Statement of Chairwoman Edith Ramirez and Commissioner Julie Brill
In the Matter of Apple Inc.
FTC File No. 1123018
January 15, 2014

The Commission has issued a complaint and proposed consent order to resolve allegations that Apple Inc. unfairly failed to obtain informed consent for charges incurred by children in connection with their use of mobile apps on Apple devices in violation of Section 5 of the Federal Trade Commission Act. Consistent with prior application of the Commission's unfairness authority, our action today reaffirms that companies may not charge consumers for purchases that are unauthorized – a principle that applies regardless of whether consumers are in a retail store, on a website accessed from a desktop computer, or in a digital store using a mobile device.

As alleged in the Commission's complaint, Apple violated this basic principle by failing to inform parents that, by entering a password, they were permitting a charge for virtual goods or currency to be used by their child in playing a children's app and at the same time triggering a 15-minute window during which their child could make unlimited additional purchases without further parental action. As a consequence, at least tens of thousands of parents have incurred millions of dollars in unauthorized charges that they could not readily have avoided. Apple, however, could have prevented these unwanted purchases by including a few words on an existing prompt, without disrupting the in-app user experience. As explained below, we believe the Commission's allegations are more than sufficient to satisfy the standard governing the FTC Act's prohibition against "unfair acts or practices."

I. Overview of In-App Purchases on Apple Mobile Devices

Apple distributes apps, including games, that are likely to be used by children on Apple mobile devices through its iTunes App Store. While playing these games, kids may incur charges for the purchase of virtual items such as digital goods or currency (known as "in-app charges") at prices ranging from $.99 to $99.99. These in-app charges are billed to their parents' iTunes accounts. Apple retains thirty percent of the revenues from in-app charges. As part of the in-app purchasing process, Apple displays a general prompt that calls for entry of the password for the iTunes account associated with the mobile device. Apple treats this password entry as authorizing a specific transaction and simultaneously allowing additional in-app purchases for 15 minutes.

While key aspects of the in-app purchasing sequence have changed over time, as described in the Commission's complaint, one constant has been that Apple does not explain to parents that entry of their password authorizes an in-app purchase and also opens a 15-minute window during which children are free to incur unlimited additional charges. We allege that, since at least March 2011, tens of thousands of consumers have complained about millions of dollars in unauthorized in-app purchases by children, with many of them individually reporting hundreds to thousands of dollars in such charges. As a result, we have reason to believe, and have alleged in our complaint, that Apple's failure to disclose the 15-minute window is an unfair

practice that violates Section 5 because it has caused or is likely to cause substantial consumer injury that is neither reasonably avoidable by consumers nor outweighed by countervailing benefits to consumers or competition.[1]

The proposed consent order resolves these allegations by requiring Apple to obtain informed consent to in-app charges. The order also requires Apple to provide full refunds, an amount no less than $32.5 million, to all of its account holders who have been billed for unauthorized in-app charges incurred by minors.[2]

II. Application of the Unfairness Standard

Importantly, the Commission does not challenge Apple's use of a 15-minute purchasing window in apps used by kids. Rather, our charge is that, even after receiving at least tens of thousands of complaints about unauthorized charges relating to in-app purchases by kids, Apple continued to fail to disclose to parents and other Apple account holders that entry of a password in a children's app meant they were approving a single in-app charge plus 15 minutes of further, unlimited charges.

In asserting that Apple violated Section 5's prohibition against unfair practices by failing to obtain express informed consent for in-app charges incurred by kids, we follow a long line of FTC cases establishing that the imposition of unauthorized charges is an unfair act or practice.[3] This basic tenet applies regardless of the technology or platform used to bill consumers and regardless of whether a company engages in deliberate fraud. Indeed, there is nothing in the unfairness authority we have been granted by Congress or in the Commission's Unfairness Policy Statement to suggest that our power is in any way constrained or should be applied differently depending on the technology or platform at issue, or the intentions of the accused party.[4]

Our task here, as in all instances in which we assert jurisdiction over unfair acts or practices, is to determine whether the alleged unlawful conduct causes or is likely to cause substantial injury that is not reasonably avoidable by consumers and is not outweighed by countervailing benefits to consumers or competition. After a full investigation, we have reason to believe that Apple's conduct constitutes an unfair practice.

