

Center for Regulatory Effectiveness

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via mail, e-mail, and fax: 202-326-2012

Mr. Donald S. Clark
Secretary
Federal Trade Commission
600 Pennsylvania Ave., NW
Washington, DC 20580

Petition to Commence Trade Regulation Rule Proceedings

Dear Mr. Clark:

This petition is being filed by the Center for Regulatory Effectiveness (“CRE”) under 16 CFR § 1.9,¹ 15 U.S.C. § 57a(a)(1)(B)² and 5 U.S.C. § 553(e).³ The purpose of the petition is to request the Commission commence a notice-and-comment trade regulation rule proceeding that will “define with specificity acts or practices which are unfair or deceptive acts or practices in or affecting commerce” within the meaning of §§ 5 and 18 of the FTC Act (15 U.S.C. §§ 45(a)(1)⁴ and 57a(a)(1)(B))⁵ for web-based companies providing search capabilities, social networking services and online advertising to the general public. The proposed trade regulation would need to be consistent with 5 U.S.C. § 45(n) which states that:

The Commission shall have no authority . . . to declare unlawful an act or practice on the grounds that such act or practice is unfair unless the act or practice causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or to competition.

¹ “Trade regulation rule proceedings may be commenced by the Commission ... pursuant to written petition filed with the Secretary by any interested person stating reasonable grounds therefore.”

² “[T]he Commission may prescribe -- (B) rules which define with specificity acts or practices which are unfair or deceptive acts or practices in or affecting commerce (within the meaning of section 45(a)(1) of this title). ... Rules under this subparagraph may include requirements prescribed for the purpose of preventing such acts or practices.”

³ “Each agency shall give an interested person the right to petition for the issuance, amendment, or repeal of a rule.”

⁴ “Unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce are hereby declared unlawful.”

⁵ *Id.*, note 2, *supra*.

Google, Facebook, Twitter and the FTC

Google, Facebook and Twitter have much in common. All three firms are very popular web-based firms that have pioneered or reinvented their primary area of expertise. All three businesses are American companies that have changed how the world uses the internet. Of particular note, all three companies provide their primary services to consumers for free.

Also of note, all three firms are reported to be either under FTC investigation (Google and Twitter) or the subject of a petition to the FTC to be investigated (Facebook).

Google, Facebook and Twitter share another commonality, one that has direct implications for assessing their business practices and which sets them apart from many other IT-related firms – all three companies are examples of businesses which operate in two-sided markets serving two interdependent sets of customers.

The defining characteristic of firms operating in two-sided markets is that they have two distinct supply and demand curves, one set for each side of the market, newspapers being a classic example. No one would expect newspaper subscribers and advertisers to share the same elasticity of demand since advertisers value and pay more for access to the newspaper (and its readers) than readers are willing to pay for the paper and access to its advertisers.

The trade regulation developed by the Commission should take into account that web-service companies need to appeal to, and bring together, two distinct groups of clients. As Evans and Schmalensee explained,

Antitrust analysis, tools, and techniques require modification when two-sided platforms account for a significant portion of supply. Failure to account for the consequences of interlinked demand between the two sides can lead antitrust analysis into serious error.⁶

Before commencing/continuing with their investigations, the FTC needs to develop a trade regulation that provides for objective assessment as to whether the business strategies and practices of web-based services companies in two-sided markets are unfair. In the absence of the rule, the agency would lack a sound intellectual and legal framework for its work which would open the door to inadvertently harming, not enhancing, the global competitiveness of American businesses and consumer welfare.

Objectively Defining Unfair Competition: An Integral Component of a Trade Regulation

The key function of a trade regulation for web-based services would be to provide Commission staff and the companies themselves with guidance, within the context of Subsection “n,” as to what constitutes unfair or harmful conduct. Commissioner Kovacic recently discussed the importance of a competition agency setting transparent measures for assessing conduct in the *European Competition Journal*, when he explained that:

⁶ David S. Evans & Richard Schmalensee, Markets with Two-Sided Platforms, in 1 ISSUES IN COMPETITION LAW AND POLICY 667 (ABA Section of Antitrust Law 2008), p. 667.

The clear definition of goals increases transparency and facilitates public discussion about the agency's performance. By articulating its aims and supporting assumptions, the agency gives better guidance to external groups—for example, business managers—about its priorities, its understanding of the law and its decision-making processes. Such disclosure is likely to have a knock-on effect by allowing the agency to have influence in the market by means beyond enforcement actions alone.⁷

The Commissioner's discussion was in the context of assessing and improving the performance of competition agencies such as the FTC. The need for transparent, objective competition assessments however, holds true irrespective of whether they are used to measure the Commission's performance or the performance of the companies it regulates since these are two sides of the same coin.

