

Berkeley Center for Law & Technology

The Price of “Free”



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“Old” media & communications cost money

New Media is “Free”

facebook

Email

☐ Keep me logged in

Password

Forgot your

disabled on your browser

JavaScript or upgrade to a JavaScript-capable browser to use Facebook. Alternatively, you can access the [mobile version](#) of Facebook.

Facebook helps you connect and share with
the people in your life.

Sign Up

It's free and always will be.

CHART OF THE DAY:

Here's How Much A Unique Visitor Is Worth

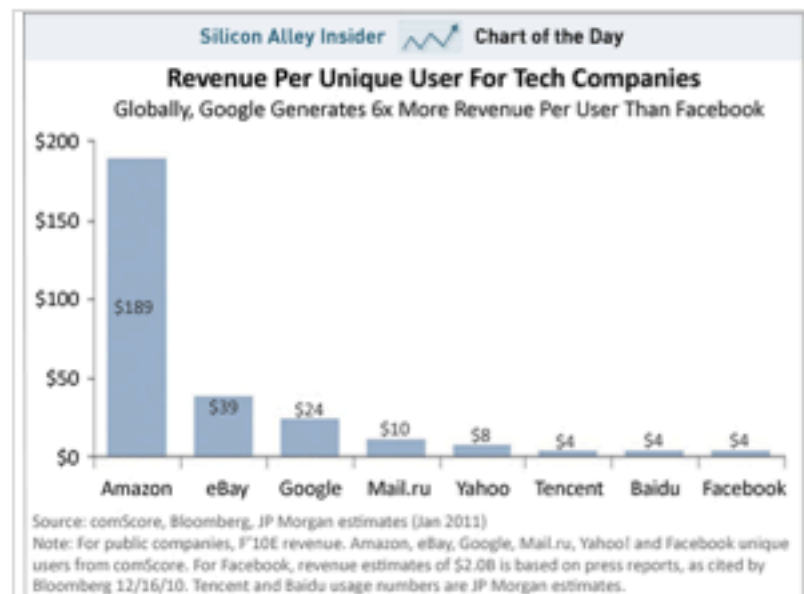
Jay Yarow | January 05, 2011 | 🔥 15,442 | 💬 9

Want to get the Chart Of The Day a day earlier? Sign up for our Chart of the Day email.

How much is a unique visitor worth on the Internet?
Depends on who you are.

Amazon (e-commerce) is generating \$189 per user. Google (search) is generating \$24 per user. Facebook (social networking) is only generating \$4 per user according to this chart from JP Morgan's Imran Khan.

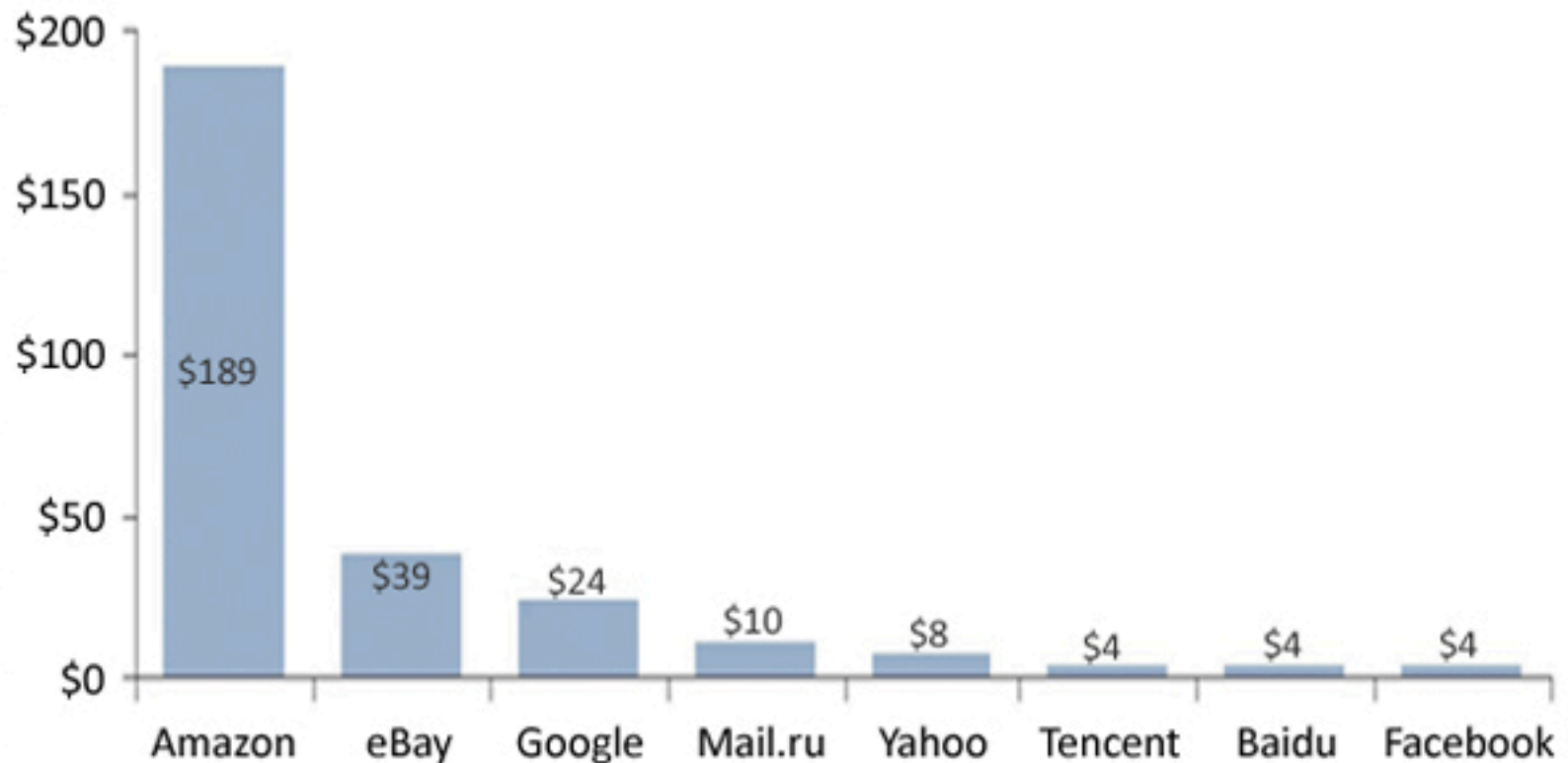
Khan is optimistic Facebook starts bringing in more revenue over time. He sees Facebook as a new platform for the web and thinks it will be able to pick up revenue from applications and games.





