Supporting Statement
Trade Regulation Rule
Rule on the Use of Prenotification Negative Option Plans
16 C.F.R. Part 425
(Control Number: 3084-0104)

(1) Necessity for Collecting the Information

The Trade Regulation Rule on the Use of Prenotification Negative Option Plans ("Negative Option Rule" or "Rule") (16 C.F.R. Part 425) governs the operation of prenotification subscription plans. Under these plans, sellers ship merchandise, such as books, compact discs, or tapes automatically to their subscribers and bill them for the merchandise if consumers do not expressly reject the merchandise within a prescribed time. The Rule protects consumers by: (a) requiring that promotional materials disclose the terms of membership clearly and conspicuously; and (b) establishing procedures for the administration of such "negative option" plans.

(2) Use of the Information

Consumers use the Rule's required disclosures to weigh the benefits and burdens of negative option plans. These disclosures inform existing and potential subscribers of their rights under the Rule. Specifically, the seller must disclose the following information:

- that the subscriber will have at least ten days in which to decline the merchandise;
- the subscriber's minimum purchase obligation;
- the subscriber's right to cancel the membership after meeting the minimum obligation;
- the frequency with which the seller will send announcements and the maximum number of announcements that will be sent in a 12-month period;
- whether billing charges will include postage and handling; and
- that the seller will give full credit, and guarantee return postage, for merchandise returned by a subscriber who has not had at least ten days in which to mail a merchandise rejection form.

The failure to make these disclosures is an unfair or deceptive act or practice.

(3) Consideration of Using Improved Information Technology to Reduce Burden

The Rule's disclosure requirements are technology-neutral and apply to advertisements and other promotional materials regardless of format. Thus, so long as the Rule's requirements are satisfied, an advertisement or other promotional material would not violate the Rule merely because it is disseminated in electronic form (*e.g.*, Internet, e-mail). In this way, the Rule leaves regulated entities free to take advantage of improved information technology and is consistent with the Government Paperwork Elimination Act, 44 U.S.C. § 3504 note.

(4) Efforts to Identify Duplication/Availability of Similar Information

The Restore Online Shoppers' Confidence Act (ROSCA) relates to negative option marketing on the Internet. 15 U.S.C. §§ 8401 *et seq*. This new law makes it unlawful for Internet sellers to charge for any goods or services sold using negative option marketing, unless they: (a) disclose all material terms of sales transactions clearly and conspicuously before obtaining consumers' billing information; (b) obtain consumers' express informed consent before charging consumers; and (c) provide simple mechanisms for stopping recurring charges.

Notwithstanding ROSCA's overlap with the Negative Option Rule, the Rule's reach is broader, extending beyond Internet sales to other forms of prenotification negative option plan marketing and advertising, such as direct-mail solicitations. In addition, the Rule requires specific disclosures and certain procedures for administering prenotification negative option plans (e.g., sellers must send consumers forms they can use to reject merchandise before it is shipped) that are not addressed by ROSCA

Some states regulate negative option marketing, requiring disclosures similar to those required by the Rule. Nonetheless, the primary industries using negative option plans - book, music, and video clubs - have a nationwide customer base that necessitates federal regulation, and the Negative Option Rule has prevented a proliferation of conflicting state laws.

(5) Efforts to Minimize Burden on Small Businesses

Although the Rule does not exclude small businesses, negative option plans covered by the Rule are generally - if not exclusively - offered by book and record clubs that are operated by large, national companies. The Commission's review of the Rule in 1997 - 1998 under its systematic rule review program found that the Rule imposed no significant economic impact on small businesses. *See* 63 Fed. Reg. 44,555, 44,558 (August 20, 1998).

(6) Consequences of Conducting Collection Less Frequently

The Rule's disclosure requirements do not apply to all promotional materials. The Rule limits its disclosure requirements to promotional materials that contain a means to join a plan, such as an enrollment form. The disclosures enable consumers to make informed purchasing decisions and protect consumers from incurring financial obligations for merchandise they do not want. Not requiring disclosures of material terms for this limited category of promotional

materials could potentially injure consumers in that they might use enrollment forms to join negative option plans before learning that they are taking on the future obligation to affirmatively reject merchandise shipped on a periodic basis.

For each item of merchandise a seller ships under a plan, the Rule also requires the seller to send to subscribers pre-shipment both an announcement identifying the merchandise and a form to reject it before it is shipped. The Rule does not require the seller to repeat the material terms of a negative option plan in the merchandise announcements or rejection forms.

Not requiring sellers to mail rejection forms to subscribers in advance of prospective shipments would result in subscribers receiving unwanted merchandise.

(7) Circumstances Requiring Collection Inconsistent with Guidelines

The collection of information in the Rule is consistent with guidelines contained in 5 C.F.R. 1320.5(d)(2).

(8) Consultation Outside the Agency

In 1997, the Commission sought, as part of its systematic ten-year review of all current regulations and guides as resources permit, public comment about the overall costs and benefits and the continuing need for the Negative Option Rule.[1] Comments indicated that the Rule is working effectively in regulating prenotification negative option plans for the sale of goods. Most of the comments supported retaining the Rule without change. The comments stated that both consumers and the industry benefit from the Rule because its required disclosures educate consumers about their responsibilities under prenotification negative option plans while other Rule requirements ensure that plan operators follow procedures that help protect consumers. Consumer and industry members alike believe that the Rule fosters long-term relationships between consumers and sellers. At the conclusion of its review, the Commission decided to retain the Rule without substantive change and made only minor, technical amendments that did not impose any additional information collection requirements.

