



FTC Informal Hearing on Proposed Amendments to the Negative Option Rule January 31, 2024

Judge Foelak:

Good morning. This is an informal hearing in the Negative Option Rulemaking matter, and I am Judge

Sarah Davies:

Hi, good morning, Your Honor. I'm Sarah Davies with the International Franchise Association. We will not be calling any witnesses, and I estimate approximately 10 minutes for our presentation today.

Judge Foelak:

Okay. I guess the NCTA is not going to appear.

April Taber:

Your Honor, this is April Taber, the secretary of the commission, the NCTA submitted a document at approximately 11:20 last night stating that they would not be appearing at today's hearing, but they did submit documents in lieu of testimony, which we have forwarded to your attention.

Judge Foelak:

Thank you. Those documents will be admitted as comments in the rulemaking. Okay. Please proceed, Miss Johnson.

Katherine Johnson:

Hi, good morning, Your Honor. As I indicated earlier, the Bureau of Consumer Protection will not be introducing any witnesses this morning.

Judge Foelak:

Okay, and you're not going to make any presentation. Okay. Okay, next. The IAB is up next.

Lartease Tiffith:

Great. Thank you, Your Honor, and thank you for this opportunity to speak today. Today we want to just again highlight some concerns we have about some of the substantive and procedural deficiencies with this process. First, IAB, we feel as though we've been prevented from exercising the statutory right to engage in cross examination, because the commission has not been ordered to put forward a witness in support of the facts underpinning the proposed rule.

Although the presiding officer's ruling states that, prior ruling, states ~~wit~~witnesses may be cross examined during the hearing, the commission has not designated any witnesses and the ruling does not require them to do so. Second, IAB and other interested person were given only three business days to prepare for this hearing, which deals with two disputed issues of material fact, designated for the first time by the presiding officer on January 25th. Thus, even if the commission decides or decided today to put forward a witness at the hearing, IAB would not have had a notice of the identity of that person and no ability to meaningfully prepare.

Finally, IAB, we've raised numerous other deficiencies with the informal hearing that have not been addressed, including that additional disputed issues of material fact be designated as such. All of the substantive and procedural defects have prevented the development of the record on issues that are critical to the promulgation of an appropriate rule. Any upcoming hearing, here, this hearing, exacerbates these problems rather than remedying them.

In addition to our prior objections and concerns, I also would highlight that even though the burden is not on us to put forward evidence, it is on the commission to support their rulemaking, we actually have put forward two expert reports, that you've seen prior to yesterday, which was one from Professor Nguyen from Morton, the other one that we have put forward yesterday is an additional one that's a

joint report by two experts, Professor Christopher Carrigan, who's at the George Washington University, and also from Scott Walster, who is a former assistant director in the Division of Economic and Risk Analysis at the FCC. They both are expert reports and all three experts support that there is a deficiency in the rulemaking process, and that the BCP and the commission have not met the burden, and that the costs are actually way higher than what they projected, so over \$100 million dollars easily. So I would just refer Your Honor to review those reports, and on behalf of everyone, we also believe that there is still time to have more process involved here, and that the commission should be forced to meet its burden before moving forward with the rulemaking.

Judge Foelak:

Thank you, sir.

Lartease Tiffith:

YepL s8(rd)4(.e)-2(q0.39 3xp9(s t) r)1er 669hTf2 0 ben 02 evarMare s9hTf2 0 612 7s0 1 0 0oe n4(fassu(y)-3(

dy(tge)fr 72a12 rttir 669hTf2r [(co)le(o)-5 0 g f 72.(o)-5iW* n BT e1.04 T* n BT /F2 11 rtwon(o)-24 467. G [n

Many of those arguments you put forth in your petition, firstly in reference to the FTC not putting forth a witness, well, if there is a disputed material fact and there's no evidence on one side and there's evidence on the other side, then it's no contest. So that should not be a problem. Okay. The time constraints that you refer to are real, but they're per the Federal Trade Commission rule. However, your objection is noted for the record. Correspondingly, your argument concerning that there should be more disputed issues of material fact, those arguments are also noted for the record, the objections are noted for the record here t24 669hTf2 0 612 7s0 1 0 0 by two experts, P .sTfe ,05e00000912 0 612 792 re W* n BT

How about this idea? How about another hearing session next week at which one or both of the experts would appear?

