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## In-App Purchases: When They Are Not Just Child's Play...

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On January 15, 2014, the Federal Trade Commission ("FTC" or "Commission") announced a proposed settlement with technology giant Apple Inc. that will require the company to pay at least \$32.5 million in refunds to consumers. The proposed 20-year settlement resolves allegations that Apple violated the "unfairness" prong of Section 5 of the FTC Act by failing to obtain the express informed consent of parents before billing parents' iTunes accounts for in-app purchases made by children while playing popular mobile games. The FTC complaint and settlement order illustrate that the FTC remains focused on mobile platforms and mobile apps, especially where children are potential users.

### The FTC's Complaint

The FTC's administrative complaint alleges that Apple offers free and paid apps through its App Store, many of which are apps rated for children 4+, 9+, or 12+. Some of these apps



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allow a user to make virtual purchases within the app, such as acquiring virtual treats for use in a game. These in-app charges can range from \$0.99 to \$99.99 and can be incurred in unlimited amounts. For child-rated apps, Apple bills the parent for any in-app purchases through the parent's iTunes account, which is, in turn, funded by a credit card, prepaid card, gift card, or other account. Apple retains 30 percent of revenue for App Store transactions and in-app purchases. To make in-app purchases, the user is prompted to enter his or her iTunes password. In most cases, the parent enters the password on behalf of the child, which authorizes the child to make in-app purchases.

The FTC took issue with several of Apple's features for in-app purchases made in these child-rated games. First, the FTC contends that many of these apps were labeled as "FREE" in the App Store. Prior to download, the user was informed of in-app purchases through small print on a separate information page that stated "Offers In-App Purchases." Prior to April 2013, Apple did not display this language. The FTC alleges that neither the Search Tile of the app nor the Info Page explains what "In-App Purchases" are, including that they cost real money, how much they cost, or that entering the iTunes password will allow the user to incur in-app charges.

Second, the FTC alleges that Apple failed to inform parents that, by entering a password, the app could incur unlimited charges for the next 15 minutes. Specifically, when a user engages in an activity associated with an in-app charge, Apple displays a pop-up containing information about the virtual item and the amount of the charge. This pop-up, however, is displayed before the parent is prompted to enter his or her password, and children can clear the pop-up by pressing a "Buy" button. The FTC notes that Apple revised its order

process in September 2013, so that consumers were prompted to enter their iTunes password prior to choosing to "buy" within the app.

Lastly, after a parent enters the iTunes password, in some instances, the password is cached, or stored, for 15 minutes. During this time

period, Apple does not display additional password prompts for in-app purchases. The FTC alleged that this streamlined process allows a child user to incur additional, unlimited charges for those 15 minutes, which may not be authorized by the parent. The FTC contends that neither the charge popup nor the password prompt explains that entering the iTunes password approves the charge described on the charge popup and initiates a 15-minute window during which children can incur additional charges without further action by the account holder.

Through these practices, the Commission claims that Apple failed to give parents sufficient information for them to provide informed consent to the charges their children incurred, and that this omission is "unfair." The FTC's administrative complaint thus asserts a single claim for "unfairness" under the FTC Act on the basis of unfair billing, alleging that Apple failed to obtain the express informed consent of the account holder before allowing children to make in-app charges.

### Proposed Settlement

#### *Express Informed Consent for Purchases*

The proposed settlement, which will remain in effect for 20 years once finally approved, prohibits Apple from billing any account holder for any in-app purchase without having obtained the "express, informed consent" of the user. The settlement defines "express, informed consent" to mean that the user must be presented with options to provide or withhold consent, and must take an affirmative act communicating the informed authorization of the in-app charges.

If consent is sought for a specific in-app charge, the user must be informed of the in-app activity associated with the charge and that the account holder will be billed for the charge. In addition, if consent is sought for potential

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future in-app charges, the account holder must be informed of: (1) the scope of the charges for which consent is sought, including the duration and app or apps to which the consent applies; (2) the account that will be billed for the charge; and (3) any methods that the account holder can use to revoke or modify her consent.

#### *Clear and Conspicuous Disclosures of In-App Charges*

In addition, Apple must ensure that any disclosures are provided clearly and conspicuously before the user can incur an in-app charge. Such disclosures must be made proximate to the in-app activity for which there will be a charge. For purposes of settlement, the proposed order defines “clear and conspicuous” to mean that the disclosure in the app must be “in noticeable type, size, and location, using language and syntax comprehensible to an ordinary consumer.” Additional requirements are provided for audible and video disclosures. The disclosure also must not be combined with any other text or information that is unrelated or immaterial to the subject matter of the disclosure.

#### *At Least \$32.5M in Refunds*

The proposed settlement requires Apple to provide refunds to all iTunes account holders who incurred in-app charges by a minor when the charge was accidental or unauthorized. Apple is required to refund no less than \$32.5 million. Depending on the number of users who request a refund, Apple may be required to pay more than this amount. If this floor is not met, Apple will pay the difference directly to the FTC.

