THE FTC AND NEW PATERNALISM

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INTRODUCTION

We are witnessing a renaissance of paternalism in legal scholarship. This revival has been fueled by the rise of behavioral law and economics,[1] a multidisciplinary movement committed to the idea that legal regulation ought to be based upon a more realistic conception of human decisionmaking than is personified in *Homo economicus*—the "calculating, unemotional maximizer[]"[2] at the heart of neoclassical microeconomics.[3] In contrast to traditional law and economics models, behavioral law and economics (BLE) scholars draw on social science research to demonstrate that people make potentially suboptimal or irrational choices in a wide range of significant life activities—"decisions that are unwise *even according to their own values and preferences*."[4] The regulatory implications of these types of claims are dramatic: BLE provides a rationale for enacting paternalistic legal rules geared toward reducing distortion in the expression of consumer preferences, thus empowering consumers to make choices more consistent with their own "true" values and desires.[5] Despite these benevolent intentions, scholars and government actors who are skeptical of regulation will be dubious of the assertion that this new paternalism does not aim to substitute consumers' best judgments with consumption decisions made by government bureaucrats. They will see the new paternalism as a disturbing revival of the heavy-handed, stifling government regulation of the pre-Reagan era, against which they labored so mightily.

Given the Federal Trade Commission's (FTC or Commission) consumer protection mission, it is inevitable that the Commission will face calls for regulation based upon BLE. New paternalists will ask the Commission to engage in rulemaking or to bring unfairness or deception actions against industry actors that allegedly seek to exploit suboptimal consumer

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1. *See infra* Part I.
2. Sendhil Mullainathan & Richard H. Thaler, *Behavioral Economics*, *in* INTERNATIONAL ENCYCLOPEDIA OF THE SOCIAL AND BEHAVIORAL SCIENCES 1094, 1094 (2004) ("Economics traditionally conceptualizes a world populated by calculating, unemotional maximizers that have been dubbed Homo Economicus.").
3. *See* Herbert Gintis, *Beyond* Homo Economicus*: Evidence from Experimental Economics*, 35 ECOLOGICAL ECON. 311, 312 (2000) (discussing the characteristics of Homo economicus). *Homo economicus* is also referred to as "Chicago man" in academic literature. *See* Daniel McFadden, *Rationality for Economists?*, 19 J. RISK & UNCERTAINTY 73, 76 (1999); Robert A. Prentice, *Chicago Man, K-T Man, and the Future of Behavioral Law and Economics*, 56 VAND. L. REV. 1663, 1670 (2003).
4. Glen Whitman, *Against the New Paternalism: Internalities and the Economics of Self-Control*, POL'Y ANALYSIS 563 (Cato Inst., Wash., D.C.) Feb. 22, 2006, at 2.
5. *See, e.g.*, J.D. Trout, *Paternalism and Cognitive Bias*, 24 LAW & PHIL. 393, 394 (2005) (making "the case for the legitimacy of governmental regulation on behalf of a person's good for selected classes of cognitive bias").

behavior. Indeed, the FTC, which is well aware of these developments, is beginning to consider how to incorporate behavioral economics into its consumer protection mission. This Article addresses some of the challenges that BLE and the new paternalism bring to the FTC. Part I provides a brief survey of rational choice theory, followed by an overview of the behavioral law and economics movement in legal academia. The goal of Part I is to provide readers with a basic understanding of BLE and the theoretical underpinnings of the new paternalism.

Part II surveys the history of the legal concept of unfairness as the Federal Trade Commission Act uses that term.[6] Part II demonstrates that any move away from a rational actor model runs counter to a major FTC trend over the past three decades: growing reliance on the notion of consumer sovereignty, a concept closely tied to rational choice theory in economics. The goal of Part II is to show why the FTC is likely to be cautious in its use of BLE and resistant to more radical strains of the new paternalism.

Part III uses three practical examples of alleged behavioral exploitation—mail-in consumer rebates, inducement of supermarket impulse purchases, and payday lending—to explore possible FTC responses to the new paternalism. The goal of Part III is to illustrate the challenges that the FTC will face in light of the historical and legal background traced in Part II if the Commission brings unfairness claims based upon behavioral exploitation. This Article leaves for other commentators, however, to determine whether difficulties in proving behavioral unfairness claims indicate a limitation in the new paternalism or a fundamental flaw with current unfairness jurisprudence.

I. RATIONAL CHOICE THEORY, BEHAVIORAL LAW AND ECONOMICS, AND THE NEW PATERNALISM

A. Rational Choice Theory: A Brief Overview

Economic accounts of decisionmaking rely upon some version of rational choice theory (RCT).[7] The thinnest conception of rationality is

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6. This Article will focus on federal unfairness standards. For overviews of state unfairness law, see DEE PRIDGEN, CONSUMER PROTECTION AND THE LAW (2006); JONATHAN SHELDON & CAROLYN L. CARTER, UNFAIR AND DECEPTIVE ACTS AND PRACTICES (6th ed. 2004).

7. For an extraordinarily helpful treatment of this subject, see Russell B. Korobkin & Thomas S. Ulen, *Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics*, 88 CAL. L. REV. 1051 (2000) [hereinafter Korobkin & Ulen, *Rationality Assumption*]; *see also* Thomas S. Ulen, *Rational Choice Theory in Law and Economics*, *in* ENCYCLOPEDIA OF LAW AND ECONOMICS 790 (Boudewijn Bouckaert & Geerit De Geest eds., 2000) [hereinafter Ulen, *Rational Choice*].

that people maximize their own ends.[8] This account, while elegant in its simplicity, provides little basis for generating testable or falsifiable propositions.[9] If a person is willing to paint a house in exchange for three gherkin pickles, this could be considered "rational" because we would conclude that the house painter values gherkin pickles sufficiently to motivate him to enter into this bargain (absent proof of duress or mental incapacity). If the painter placed less of a value on gherkin pickles, then he would refuse to enter into the contract. Robert H. Frank uses a vivid example: "If someone drinks a gallon of used automobile crankcase oil, then writhes in agony and dies . . . the person must have *really* liked crankcase oil."[10] Jolls, Sunstein, and Thaler explain the point with a similar illustration:

> If rationality is used to mean simply that people "choose" what they "prefer" in light of the prevailing incentives, then the notion of rationality offers few restrictions on behavior. The person who drinks castor oil as often as possible is rational because she happens to love castor oil. Other self-destructive behavior (drug addiction, suicide, etc.) can be explained on similar grounds. It is not even clear on this view whether rationality is intended as a definition of "preference" or as a prediction.[11]

The "expected utility" version of RCT is more widely used than the thinnest definitional version of RCT. Under expected utility theory,[12] "decisionmakers conduct an explicit or implicit cost-benefit analysis of

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8. Korobkin & Ulen, *Rationality Assumption*, *supra* note 7, at 1061.

9. *See* Russell Korobkin, *A Multi-Disciplinary Approach to Legal Scholarship: Economics, Behavioral Economics, and Evolutionary Psychology*, 41 JURIMETRICS 319, 331 (2001) ("The thinnest version of rational choice theory provides that individuals will act to maximize their expected utility, a completely nonfalsifiable proposition standing alone."); Korobkin & Ulen, *Rationality Assumption*, *supra* note 7, at 1061–62, 1067; *see also* Robert J. Meyer & Barbara E. Kahn, *Probabilistic Models of Consumer Choice Behavior*, *in* HANDBOOK OF CONSUMER BEHAVIOR 85, 88 (Thomas S. Robertson & Harold H. Kassarjian eds., 1991) (observing the tautological nature of utility maximization claims); Tanina Rostain, *Educating* Homo Economicus*: Cautionary Notes on the New Behavioral Law and Economics Movement*, 34 LAW & SOC'Y REV. 973, 977 (2000) ("When the content of a rational actor's preferences is left open, however, the theory is too indeterminate to yield many empirically falsifiable predictions.").

10. Robert H. Frank, *Departures from Rational Choice: With and Without Regret*, *in* THE LAW AND ECONOMICS OF IRRATIONAL BEHAVIOR 17, 19 (Francesco Parisi & Vernon L. Smith eds., 2005).

11. Christine Jolls, Cass R. Sunstein & Richard Thaler, *A Behavioral Approach to Law and Economics*, 50 STAN. L. REV. 1471, 1488 (1998); *see also* Colin F. Camerer, *Wanting, Liking, and Learning: Neuroscience and Paternalism*, 73 U. CHI. L. REV. 87, 91 (2006) [hereinafter Camerer, *Wanting, Liking, and Learning*] ("If my neighbor thumps his head repeatedly with a ball-peen hammer, do I have no alternative but to infer that hammering his head with a ball-peen hammer is the most fun he can have?").

12. This theory is sometimes referred to as "subjective expected utility." *See* Korobkin & Ulen, *Rationality Assumption*, *supra* note 7, at 1062 n.34 ("The addition of the word 'subjective' merely allows for the probabilities by which the decisionmaker weighs the utilities of uncertain outcomes to be subjective, rather than objective.").

competing options and select the optimal method of achieving their goals."[13] As with the thinnest definitional version of RCT discussed above, the chosen ends or preferences are exogenous to the economic model[14]—an actor can attempt to maximize whatever she desires, although the ends are usually assumed to be one's own self-interest, broadly defined.[15] In the thickest and most controversial version of RCT,[16] the decisionmaker's goal is assumed to be wealth maximization—"the prediction that actors will attempt to maximize their financial well-being or monetary situation."[17] According to expected utility theory, rational decisionmakers should exhibit[18] (1) commensurability,[19] (2) transitivity,[20] (3) invariance,[21]

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13. *Id.* at 1063; RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW § 1.3, at 15 (7th ed. 2007) ("Rationality means little more to an economist than a disposition to choose, consciously or unconsciously, an apt means to whatever ends the chooser happens to have selected, consciously or unconsciously."). For those readers interested in representative utility equations, see Roger G. Noll & James E. Krier, *Some Implications of Cognitive Psychology for Risk Regulation*, 19 J. LEGAL STUD. 747, 751–53 (1990).

14. *See* ROBERT COOTER & THOMAS ULEN, LAW & ECONOMICS 18 (4th ed. 2004). Cooter and Ulen note that:

> [T]he preferences of the consumer are *subjective*. Different people have different tastes . . . . Economists leave to other disciplines, such as psychology and sociology, the study of the source of these preferences. We take consumer tastes or preferences as given, or, as economists say, as *exogenous*, which means that they are determined outside the economic system.

Id. at 22.

15. Although the actor's self-interest need not be defined solely in terms of wealth maximization, the implication is that the well-being of others is not a concern in the decisionmaking process. *See* Korobkin & Ulen, *Rationality Assumption*, *supra* note 7, at 1064–66.

16. *See id.* at 1060–61 (explaining differences between thin and thick versions of rational choice theory) (citing DONALD P. GREEN & IAN SHAPIRO, PATHOLOGIES OF RATIONAL CHOICE THEORY: A CRITIQUE OF APPLICATIONS IN POLITICAL SCIENCE 17–18 (1994)).

17. *Id.* at 1066.

18. For a slightly different list, see Jon D. Hanson & Douglas A. Kysar, *Taking Behavioralism Seriously: The Problem of Market Manipulation*, 74 N.Y.U. L. REV. 630, 641–42 (1999) (derived from Colin Camerer, *Individual Decision Making*, *in* THE HANDBOOK OF EXPERIMENTAL ECONOMICS 587, 618 (John H. Kagel & Alvin E. Roth eds., 1995) [hereinafter Camerer, *Individual Decision Making*]); *see also* Colin Camerer et al., *Regulation for Conservatives: Behavioral Economics and the Case for "Asymmetric Paternalism"*, 151 U. PA. L. REV. 1211, 1217 (2003) [hereinafter Camerer et al., *Regulation for Conservatives*] (describing the basic components of rationality).

19. Korobkin & Ulen, *Rationality Assumption*, *supra* note 7, at 1064 ("*Commensurability*: actors should be able to compare the utility consequences of all alternatives to each other.").