Lartease Tiffith:

Your Honor, both of the experts are actually professors and they have difficult schedules. I think the earliest that they could be available is on the day of the 14th of February, so we can make them available that day, but that's based on their schedule.

Judge Foelak:

Okay. Well, if they're not available, they're not available. Okay. Until the 14th. Okay. So we will schedule a hearing with them by the same virtual means at 10:00 AM on ~~the~~ ~~the~~.

Lartease Tiffith:

And Your Honor, I would also ask that the Commission be required to put forth support for its basis for that there is the cost of compliance and so forth for this rulemaking would be under \$100 million. I think in fairness that they have not met their burden and that they should be required to do so at this next hearing. So through their own evidence, their own witness in particular, would be I think appropriate for you to require that they submit someone for ~~exa~~ ~~exa~~mination on that date. Perhaps, Mr. Harris.

Judge Foelak:

Does the BCP have any response to that?

Harris Senturia:

Well, Your Honor, as Ms. Johnson said earlier, we are not presenting any witnesses and as far as the basis, the FTC's sort of discussion of its basis, the actual reports, both Professor Wynn's and, I think it's Wynn, and the one we received last night, cite heavily to the NPRM, and so we think that the basis that are listed in the NPRM are therefore within the record.

As far as going forward, Your Honor, candidly, I'm not authorized to say anything other than we don't have any witnesses, but we do appreciate the opportunity to ask some questions about the assumptions behind the experts' reports.

Judge Foelak:

Very good. Like I said before, Mr. Tiffith, if there's no evidence put forth on one side and evidence put forth on the other side, then there's actually no issue, so it shouldn't really be a problem for you. Okay. Do we have anything more for the IAB matter or should we move on

Lartease Tiffith:

No, I

Judge Foelak:

Go ahead.

Lartease Tiffith:

Yeah, no, I think from the IAB perspective, we understand Your Honor's decision about having a further opportunity for our experts to appear on the 14th.

Judge Foelak:

Okay, very good. Next, Ms. Davies.

Ms. Davies:

Hi, good morning again. I'm Sarah Davies, and again, appreciate the opportunity to testify on behalf of the International Franchise Association, the world's oldest and largest organization representing franchising and our membership, which is comprised of franchisors and franchisees and suppliers to franchise companies.

Your Honor has identified two disputed issues of material fact that are the focus of today's hearing. And I want to focus on the second issue related to cost of compliance with disclosure and record keeping requirements under the FTC's proposed negative option goal. To understand the impact of cost we need to consider first the parties bearing the cost. I'm here today on behalf of our small business members. Franchising is small business. More than 80% of franchise owners operate just one location. More than 50% of brands in operation today have less than 20 units, and nearly a third of all franchisors make less than 5 million per year.

So while franchise businesses operate under the same trademark ~~system~~, they're independent

seek technology modifications from third party providers of membership agreement management and payment processing services all at additional cost. These costs were not considered by the FTC and its analysis when issuing the proposed rule, and they far exceed the estimates provided by the FTC and its notice of proposed rulemaking. And these costs are costs that small businesses cannot sustain, particularly in the current economic climate.

The FTC should pause what feels like a rush rulemaking and conduct a thorough cost benefit analysis as required under Section Five of the Magnuson Act and the other federal statutes. We also renew our requests of the FTC undertake a small business regulatory impact analysis so that its rulemaking may be informed by data of the actual cost incurred by small business owners, particularly those in franchise systems and their consumers.

IFA and its members welcome the opportunity to work with the FTC to provide such data and cost information. Thank you

Ms. Davies:

... again for the opportunity to appear and share the concerns of the franchise community.

Judge:

Thank you. Okay. That concludes-the

Katherine Johnson:

Your Honor, this is Jonathan Ware from the Bureau of Consumer Protection. Similar to with Mr. Tiffith, we had some questions and appreciate the opportunity to address to Ms. Davies.

Judge:

Okay. Please do.

Katherine Johnson:

Good morning, Ms. Davies, and thank you for your comments here today, as well as the January 23rd, 2024 submission on behalf of the International Franchise Association, as well as the comments from last summer the IFA submitted in response to the notice of proposed rulemaking, the NPRM, that's at 88 Federal Register at page-246.

