

**PREPARED STATEMENT OF ROBERT M. MCKENNA
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Before the

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

Washington, D.C.

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Thank you to Chairman Rockefeller, Ranking Member Hutchinson, and the Members of the Committee on Commerce, Science, and Transportation for inviting me to provide my written statement to the Committee.

I am Robert M. McKenna, Attorney General of the State of Washington. The subject matter of this hearing is of great importance to the consumers of this country, and I therefore commend the Committee for being responsive to the increasing number of consumer complaints regarding the marketing and billing practices of the companies under investigation by the Committee.

The Attorney General is the primary state official who responds to consumer complaints and enforces state laws designed to protect consumers from unfair and deceptive business practices. My office has taken the lead in enforcing those laws in the Internet marketplace with the creation of our High-Tech Unit over ten years ago. As e-commerce has flourished, so, too, unfortunately, have deceptive practices on the Internet. One of the significant advantages for consumers to shopping online has been the convenience and efficiency of the experience. What might take hours in the brick and mortar world to accomplish may take only a few minutes online. This has not been lost on some unscrupulous marketers who are exploiting consumers' expectations of a quick and efficient transaction process. Certain sellers and marketers have been interrupting consumers' online transactions by making offers that appear to relate to the consumers' transaction, but, in fact, do not. The marketing offers instead involve a subscription to an unrelated membership program that is billed on a recurring basis. As soon as my office noticed a trend in complaints relating to this form of marketing, we opened several investigations into companies conducting such marketing. These investigations have been time-consuming, resource-intensive, and complex, but they have provided us with voluminous evidence of the harmful effects of these marketing practices on consumers.

There are three general marketing methods that our office has found, when combined, deceive a substantial portion of consumers and result in their unknowing enrollment in membership programs. First, sellers offer consumers free trials for services or products that automatically convert to paid subscriptions unless the consumer affirmatively cancels during the free trial period to induce consumers to purchase services or products (known as "free-to-pay conversion offers"). Second, sellers obtain consumers' financial account information from third parties so that they are able to bill consumers for products or services without the consumer having to provide their account information directly to the seller during the transaction process (referred to as "preacquired account marketing" or a "data pass" process). And third, sellers market their products and services during the consumer's transaction process with a third party (sometimes referred to as "post-transaction marketing" or "interstitial marketing"). Unscrupulous marketers and sellers have designed marketing campaigns that combine each of these marketing methods in such a way as to deceive consumers into enrolling in membership programs for which consumers are billed on a recurring basis.

A typical example of this type of marketing as it appears on the Internet is as follows:

After a consumer places an order for a product or service and enters his or her payment information on an ecommerce site, an offer for \$10 cash back for filling out a survey appears on the screen. The impression left on the consumer by the Web page is that he or she should fill in the survey, enter his or her email address (sometimes twice) and click on the button to complete his or her purchase and claim the \$10 cash back. In fact, by clicking on the button, the consumer is purportedly agreeing to be enrolled in a free trial for a membership program that will be charged automatically on a recurring monthly (or, in some cases, annual) basis to the account the consumer used to make the purchase of the product or service. The fine print on the Web page discloses that by clicking on the button associated with completing the purchase or submitting the survey, the consumer is purportedly authorizing the e-commerce site to transmit the consumer's financial account information to an undisclosed third party. Despite the disclosures, the offer misleads consumers into believing that the offer is for \$10 cash back for taking a survey, not an offer for a trial in a membership program, which is the "true" offer and is disclosed only in the fine print. In general, the offers appear to be coming from the e-commerce site and do not disclose the third party that is actually making the offer.

The Washington Attorney General's Office has been able to identify several hundred consumer complaints filed with our office in the last two years alone that involve the consumer having been enrolled in a membership program without his or her knowledge and having been automatically billed for the program without his or her authorization.

Based upon these complaints and extensive investigations, we have observed a number of significant problems with this form of marketing, including:

1. Consumers do not expect that the financial account information that they provide for one transaction will result in ongoing charges placed by a third-party company;
2. Consumers have difficulty identifying and contacting the seller of the membership program to cancel or otherwise terminate any ongoing or recurring obligation because the sellers frequently do not identify themselves in the offers;
3. Sellers use a variety of distractions to obscure the "true" offer, e.g., offering cash back on the consumer's primary purchase and using "consumer surveys"; and
4. The use of words "free" or "trial offer" to market free-to-pay conversions leads consumers to believe that they do not have to take further action in order to avoid ongoing charges.

