversions, it is our firm view that improved disclosure of terms will not adequately protect consumers. Rather, there is a need for substantive regulatory provisions to ameliorate the harmful aspects of this form of negative option plan.

³² Retrieved from <http://www.the-cma.org/?WCE=C=47%7CK=225849>; (Section K3, L3, J4, etc).

The Attorney General of Vermont goes on to propose the following remedies:

Therefore, we strongly encourage the FTC to add new provisions . . . to regulate trial conversions, and, with respect to that form of negative option, to (1) prohibit charges following a "free" trial without receiving the affirmative consent of the consumer at the end of the trial; (2) mandate periodic notification to consumers of charges to their accounts in trial conversions; (3) set a cap on the number of months that a consumer may be charged and require an affirmative opt-in by the consumer to exceed that time limit; (4) require companies to permit consumers to cancel in the same method of communication as the solicitation to the consumer; and (5) include "services" under the [purview of the regulations].³³

It is worth noticing that the remedies proposed above are echoed by the Consumers' Association of Canada (CAC), an independent, non-profit organization founded in 1947 whose purpose is to inform and educate Canadian consumers on marketplace issues. The CAC is part of a worldwide federation of consumer groups called Consumers International. Among the consumer rights that the CAC strives to uphold, there is "the right to redress,"³⁴ which specifically refers to the right to "working with established mechanisms to have problems corrected" (as explained on the official website of the Office of Consumer Affairs & Business Regulation) and "to receive a fair settlement of just claims, including compensation for misrepresentation" (as stated in the United Nations Guidelines for Consumer Protection).³⁵

Some of these remedies have been adopted in North America, but not all – as noted in the final section below. Fewer appear to have been adopted in the Asia-Pacific marketplace, where negative option billing is almost as commonly observed as in North America.

5 Conclusion

The U.S. and Canadian policy makers have, thus far, only partly responded to the calls for better regulation. The Canadian Bill C-276 dealt with negative option billing by cable TV operators and had some applicability elsewhere on requiring full disclosure. The U.S. FTC rule on Use of Prenotification Negative Option Plans also focuses on prominent disclosure, but both of these fall short of the remedies proposed by the Attorney General of Vermont (on behalf of 20 U.S. states).

The U.S. "Restore Online Shoppers' Confidence Act," introduced and signed into U.S. law in 2010, largely addresses the problem of hidden data passing to third parties and the preservation of privacy (in Section 3 of the Act). The law goes on to specifically provide the following:³⁶

SEC. 4. NEGATIVE OPTION MARKETING ON THE INTERNET.

It shall be unlawful for any person to charge or attempt to charge any consumer for any goods or services sold in a transaction effected on the Internet through a negative option feature (as defined in the Federal Trade

³³ FTC rule on Use of Prenotification Negative Option Plans, 16 C.F.R. Part 425]. Retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/543809-00098.pdf>.

³⁴ Retrieved from <http://www.consumer.ca/1625>.

³⁵ Retrieved from http://en.wikipedia.org/wiki/Consumer_Bill_of_Rights.

³⁶ Retrieved from <http://www.ftc.gov/ogc/stat3/online-shoppers-enrolled.pdf>.

Commission's Telemarketing Sales Rule in part 310 of title 16, Code of Federal Regulations), unless the person—

- 1) provides text that clearly and conspicuously discloses all material terms of the transaction before obtaining the consumer's billing information;
- 2) obtains a consumer's express informed consent before charging the consumer's credit card, debit card, bank account, or other financial account for products or services through such transaction; and
- 3) provides simple mechanisms for a consumer to stop recurring charges from being placed on the consumer's credit card, debit card, bank account, or other financial account.

These provisions only partly adopt the Attorney General of Vermont's proposals, however. Section 4.2 of the U.S. bill does appear to coincide with the Attorney General of Vermont's proposal to "(1) prohibit charges following a 'free' trial without receiving the affirmative consent of the consumer at the end of the trial;"³⁷ the wording of Section 4.2 is not as specific and may be open to less vigorous application. Checking off a box on a webpage only once would seem sufficient to comply with Section 4.2, but there is no requirement for affirmative consent at the end of a trial period before billing starts. This potential loophole will depend on how the FTC and the Attorneys General of the U.S. states apply these regulations and on how the courts enforce these laws. Similarly, Section 4.3 appears to address the Vermont proposal to "(4) require companies to permit consumers to cancel in the same method of communication as the solicitation to the consumer" – but again, the wording in Section 4.3 is less specific than the Vermont proposal.³⁸

Moreover, there is no provision in the "Restore Online Shoppers' Confidence Act" for addressing the Attorney General of Vermont's proposals to

- (2) mandate periodic notification to consumers of charges to their accounts in trial conversions; (3) set a cap on the number of months that a consumer may be charged and require an affirmative opt-in by the consumer to exceed that time limit.³⁹

The "Restore Online Shoppers' Confidence Act" thus makes several steps toward avoiding the problems associated with data passing to third parties and negative option marketing. But the law comes short of adopting all the proposals suggested by the Attorney General of Vermont.

More generally, most policymakers agree that their desire is to promote healthy, unfettered commerce. As stated by Michael Janigan, Executive Director of the Public Interest Advocacy Centre (PIAC), in the debate over Canadian Bill C-276,

The concern associated with the practice of negative option billing has its origins in the nature of a contract of purchase and sale, as recognized in common law. As every first year law student learns, such a contract consists

³⁷ FTC rule on Use of Prenotification Negative Option Plans, 16 C.F.R. Part 425]. Retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/543809-00098.pdf>.

³⁸ FTC rule on Use of Prenotification Negative Option Plans, 16 C.F.R. Part 425]. Retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/543809-00098.pdf>.

³⁹ FTC rule on Use of Prenotification Negative Option Plans, 16 C.F.R. Part 425]. Retrieved from <http://www.ftc.gov/os/comments/negoprulereopen/543809-00098.pdf>.

of an offer and an acceptance. The history of consumer protection statutes is a chronicle of legislators attempting to ensure that the offer is conveyed without misrepresentation by the vendor to a purchaser who has an opportunity to make an informed choice to accept or refuse the offer. This is because a contract that is made with a consumer who is unaware of key elements of the contract such as price, quantity and quality of the goods to be delivered is subversive of the efficiency of the market as a whole.⁴⁰

In summary, the ultimate issue is whether the current practices of negative option billing are obfuscating customers' ability to make a fully-informed choice to accept or refuse the offer. Recent laws have cut back on the ability of online providers to induce a choice by consumers who do not fully appreciate the future implications of their actions. The earlier Canadian law and recent U.S. law moved in the right direction, and recent action by the Province of Ontario, the U.S. FTC, and the Competition Bureau of Canada improved regulation and enforcement. The U.S. "Restore Online Shoppers' Confidence Act" has directly addressed the problems with third-party billing. But all these legal actions have not come as far in providing regulatory protection as the Attorneys General of 20 U.S. states have proposed. Beyond North America and especially in Asia-Pacific areas, fewer explicit actions appear to have been taken that go beyond enforcement of pre-existing regulations limiting fraudulent practices. Overall, the jury is still out as to whether what has been done is sufficient to address the problems with negative option billing and related practices. We expect that some problems have been solved, but others are only partly dealt with and will need further action.

⁴⁰ See Michael Janigan, (1999, December 2), Negative options marketing: Speaking notes before the house of commons standing committee on Industry – Bill C-276: by executive director/general counsel of the public interest advocacy centre. Retrieved from http://www.piac.ca/financial/negative_option_marketing/.