Thus, development and promulgation of a trade regulation for web-based services companies operating in two-sided markets would be, in and of itself, beneficial for competition and the agency's performance. As Commissioner Kovacic stated,

A competition agency that does not release meaningful information impedes the assessment of its work. Good disclosure is an essential ingredient of the transparency that holds government agencies accountable and promotes improvements in public policy. Thus, a key measure of the quality of an agency's process is quality of disclosure.⁸

The Role of the Emerging Technologies Interagency Policy Coordination Committee

On March 11, 2011, three senior White House officials sent a Memorandum to the heads of all Departments and Agencies establishing principles for regulation and oversight of emerging technologies.

In the memo, the Administrator of the Office of Information and Regulatory Affairs (OIRA), the Director of the Office of Science and Technology Policy (OSTP) and the Chief Agricultural Negotiator for the United States Trade Representative (USTR) directed that agencies adhere to an extensive set of regulatory principles including using benefit-cost analysis, using the "best reasonably obtainable scientific, technical, economic, and other information" and engaging in interagency and international coordination.

The advanced algorithms which determine everything from how online advertising is targeted at specific users to how search results are displayed are unquestionably an emerging technology.

The agency which FTC needs to coordinate its web-based services competition policy with is the Department of Justice/Antitrust.

⁷ W.E. Kovacic, H.M. Hollman and P. Grant, "How Does Your Competition Agency Measure Up?" European Competition Journal, April 2011, p. 31 available at <http://www.ftc.gov/speeches/kovacic/1104agencycompetition.pdf>

⁸ Id., p. 40 [Emphasis added].

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Of particular note, the memo from the Co-Chairs of the White House's Emerging Technologies Interagency Policy Coordination Committee (ETIPC) emphasized that "relevant information should be developed with ample opportunities for stakeholder involvement and public participation."

The Role of the Data Quality Act

The Data Quality Act (DQA)⁹ requires that all information disseminated by the Commission meet OMB and FTC standards for quality including utility, objectivity and integrity. The trade regulation requested by this petition, and any supporting data and/or studies, will need to comply with the requirements of the DQA as evidenced through the agency's pre-dissemination review of the document.

The U.S. Court of Appeals for the D.C. Circuit explained that agency compliance with the DQA is a non-discretionary duty. In *Prime Time Int'l Co. v. Vilas*, 599 F.3d 678 (D.C. Cir. 2010), the court ruled that OMB's DQA guidelines were "binding" because they contained a permissible interpretation of the DQA under *Chevron*. In doing so, the Court clearly held that the OMB interpretation was entitled to *Chevron*-level deference (as opposed to a lower level of deference under *Skidmore*), because the OMB guidelines have the "force of law," having been promulgated under a specific Congressional delegation in the DQA.

The Department of Justice was extraordinarily concerned about the implications of the opinion and filed a petition for a rehearing. Justice's petition cited CRE's analysis explaining that the *Prime Time* opinion effectively held that the DQA Guidelines have the force of law as the motivating force behind their appeal. The Department even included a lengthy printout of CRE's website as an Appendix to their petition.¹⁰

In short, the Court held that the OMB guidelines are legally binding, not just internally binding, or as might be the case with many Executive orders and agency manuals or handbooks.

Conclusion

It is premature for the FTC to proceed into any investigation of web based services until the petitioned-for rules are developed through a notice and comment process.

In summary, the Commission needs to develop and publish for public comment a proposed trade regulation, consistent with the statutory requirement that a practice may not be determined unfair unless it "causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and not outweighed by countervailing benefits to consumers or to competition."

⁹ Consolidated Appropriations Act, Pub. L. No. 106-554, § 515, 114 Stat. 2763, 2763A-153 (2000).

¹⁰ DOJ's Petition for Rehearing is available at http://thecre.com/pdf/20100527_PrimeTime_GovPetfon.pdf. The court opinion is available at http://thecre.com/pdf/20100414_DQA_Prime.pdf.

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Unless the Commission has a trade rule in place for web-based services companies that operate in two-sided markets, *e.g.*, Google, Facebook and Twitter, prior to commencing an investigation, the result would be a public perception of the agency interpreting ambiguous rules to obtain a preconceived solution.

Respectfully,

A handwritten signature in black ink, appearing to read "Jim J. Tozzi". The signature is stylized with a large initial "J" and "T".

Jim J. Tozzi
Member, CRE Board of Advisors