I wanted to start first just making sure the record's clear of what's been submitted. In your January 23rd, 2024 letter, you cite some cost estimates from a preventive healthcare franchise and some fitness franchise system. Were any of those businesses among the 16,000 comments that were submitted to the FTC last summer in response to the NPRM?

Ms. Davies:

They were not.

Katherine Johnson:

The comments you've provided note that the franchising covers 3000 brands and 800,000 in businesses. You've talked about a couple examples today and in your letter of January 23rd. Can you tell us a little bit about how those examples were chosen and how reflective they might be of IFA members in those particular industries?

Ms. Davies:

Sure. So they were selected to provide a cross section of the industries that are impacted by the rule. IFA's membership spans hundreds of industries. Not all of those industries are impacted by the rule, but that there are substantial number of industries that are including the ones that I highlighted here today and represents a significant portion of IFA's membership. It goes beyond just what you would typically think of in the membership space in fitness to a number of other industries that access and use monthly membership models.

Katherine Johnson:

Okay. And I just want to understand and appreciate there's limits to what you may be able to be informed to talk about, is it right that the cost estimates you've given are things that were conveyed to IFA that you're now passing along to the presiding officer?

Ms. Davies:

Correct.

Katherine Johnson:

And can you tell us a little bit about how you received those? Is it a phone call? Is there some sort of detailed accounting documentation that you received that you then summarized? What can you describe about how these estimates came to you?

Ms. Davies:

Communications from our member brands based on conversations that we've had, and internal resolution.

Katherine Johnson:

Okay. And

Ms. Davies:

Go ahead.

Katherine Johnson:

No, sorry for speaking over you. Looking at your January 23rd, 2024 letter, it looks like it's describing a singular preventive healthcare franchise system that's on page one and two. Is that right? It's one preventive healthcare?

Ms. Davies:

Correct. Yes.

Katherine Johnson:

And what can you tell us about the scale, size, and complexity of that entity in terms of things like employees, locations, number of consumers, service, transactions, revenue, so we can get a sense of its relative proportion to the other entities in that industry?

Ms. Davies:

I would have to provide, I mean, I would have to look into additional information as to the number of transactions, their membership rates. It's for us, it's an average size system in that space. So I mean, it could estimate a couple hundred units, systemwide, few hundred, but I would have to confirm the precise number.

Katherine Johnson:

I believe I've read in some of your comments that something like 90% of healthcare franchises are 10 or fewer locations. Is that approximate

businesses. It's not as simple as updating the terms of service, on a digital subscription and clicking agree to continue using the app.

Katherine Johnson:

So I just want to be clear, because at the outset I was asking about the scale, size, and complexity of the source of this information, and I understood you to say you didn't have information on that size and now you're describing it as a small business. Can you elaborate or have you been able to refresh your recollection of the size, scope, or complexity of the preventative healthcare system that gave you this information that's in your January 23rd, 2024 letter?

Ms. Davies:

Right. No, it's not inconsistent. I mean, the reference to small business is that this is a franchise system that is comprised of hundreds of small businesses. And so while the information is provided by our member brands, which are the franchisors, it's ultimately the small businesses that will have to comply that operate under those marks. So these are not isolated businesses that I'm testifying on behalf of franchise systems or networks, small businesses, significant number of small businesses.

Katherine Johnson:

Forgive me if I'm confused because I understand the example again, we're talking about of the preventative healthcare franchise system is one entity that perhaps has franchisees beneath it and I hear you talking about the data is about multiple entities in the business. Can you help get clarity of the example again, you're giving on page one of your January 23rd, 2024 letter. That relates to a singular preventative healthcare franchise system, is that right?

Ms. Davies:

Ms. Davies:

Those estimates relate to the costs that are anticipated to be incurred by the franchisor. It doesn't take into account the additional costs that will be required for compliance at the individual unit level by all of the independent small businesses.

Katherine Johnson:

Okay. And you don't know anything about the size or scale or scope of that franchisor as you sit here now?

Ms. Davies:

I'm happy to provide information. They were included as examples. We would be happy to work with the FTC on a more robust cost-benefit analysis related to the role, so that the FTC can meet its burden of doing a cost-benefit analysis. But as I sit here today, no, I cannot provide the stats on the number of units in that specific system.

Katherine Johnson:

Okay. And I fully understand and appreciate you are a representative of the association and you're relaying the information you got secondhand. So I don't at all mean to come across as confrontational. I