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[1] 15 U.S.C. § 45(n).

[2] Any sum below $32.5 million that is not returned to account holders is to be paid to the FTC.

[3] *See, e.g.*, *FTC v. Willms*, No. 2:11-CV-828 MJP, 2011 WL 4103542, at *9 (W.D. Wash. Sept. 13, 2011); *FTC v. Inc21.com Corp.*, 745 F. Supp. 2d 975 (N.D. Cal. 2010), *aff'd*, 475 Fed. Appx. 106 (9th Cir. Mar. 30, 2012); *FTC v. Crescent Publ'g Grp., Inc.*, 129 F. Supp. 2d 311, 322 (S.D.N.Y. 2001); *see also* Complaint, *FTC v. Jesta Digital, LLC*, No. 1:13-cv-01272 (D.D.C. filed Aug. 20, 2013).

[4] The FTC need not prove intent to establish a violation of the FTC Act. *See, e.g.*, *Orkin Exterminating Co. v. FTC*, 849 F.2d 1354, 1368 (11th Cir. 1988); Federal Trade Commission Policy Statement on Unfairness, appended to *Int'l Harvester Co.*, 104 F.T.C. 949, 1070 (1984) ("FTC Unfairness Statement").

A. Substantial Injury to Consumers

We begin by addressing the issue of harm. It is well established that substantial injury may be demonstrated by a showing of either small harm to a large number of people or large harm in the aggregate.[5] Both are present here. As alleged in the complaint, in many individual instances, Apple customers paid hundreds of dollars in unauthorized charges while thousands of others incurred lower charges that together totaled large sums. We allege that, in the aggregate, at least tens of thousands of consumers have complained of millions of dollars of unauthorized in-app charges by children. Moreover, we have reason to believe that, for a variety of reasons, many more affected customers never complained. Some, for example, were undoubtedly deterred by Apple's stated policy that all App Store transactions are final. Others who incurred low charges likely did not protest because of the relatively small dollar value at issue. Indeed, extensive Commission experience teaches that consumer complaints typically represent only a small fraction of actual consumer injury.[6]

In his dissent, Commissioner Wright expresses the view that the harm alleged by the Commission involves "a miniscule percentage of consumers" and is therefore insubstantial.[7] We respectfully disagree. We find it of little consequence that the number of complainants is a small fraction of all app downloads, as Commissioner Wright asserts.[8] As an initial matter, our complaint focuses on conduct affecting Apple account holders whose children may unwittingly incur in-app charges in games likely to be played by kids. The proportion of complaints about children's in-app purchases as compared to total app downloads, revenue from the sale of Apple mobile devices, or Apple's total sales revenue sheds no light on the extent of harm alleged in this case. More fundamentally, the FTC Act does not give a company with a vast user base and product offerings license to injure large numbers of consumers or inflict millions of dollars of harm merely because the injury affects a small percentage of its customers or relates to a fraction of its product offerings.

It is also incorrect that "in order to qualify as substantial, the harm must be large compared to any offsetting benefits."[9] This conflates the third prong of the unfairness test, calling for a weighing of countervailing benefits against the relevant harm, with the substantial injury requirement. As shown above, the allegations in the complaint are more than sufficient to establish substantial injury.[10]

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[5] *See FTC v. Neovi, Inc.*, 604 F.3d 1150, 1157 (9th Cir. 2010), *amended*, 2010 WL 2365956 (9th Cir. June 15, 2010); *Orkin*, 849 F.2d at 1365; FTC Unfairness Statement n.12.