The Negative Option Rule is again under agency review. *See* 76 Fed. Reg. 41,150 (July 13, 2011).[2] Additionally, the Commission recently sought public comment in connection with its latest PRA clearance request for this Rule. *See* 76 Fed. Reg. 47,186 (Aug. 4, 2011) (no comments were received), and is doing so again contemporaneously with this submission.

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[1] The Commission issued the Rule on June 7, 1974, pursuant to the Federal Trade Commission Act, 15 U.S.C. §§ 41-58.

[2] On May 14, 2009, the Commission published an Advance Notice of Proposed Rulemaking seeking comment on the overall costs, benefits, necessity, and regulatory and economic impact of the Rule. See 74 Fed. Reg. 22,720 (May 14, 2009). Shortly thereafter, the Commission re-opened the time period for filing public comments for sixty (60) days, to October 13, 2009. See 74 Fed. Reg. 40,121 (Aug. 11, 2009).

(9) Payments or Gifts to Respondents

Not applicable.

(10) & (11) Assurances of Confidentiality/Matters of a Sensitive Nature

No confidentiality issues and no issues involving questions of a sensitive nature are involved.

(12) Annual Hours Burden

Estimated annual hours burden: 3,875 hours

Staff estimates that approximately 45 existing clubs each require annually about 75 hours to comply with the Rule's disclosure requirements, for a total of 3,375 hours (45 clubs x 75 hours). These clubs should be familiar with the Rule, which has been in effect since 1974, with the result that the burden of compliance has declined over time. Moreover, a substantial portion of the existing clubs likely would make these disclosures absent the Rule because they have helped foster long-term relationships with consumers.

Approximately 5 new clubs come into being each year. These clubs require approximately 100 hours to comply with the Rule, including start up-time. Thus, the cumulative PRA burden for new clubs is about 500 hours. Combined with the estimated burden for established clubs, the total burden is 3,875 hours.

Estimated annual labor costs: $167,125

Based on recent data from the Bureau of Labor Statistics,[3] the mean hourly wage for advertising managers is approximately $47 per hour. Compensation for office and administrative support personnel is approximately $17 per hour. Assuming that managers perform the bulk of the work, while clerical personnel perform associated tasks (*e.g.*, placing advertisements and responding to inquiries about offerings or prices), the total cost to the industry for the Rule's information collection requirements would be approximately $167,125 [(65 hours managerial time x 45 existing clubs × $47 per hour) + (10 hours clerical time × 45 existing clubs × $17 per hour) + (90 hours managerial time × 5 new clubs × $47 per hour) + (10 hours clerical time × 5 new clubs × $17)].

(13) Estimated Annual Capital and/or Other Non-labor Related Costs

Because the Rule has been in effect since 1974, the vast majority of the negative option clubs have no current start-up costs. For the few new clubs that enter the market each year, the

[3] Occupational Employment And Wages - May 2010, Table 1, at http://www.bls.gov/news.release/pdf/ocwage.pdf.

costs associated with the Rule's disclosure requirements, beyond the additional labor costs discussed above, are minimal. Negative option clubs already have access to the ordinary office equipment necessary to achieve compliance with the Rule. Similarly, the Rule imposes few, if any, printing and distribution costs. The required disclosures generally constitute only a small addition to the advertising for negative option plans. Because printing and distribution expenditures are incurred to market the product regardless of the Rule, adding the required disclosures results in only marginal incremental expense.

(14) Estimate of Cost to Federal Government

The Rule has been in existence for 37 years and businesses covered by the Rule already generally comply. Accordingly, the estimated cost to the Federal government of enforcing the Rule is minimal and is generally confined to reviewing advertisements to ensure that the required disclosures are made. Staff may also answer inquiries about the Rule. Staff estimates that the annualized cost to the Commission (per year over the 3-year clearance renewal being sought) to administer the disclosure requirements will be approximately $15,500 representing approximately one-tenth of an attorney/economist work-year, inclusive of incidental benefits.

(15) Changes in Burden

The burden estimate has been reduced by 9,085 hours (from 12,960 hours in 2008 to 3,875 in 2011) reflecting the decreased number of existing clubs (from 158 in 2008 to 45 in 2011) and new clubs (from 7/year in 2008 to 5/year in 2011) due to consolidation in the industry and the economic downturn. In addition, given industry input, we have lowered the estimate of the hours required for new club disclosures from 120 hours to 100 hours.[4]

(16) Statistical Use of Information

There are no plans to publish any information for statistical use.

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[4] According to information provided by Anne Darr of DeHart & Darr Associates, Inc., and Eileen DeMilt Conboy, Vice President, Legal and Business Affairs, Direct Brands, Inc., the reduced estimate from 120 to 100 is due to new plans conducted by companies that have operated other plans previously, have acquired much experience with the required disclosures, and often use disclosure templates that reduce the burden of making the disclosures. Notwithstanding these considerations, the estimate is not reduced still further to the estimate accorded existing plans because new plans work to improve on past practices, reviewing required disclosures to determine how to convey them more effectively, including through the use of new technologies, such as the Internet.

According to its website (http://www.directbrands.com/), Direct Brands, together with its sister company Bookspan, is the largest direct-to-consumer distributor of media products in the United States. DeHart & Darr provides legislative and regulatory monitoring services to businesses including sellers that offer negative option membership plans.

(17) Failure to Display the Expiration Date for OMB Approval

Not applicable

(18) Exceptions to the Certification for Paperwork Reduction Act Submissions

Not applicable.