20. *Id.* ("*Transitivity*: if an actor prefers choice A to choice B and choice B to choice C, he should then prefer choice A to choice C."); Ulen, *Rational Choice*, *supra* note 7, at 792 ("Transitive preferences are those for which, if some good or bundle of goods denoted *A* is preferred to another good or bundle of goods denoted *B* and *B* is preferred to a third good or bundle of goods denoted *C*, then it must be the case that *A* is preferred to *C*.").

21. Korobkin & Ulen, *Rationality Assumption*, *supra* note 7, at 1064 ("*Invariance*: the preference between two or more choices should not depend on how the choice is presented or structured, so long as the outcome possibilities are constant."); *see also* Camerer, *Individual Decision Making*, *supra* note 18, at 652 (noting that "different representations of the same choice problem, and different elicitation procedures, should yield the same

(4) cancellation,[22] and (5) dominance.[23] Moreover, "in situations that involve uncertainty, people have well-formed beliefs about how uncertainty will resolve itself, and when new information becomes available, they update their beliefs using Bayes's law—the presumed ability to update probabilistic assessments in light of new information."[24] If a decisionmaker fails to make decisions consistently with these logical rules, then we can say that he is not acting rationally.[25] Note that the decisionmaking process can be hypothetical—the expected utility version of RCT is not a descriptive account about how consumers actually make decisions. In fact, as long as the choices do not violate these precepts of rationality, it is irrelevant to whether the decision was the product of any conscious action. Owen D. Jones and Timothy H. Goldsmith explain:

> When economists refer to a choice or behavior as "rational," they generally are referring not to the *process* that leads to the behavior, but rather to the substantive nature of the *outcome* of the behavior. To clarify the distinction, behavior is *procedurally rational* when it is the product of deliberative, conscious analysis. But behavior is *substantively rational* when it is appropriate for achieving particular goals, given conditions and constraints, regardless of how the behavior was actually chosen.[26]

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preference"); Hanson & Kysar, *supra* note 18, at 642 ("[W]here alternative descriptions of the same outcome are formulated, players should express the same preferences regardless of which description is presented.").

22. *See* Korobkin & Ulen, *Rationality Assumption*, *supra* note 7, at 1064 ("*Cancellation*: a choice between options should not depend on features of the options that are identical."); *see also* Amos Tversky & Daniel Kahneman, *Rational Choice and the Framing of Decisions*, 59 J. BUS. S251, S252 (1986) (elaborating further on cancellation).

23. Korobkin & Ulen, *Rationality Assumption*, *supra* note 7, at 1064 ("*Dominance*: an actor should never choose an option in which every feature is only as good as the features of a competing option, and at least one feature is not as good.").

24. Camerer et al., *Regulation for Conservatives*, *supra* note 18, at 1215; *see also* Camerer, *Individual Decision Making*, *supra* note 18, at 596 (illustrating Bayes's law as a formula).

25. *See* Korobkin & Ulen, *Rationality Assumption*, *supra* note 7, at 1064 ("If an actor fails to follow one or more of these principles, he cannot be making decisions consistent with the expected utility model. Consequently, the predictions of the model are testable, at least at some minimum level."); *see also* Gregory Mitchell, *Why Law and Economics' Perfect Rationality Should Not Be Traded for Behavioral Law and Economics' Equal Incompetence*, 91 GEO. L.J. 67, 81 (2002) [hereinafter Mitchell, *Equal Incompetence*] ("[W]hen the legal decision theorists say that some legally relevant behavior is supposedly 'nonrational,' 'quasi-rational,' or 'irrational,' they simply mean that a legal actor failed to apply the proper rules or norms for arriving at a judgment or decision, not that the action taken has an irrational purpose or unwise goal.").

26. Owen D. Jones & Timothy H. Goldsmith, *Law and Behavioral Biology*, 105 COLUM. L. REV. 405, 443 (2005).

B. Behavioral Law and Economics Challenges to Rational Choice Theory

Virtually any version of RCT can be challenged as an inaccurate account of human decisionmaking.[27] Edward L. Rubin makes this point when he observes that "the problem with rational choice theory, as a universal characterization of human behavior, is that it is demonstrably false."[28] This insight, at the core of behavioral economics,[29] has spurred voluminous literature[30] on behavioral law and economics[31] or legal decision theory.[32] BLE scholars are committed to enriching (or displacing) classic law and economics models with findings from fields such as social and cognitive psychology and experimental economics.[33] In particular, BLE scholars

27. *See* Jeremy A. Blumenthal, *Law and the Emotions: The Problems of Affective Forecasting*, 80 IND. L.J. 155, 158 (2005) [hereinafter Blumenthal, *Law and Emotions*] (noting that the central tenet of the rational decisionmaker and its underlying assumptions are "flawed"); Larry T. Garvin, *Small Business and the False Dichotomies of Contract Law*, 40 WAKE FOREST L. REV. 295, 314 (2005) ("The experimental literature has shown many departures from conventional expected utility theory—enough to warrant the comment that if expected utility theory 'is an empirical, testable theory, then it is, in any conventional sense, untrue.'") (quoting PAUL ANAND, FOUNDATIONS OF RATIONAL CHOICE UNDER RISK 19 (1993)).

28. Edward L. Rubin, *Rational Choice and Rat Choice: Some Thoughts on the Relationship Among Rationality, Markets, and Human Beings*, 80 CHI.-KENT L. REV. 1091, 1098 (2005).

29. For an overview of behavioral economics, see Colin Camerer & George Loewenstein, *Behavioral Economics: Past, Present, Future*, *in* ADVANCES IN BEHAVIORAL ECONOMICS 3 (Colin Camerer et al. eds., 2004) [hereinafter ADVANCES IN BEHAVIORAL ECONOMICS].

30. The extraordinary volume of recent behavioral law and economics (BLE) scholarship makes it difficult to provide a comprehensive list of valuable contributions to the field, but the following sources are good starting points: BEHAVIORAL LAW AND ECONOMICS (Cass R. Sunstein ed., 2000); THE LAW AND ECONOMICS OF IRRATIONAL BEHAVIOR (Francesco Parisi & Vernon L. Smith eds., 2005) [hereinafter LAW AND ECONOMICS OF IRRATIONAL BEHAVIOR]; Symposium, *Empirical Legal Realism: A New Social Scientific Assessment of Law and Human Behavior*, 97 NW. U. L. REV. 1075 (2003); Symposium, *The Legal Implications of Psychology: Human Behavior, Behavioral Economics, and the Law*, 51 VAND. L. REV. 1495 (1998).

31. *See* Cass R. Sunstein, *Behavioral Law and Economics: A Progress Report*, 1 AM. L. & ECON. REV. 115, 115 (1999) ("The last decade has seen an outpouring of work in 'behavioral law and economics;' in the last few years, the outpouring has become a flood.").

32. Scholars have debated the proper term to describe this movement in legal academia. *See* Blumenthal, *Law and Emotions*, *supra* note 27, at 159 (listing names for this movement); Owen D. Jones, *Time-Shifted Rationality and the Law of Law's Leverage: Behavioral Economics Meets Behavioral Biology*, 95 NW. U. L. REV. 1141, 1142 n.2 (2001) ("This outpouring of scholarship appears under various names. These include 'behavioral law and economics,' 'law and behavioral science,' 'behavioral analysis of law,' 'behavioral economic analysis of law,' 'the behavioral approach to law and economics,' 'behavioral economics analysis,' and 'law and the "new" psychology.'"); Mitchell, *Equal Incompetence*, *supra* note 25, at 78–79 (discussing the debate over the terminology and choosing to use the term "legal decision theory").

33. *See* David A. Hoffman, *The "Duty" to Be a Rational Shareholder*, 90 MINN. L. REV. 537, 546 (2006) ("Behavioral law and economics undermines the rationality assumption by using data from psychological experiments to radically alter our view of how humans make choices. BLE documents how individuals' choice-making behavior systematically diverges from the predictions of the rational-actor model of human behavior.") (citations omitted);

have explored the ways in which individuals may systematically deviate from the various forms of RCT due to bounded self-interest, bounded willpower, and bounded rationality.[34] The first of these, bounded self-interest, refers "to an important fact about the utility function of most people: They care, or act as if they care, about others, even strangers, in some circumstances."[35] We also are familiar with bounded willpower. Even when people know what is best for them, they often lack the willpower or impulse control to make optimal choices.[36] Chronic overeating, drug use, and unprotected sexual activity are three examples where one's actions may be due to limited willpower[37] or emotion, rather than a rational balancing of costs and benefits.[38]

Jonathan Remy Nash, *Framing Effects and Regulatory Choice*, 82 NOTRE DAME L. REV. 313, 316 (2006) ("Behavioral law and economics seeks to improve the predictive power of traditional law and economics by incorporating behavioral considerations into the model."); Avishalom Tor, *The Fable of Entry: Bounded Rationality, Market Discipline, and Legal Policy*, 101 MICH. L. REV. 482, 484 (2002) (noting that hallmark of the BLE approach "is the replacement of the perfectly rational actor with a 'boundedly rational' decisionmaker who, apart from being affected by emotion and motivation, has only limited cognitive resources"); *see also* Rostain, *supra* note 9, at 980 ("The point of this new movement, these writers insist, is not to displace the law and economics model, but to enhance its descriptive and predictive powers by importing insights from cognitive and social psychology and behavioral economics.") (citations omitted). Rostain is skeptical, however, of this goal. *See id.* at 984 ("Incorporating behavioral insights into legal analysis provides a richer and 'truer' account of human decisionmaking and behavior, but not necessarily one with significant predictive power.").

34. For ease of exposition, this framework is taken from Jolls et al., *supra* note 11.

35. *Id.* at 1479; *see also* Joseph Henrich et al., *In Search of Homo Economicus: Behavioral Experiments in 15 Small-Scale Societies*, 91 AM. ECON. REV. 73 (2001) ("[I]n addition to their own material payoffs, many experimental subjects appear to care about fairness and reciprocity, are willing to change the distribution of material outcomes at personal cost, and are willing to reward those who act in a cooperative manner while punishing those who do not even when these actions are costly to the individual."); Rostain, *supra* note 9, at 979 ("People are not consistently self-interested, as such theories would hold, but have been shown to have other regarding preferences that are seemingly not reducible to material, or even reputational, interests. Such non-self-interested preferences are reflected in conduct governed by social norms, such as norms of fairness.").

36. *See* Camerer et al., *Regulation for Conservatives*, *supra* note 18, at 1217 (observing that "a substantial body of literature examines how people with self-control problems may fail to carry out their desired course of action") (citing David Laibson, *Golden Eggs and Hyperbolic Discounting*, 112 Q.J. ECON. 443, 444–45 (1997); George Loewenstein, *Out of Control: Visceral Influences on Behavior*, 65 ORG'L BEHAV. & HUM. DECISION PROCESSES 272, 272–73 (1996); Ted O'Donoghue & Matthew Rabin, *Doing It Now or Later*, 89 AM. ECON. REV. 103, 118–20 (1999)); Jolls et al., *supra* note 11, at 1479 ("[P]eople often display bounded willpower. This term refers to the fact that human beings often take actions that they know to be in conflict with their own long-term interests.").

37. *See* Ole-Jørgen Skog, *Addiction, Choice, and Irrationality*, *in* LAW AND ECONOMICS OF IRRATIONAL BEHAVIOR, *supra* note 30, at 135 (arguing that the "central features of addiction cannot be adequately dealt with by theories embedded within the framework of standard rational choice theory"). Herbert Gintis has a slightly different take on addiction:

> Drug addiction may seem a perfect example of people making choices that are not in their self-interest. However, a much larger fraction of those who try drugs either give them up or maintain their use at recreational levels than become addicted. Therefore drug taking may be a risky behavior the net benefit of which is positive, even though it has a negative payoff for some.

"Bounded rationality" covers several different deviations from rational choice theory. First, humans are imperfect decisionmakers due to natural cognitive limitations:[39] we have "limited working memory and limited computational capabilities."[40] Second, when faced with complex choices and limited time and resources,[41] people use heuristics[42] or mental shortcuts[43] to make decisions,[44] which may or may not lead to utility-enhancing decisions, depending on the choice environment.[45]

Gintis, *supra* note 3, at 312.