#### *Comments by the Commissioners*

The Commission approved the proposed consent order by a vote of 3-1, with Commissioner Wright dissenting. Commissioner Wright’s dissent is based on his view that there was limited harm to consumers, stating that these in-app charges apply only to “an extremely small – and arguably diminishing – subset of consumers.” Wright explains that the Commission should have conducted a more robust analysis to determine whether the injury to this small group of consumers justifies the finding of unfairness and the imposition of a remedy. Specifically, under the Commission’s unfairness authority, the FTC must not only show that the alleged injury is substantial, but that it is not “outweighed by any countervailing benefits to consumers or competition that the practice produces” and “it must be an injury that consumers themselves could not reasonably have avoided.” Commissioner Wright stated he did not believe that the FTC met this burden. Although there is

some injury to consumers that flows from Apple’s choice of disclosure and billing practice, this is “outweighed considerably by the benefits to competition and to consumers that flow from the same practice.”

Chairwoman Ramirez and Commissioner Brill also issued a joint statement, disagreeing with Commissioner Wright’s characterization of the injury and harm. The Commissioners state that the FTC’s actions apply to “at least tens of thousands of parents [who] have incurred millions of dollars in unauthorized charges that they could not have readily avoided.” They added that the FTC’s decision follows a long line of cases establishing that the imposition of unauthorized charges – regardless of the technology or platform used – is an unfair act or practice.

Commissioner Ohlhausen provided a separate statement in which she notes her concern about the use of the Commission’s unfairness authority in a way that might hamper incentives for innovation, but, in this case, she did not think that was the issue because a company has an obligation to notify customers of what they may be charged for and when prior to billing them. She noted that, here, Apple became aware of the billing issue from heavy complaints and failed to address it in subsequent design iterations of its product. She did not believe this Apple settlement should be understood to mean that a company has an obligation to anticipate every potential issue in its platform, but rather, once a company becomes aware of a sizeable billing issue, and particularly where there is already an iterative process to make updates, then it would be prudent to consider how to promptly make such design (including disclosure) updates.

#### **FTC’s Continued Interest In Mobile Platforms And Children’s Mobile Apps**

The proposed settlement with Apple is consistent with the FTC’s laser focus on mobile platforms and privacy and disclosures specific to children’s mobile apps. In February 2012, the FTC issued a staff report, entitled “Mobile Apps for Kids: Current Privacy Disclosures are Disappointing,” after surveying a number of mobile apps for children. The report recognized that “parents need consistent, easily accessible, and recognizable disclosures regarding in-app purchase capabilities so that they can make informed decisions about whether to allow their children to use apps with such capabilities.”

In December 2012, the FTC released a followup report, entitled “Mobile Apps for Kids: Disclosures Still Not Making the Grade.” The report notes that although both the Apple and

Android operating systems provide users with certain indicators that identify the ability to make in-app purchases, parents may not recognize these indicators, understand the meaning of the term “in-app purchase,” or understand that their children can make frequent and expensive purchases. These reports effectively put mobile platforms and app developers on notice that the FTC was paying close attention to in-app purchases available in children’s apps.

#### **Key Takeaways And Other Considerations**

In February 2013, Apple also entered into a settlement to resolve a class action lawsuit brought by parents similarly alleging that they were charged for unauthorized in-app purchases in children’s game apps. The settlement permitted qualified class members to receive a \$5 iTunes store credit or, if the charges totaled more than \$30, qualified class members could receive a cash refund for the aggregate charged. While that settlement was approved, it did not mean finality on the issue for the company. Indeed, this FTC settlement illustrates that, where a regulator believes a class action settlement falls short on required relief (injunctive or monetary, or both), it will not hesitate to initiate its own investigation and require additional relief.

The settlement also illustrates the Commission’s ongoing efforts to hold a company responsible for the conduct of third parties where a company financially benefits from the conduct of such third parties, and knew or should have known of potential conduct by such third parties that is deceptive or unfair. Here, the FTC alleged that Apple was aware of a high number of consumer complaints about unauthorized charges associated with in-app purchases by third-party apps that were downloaded or purchased in Apple’s App Store, but did not make sufficient changes to its mobile marketplace in response to such complaints. This settlement and other FTC actions against app developers reflect the Commission’s position that both the mobile marketplace and individual app developers are responsible for ensuring that charges to a consumer’s financial account are clearly and conspicuously disclosed and authorized, and that the failure to diligently ensure these steps are taken can result in a 20-year settlement with the Commission.

Thus, the settlement is a good reminder for app developers to review their advertising, marketing, and game experience (as well as consumer complaints) to assess whether existing disclosures may benefit from disclosure and process enhancements in line with the terms set forth in this latest settlement.