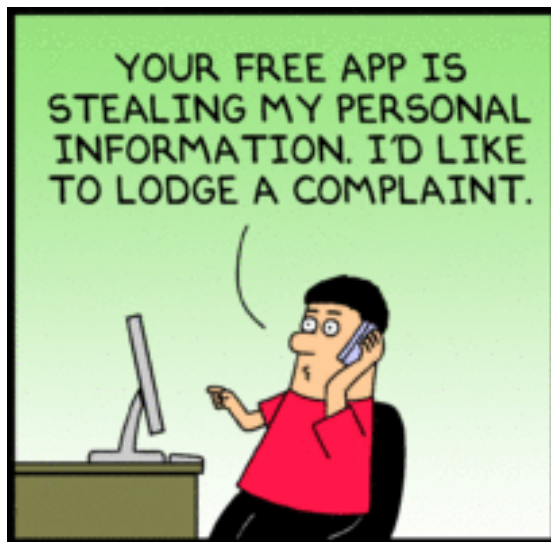
Revenue Per Unique User For Tech Companies

Globally, Google Generates 6x More Revenue Per User Than Facebook



Source: comScore, Bloomberg, JP Morgan estimates (Jan 2011)

Note: For public companies, F'10E revenue. Amazon, eBay, Google, Mail.ru, Yahoo! and Facebook unique users from comScore. For Facebook, revenue estimates of \$2.0B is based on press reports, as cited by Bloomberg 12/16/10. Tencent and Baidu usage numbers are JP Morgan estimates.



Dilbert.com DilbertCartoonist@gmail.com



5-3-12 ©2012 Scott Adams, Inc. /Dist. by Universal Uclick



“People also seem to understand there's no such thing as a free lunch, even online, summarized by the truism ‘If you're not paying for something, then you're not the customer—you're the product being sold.’ ”

L. Gordon Crovitz, *Will Regulators Unfriend Facebook?*, WSJ, May 21, 2012

Caveats

Not addressing “true gifts.” These are really free to the consumer

Sample of food at the shopping mall

Not addressing introductory offers. Consumers understand these bargains.

Mead Paradox: under existing FTC decisions, businesses may attach a commercial obligation to a free offer, so long as it is clearly disclosed!

David Friedman— Behavioral Econ & Free Offers

Free offers skew consumers’
understanding of value through
bundling

Free offers create reciprocity
norms that are powerful,
uneconomical

38 New Mex. L. R. 49 (2008)

FREE OFFERS: A NEW LOOK

DAVID ADAM FRIEDMAN*

INTRODUCTION

Free offers—the practice wherein firms market goods, services, and their brand to consumers by claiming that they are “free”¹—have been overlooked for too long. These offers have become so ingrained into consumer culture² that they often go unnoticed, viewed as part of the natural commercial landscape. The courts and the Federal Trade Commission (FTC) have effectively left free offer regulation untouched since the 1950s.³ Even legal scholarship has largely ignored free offers.⁴ This Article argues that advances in the study of human behavior require a new look and a new approach to the half-century-old free offer regulatory regime.