38. Of course, any discussion about poor impulse control can lead to difficult questions over the very nature of happiness and the differences between what we want, need, like, and find pleasurable over the course of our lives. For an excellent discussion of these issues, see Camerer, *Wanting, Liking, and Learning*, *supra* note 11. An additional layer of complex issues emerges if we consider these matters over time and question whether people are capable of predicting accurately what will give them future happiness. *See generally* Blumenthal, *Law and Emotions*, *supra* note 27.

39. *See* Jolls et al., *supra* note 11, at 1477 ("Bounded rationality, an idea first introduced by Herbert Simon, refers to the obvious fact that human cognitive abilities are not infinite. We have limited computational skills and seriously flawed memories.") (citation omitted); Jones & Goldsmith, *supra* note 26, at 445 (noting "constraints on the brain's information capacities, wiring, and computing speed"); Troy A. Paredes, *Blinded by the Light: Information Overload and Its Consequences for Securities Regulation*, 81 WASH. U. L.Q. 417, 435 (2003) ("Cognitive capabilities are scarce resources that have to be allocated; because of limited cognitive capabilities, people cannot attend to all the information made available to them and cannot evaluate all their choices perfectly."). *But see* Gerd Gigerenzer, *Is the Mind Irrational or Ecologically Rational?*, *in* LAW AND ECONOMICS OF IRRATIONAL BEHAVIOR, *supra* note 30, at 39 (2005) (criticizing Jolls, Sunstein, and Thaler for misrepresenting Simon's views).

40. James R. Bettman et al., *Constructive Consumer Choice Processes*, 25 J. CONSUMER RES. 187, 187 (1998).

41. *See* Jones, *supra* note 32, at 1150 ("Bounded rationality essentially captures the idea that there are very real, very important constraints on the actual human capacity to gather and process information."); Jones & Goldsmith, *supra* note 26, at 445 (noting "constraints on time and energy for gathering perfect information").

42. *See* Jeffrey J. Rachlinski, *The Uncertain Psychological Case for Paternalism*, 97 NW. U. L. REV. 1165, 1170–75 (2003) (reviewing the availability heuristic, the representativeness heuristic, anchoring and adjustment, hindsight bias, and self-serving biases, such as overoptimism, overconfidence, and egocentrism).

43. One example is what Herbert Simon referred to as "satisficing." *See* Herbert A. Simon, *Rational Choice and the Structure of the Environment*, 63 PSYCHOL. REV. 129 (1956); Herbert A. Simon, *A Behavioral Model of Rational Choice*, 69 Q.J. ECON. 99 (1955); *see also* Garvin, *supra* note 27, at 308–09 (discussing "satisficing"); Paredes, *supra* note 39, at 435–36 (discussing Herbert Simon's work). Simon's work on "satisficing" led to work that explores a variety of non-compensatory decisionmaking strategies. *See* SCOTT PLOUS, THE PSYCHOLOGY OF JUDGMENT AND DECISION MAKING 102 (1993) ("A compensatory strategy trades off low values on one dimension against high values on another."); Paredes, *supra* note 39, at 437–40 (surveying decisionmaking strategies including the lexicographic strategy and elimination by aspects).

44. *See* Mitchell, *Equal Incompetence*, *supra* note 25, at 82 ("[W]e must rely on often unconscious mental shortcuts or rules of thumb to assess evidence, draw inferences, and make predictions, because deliberate, careful computations pursuant to rules of procedural rationality simply would be too mentally taxing or time consuming."). For an in-depth discussion of various decisionmaking heuristics and biases, see Korobkin & Ulen, *Rationality Assumption*, *supra* note 7, at 1084–1102; *see also* PLOUS, *supra* note 43, at 109–88.

45. Korobkin and Ulen point out:

In addition to cognitive limitations and the use of heuristics or mental shortcuts, research in the area of prospect theory has shown that decisionmakers are subject to automatic biases in decisionmaking[46] that lead to violations of the principle of invariance.[47] These biases, which are often grouped together,[48] include the status quo bias,[49] endowment effects,[50] and loss aversion.[51] Thus, how decisions are framed (as gains or

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> The widespread use of heuristics, at least in many cases, is no doubt a quite useful evolutionary adaptation; without such mental shortcuts, the task of making even relatively simple decisions would become so complex that daily life would almost certainly grind to a halt. But the use of heuristics surely results in the widespread failure of decision makers to maximize their expected utility in particular decision situations.

Korobkin & Ulen, *Rationality Assumption*, *supra* note 7, at 1076 (citation omitted); *see also* Patricia A. McCoy, *Predatory Lending Practices: Definition and Behavioral Implications*, *in* WHY THE POOR PAY MORE: HOW TO STOP PREDATORY LENDING 81, 93 (Gregory D. Squires ed., 2004) ("All consumers . . . use heuristic principles of one sort or another to simplify their financial decisions. When these principles are sound, they can provide a useful shortcut to financial decision-making. Other choice heuristics, however, can lead to grave and systematic errors in weighing risks and benefits.") (citing Amos Tversky & Daniel Kahneman, *Judgment Under Uncertainty: Heuristics and Biases*, 185 SCIENCE 1124 (1974)); Mitchell, *Equal Incompetence*, *supra* note 25, at 83 (observing that "over-reliance on, or unthinking use of heuristics can bias judgment and cause errors in decisions").

46. A contrast can be drawn between "'deliberate' choice heuristics," which are simplifying decision strategies that may be adaptive, and "'automatic' judgmental heuristics." *See* Shane Frederick, *Automated Choice Heuristics*, *in* HEURISTICS AND BIASES: THE PSYCHOLOGY OF INTUITIVE JUDGMENT 548, 549 (Thomas Gilovich et al. eds., 2002) [hereinafter HEURISTICS AND BIASES]; Gerd Gigerenzer, *Is the Mind Irrational or Ecologically Rational?*, *in* LAW AND ECONOMICS OF IRRATIONAL BEHAVIOR, *supra* note 30, at 37; Gerd Gigerenzer et al., *How Good Are Fast and Frugal Heuristics?*, *in* HEURISTICS AND BIASES, *supra* note 30, at 559.

47. *See supra* note 21 and accompanying text.

48. *See* Camerer, *Individual Decision Making*, *supra* note 18, at 652.

49. *See* Russell Korobkin, *The Endowment Effect and Legal Analysis*, 97 NW. U. L. REV. 1227, 1228–29 (2003) [hereinafter Korobkin, *Endowment Effect*] ("[I]ndividuals tend to prefer the present state of the world to alternative states, all other things being equal."); *see also* Colin Camerer, *Prospect Theory in the Wild: Evidence from the Field*, *in* ADVANCES IN BEHAVIORAL ECONOMICS, *supra* note 29, at 148, 154 ("Samuelson and Zeckhauser . . . coined the term *status quo bias* to refer to an exaggerated preference for the status quo . . . .").

50. Korobkin, *Endowment Effect*, *supra* note 49, at 1228 & n.3 ("[P]eople tend to value goods more when they own them than when they do not.") (crediting Richard Thaler for coining the term "endowment effect" in Richard Thaler, *Toward a Positive Theory of Consumer Choice*, 1 J. ECON. BEHAV. & ORG. 39, 44 (1980)); *see also* Daniel Kahneman, Jack L. Knetsch & Richard Thaler, *Experimental Tests of the Endowment Effect and the Coase Theorem*, *in* ADVANCES IN BEHAVIORAL ECONOMICS 55 (Colin Camerer et al. eds., 2004).

51. Chris Guthrie, *Prospect Theory, Risk Preference, and the Law*, 97 NW. U. L. REV. 1115, 1119 (2003) ("[I]ndividuals tend to value losses more heavily than gains of the same magnitude.") (citing Daniel Kahneman & Amos Tversky, *Prospect Theory: An Analysis of Decision Under Risk*, 47 ECONOMETRICA 263 (1979)); Jolls et al., *supra* note 11, at 1535 & n.182 ("[O]ne of the central features of Kahneman and Tversky's prospect theory is that people evaluate outcomes based on the change they represent from an initial reference point, rather than based on the nature of the outcome itself; also, losses from the initial reference point are weighted much more heavily than gains.") (citing Kahneman & Tversky, *supra*, at 277–79). Russell Korobkin breaks loss aversion down further based upon various second-

losses) and the allocation of initial entitlements will affect choice processes,[52] even though these matters ought to be irrelevant for a decisionmaker's overall wealth maximization.[53] Finally, no discussion of irrational or suboptimal behavior would be complete without noting that some scholars have begun to address the central role that emotions play in decisionmaking.[54] Not only do our moods greatly affect the quality of our decisionmaking, but "people tend to inaccurately predict their own future emotional states—as well as those of others—even when the predictions concern important self-relevant events or, in some cases, are even minutes in the future."[55]

C. Implications of Behavioral Law and Economics on Policymaking: The New Paternalism

Legal scholars and economists continue to debate the implications of behavioral law and economics on public policymaking and legal decisionmaking.[56] Some scholars, however, believe that the current social science evidence serves to weaken normal arguments against paternalism,[57] and may even be sufficient to justify—in certain carefully delineated

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order explanations for loss aversion. *See* Korobkin, *Endowment Effect*, *supra* note 49, at 1250–55.

52. Korobkin & Ulen, *Rationality Assumption*, *supra* note 7, at 1104–07 (discussing framing); PLOUS, *supra* note 43, at 64–76 (providing an overview of framing with an emphasis on Tversky and Kahneman's work); Rostain, *supra* note 9, at 978 ("Contrary to the requirement of description and process invariance, experimental evidence establishes that preferences depend importantly on how choices are described."). *But see* James N. Druckman, *Political Preference Formation: Competition, Deliberation, and the (Ir)relevance of Framing Effects*, 98 AM. POL. SCI. REV. 671, 683 (2004) ("[F]raming effects depend in critical ways on context. As a result, framing effects appear to be neither robust nor particularly pervasive."); Gregory Mitchell, *Taking Behavioralism Too Seriously? The Unwarranted Pessimism of the New Behavioral Analysis of Law*, 43 WM. & MARY L. REV. 1907, 1961–63, 2005–11 (2002) [hereinafter Mitchell, *Unwarranted Pessimism*] (providing a skeptical discussion of framing effects literature).

53. *See generally* Guthrie, *supra* note 51; Korobkin, *Endowment Effect*, *supra* note 49.

54. *See, e.g.*, Jeremy A. Blumenthal, *Emotional Paternalism*, 35 FLA. ST. U. L. REV. 1 (2007) [hereinafter Blumenthal, *Emotional Paternalism*]; Blumenthal, *Law and Emotions*, *supra* note 27; Peter H. Huang & Jeremy A. Blumenthal, *Positive Law and Policy*, *in* ENCYCLOPEDIA OF POSITIVE PSYCHOLOGY (Shane J. Lopez ed., forthcoming 2008).

55. Blumenthal, *Emotional Paternalism*, *supra* note 54, at 3.

56. *See, e.g.*, Richard A. Epstein & Oren Bar-Gill, *Consumer Contracts: Behavioral Economics vs. Neoclassical Economics* (NYU Sch. of Law, Working Paper No. 07-17, 2007), *available at* http://lsr.nellco.org/cgi/viewcontent.cgi?article=1095&context=nyu/lewp; *see also supra* note 30 (listing recent symposia dedicated to the implications of behavioral law and economics on public policymaking and legal decisionmaking).

