

LEGAL

## Ecommerce's pitfalls: Diving into FTC's mail order rule

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The online retail landscape is not without its challenges, and the Federal Trade Commission (FTC) has recently spotlighted one such case involving Hey Dude Inc., an online shoe retailer.

While the \$1.95 million settlement announced in September is significant, the FTC's complaint underscores broader issues concerning retailer practices and adherence to FTC regulations.

In this article, I use this recent case as a lens to explore the FTC's "Mail Order Rule" along with other pitfalls in online retail operations.

Whether you are a seasoned online seller or new to ecommerce, understanding these crucial aspects is essential for cultivating a compliant and transparent business model while fostering and safeguarding consumer trust.

### Background

The FTC filed a complaint and proposed order and settlement against retailer Hey Dude, accusing the company of a number of deceptive practices, including violations of the FTC's "Mail Order Rule," as well as violations for allegedly suppressing negative reviews.

Hey Dude, which was acquired by Crocs Inc. in February 2022, allegedly misled consumers by suppressing negative reviews, omitting more than 80 percent of reviews with less than four stars out of five. Between January 2020 and June 2022, Hey Dude selectively published only positive reviews, changing its approach only when under FTC investigation.

The FTC also claimed Hey Dude violated the FTC's Mail Order Rule by not issuing shipping delay notices, failing to cancel orders and provide timely refunds, and issuing gift cards instead of required refunds.

The proposed court order aims to prevent future violations, mandating the publication of all reviews with limited exceptions, and imposes a \$1.95 Million monetary judgment to compensate affected consumers.

### Mail Order Rule

The FTC rule requires a retailer to have a "reasonable basis" for any promised shipping date. If no specific date is given, then the FTC sets 30 days as the default. Reasonable basis means that there is sufficient objective information for a businessperson to be satisfied that the representation is correct.

Relevant factors to consider include anticipated demand, supply, fulfillment procedures and record-keeping logistics associated with the order.

A seller has to continually evaluate whether the promised shipping time is reasonable and will likely be satisfied. If the facts change such as a delay from suppliers or a surge in orders, sellers need to reevaluate any promised shipping times. Such reviews are often done in any event by online sellers, so compliance is not going to be difficult. Doing so with an eye to FTC compliance avoids potentially costly fines.

What if orders are delayed?

Delays happen despite the best of good faith intentions. What then?

One option is to cancel the order, for a full refund. If the seller does not believe it will be able to fulfill the order, the FTC requires that it *must* cancel the order and provide a full refund.

If, on the other hand, the seller believes it will eventually be able to fill the order, but only that it will be delayed, then it can provide a delay notice to customers. The delay notice has to provide a new expected shipping date and offer the customer the option to cancel the order for a full refund.

The first time there is a delay, the seller may state that if the customer does not cancel, it will assume that the customer agrees to the delayed shipment, so long as the new shipping date is not more than 30-days out from the notice of delay.

When delays happen, then it is important that the delay notice be carefully reviewed to make sure that it complies with the FTC rule, and that customers are offered an easy and cost-free method of cancelling. Doing so is an easy way to avoid expensive trouble with the FTC.

Refunds: Full credit

Required refunds must be provided within seven days. Refunds must be through a credit to the customer's credit card or other payment method, like PayPal, *not* through vouchers, scrip or store credit. This is one of the rules that Hey Dude allegedly violated, and the FTC tends to be very strict about enforcing.

Recommended record keeping

The FTC strongly recommends that merchants keep records that substantiate compliance with the rule, and warns that if it takes action against a seller, then the seller bears the burden of proving that it has complied with the FTC rule. Without contemporaneous adequate records, this may be impossible.

Such documentation should provide answers to the following questions:

*Is there substantiation for shipment representations?*

- How is demand anticipated?
- How is inventory monitored?
- How is inventory acquisition coordinated with customer demand and order cancellation?
- How are demand needs communicated to and met by buyers/suppliers/drop shippers?

*How does the fulfillment system work?*

- How is the fulfillment system designed to meet the requirements of the FTC's rule?
- Are the delay option notices in compliance?
- Does the customer's exercise of a cancellation option result in a prompt refund response?

*Is recordkeeping adequate?*

*Are adequate records kept for each individual order?*

- Date the order was received
- The contents of and date of any delay option notice
- The date any exercise of a cancellation option was received
- The date of any shipment and the merchandise shipped
- The date of any refund and the merchandise for which the refund was made?

Best practices are to maintain these records for five years, the statute of limitations for FTC enforcement. Of course, in

Best practices are to maintain these records for five years, the statute of limitations for FTC enforcement. Of course, in the age of computers, maintaining such records should be fairly easy, so long as a proper system is set up to substantiate compliance.

Compliance with the FTC rule is the seller's responsibility

It is the *seller* who is responsible for compliance with the rules. Sellers who rely on third parties, such as drop-shippers or Amazon's fulfillment services, to fill orders cannot use delays caused by these third parties as an excuse to avoid the rule. Sellers have to take all reasonable efforts to make sure that the third-party is acting consistently with any promises made by the seller.

Substitutions

If a seller cannot fill the order, can it substitute a different, comparable item? The answer depends on whether the substitute is "materially different" from what was ordered. If not materially different, then the substitution can be made. But if it is materially different, then the FTC requires that the customer must consent to the substitution, or be offered a refund.

"Materially different" means that the merchandise differs in some manner that is likely to affect the customer's choice of the merchandise. This can include many seemingly minor differences, including differences in design, style, color, fabric or promoted end use. The FTC considers *any* product characteristics mentioned or depicted in advertising to be "material."

Again, once properly understood, this rule is not difficult with which to comply. The easiest course and also the most customer friendly is to always offer the customer the option of a refund or substitution. Inattention to this requirement potentially can lead to expensive FTC enforcement.

Avoiding enforcement by the FTC

The FTC is charged by law in enforcing these rules, and the enforcement can be painful, including steep civil fines and orders for consumer refunds. The Hey Dude settlement is only the latest of numerous FTC settlements for violations of the Mail Order Rule.

Given this history of large settlements, online sellers are well advised to invest some time and effort to ensure they are in compliance with the FTC rules. The relative cost of ensuring compliance is small and may well avoid much larger expenses down the road.

*The views expressed in this article are purely the author's.*

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