Why do these offers exist? After all, the purpose of a commercial enterprise is not rooted in the altruism of giving away goods and services for free. Free offers exist to lure potential customers to a specific offering, to bring them to the commercial enterprise where an offering can be presented, or to create an often-hidden psychological tie between customers and the enterprise that helps induce a sale.

A truly free offer would be a gift. In contrast, a “free” offer attached to another definite commercial commitment is not free under a common understanding of the word. Under the current legal standard, however, the use of the word “free” is lawful provided there is adequate disclosure of the attached commercial commitment.⁵

Jens Grossklags & Alessandro Acquisti



Behavioral Econ & Privacy

Bounded rationality

Consumers don't know the rules (Turow et al. 2009)

Problem of the privacy resilient & privacy vulnerable

Many probably think the internet is like a TV

Information asymmetries

Optimism bias

Transaction Cost Economics

In TCE, price is important, but so is efficiency

What are the special attributes of personal info transactions?

What governance structures will align parties, and prevent ex post maladaptation?

Attributes of PII Transactions

Email Marketing Unsubscribe.

You can use this page to unsubscribe from SMI email marketing campaigns. Please see typical reference looks like 'F43 M PZ 12345678' or 'URN 12345678' - the numbers in Please allow up to **14 days** for your removal request to be processed.

☐ Please unsubscribe me from Email campaigns

Unique Reference Number:

Email:

submit >>

Attributes of PII Transactions

Barriers to opting out (Schwartz, Janger, Sovern, Shah)

Monitoring costs

- Dr. Koop.com > sold to vitamin company

- FB' s shifting default from private to public

- Gag order provisions make monitoring impossible

Search & negotiation

- TLDR

- Counter-advertising lacking

Attributes Continued

Circumvention of selective revelation

- Enhancement/data appends

- Pineda/Acxion phone lookups

Insecurity

- Epsilon breach

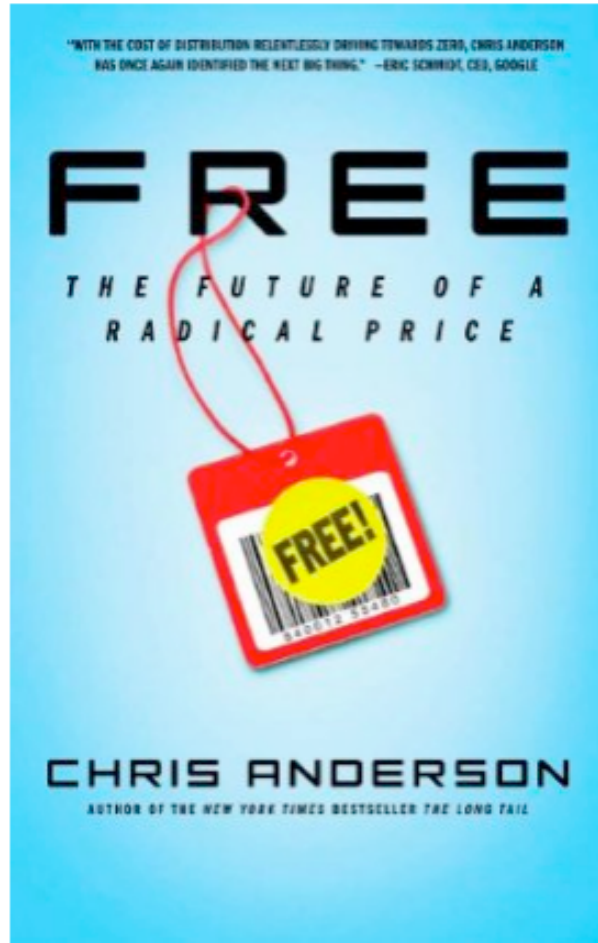
No exit

- Data are scooped up by bottom feeding sites

Displacement of better products

PII transactions are not free

Chris Anderson's Free



BOOKS

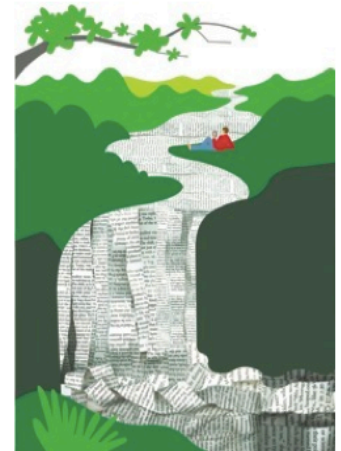
PRICED TO SELL

Is free the future?