57. *See* Daniel Kahneman et al., *Back to Bentham? Explorations of Experienced Utility*, 112 Q.J. ECON. 375, 397 (1997) ("The point of these observations is not to support paternalism, but to reject one of the arguments commonly raised against it. The claim that agents should be left alone because they generally know what is good for them is less secure than is generally assumed in economic discourse.").

cases—some degree of paternalistic intervention into the marketplace.[58] One author observes that "virtually every scholar who has written on the application of psychological research on judgment and choice to law has concluded that cognitive psychology supports institutional constraint on individual choice."[59] Thus, BLE has been a major force behind the rise of a "new paternalism"—academic advocacy of various forms of soft, rather than hard,[60] paternalism.[61] As one critical economist sums it up: "In short, the old paternalism said, 'We know what's best for you and we'll make you do it.' The new paternalism says, '*You* know what's best for you, and we'll make you do it.'"[62] Notably, Cass R. Sunstein and Richard H. Thaler have advocated a soft form of paternalism, which they term *libertarian paternalism*,[63] while Colin Camerer, Samuel Issacharoff, George Loewenstein, Ted O'Donoghue, and Matthew Rabin have made the case for *asymmetrically paternalistic regulation*:

> A regulation is asymmetrically paternalistic if it creates large benefits for those who make errors, while imposing little or no harm on those who are fully rational. Such regulations are relatively harmless to those who reliably make decisions in their best interest, while at the same time advantageous to those making suboptimal choices.[64]

Thus, instead of directly forbidding the use of certain contract terms, behavioral paternalists are more likely to call for regulatory options that improve decisionmaking while treading lightly on consumer sovereignty and autonomy.[65] Such options include setting certain default contract

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58. *See* Trout, *supra* note 5, at 394 ("Regulation can be permissible even when it runs counter to that person's spontaneous wishes, particularly when the regulation advances the agent's considered judgments or implicit long-term goals.").

59. Rachlinski, *supra* note 42, at 1166.

60. Jonathan Klick & Gregory Mitchell, *Government Regulation of Irrationality: Moral and Cognitive Hazards*, 90 MINN. L. REV. 1620, 1621 (2006) (explaining that under "hard forms of paternalism, . . . the government determines what is best for citizens and accordingly restricts the freedom of citizens to act otherwise"); Cass R. Sunstein, *Boundedly Rational Borrowing*, 73 U. CHI. L. REV. 249, 254 (2006) ("[S]trong paternalism forecloses choice, typically on the ground that all or most people will choose unwisely."); *see also* Gerald Dworkin, *Paternalism*, *in* STANFORD ENCYCLOPEDIA OF PHILOSOPHY, *available at* http://plato.stanford.edu/entries/paternalism (last visited Jan. 25, 2008) (comparing hard and soft paternalism).

61. For discussions of the many definitions of paternalism, see Blumenthal, *Emotional Paternalism*, *supra* note 54, at 5–6; Trout, *supra* note 5, at 408–13.

62. Whitman, *supra* note 4, at 2.

63. *See* Cass R. Sunstein & Richard H. Thaler, *Libertarian Paternalism Is Not an Oxymoron*, 70 U. CHI. L. REV. 1159, 1159 (2003).

64. Camerer et al., *Regulation for Conservatives*, *supra* note 18, at 1212; *see also* Gregory Mitchell, *Libertarian Paternalism Is an Oxymoron*, 99 NW. U. L. REV. 1245, 1248 n.10 (2005) [hereinafter Mitchell, *Libertarian Paternalism*] (contrasting both forms of regulation); Sunstein, *supra* note 60, at 257 (discussing similarities and differences between asymmetrical paternalism and libertarian paternalism).

65. *See* Klick & Mitchell, *supra* note 60, at 1621 (noting that under "softer forms of paternalism . . . the government regulates the form in which information and options are presented to citizens and restricts the role of laypersons in the market, legal, and political

terms[66] (which can be overridden by the parties), cooling-off periods for certain types of contracts,[67] and the classic example of asymmetrically paternalistic regulation—mandatory disclosure laws such as the Federal Truth in Lending Act.[68] Paternalists favor disclosure laws because, in some circumstances, they provide a great benefit to uninformed consumers while imposing little cost on informed consumers,[69] and because they are more politically feasible than other forms of regulation.[70]

The superstar status of those scholars at the forefront of the new paternalism or "anti-antipaternalism"[71] movement is undeniable. Their impressive reputations alone compel us to consider whether BLE justifies additional government regulation of consumer markets. Nevertheless, other prominent scholars have argued quite forcefully against this new paternalism.[72] Some criticisms are methodological, revolving around whether present social science research on decisionmaking and the findings of laboratory experiments can be generalized to the myriad of consumer choice environments discussed by behavioral paternalists.[73] Other critics

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systems without completely controlling choices"); Edward L. Glaeser, *Paternalism and Psychology*, 73 U. CHI. L. REV. 133, 149 (2006) ("Typical examples of soft or libertarian paternalism include 'debiasing' campaigns, default rules, and other interventions that change beliefs and attitude without impacting formal prices faced by consumers.").

66. *See* Camerer et al., *Regulation for Conservatives*, *supra* note 18, at 1224–30 (discussing use of default rules in insurance contracts and retirement savings accounts).

67. *See id.* at 1238–47 (discussing the use of cooling-off periods in various contexts, including certain consumer purchases and loans, marriage licensure, and mediated settlements).

68. 15 U.S.C. §§ 1601–1667(f) (2000); *see also* Camerer et al., *Regulation for Conservatives*, *supra* note 18, at 1237–48 (discussing the Truth in Lending Act's purposes).

69. *See* Oren Bar-Gill, *Informing Consumers About Themselves* 63–67 (NYU School of Law, Working Paper No. 111, 2007), *available at* http://lsr.nellco.org/nyu/lewp/papers/111/ (discussing costs and limits of disclosure); *see also* Matthew A. Edwards, *Empirical and Behavioral Critiques of Mandatory Disclosure: Socio-Economics and the Quest for Truth in Lending*, 14 CORNELL J.L. & PUB. POL'Y 199, 217 n.101 (2005) (noting costs incurred by those who must provide mandatory disclosures).

70. Bar-Gill, *supra* note 69, at 63.

71. *See* Jolls et al., *supra* note 11, at 1541 ("[B]ounded rationality pushes toward a sort of anti-antipaternalism—a skepticism about antipaternalism, but not an affirmative defense of paternalism."); *see also* Stephen J. Choi & A.C. Pritchard, *Behavioral Economics and the SEC*, 56 STAN. L. REV. 1, 4 (2003) ("[T]he behavioral economics school generally subscribes to an 'anti-antipaternalism.' As any high school English teacher no doubt could translate, this means a belief in the benefit of 'paternalism.'") (citation omitted).

72. *See* Garvin, *supra* note 27, at 315 n.80 (2005) (collecting sources critical of BLE); Jones, *supra* note 32, at 1156–61 (surveying criticisms of BLE). For an argument that BLE scholars have not gone far enough to discredit the rational actor model, see Jon Hanson & David Yosifon, *The Situational Character: A Critical Realist Perspective on the Human Animal*, 93 GEO. L.J. 1 (2004).

73. Gregory Mitchell has been a leader on this issue. *See* Mitchell, *Unwarranted Pessimism*, *supra* note 52; Gregory Mitchell, *Tendencies Versus Boundaries: Levels of Generality in Behavioral Law and Economics*, 56 VAND. L. REV. 1781 (2003); Mitchell, *Equal Incompetence*, *supra* note 25; *see also* Hoffman, *supra* note 33, at 547 n.41 ("Some argue that BLE experiments are flawed in design or execution."); David A. Hoffman, *How Relevant is Jury Rationality?*, 2003 U. ILL. L. REV. 507, 517 ("Critics of behavioralism's empirical findings argue that isolating decision making in this way is an especially poor way

question the efficacy of government intervention by suggesting that government regulators aiming to reduce consumer irrationality will themselves fall prey to decisionmaking biases and cognitive defects in their efforts to correct suboptimal consumer behavior.[74] Moreover, paternalistic government intervention itself might be counterproductive if it stifles individual learning and impairs consumer decisionmaking capabilities.[75] Finally, it is always possible to question whether scholars or government decisionmakers are capable of determining what is "best" for consumers and thus what ought to be deemed suboptimal or irrational behavior.[76]

The Federal Trade Commission is in an ideal position to play an active role in this debate between the new paternalists and the anti-paternalists. In particular, FTC expertise would be valuable in determining the potential forms that BLE-influenced regulation might take and the particular contexts in which it is likely to be most successful. Observers of the FTC may find, however, that the Commission is likely to proceed rather cautiously in response to the teachings of BLE. Part II of this Article reviews the history of FTC unfairness law to demonstrate why the FTC might be reticent to embrace the new paternalism wholeheartedly.

II. THE FEDERAL LAW OF UNFAIRNESS

A. Unfairness Under the Federal Trade Commission Act: 1914–1980

The Federal Trade Commission's unfairness authority has a fascinating legal and political history.[77] The original Federal Trade Commission Act,

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to test human rationality. In laboratories, subjects lack context from which to make decisions—they are given no feedback or opportunity to learn from their mistakes."). For vigorous counterarguments to Mitchell's work, see Prentice, *supra* note 3.

74. *See* Choi, *supra* note 71 (applying behavioral law and economics theory to the SEC and other regulators); Glaeser, *supra* note 65, at 134 (contending that "there are good reasons why we might think that public decisionmaking is likely to be more flawed than private decisionmaking").

75. *See* Klick & Mitchell, *supra* note 60, at 1622–23. For example, the provision of certain types of information to "de-bias" consumers may lead consumers to overestimate whatever risks they face in a particular market transaction. *See* Richard A. Epstein, *Behavioral Economics: Human Errors and Market Corrections*, 73 U. CHI. L. REV. 111, 131 (2006) (discussing credit cards).

76. *See* Blumenthal, *Emotional Paternalism*, *supra* note 54, at 61–62 (noting the "classic objection" that "people know their tastes and preferences, and act rationally to achieve them, certainly better than any third party might know or do"); Mitchell, *Libertarian Paternalism*, *supra* note 64, at 1267–70 (explaining the difficulty for a third party to make judgments about another individual's utility); Eyal Zamir, *The Efficiency of Paternalism*, 84 VA. L. REV. 229, 237–39 (1998) (discussing and rejecting anti-paternalism arguments based upon the inability of policymakers to assess the well-being of different people).

77. Much of this territory has been covered quite ably elsewhere. *See, e.g.*, Neil W. Averitt, *The Meaning of "Unfair Acts or Practices" in Section 5 of the Federal Trade Commission Act*, 70 GEO. L.J. 225 (1981); J. Howard Beales III, *The Federal Trade Commission's Use of Unfairness Authority: Its Rise, Fall, and Resurrection*, 22 J. PUB.

as passed in 1914, granted the FTC authority over "unfair methods of competition."[78] During the next twenty years or so, questions arose as to whether this broad language[79] covered consumer protection cases where proof of harm to competition was absent.[80] For example, in *FTC v. Raladam Co.*,[81] the Supreme Court held that the FTC lacked jurisdiction over false claims by the manufacturer of a "quack obesity cure"[82] because there was no evidence in the record that the sale of this product harmed any competing business.[83] The Court explained:

> It is obvious that the word "competition" imports the existence of present or potential competitors, and the unfair methods must be such as injuriously affect or tend thus to affect the business of these competitors—that is to say, the trader whose methods are assailed as unfair must have present or potential rivals in trade whose business will be, or is likely to be, lessened or otherwise injured.[84]

POL'Y & MARKETING 192 (2003); David L. Belt, *The Standard for Determining "Unfair Acts or Practices" Under State Unfair Trade Practices Acts*, 80 CONN. BAR J. 247 (2006); Jean Braucher, *Defining Unfairness: Empathy and Economic Analysis at the Federal Trade Commission*, 68 B.U. L. REV. 349 (1988) [hereinafter Braucher, *Defining Unfairness*]; Stephen Calkins, *FTC Unfairness: An Essay*, 46 WAYNE L. REV. 1935 (2000); Dara J. Diomande, *The Re-Emergence of the Unfairness Doctrine in Federal Trade Commission and State Consumer Protection Cases*, 18 ANTITRUST 53 (2004); Ernest Gellhorn, *Trading Stamps,* S & H*, and the FTC's Unfairness Doctrine*, 1983 DUKE L.J. 903; TIMOTHY J. MURIS & J. HOWARD BEALES III, THE LIMITS OF UNFAIRNESS UNDER THE FEDERAL TRADE COMMISSION ACT (1991); David A. Rice, *Consumer Unfairness at the FTC: Misadventures in Law and Economics*, 52 GEO. WASH. L. REV. 1 (1983); Roger E. Schechter, *The Unfairness of Click-On Software Licenses*, 46 WAYNE L. REV. 1735 (2000). An excellent judicial review of the FTC's unfairness authority can be found in *American Financial Services Ass'n v. FTC*, 767 F.2d 957, 965–72 (D.C. Cir. 1985).