More specifically, our investigations have shown that hundreds of thousands of consumers in Washington State alone have found themselves subscribed to membership programs as a result of shopping online and that the vast majority of enrolled members have not used the benefits associated with the membership programs.

I cannot overstate the consumer injury that is occurring because of these marketing methods. Based upon our office's investigations, we estimate that well over \$50 million has been deceptively obtained from Washington consumers over the course of the last four years by a relatively small handful of businesses conducting the type of marketing at issue in this Committee's investigation.

Our investigations have gathered an extraordinary amount of evidence showing that companies engaging in this form of marketing are aware that their marketing and billing practices are deceiving consumers and that the vast majority of consumers enrolled in their membership programs never authorized the enrollment. The companies under investigation in Washington have received thousands of consumer complaints both directly from consumers and through the Better Business Bureaus and the offices of the state attorneys general. These companies have done little to nothing to stop the deception despite knowing that they are obtaining unauthorized enrollments. Some of these companies make it very difficult for the consumer to cancel the membership if and when the consumer discovers the charges. They add insult to injury by refusing to provide complete refunds to consumers unless they complain to an outside agency, such as an attorney general's office.

Many of these companies believe that the disclosures that are made in the marketing offers insulate them from liability, despite the substantial evidence in front of them that consumers are inadvertently enrolling in the membership programs. Our investigations have shown that disclosures in this kind of marketing are not sufficient to overcome the inherent potential for deception. Because there is such overwhelming and compelling evidence that this form of marketing deceives consumers, I have requested state legislation to regulate the practices at the heart of the deception. My office proposes state law that would require sellers using free-to-pay conversion offers to obtain the consumer's financial account information directly from the consumer during the transaction for the free-to-pay product or service. The proposed legislation, which did not pass when originally introduced in the Washington legislature last year, was opposed by some businesses. We expected such opposition, because our investigations have revealed that marketing using a free-to-pay conversion where the seller has preacquired account information or uses a data pass process is extremely lucrative; however, these profits are the result of unfair and deceptive practices and belong back in the pockets of consumers.

Of course, using preacquired account information or a data pass process to market products and services by means of free-to-pay conversion offers during the consumer's transaction with a third party is not a new marketing technique. A \$14.5 million multi-state settlement with Trilegiant, now known as Affinion, and Chase Bank in 2006 attempted to curtail deceptive marketing practices involving free-to-pay conversion offers

and preacquired account marketing by imposing greater disclosure requirements in direct mail offers. Furthermore, numerous states have entered into settlements with MemberWorks, now known as Vertrue, to address that company's deceptive negative-option marketing. In fact, both the Federal Trade Commission ("FTC") and the states have a decade-long history of enforcement and consumer education efforts to tackle the deceptive marketing of services and products through free trial offers and the improper transfer or misuse of consumers' account information. However, we have found that truthful disclosures are insufficient to cure the inherent potential for deception in preacquired account marketing or the data pass process in conjunction with free trial offers.

The FTC recognized the inherent potential for consumer deception in sales situations in which the seller had preacquired consumer account information when it created the requirement in the Telemarketing Sales Rule (TSR), which implements the Telemarketing and Consumer Fraud and Abuse Prevention Act, 15 U.S.C. §§ 6101-6108, as amended, that sellers must audiotape transactions involving free-to-pay conversions where the seller has preacquired account information of the consumer. In addition, the seller must obtain from the customer, at a minimum, the last four digits of the account number to be charged.

The complaints we have received, along with our investigations, point to one conclusion: preacquired account marketing (or use of a data pass process) in conjunction with free-to-pay conversion offers has the inherent potential to deceive, despite the presence of disclosures. The stark fact of how many consumers have actually been deceived by this form of marketing – in the telemarketing, direct mail, and Internet channels – is overwhelmingly persuasive.

Thank you for the opportunity to provide this statement and to inform the Committee of the experiences my office has had in investigating and combating the deceptive business practices that are at issue in the Committee's investigation. I would be happy to provide further information at the Committee's request.