BY MALCOLM GLADWELL

JULY 6, 2009

At a hearing on Capitol Hill in May, James Moroney, the publisher of the *Dallas Morning News*, told Congress about negotiations he'd just had with the online retailer Amazon. The idea was to license his newspaper's content to the Kindle, Amazon's new electronic reader. "They want seventy per cent of the subscription revenue," Moroney testified. "I get thirty per cent, they get seventy per cent. On top of that, they have said we get the right to republish your intellectual property to any portable device." The idea was that if a Kindle subscription to the *Dallas Morning News* cost ten dollars a month, seven dollars of that belonged to Amazon, the provider of the gadget on which the news was read, and just three dollars belonged to the newspaper,



"In the digital realm you can try to keep Free at bay," Chris Anderson writes, "but eventually the force of economic gravity will win."

Anderson

“Twenty-first-century Free is different from twentieth-century Free. Somewhere in the transition from atoms to bits, a phenomenon that we thought we understood was transformed. ‘Free’ became Free.”

Hoofnagle & Whittington

But 21st century free really is no different...

“Free” credit reports

Scams, hidden costs

Club Penguin

Hidden costs

Anderson’s example of “free” DVRs

Hidden costs

Chris Anderson's "Free"



How can a DVR be free?

- A) Add hidden fees. Comcast charges a \$19.99 installation fee to every new DVR customer.
- B) Charge a monthly subscription. Comcast customers pay \$13.95 a month to use the DVR box. Even if Comcast paid \$250 for its DVRs—a very high estimate—the boxes would pay for themselves within 18 months.
- C) Upsell other services...

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Federal Regulation of “Free”

FTC Guide Concerning Use of the Word “Free” and Similar Representations.

Promulgated in 1971

On regulatory review calendar for 2017!

16 CFR § 251 (2011)

FTC Free Contours I/4

No direct cost recovery. Cannot simply charge more for some other product to subsidize “free” offer

In the Matter of The Perfect Manufacturing Co., D/B/A The So-Lo Works, 43 F.T.C. 238 (1946-47)(“the cost of its product offered as ‘free’ was included in the purchase price of other merchandise purchased, and the so-called ‘free offer’ was nothing more nor less than a combination offer.”)

Contours Continued 2/4

Seller must establish a regular price

The FTC has also been concerned with sellers representing that a product is free “for a limited time,” when in fact there is no temporal bound to the offer.

In the Matter of Carpets R ’ Us, Inc., 87 F.T.C. 303 (1976), the Commission objected to a carpet seller who offered free installation. The Commission ordered the company to refrain from making free offers, unless they were based upon some established price.

Contours Continued 3/4

FTC has relied upon price attributes rather than PII for enforcement

In the Matter of S. W. Pike, Seedsman, Inc., 18 F.T.C. 82 (1933-34), a seed seller represented that it, “would send free...packages of assorted flower seed...for five names of friends who love flowers and 20 cents to cover packing and postage...” In reality, in order to enjoy the free seeds, the customer had to make an order from the seller’s catalog. The FTC ordered the retailer to cease and desist from representing the seeds, bulbs, and flowers as “free.”

Contours Continued 4/4

“Mead Paradox:” pecuniary obligations can be attached to a “free” offer!

The FTC declared the use of free offers was general unfair and deceptive, unless two conditions were met. First, conditions and obligations must be set forth at the outset of the offer, “so as to leave no reasonable probability that the terms of the advertisement or offer might misunderstood.” Second, sellers cannot offset the cost of providing a free product by increasing the ordinary price, quality, or size of the product that must be purchased in order to obtain the free offer. *Walter J. Black, Inc.*, 50 F. T. C. 235-6 (1953).

Are Free Users “Consumers?”

“Because Plaintiffs allege that they received Defendant's services for free, as a matter of law, Plaintiffs cannot state a UCL claim under their own allegations.”

In re Facebook Litigation, 791 F.Supp.2d 705 (N.D. Cal. May 5, 2011)
CT distinguished Doe I v. AOL, 719 F.Supp.2d 1102 (N.D.Cal.2010), bc AOL users paid and bc of “sensitive” nature of info.

Possible Policy Approaches

Exchange for value

Caveat emptor

Anderson: makes it easy to try new services

May be better for privacy than payment

- No evidence that payment = less tracking

FTC: allow “free” with prominent disclosures of price (continue the “Mead Paradox”)

Require establishment of price

Friedman: allow introductory offers, samples, but ban Mead Paradox “free” offers

TCE Approach Goals

Make transactions more efficient

Avoid maladaptation

Have businesses shoulder the risk of “free” offers

Bring the costs, not the price, of free offers into focus

TCE Proposals

No third party sale

Bc makes consumer shoulder the cost

Bc of “take it or leave it” offers

Quick cancel & Deletion

Defaults

Portability

Ban on gag clauses

Anti-circumvention rules