78. Federal Trade Commission Act, ch. 311, § 5, 38 Stat. 717, 719 (1914) (codified at 15 U.S.C. § 45 (2000)).

79. A House Report explained the purpose of this open-ended language as follows: "There is no limit to human inventiveness in this field. Even if all known unfair practices were specifically defined and prohibited, it would be at once necessary to begin over again. If Congress were to adopt the method of definition, it would undertake an endless task." H.R. REP. NO. 63-1142, at 19 (1914).

80. *See* Robert A. Skitol, *How BC and BCP Can Strengthen Their Respective Policy Missions Through New Uses of Each Other's Authority*, 72 ANTITRUST L.J. 1167, 1168 (2005) (noting that between 1914 and 1936, "deception and other practices deemed to be 'oppressive' to consumers were common targets of Commission activity even as the Supreme Court flip-flopped over the central issue of whether the agency had authority to reach these practices without a showing of adverse effect on competition or competitors") (*comparing* FTC v. Gratz, 253 U.S. 421 (1920), *and* FTC v. Raladam Co., 283 U.S. 643 (1931), *with* FTC v. R.F. Keppel & Bros., 291 U.S. 304 (1934)). Neil Averitt points out that in most cases, harm to competition accompanied harm to consumers, a fact that case law from this period recognized. *See* Averitt, *supra* note 77, at 231–32.

81. 283 U.S. 643 (1931).

82. Calkins, *supra* note 77, at 1949.

83. *Raladam*, 283 U.S. at 654.

84. *Id.* at 649.

Congress eventually responded to this restrictive reading of the FTC's § 5 authority by passing the Wheeler-Lea Amendment in 1938,[85] which expanded the Commission's mandate to cover "unfair or deceptive acts or practices in [or affecting] commerce."[86] As the Supreme Court later explained, this amendment "made it clear that Congress, through § 5, charged the FTC with protecting consumers as well as competitors."[87]

Until the early 1960s, the Commission treated unfair and deceptive acts as a unitary concept.[88] This approach changed, however, in the context of the agency's effort to require health warnings on cigarettes, as the FTC took the position that unfairness was a distinct basis for regulation, separate from deception.[89] The FTC articulated its view in the "Cigarette Rule,"[90] which set forth three factors to be considered in determining whether an act or practice is unfair:[91]

> (1) [W]hether the practice, without necessarily having been previously considered unlawful, offends public policy as it has been established by statutes, the common law, or otherwise—whether, in other words, it is

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85. *See* Calkins, *supra* note 77, at 1936 ("Unhappy with a cramped Supreme Court interpretation of this prohibition in *FTC v. Raladam Co*., Congress in 1938 supplemented this language by declaring that 'unfair or deceptive acts or practices' are also 'unlawful.'") (citations omitted); J.R. Franke & D.A. Ballam, *New Applications of Consumer Protection Law: Judicial Activism or Legislative Directive?*, 32 SANTA CLARA L. REV. 347, 363 (1992) (viewing the Wheeler-Lea Amendment as a response to the Supreme Court's decision in *Raladam*); MURIS & BEALES, *supra* note 77, at 10.

86. Wheeler-Lea Act, ch. 49, § 3, 52 Stat. 111 (1938). As amended, section 5(a)(1) of the Federal Trade Commission Act now provides: "Unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are hereby declared unlawful." 15 U.S.C. § 45(a)(1) (2000).

87. FTC v. Sperry & Hutchinson Co., 405 U.S. 233, 244 (1972).

88. *See* Beales, *supra* note 77, at 192 ("Prior to 1964, the commission largely ignored the word 'or' in the amendment and described acts it found offensive as 'unfair and deceptive' without making any attempt to distinguish between 'unfair' on the one hand and 'deceptive' on the other hand."); Schechter, *supra* note 77, at 1761 ("From the mid-thirties through the early sixties the FTC . . . did not attempt to distinguish between 'deceptive' practices and those that were 'unfair.' Instead, it would allege an 'unfair-and-deceptive-practice' as if the term constituted a single compound word, defining a unitary phenomenon."); *see also* PETER C. WARD, FEDERAL TRADE COMMISSION: LAW, PRACTICE AND PROCEDURE § 5.01, at 5-2 (1996) (describing how the FTC treated unfairness and deception as a unitary concept).

89. *See* Teresa M. Schwartz, *Regulating Unfair Practices Under the FTC Act: The Need for a Legal Standard of Unfairness*, 11 AKRON L. REV. 1, 4–6 (1977) (describing the FTC's first articulation of the unfairness theory in a rulemaking procedure).

90. Unfair or Deceptive Advertising and Labeling of Cigarettes in Relation to the Health Hazards of Smoking, 29 Fed. Reg. 8324 (1964) [hereinafter *Cigarette Rule*].

91. Ironically, even though he later was the intellectual leader of the law and economics movement that contributed to the demise of the Cigarette Rule, "FTC lore holds that the principal author of this document was Richard Posner, then a 25-year-old attorney adviser to Commissioner Philip Elman." Beales, *supra* note 77, at 193 n.4 (citing *The Reminiscences of Philip Elman*, Oral History Research Office, Columbia University, at 372–73 (1986)). Judge Posner confirmed this fact with the author via e-mail. E-mail from Richard Posner, Judge, United States Court of Appeals for the Seventh Circuit, to author (May 30, 2007, 02:52:00 EST).

> within at least the penumbra of some common-law, statutory, or other established concept of unfairness; (2) whether it is immoral, unethical, oppressive, or unscrupulous; [and] (3) whether it causes substantial injury to consumers (or competitors or other businessmen).[92]

Congress intervened and preempted both FTC and state regulation of cigarettes,[93] and by the end of the 1960s the bold statement of unfairness authority in the Cigarette Rule faded into the background as critics assailed the FTC for "having become preoccupied with trivial cases, while ignoring serious consumer harms."[94] In particular, two well-publicized studies of the Commission—one by a group of students known as "Nader's Raiders"[95] and the other by the American Bar Association[96]—"ruthlessly criticized the FTC's performance":[97]

> Since at least the publication of the Nader's Raiders' exposé and the American Bar Association's critique, the 1960s has been regarded by many as a decade of trivial pursuits for the Federal Trade Commission. The Commission's reputation for chasing small-time con artists, challenging inconsequential business practices, turning a blind eye to politically connected corporations, and doing it all with a lethargy that exemplified popular notions of bureaucratic inertia, earned it the ridicule of consumer activists and the disdain of the regulatory bar.[98]

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92. *Cigarette Rule*, *supra* note 90, at 8355. The Cigarette Rule begins with this guidance:

> No enumeration of examples can define the outer limits of the Commission's authority to proscribe unfair acts or practices, but the examples should help to indicate the breadth and flexibility of the concept of unfair acts or practices and to suggest the factors that determine whether a particular act or practice should be forbidden on this ground.

Id.

93. *See* William MacLeod et al., *Three Rules and a Constitution: Consumer Protection Finds Its Limits in Competition Policy*, 72 ANTITRUST L.J. 943, 946–48 (2005) (reviewing the congressional response to the Cigarette Rule, culminating in the passage of the Federal Cigarette Labeling and Advertising Act in 1969); Schechter, *supra* note 77, at 1762 ("The FTC's effort to promulgate a final cigarette rule eventually foundered in the face of the complicated politics of tobacco, and Congress took direct legislative action to deal with the problem, rather than leaving it to administrative resolution." (citing Federal Cigarette Labeling & Advertising Act, Pub. L. No. 89-92 (1965) (codified as amended at 15 U.S.C. § 1333 (2000))); Schwartz, *supra* note 89, at 6 (noting that the Act "effectively overruled the Commission's trade regulation rule").

94. Schechter, *supra* note 77, at 1762.

95. EDWARD F. COX ET AL., THE NADER REPORT ON THE FEDERAL TRADE COMMISSION 66–73 (1969).

96. REPORT OF THE ABA COMMISSION TO STUDY THE FEDERAL TRADE COMMISSION (1969).

97. Sheila B. Scheuerman, *The Consumer Fraud Class Action: Reining in Abuse by Requiring Plaintiffs to Allege Reliance as an Essential Element*, 43 HARV. J. ON LEGIS. 1, 12 (2006).

98. MacLeod et al., *supra* note 93, at 943.

These critiques helped to usher in a new era of consumer regulation at the FTC in the early 1970s,[99] a movement strengthened by two legal events. First, in *FTC v. Sperry & Hutchinson Co*., the Supreme Court explicitly approved the FTC's broad unfairness authority, stating that the "Federal Trade Commission does not arrogate excessive power to itself if, in measuring a practice against the elusive, but congressionally mandated standard of fairness, it, like a court of equity, considers public values beyond simply those enshrined in the letter or encompassed in the spirit of the antitrust laws."[100] The *Sperry & Hutchinson* Court even cited the Cigarette Rule with some degree of approval.[101] Although the extent of the *Sperry & Hutchinson* Court's endorsement of the Cigarette Rule was open to debate,[102] the FTC responded by establishing "an internal task force charged with developing proposals to explore the contours of the . . . decision."[103] A second noteworthy event occurred in 1975 when Congress passed the Magnuson-Moss/FTC Improvements Act (Magnuson-Moss Act), which gave the FTC explicit rulemaking authority[104] (though with greater procedural requirements than before)[105] and expanded the remedies

99. For discussions of President Nixon's and the FTC's responses to the critiques of the agency, see KENNETH W. CLARKSON & TIMOTHY J. MURIS, THE FEDERAL TRADE COMMISSION SINCE 1970: ECONOMIC REGULATION AND BUREAUCRATIC BEHAVIOR 3–4 (1981); Mark Silbergeld, *The Revitalization of the FTC*, *in* KENNETH J. MEIER & E. THOMAS GARMAN, REGULATION AND CONSUMER PROTECTION 115–16 (2d ed. 1995).

100. 405 U.S. 233, 244 (1972).

101. *Id.* at 244 n.5.

102. *See* Averitt, *supra* note 77, at 245 n.130 ("Although the Court merely quoted the Commission's statement without expressly assenting to it, the overall context implied approval."); Braucher, *Defining Unfairness*, *supra* note 77, at 408 (noting "protracted debate about whether the Supreme Court really approved of the criteria"); Calkins, *supra* note 77, at 1952 ("The Cigarette Rule Statement's factors acquired talismanic status when the Supreme Court cited them with apparent approval in *FTC v. Sperry & Hutchinson Co*."); Rice, *supra* note 77, at 24–25 ("Close consideration of the [*Sperry & Hutchinson*] opinion, and the petition and brief in the case, demonstrates that the Commission did not seek the Supreme Court's approbation of the Cigarette Rule test and that the Court's quotation of the test in a footnote to its broad dictum expressed neither approval nor disapproval.") (citation omitted); Schechter, *supra* note 77, at 1763 ("While not strictly germane to the issue before it, the Court made favorable reference to the FTC unfairness definition in a footnote.").

103. MURIS & BEALES, *supra* note 77, at 12.

104. Prior to enactment of the Magnuson-Moss Act, the FTC claimed that it had substantive rulemaking authority under section 6(g) of the FTC Act, which gives the Commission authority "to make rules and regulations for the purpose of carrying out the provisions of" the FTC Act. 15 U.S.C. § 46(g) (2000). The D.C. Circuit endorsed the FTC's view in *National Petroleum Refiners Ass'n v. FTC*, 482 F.2d 672, 697–98 (D.C. Cir. 1973). Nonetheless, the passage of the Magnuson-Moss Act removed all doubt. *See* Mark E. Budnitz, *The FTC's Consumer Protection Program During the Miller Years: Lessons for Administrative Agency Structure and Operation*, 46 CATH. U. L. REV. 371, 414–16 (1997) (discussing the history of FTC rulemaking authority); WARD, *supra* note 88, § 13.01, at 13-2 to 13-6 (elaborating on rulemaking authority under FTC Act § 6(g)).