[6] Likewise, there is research indicating consumers do not register the vast majority of their complaints about problems with goods and services. *See* Amy J. Schmitz, *Access to Consumer Remedies in the Squeaky Wheel System*, 39 PEPP. L. REV. 279, 286 (2012).

[7] Dissenting Statement of Commissioner Joshua D. Wright ("Wright Dissent") at 1.

[8] *See id*. at 6.

[9] *Id.* (citation and internal quotation marks omitted).

[10] *See, e.g., Orkin*, 849 F.2d at 1365 (substantial injury demonstrated by small injury to large number of customers); *FTC v. Neovi, Inc.*, 598 F. Supp. 2d 1104, 1115 (S.D. Cal. 2008) (substantial consumer injury resulted from unauthorized charges to tens of thousands of consumers), *aff'd*, 604 F.3d 1150 (9th Cir. 2010); *FTC v. Global Mktg. Group, Inc.*, 594 F. Supp. 2d 1281, 1288-89 (M.D. Fla. 2008) (millions of dollars in unlawful charges demonstrated

B. Injury Not Reasonably Avoidable by Consumers

We also have reason to believe that consumers could not reasonably avoid the alleged injury. An injury is not reasonably preventable by consumers unless they had an opportunity to make a "free and informed choice" to avoid the harm.[11] Before billing parents for in-app charges by children, Apple presented parents with a generic password prompt devoid of any explanation that password entry approves a single charge as well as all charges within the 15 minutes to follow. We do not think parents acted unreasonably by not averting harm from a 15-minute window that was not disclosed to them. Consumers cannot avoid or protect themselves from a practice of which they are not made aware, and companies like Apple cannot impose on consumers the responsibility for ferreting out material aspects of payment systems, as FTC enforcement actions in a variety of contexts make clear.[12] Apple's disclosure of the 15-minute window in its Terms and Conditions was not sufficient to provide consumers with adequate notice.

Over time, through experience, some parents may infer that entry of a password opens a 15-minute window during which unlimited purchases can be made. The receipt of an invoice with unauthorized charges may be sufficient to alert some parents about the unwanted charges. But that does not relieve Apple of the obligation to take reasonable steps to inform consumers of the 15-minute window before the user opens that window and before Apple places charges on a bill. In light of Apple's failure to disclose the 15-minute purchasing window, it was reasonable for parents not to expect that when they input their iTunes password they were authorizing 15 minutes of unlimited purchases without the child having to ask the parent to input the password again. There was nothing to suggest this and thus no "obligation for them to investigate further" as Commissioner Wright suggests.[13]

C. Injury Not Outweighed by Benefits to Consumers or Competition

Finally, we also have reason to believe that the harm alleged outweighs any countervailing benefits to consumers or competition from Apple's practices. This is not a case about Apple's "choice to integrate the fifteen-minute window into Apple users' experience on the platform," as Commissioner Wright implies.[14] What is at issue is Apple's failure to disclose the 15-minute window to parents and other account holders in connection with children's apps, not Apple's use of a 15-minute window as part of the in-app purchasing sequence.

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substantial injury); *FTC v. Windward Mktg., Inc.*, No. 1:96-CV-615F, 1997 WL 33642380, at *11 (N.D. Ga. Sept. 30, 1997) (harm to large number of consumers sufficient to establish substantial injury).

[11] *Neovi*, 598 F. Supp. 2d at 1115.

[12] *See, e.g.*, *Facebook, Inc.*, No. C-4365, at 4 (F.T.C. July 27, 2012) (consent order) (requiring "clear and prominent" disclosure of certain information material to privacy protections "separate and apart from" the detailed privacy policy or terms of use); *Google Inc.*, No.C-4336, at 3-4 (F.T.C. Oct. 13, 2011) (consent order) (setting similar requirements).

[13] Wright Dissent at 10.

[14] *Id.* at 4.