105. *See* WARD, *supra* note 88, § 13.01, at 13-4 (discussing the more "elaborate procedures" under the Magnuson-Moss/FTC Improvement Act).

available to the Commission.[106] Emboldened and operating in what appeared to be a favorable political environment,[107] the FTC proposed trade regulation rules in a wide variety of areas:[108]

> The agency proposed over two dozen industry-wide rules from 1971 through 1980 . . . . And the proposed rules were just a harbinger of what the Commission's leaders had in mind. President Carter's Chairman, Michael Pertschuk, who inherited most of these proceedings from his predecessor, suggested that the Commission was far from done. Whole new categories of potential rules could be based on public policy grounds, he announced—for example, to prohibit businesses from hiring illegal aliens, to prevent companies from cheating on taxes, and to require companies with repeated environmental violations to place an environmentalist on their boards.[109]

According to the conventional wisdom, the FTC, led by overzealous Chairman Michael Pertschuk, finally overstepped its bounds with Kid Vid[110]—an unsuccessful and controversial rulemaking effort aimed at restricting children's television advertising—especially advertising of heavily sugared foods.[111] Even the "normally friendly"[112] *Washington Post* editorial page heaped scorn on the FTC by branding it a "National Nanny."[113] As Pertschuk later observed:

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106. *See* Pub. L. No. 93-637, 88 Stat. 2183 (1975) (codified at 15 U.S.C. § 57a(a)(1)(B) (2000)) (providing authority to promulgate "rules which define with specificity acts or practices which are unfair or deceptive acts or practices in or affecting commerce").

107. *See* Budnitz, *supra* note 104, at 376 (noting the support of the Nixon administration and Congress for increased FTC activism).

108. *See* MacLeod et al., *supra* note 93, at 953–54 (listing twenty-eight major rulemakings in the 1970s). Actually, some of the successful FTC rulemaking efforts in the 1970s began prior to publication of the Supreme Court's opinion in *FTC v. Sperry & Hutchinson Co.* (decided Mar. 1, 1972) and enactment of the Magnuson-Moss Act (signed into law by President Ford on Jan. 4, 1975). For these rules, it would be erroneous to suggest that they were inspired by those events. *See, e.g.*, Posting of Minimum Octane Numbers on Gasoline Dispensing Pumps, 36 Fed. Reg. 23,871 (Dec. 16, 1971) (codified at 16 C.F.R. pt. 422); Care Labeling of Textile Wearing Apparel, 36 Fed. Reg. 23,883 (Dec. 16, 1971) (codified at 16 C.F.R. pt. 423); Cooling-Off Period for Door-to-Door Sales, 37 Fed. Reg. 22,934 (Oct. 26, 1972) (codified at 16 C.F.R. pt. 429).

109. MacLeod et al., *supra* note 93, at 952–54.

110. *See id.* at 944 (using the term "Kid Vid" to describe the Children's Advertising rulemaking). Other sources use the term "kidvid" or "Kidvid." *See, e.g.*, J. Howard Beales III, *Advertising to Kids and the FTC: A Regulatory Retrospective that Advises the Present*, 12 GEO. MASON L. REV. 873, 878 (2004) [hereinafter Beales, *Advertising to Kids*]; Tamara R. Piety, *"Merchants of Discontent": An Exploration of the Psychology of Advertising, Addiction, and the Implications for Commercial Speech*, 25 SEATTLE U. L. REV. 377, 442 (2001).

111. Children's Advertising, 43 Fed. Reg. 17,967 (Apr. 27, 1978).

112. J. Howard Beales III, *Brightening the Lines: The Use of Policy Statements at the Federal Trade Commission*, 72 ANTITRUST L.J. 1057, 1065 (2005) [hereinafter Beales, *Brightening the Lines*]; MacLeod et al., *supra* note 93, at 955 (referring to the *Washington Post* as "a typically friendly observer").

113. *See* Editorial, *The FTC as National Nanny*, WASH. POST, Mar. 1, 1978, at A22 (asserting that flat bans on advertising to children are "a preposterous intervention that would turn the agency into a great national nanny").

> The source of the "National Nanny" editorial was not *Broadcasting* magazine or a Washington spokesman for the Association of National Advertisers or the American Association of Advertising Agencies, but the "liberal establishment organ." It came, as one of the advertising trade association Washington representatives told me with mingled delight and disbelief, "not from *our* guys but from *your* guy."[114]

Whether Pertschuk was to blame,[115] the failed Kid Vid rulemaking effort,[116] along with other pending FTC action, precipitated a major conflict with Congress and a crisis in the agency,[117] as J. Howard Beales explains:

> The children's advertising proceeding was toxic to the Commission as an institution. Congress allowed the agency's funding to lapse, and the agency was literally shut down for a brief time. The FTC's other important law enforcement functions were left in tatters. Newspapers ran stories showing FTC attorneys packing their active investigational files in boxes for storage, and entire industries sought restriction of, or even outright exemptions from, the agency's authority. Congress passed a law prohibiting the FTC from adopting any rule in the children's advertising rulemaking proceeding, or in any substantially similar proceeding, based on an unfairness theory. It was more than a decade after the FTC terminated the rulemaking before Congress was willing to reauthorize the agency.[118]

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114. MICHAEL PERTSCHUK, REVOLT AGAINST REGULATION 70 (1982) (emphasis in original).

115. Mark Budnitz questions this account:

> The conventional wisdom, which views Pertschuk as the chairman who defied Congress by taking the FTC down the path of increased activism against Congress's wishes, clearly is wrong. Pertschuk was chided for his wide-ranging effort to promulgate trade regulation rules, but most of that activity began when Nixon was President, and it was Congress that had enacted the Magnuson-Moss . . . Act, which conferred broad rulemaking authority upon the FTC. Although Pertschuk was vilified by Congress and others for his "kid vid" initiative, Congress itself had recommended FTC action to protect children from television advertisements. The conflicting messages may be more a reflection of the election of a more conservative Congress than a principled objection to the Pertschuk agenda.

Budnitz, *supra* note 104, at 376 (internal citations omitted).

116. *See* Children's Advertising, 46 Fed. Reg. 48,710 (Oct. 2, 1981) (terminating the Children's Advertising rulemaking process). For a helpful review of the process by which the FTC decided not to pursue the Kid Vid rulemaking, see MacLeod et al., *supra* note 93, at 956–58 (discussing an FTC Staff Report on Television Advertising to Children (Mar. 14, 1978) and an FTC Final Staff Report and Recommendation (Mar. 31, 1981)).

117. *See* Budnitz, *supra* note 104, at 371 ("The conventional wisdom is that the Federal Trade Commission . . . under President Carter's Chairman, Michael Pertschuk, turned the FTC into a renegade agency which engaged in runaway consumer protection, hamstringing business with excessive regulation to such an extent it became known as the 'national nanny.'"); Calkins, *supra* note 77, at 1953–54 (discussing FTC overreaching and congressional backlash); MURIS & BEALES, *supra* note 77, at 14–15 (noting legislative, press, and business responses to "unfocused unfairness theories").

118. Beales, *Advertising to Kids*, *supra* note 110, at 879–80 (internal citations omitted); *see also* Am. Fin. Servs. Ass'n v. FTC, 767 F.2d 957, 969–70 (D.C. Cir. 1985) (citing Federal Trade Commission Improvements Act of 1980, Pub. L. No. 96-252, 94 Stat. 374

B. Law and Economics Ascendant: Federal Trade Commission Unfairness from 1980 to Present

Chastened from the battles of the late 1970s,[119] the FTC abandoned not only many of its pending rulemaking efforts,[120] but even the Cigarette Rule itself. In response to congressional inquiries[121] and possible legislative action against the agency,[122] the FTC issued a new Policy on Unfairness Statement,[123] which focused on one element of the Cigarette Rule:[124] unjustified consumer injury.[125] The FTC Unfairness Policy Statement,

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(codified as amended in scattered sections of 15 U.S.C.)) (noting that the congressional response to Kid Vid included enactment of a federal law that "suspended the Commission's controversial rulemaking on children's advertising and placed a moratorium on the initiation of any new rulemakings aimed at regulating commercial advertising as an unfair practice pending congressional oversight hearings"); MacLeod et al., *supra* note 93, at 961 ("The FTC Improvements Act of 1980 . . . revoked the Commission's authority to promulgate any rule invoking a theory of unfairness to govern advertising and terminated other proceedings."); Sidney M. Milkis, *The Federal Trade Commission and Consumer Protection: Regulatory Change and Administrative Pragmatism*, 72 ANTITRUST L.J. 911, 925 (2005) ("The controversy surrounding 'Kid Vid' proved to be a lightning rod, which led eventually to efforts by Congress and the Reagan administration that halted, at least for a decade, consumer activism in the Commission.").

119. *See* Piety, *supra* note 110, at 443 ("The FTC that emerged from these disputes was a distinctly chastened one for many years thereafter.").

120. *See* MacLeod et al., *supra* note 93, at 953–54 (chart indicating that fourteen of twenty-one rulemakings from 1974 to 1980 were terminated by the FTC); Thomas O. McGarity, *Some Thoughts on "Deossifying" the Rulemaking Process*, 41 DUKE L.J. 1385, 1389–90 (1992) (observing that "[o]f the nineteen major rules and amendments proposed . . . during the latter part of the 1970s . . . only seven were completed") (internal citations omitted).

121. *See* S. COMM. ON COMMERCE, SCI., AND TRANSP., 96TH CONG., 2D SESS., UNFAIRNESS: VIEWS ON UNFAIR ACTS AND PRACTICES IN VIOLATION OF THE FEDERAL TRADE COMMISSION ACT (Comm. Print 1980).

122. *See* Beales, *Brightening the Lines*, *supra* note 112, at 1063 ("The Unfairness Policy Statement emerged as the Commission's response to mounting external political pressure. As concerns grew about the breadth of the Commission's authority to declare a practice unfair, the agency faced serious threats to important parts of its consumer protection jurisdiction."); Braucher, *Defining Unfairness*, *supra* note 77, at 409 (discussing the Unfairness Policy Statement's political purposes).

123. *See* Letter from the FTC to Hon. Wendell Ford and Hon. John Danforth, S. Comm. on Commerce, Sci., and Transp., Comm. Statement of Policy on the Scope of Consumer Unfairness Jurisdiction (Dec. 17, 1980), *reprinted in* Int'l Harvester Co., 104 F.T.C. 949, 1070–76 (1984) [hereinafter FTC Unfairness Policy Statement]. In 1982, the FTC reaffirmed the 1980 Unfairness Policy Statement in a letter from Chairman Miller to Senators Packwood and Kasten (Mar. 5, 1982), *reprinted in* H.R. REP. NO. 99-162, at 28 (1985).

124. Some sources refer to the three part test as the Cigarette Test, due to its original administrative pedigree, *see Cigarette Rule*, *supra* note 90, whereas other sources refer to it as the *S&H* standard because of the Supreme Court's purported endorsement of the Cigarette Test in *FTC v. Sperry & Hutchinson*. *See supra* notes 100–02 and accompanying text.

125. *See* FTC Unfairness Policy Statement, *supra* note 123, at 1073 ("Unjustified consumer injury is the primary focus of the FTC Act, and the most important of the three *S&H* criteria. By itself it can be sufficient to warrant a finding of unfairness."); MURIS & BEALES, *supra* note 77, at 15; Michael M. Greenfield, *Unfairness Under Section 5 of the FTC Act and Its Impact on State Law*, 46 WAYNE L. REV. 1869, 1874 (2000) (quoting *Int'l Harvester Co.*, 104 F.T.C. at 1071). The Unfairness Policy Statement also retained the

appended to the FTC's decision in *International Harvester*,[126] held that a finding of unfairness required a consumer injury that is: (1) substantial;[127] (2) not outweighed by any offsetting consumer or competitive benefits that the practice produces;[128] and (3) not reasonably avoidable by consumers.[129] In most cases, injury means monetary or physical harm, although other harms might be cognizable under unfairness law.[130]

Most notably, the Unfairness Policy Statement rejected the Cigarette Rule's reliance on whether a challenged practice was "immoral, unethical, oppressive, or unscrupulous,"[131] noting that "[c]onduct that is truly unethical or unscrupulous will almost always injure consumers or violate public policy as well."[132] The Unfairness Policy Statement, therefore, embraced a cost-benefit view of unfairness inspired by the teachings of law and economics rather than a conception of unfairness based on some amorphous sense of public morality.[133] This understanding of unfairness is

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"public policy prong" of the Cigarette/*S&H* Test, noting that "[i]t may be used to test the validity and strength of the evidence of consumer injury, or, less often, it may be cited for a dispositive legislative or judicial determination that such injury is present." FTC Unfairness Policy Statement, *supra* note 123, at 1074–75. The FTC made clear, however, that "[t]o the extent that the Commission relies heavily on public policy to support a finding of unfairness, the policy should be clear and well-established." *Id.* at 1076.

The FTC subsequently backed off from this view, when "in 1982 a unanimous Commission . . . clarified that the use of public policy is not an independent basis for finding unfairness." MURIS & BEALES, *supra* note 77, at 18 (citing Letter from FTC to Hon. Robert Packwood and Hon. Robert Kasten at 8 (Mar. 5, 1982), *reprinted in* H.R. REP. NO. 98-156, pt. 1, at 27, 32–33 (1983)); *see also* Paul Sobel, *Unfair Acts or Practices Under CUTPA—The Case for Abandoning the Obsolete Cigarette Rule and Following Modern FTC Unfairness Policy*, 77 CONN. B.J. 105, 118 (2003) (discussing the FTC's shifting treatment of public policy). Congress later codified the FTC's stated limitation on the use of public policy. *See infra* note 163.

126. *Int'l Harvester Co*., 104 F.T.C. at 1070–76.

127. *See id.* at 1073 ("First of all, the injury must be substantial. The Commission is not concerned with trivial or merely speculative harms.").

128. *See id.* ("[T]he injury must not be outweighed by any offsetting consumer or competitive benefits that the sales practice also produces.").

129. *See id.* at 1074 ("[T]he injury must be one which consumers could not reasonably have avoided.").

130. *See* SHELDON & CARTER, *supra* note 6, § 4.3.2.2, at 193–94 ("Substantial injury must not be trivial or merely speculative harm, but will usually involve monetary harm or unwarranted health and safety risks. Emotional or other subjective harm alone will not ordinarily make a practice unfair, although invasion of privacy may be a substantial injury.") (internal citations omitted); Jean Braucher, *Delayed Disclosure in Consumer E-Commerce As an Unfair and Deceptive Practice*, 46 WAYNE L. REV. 1805, 1858 (2000) ("The essence of 'substantialness' is monetary harm."); Schechter, *supra* note 77, at 1770 (discussing injury requirement and noting that "the concept of 'injury' in the law of unfairness is surprisingly underdeveloped").

131. FTC Unfairness Policy Statement, *supra* note 123, at 1076.

132. *Id.* The Commission made clear that it "has therefore never relied on the third element of *S&H* as an independent basis for a finding of unfairness, and it will act in the future only on the basis of the first two." *Id.*

133. *See* PRIDGEN, *supra* note 6, § 9:5, at 569 ("The notion of immorality or lack of ethics (a more intuitive understanding of unfairness) plays no role in this legal construct. Instead, the discipline of economics looms large as the guiding light of the FTC's new unfairness doctrine."); Thomas B. Leary, *Unfairness and the Internet*, 46 WAYNE L. REV.

rooted in the concept of *consumer sovereignty*:[134] "the set of societal arrangements that causes that economy to act primarily in response to the aggregate signals of consumer demand, rather than in response to government directives or the preferences of individual businesses."[135] Consumer sovereignty therefore means that consumers choose what to consume. The government does not choose for consumers, as it might in a socialist, rather than a free market, economic system.[136] Consumer sovereignty is justified by rational choice theory[137] because "[a]ccording to economic theory, individual utility—and social welfare—are maximized when individuals make their own consumption choices."[138]

The law and economics era at the FTC, heralded by the adoption of the Unfairness Policy Statement in 1980, began in earnest in 1981 when President Reagan[139] appointed James C. Miller, the first economist ever to

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1711, 1713 (2000) (noting that the Cigarette Rule gave "primacy to moral and ethical concepts, and to precedent" whereas the newer standard "gives primacy to economic factors, and introduces the notion of consumer responsibility").

134. *See Int'l Harvester Co.*, 104 F.T.C. at 1061 ("The Commission does not ordinarily seek to mandate specific conduct or specific social outcomes, but rather seeks to ensure simply that markets operate freely, so that consumers can make their own decisions."); PRIDGEN, *supra* note 6, § 9:5, at 568–69 ("Indeed, the entire consumer unfairness doctrine now appears to be based solely on the idea of consumer sovereignty, *i.e.*, that consumers must be able to make their own decisions in the marketplace, free of unfair impediments.").

135. Neil W. Averitt & Robert H. Lande, *Consumer Sovereignty: A Unified Theory of Antitrust and Consumer Protection Law*, 65 ANTITRUST L.J. 713, 715 (1997) (internal citation omitted). According to Averitt and Lande, consumers are sovereign when they have "the power to define their own wants and the opportunity to satisfy those wants at prices not greatly in excess of the costs borne by the providers of the relevant goods and services." *Id.* at 716. For more on the concept of consumer sovereignty, see G. PETER PENZ, CONSUMER SOVEREIGNTY AND HUMAN INTERESTS 13–14 (Cambridge Univ. Press 1986) (discussing alternative definitions of "consumer sovereignty"); W.H. Hutt, *The Concept of Consumers' Sovereignty*, 50 ECON. J. 66, 66 (1940) (defining "consumer sovereignty" as "the controlling power exercised by free individuals, in choosing between ends, over the custodians of the community's resources, when the resources by which those ends can be served are scarce"); Joseph Persky, *Consumer Sovereignty*, 7 J. ECON. PERSP. 183, 184 (1993).

136. Averitt & Lande, *supra* note 135, at 716 ("The concept of consumer sovereignty goes so far as to embody at least some implicit notions about the proper relationship between the individual and the state. It is part of the Western world's answers to the prescriptions of Marxism.").

137. *See* Simona Botti & Sheena S. Iyenger, *The Dark Side of Choice: When Choice Impairs Social Welfare*, 25 J. PUB. POL'Y & MARKETING 24, 25–26 (2006) (discussing theoretical connections between the benefits of choice and rational choice theory).

138. Joel Waldfogel, *Does Consumer Irrationality Trump Consumer Sovereignty?*, 87 REV. ECON. & STAT. 691, 691 (2005).

139. The early years of the Reagan presidency were heady times for those sympathetic to the Chicago school law and economics movement. The academic leader of the movement, Richard Posner, was appointed to the U.S. Court of Appeals for the Seventh Circuit, along with another prominent law and economics scholar, Frank Easterbrook. *See* NEIL DUXBURY, PATTERNS OF AMERICAN JURISPRUDENCE 358 (Clarendon Press 1995). In addition, Reagan issued Exec. Order No. 12,291, which mandated cost-benefit analysis in administrative rulemaking. Exec. Order No. 12,291, 46 Fed. Reg. 13,193 (Feb. 19, 1981) ("Regulatory action shall not be undertaken unless the potential benefits to society for the regulation outweigh the potential costs to society."). Exec. Order No. 12,291 did not technically apply to the FTC, since the FTC is an independent agency. *See* Elena Kagan,

head the FTC.[140] During Miller's tenure, Timothy Muris, a law professor well-versed in economic analysis and co-editor of and contributor to a highly critical book on the FTC,[141] became the Director of the Bureau of Consumer Protection.[142] Miller and Muris were committed to transforming the manner in which the Commission did business—embracing an approach to consumer regulation that was more economically disciplined and less adversarial towards business interests.[143] This approach to regulation naturally had its critics, even within the Commission itself, where Michael Pertschuk, Miller's controversial predecessor, remained on as a Commissioner and "resident saboteur."[144] Pertschuk wrote a 242-page report to Congress criticizing Miller and his economic approach,[145] which elicited a harsh response from Miller that ran over 110 single-spaced pages in length,[146] in which Miller claimed that Pertschuk "nearly destroyed the agency with his bizarre behavior as Chairman."[147]

The FTC's new regulatory philosophy was evident in 1984, as the Commission completed a long-pending rulemaking proceeding[148] by

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Presidential Administration, 114 HARV. L. REV. 2245, 2277–78 (2001); Angel Manuel Moreno, *Presidential Coordination of the Independent Regulatory Process*, 8 ADMIN. L.J. AM. U. 461, 494–97 (1994).

140. *See* Spencer Weber Waller, *The Language of Law and the Language of Business*, 52 CASE W. RES. L. REV. 283, 303 n.86 (2001) (noting that Miller, who was "an economist sympathetic to Chicago school economics . . . was the first economist to serve on the Commission itself and the first non-lawyer in thirty years" (citing MARC ALLEN EISNER, ANTITRUST AND THE TRIUMPH OF ECONOMICS 213 (1991))).

141. *See* CLARKSON & MURIS, *supra* note 99.

142. *See* MEIER & GARMAN, *supra* note 99, at 118 ("Miller recruited numerous economists to the FTC so that he could rely on others with similar views to implement policy. Included among the personnel was Timothy J. Muris, a longtime FTC critic, to head the Bureau of Consumer Protection.") (internal citation omitted); Budnitz, *supra* note 104, at 383; MacLeod et al., *supra* note 93, at 962 (observing that two of Miller's top policy appointees had doctorates in economics and that Timothy Muris, his Director of the Bureau of Consumer Protection, was a lawyer whose work drew on economic theory). Muris later became Chairman of the Federal Trade Commission under President George W. Bush. *See Looking Back on the Muris Years in Consumer Protection: An Interview with Timothy J. Muris*, 18 ANTITRUST 9 (2004) [hereinafter *Muris Interview*].

143. *See* Budnitz, *supra* note 104, at 377–81 (discussing Miller's approach and his confirmation testimony). Miller discusses his tenure at the FTC and the Reagan administration's regulatory philosophy in JAMES C. MILLER III, THE ECONOMIST AS REFORMER: REVAMPING THE FTC, 1981–1985 (1989).

144. Letter from James C. Miller III to Hon. John D. Dingell (Sept. 21, 1984), *in* FTC REVIEW (1977–84): A REPORT PREPARED FOR THE SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS OF THE HOUSE COMMITTEE ON ENERGY AND COMMERCE 273 (Comm. Print 1984) [hereinafter FTC Review] (asserting that it was "very difficult . . . to make headway when someone in authority sees his role as resident saboteur"). For a scholarly treatment of the Miller years at the FTC, see Budnitz, *supra* note 104.

145. *See* FTC REVIEW, *supra* note 144, at 242.

146. *See id.* at 275–394, 280 (criticizing Pertschuk's report as consisting of "errors, mischaracterizations, and outright lies").

147. *Id.* at 280.

148. The rule was initially proposed in 1975. *See* Credit Practices Rule, 40 Fed. Reg. 16,347–50 (Apr. 11, 1975) (codified at 16 C.F.R. pt 444); MacLeod et al., *supra* note 93; *see also* Am. Fin. Servs. Ass'n v. FTC, 767 F.2d 957, 962–63 (D.C. Cir. 1985) (reviewing

unanimously approving[149] the Credit Practices Rule (CPR).[150] The CPR forbids certain practices in connection with consumer credit contracts, including (1) confessions of judgment, cognovits, and other waivers of the right to notice and opportunity to be heard,[151] (2) waivers of exemption from attachment or execution for personal property,[152] (3) assignment of wages or other earnings before judgment,[153] (4) non-purchase money security interests in certain household goods,[154] (5) "pyramiding" late charges for late payments,[155] and (6) failing to provide cosigners with certain warnings.[156] Regardless of whether the CPR was wise as a matter

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the history of Credit Practices rulemaking); Braucher, *Defining Unfairness*, *supra* note 77, at 412–13 (describing the history and content of the Credit Practices Rule).