Under the proposed consent order, Apple is permitted to bill for multiple charges within a 15-minute window upon password entry provided it informs consumers what they are authorizing, allowing consumers to make an informed choice about whether to open a period during which additional charges can be incurred without further entry of a password.[15] The order gives Apple full discretion to determine how to provide this disclosure. But we note that the information called for, while important, can be conveyed through a few words on an existing prompt. The burden, if any, to users who have never had unauthorized charges for in-app purchases, or to Apple, from the provision of this additional information is *de minimis*.[16] Nor do we believe the required disclosure would detract in any material way from a streamlined and seamless user experience. In our view, the absence of such minimal, though essential, information does not constitute an offsetting benefit to Apple's users that even comes close to outweighing the substantial injury the Commission has identified.

Moreover, we are confident that our action today fully preserves the incentive to innovate and develop digital platforms that are user-friendly and beneficial for consumers. In this respect, we emphasize that we do not expect companies "to anticipate *all* things that might go wrong" when designing a complicated platform or product.[17] Our action against Apple is based on its failure to provide any meaningful disclosures about the 15-minute window in the purchase sequence, despite receiving at least tens of thousands of complaints about unauthorized in-app purchases by children and despite having the issue flagged in high-profile media reports in late 2010 and early 2011.[18] We recognize that Apple did make certain changes to its in-app purchase sequence in an attempt to resolve the issue. Most notably, Apple added a password prompt to the in-app purchase sequence in March 2011. But for well over two-and-a-half years after that point, the password prompt has lacked any information to signal that the account holder is about to open a 15-minute window in which unlimited charges could be made in a children's app.

The extent and duration of the unauthorized in-app charges alleged in the complaint support our conclusion that, while Apple has strong incentives to cultivate customer goodwill in order to encourage the purchase of in-app goods and currency and promote the sale of its mobile devices, these incentives may not be sufficient to produce the necessary disclosures. Because customers are often unaware of the way in-app charges work, let alone the possibility of Apple disclosing its practices, we do not think that Commissioner Wright's belief that Apple "has more than enough incentives to disclose"[19] is justified. Indeed, his argument appears to presuppose that a sufficient number of Apple customers will respond to the lack of adequate information by

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[15] *See* Proposed Order ¶¶ 3, 5 (defining "Clear and Conspicuous" and "Express, Informed Consent").

[16] For this reason alone, it was unnecessary for the Commission to undertake a study of how consumers react to different disclosures before issuing its complaint against Apple, as Commissioner Wright suggests. We also note that the Commission need only determine that it has a "reason to believe" that there has been an FTC Act violation in order to issue a complaint. 15 U.S.C. § 45(b).

[17] Wright Dissent at 15 (emphasis in original).

[18] *See, e.g.*, Cecilia Kang, *In-app purchases in iPad, iPhone, iPod kids' games touch off parental firestorm*, WASH. POST, Feb. 8, 2011, *available at* http://www.washingtonpost.com/wp-dyn/content/article/2011/02/07/AR2011020706073.html; Associated Press, *Apple App Store: Catnip for Free-Spending Kids?*, CBS NEWS, Dec. 9, 2010, *available at* http://www.cbsnews.com/news/apple-app-store-catnip-for-free-spending-kids/.

[19] Wright Dissent at 14.

leaving Apple for other companies. But customers cannot switch suppliers easily or quickly. Mobile phone and data contracts typically last two years, with a penalty for early termination. In addition, the time and effort required to learn another company's operating system and features, not to mention the general inertia often observed for consumers with plans for cellular, data, and Internet services, could very well mean that Apple customers may not be as responsive to Apple's disclosure policies as seems to be envisioned by Commissioner Wright.

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We applaud the innovation that is occurring in the mobile arena. Today, parents have access to an enormous number and variety of apps for use by their children. We firmly believe that technological innovation and fundamental consumer protections can coexist and, in fact, are mutually beneficial. Such innovation is enhanced, and will only reach its full potential, if all marketplace participants abide by the basic principle that they must obtain consumers' informed consent to charges before they are imposed.