149. *See Am. Fin. Servs. Ass'n*, 767 F.2d at 963 ("On July 20, 1983, the Commission tentatively adopted, by unanimous vote, the revised proposed rule. The final rule was published on March 1, 1984, to become effective March 1, 1985." (citing Credit Practices Rule, 49 Fed. Reg. 7740 (Mar. 1, 1984) (codified at 16 C.F.R. pt. 444))). Although the vote was unanimous, Commissioner Pertschuk suggested that the two conservative members of the Commission, Chairman Miller and Commissioner Carol Crawford, vote in favor of the proposed rule despite their opposition because they faced defeat. *See* Pertschuk Report, *in* FTC Review, *supra* note 144, at 160–61 (describing the initial opposition to the rule that ultimately led to the unanimous vote of the commissioners).

150. *See* 16 C.F.R. § 444.1–444.4 (2007) (banning certain practices in connection with consumer credit contracts); *see also* 16 C.F.R. § 444.5 (state exemptions to Credit Practices Rule). For background of the Credit Practices Rule, see PRIDGEN, *supra* note 6, § 9:20, at 710-13; SHELDON & CARTER, *supra* note 6, § 5.1.3.1, at 278–79.

151. *See* 16 C.F.R. § 444.2(a), (a)(1) (deeming it an unfair act or practice for a lender or retail installment seller "to take or receive from a consumer an obligation that . . . [c]onstitutes or contains a cognovit or confession of judgment . . . or other waiver of the right to notice and the opportunity to be heard in the event of suit").

152. *See id.* § 444.2(a), (a)(2) (deeming it an unfair act or practice for a lender or retail installment seller "to take or receive from a consumer an obligation that . . . [c]onstitutes or contains an executory waiver or a limitation of exemption from attachment, execution, or other process on real or personal property held, owned by, or due to the consumer" with the exception of "a security interest executed in connection with the obligation").

153. *See id.* § 444.2(a), (a)(3) (deeming it an unfair act or practice for a lender or retail installment seller "to take or receive from a consumer an obligation that . . . [c]onstitutes or contains an assignment of wages or other earnings," with certain exceptions); *see also id.* § 444.2(a)(3)(i)–(iii) (listing exceptions to the prohibition on wage assignments).

154. *See id.* § 444.2(a), (a)(4) (deeming it an unfair act or practice "to take or receive from a consumer an obligation that . . . [c]onstitutes or contains a nonpossessory security interest in household goods other than a purchase money security interest").

155. *Id.* § 444.4(a) (deeming it an unfair act or practice for a creditor to levy "any delinquency charge on a payment, which payment is otherwise a full payment for the applicable period and is paid on its due date or within an applicable grace period, when the only delinquency is attributable to late fee(s) or delinquency charge(s) assessed on earlier installment(s)"). *See* Braucher, *Defining Unfairness*, *supra* note 77, at 414 n.311 (explaining pyramiding); PRIDGEN, *supra* note 6, § 9:20, at 712 (defining "pyramiding" as "any method of accounting that results in the assessment of multiple late charges based on a single late payment"); SHELDON & CARTER, *supra* note 6, § 5.1.3.1, at 278–79.

156. *See* 16 C.F.R. § 444.3(a)(2) (deeming it an unfair act or practice for a "lender or retail installment seller . . . to obligate a cosigner unless the cosigner is informed prior to becoming obligated . . . of the nature of his or her liability as cosigner"); *id.* § 444.3(c) (mandating the form of notice disclosing the obligation of liability to a cosigner); *see also id.* § 444.3(a)(1) (deeming it a deceptive act or practice "for a lender or retail installment seller . . . to misrepresent the nature or extent of cosigner liability to any person").

of public policy, the promulgation process reflected a distinctly different approach from earlier FTC rulemaking efforts. The FTC justified the CPR under a consumer sovereignty/market failure approach to unfairness, not under vague moral or ethical notions.[157] One author observes: "The Statement of Basis and Purpose for the Credit Practices Rule took great pains to show that the injurious contract clauses would not be eliminated by the proper functioning of the market."[158] This economic approach carried over when the D.C. Circuit upheld the CPR,[159] with both the majority[160] and dissenting[161] opinions focusing their discussions on whether the rule was economically justified. Similarly, most scholarly analyses of the CPR focus on whether the FTC correctly determined that the prohibition on certain creditor remedies was necessary from a market-perfecting perspective.[162]

In 1994, Congress codified the FTC's Unfairness Policy Statement[163] with a restriction on the use of public policy as a primary basis for a finding of unfairness.[164] This legislative move solidified what was apparent since the early 1980s—economics was ascendant at the FTC and unfairness was in decline.[165] J. Howard Beales explains that, in the realm of adjudication,

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157. *See* Credit Practices Rule: Statement of Basis and Purpose and Regulatory Analysis, 49 Fed. Reg. 7740 (Mar. 1, 1984) (describing the purpose and legal basis of the rule); *see also* Beales, *supra* note 77, at 194–95 (indicating that market imperfections led to consumer injuries); Braucher, *Defining Unfairness*, *supra* note 77, at 418–21 (reviewing evidence of market failure for consumer credit remedies); *id.* at 418 ("The FTC's two fundamental questions can be summed up as follows: (1) does use of a practice result from market failure; and (2) would prohibiting the practice result in a net benefit?").

158. PRIDGEN, *supra* note 6, § 9:20, at 713.

159. Am. Fin. Servs. Ass'n v. FTC, 767 F.2d 957 (D.C. Cir. 1985).

160. *See id.* at 962 (finding that the rule was justified).

161. *See id.* at 991 (Tamm, J., dissenting) (arguing that the FTC's decision exceeded its statutory authority and that the rule was not justified).

162. For an overview of the economic and empirical research, see Peter V. Letsou, *The Political Economy of Consumer Credit Regulation*, 44 EMORY L.J. 587 (1995); see also James R. Barth et al., *Benefits and Costs of Legal Restrictions on Personal Loan Markets*, 29 J.L. & ECON. 357 (1986); Peter M. Juzwiak, *Mr. Micawber Revisited: A Critique of the Credit Practices Rule*, 64 S. CAL. L. REV. 417 (1991); Robert E. Scott, *Rethinking the Regulation of Coercive Creditor Remedies*, 89 COLUM. L. REV. 730 (1989); Daniel J. Villegas, *Regulation of Creditor Practices: An Evaluation of the FTC's Credit Practice Rule*, 42 J. ECON. & BUS. 51 (1990); William C. Whitford, *The Appropriate Role of Security Interests in Consumer Transactions*, 7 CARDOZO L. REV. 959 (1986).

163. *See* 15 U.S.C. § 45(n) (2000) (providing that the Commission has no authority to declare unlawful acts or practices on the basis of unfairness "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").

164. *See id.* (permitting considerations of public policy along with other evidence, but not allowing them to serve as a primary basis in determining whether an act or practice is unfair).

165. State consumer laws that protect against unfair practices are beyond the scope of this Article. I would note, however, that the FTC Act serves both formally and informally as a model for state consumer protection laws. *See generally* Greenfield, *supra* note 125 (describing the impact of the FTC's rules on states). At the same time, many states have not

"the commission showed extreme reluctance to assert its unfairness authority. Perhaps overly chastened by the reaction to past abuses, the commission avoided pleading unfairness, sometimes twisting deception theories to get at clearly injurious acts that called for commission action."[166] The trend began to turn around in the late 1990s, as the FTC began to show a willingness to plead unfairness in cases where reliance on deception theories alone might have been insufficient or inappropriate.[167] For example, the FTC asserted unfairness claims involving unauthorized bank debits arising out of a magazine-subscription telemarketing scheme[168] and unauthorized telephone bill charges connected to purported online access to pornography.[169] In addition, the FTC has used its unfairness authority to attack a variety of deleterious online tactics such as spoofing,[170] spyware,[171] and mousetrapping.[172] In all of these cases, the

adopted the newer approach to unfairness embodied in the Unfairness Policy Statement and the revision of the FTC Act, but instead have continued to use the arguably more liberal Cigarette Rule. *See* Matthew A. Edwards, *The Law, Marketing and Behavioral Economics of Consumer Rebates*, 12 STAN. J.L. BUS. & FIN. 362, 404 n.223 (2007) [hereinafter Edwards, *Consumer Rebates*] (indicating that "most states" have not adopted the FTC's definition of unfairness).

166. *See* Beales, *supra* note 77, at 195.

167. *See id.* at 197–200 (citing instances in which the FTC utilized its unfairness authority); Diomande, *supra* note 77, at 54 (discussing the expanded use of the FTC's unfairness authority in the 1990s); *Panel Probes Revival of Unfairness Doctrine in FTC or States' Consumer Protection Cases*, 86 ANTITRUST & TRADE REG. REP. (BNA) 352, 352–53 (Apr. 9, 2004) [hereinafter *Revival of Unfairness*] (summarizing the Consumer Protection Committee program at the 52nd Annual Spring Meeting of the American Bar Association's Section of Antitrust Law in Washington, D.C.).

168. *See* FTC v. Winward Mktg, Ltd., No. 1:96-CV-615F, 1997 WL 33642380, at *2 (N.D. Ga. Sept. 30, 1997) (unpublished) (enjoining a company from marketing based on findings of its participation in false, deceptive, misleading, and unfair marketing and banking practices).

169. *See* FTC v. Verity Int'l, Ltd., 335 F. Supp. 2d 479, 498–99 (S.D.N.Y. 2004) (holding that the "defendants' practice of billing line subscribers for Internet services that they neither used, nor authorized use of, constituted an unfair trade practice in violation of Section 5(a) of the FTC Act"), *aff'd in part and vacated in part*, 443 F.3d 48 (2d Cir. 2006).

170. *See* FTC v. Westby, No. 03-C-2540, 2004 WL 1175047, at *2 (N.D. Ill. Mar. 4, 2004) (unpublished) (defining spoofing as the practice of disguising an e-mail to make the e-mail appear to come from an address from which it did not originate); *see also* Amended Complaint for Injunctive and Other Equitable Relief, FTC v. Westby, No. 03-C-2540, 2004 WL 1175047, at *3 (N.D. Ill. Mar. 4, 2004), *available at* http://www.ftc.gov/os/2003/09/marriedcomp.pdf (defining spoofing).

171. *See generally* Susan P. Crawford, *First Do No Harm: The Problem of Spyware*, 20 BERKELEY TECH. L.J. 1433, 1465–66 (2005) (discussing the FTC's response to spyware); *see also* FTC v. Seismic Entm't Prods., Inc., No. 04-377-JD, 2004 U.S. Dist. LEXIS 22788, at *15–16 (D.N.H. Oct. 21, 2004) (finding that the public's interest in preventing unauthorized access to consumers' computers by an internet marketing company to be of grave concern).

172. *See* Diomande, *supra* note 77, at 54 (referring to "mousetrapping" as "the misuse of pop-up windows to post advertisements on the Internet"); Complaint for Permanent Injunction and Other Equitable Relief ¶ 26, FTC v. Zuccarini, No. 01-CV-4854, 2001 WL 34131412 (E.D. Pa. Apr. 9, 2002) (explaining that when consumers attempted to close a browser window, they found "themselves in yet another new window and viewing yet another of Defendant's advertisements—a practice commonly referred to as

FTC determined that even if consumers were not being deceived, they were being subjected to harmful business practices that produced few offsetting benefits.

Unfairness rulemaking, however, has not enjoyed a similar renaissance at the FTC.[173] In contrast to the rules promulgated in the 1970s, most recent FTC rulemakings have responded to specific congressional mandates[174] rather than to the Commission's unfairness authority.[175] For example, when the FTC created the popular Do-Not-Call Registry in 2003,[176] it claimed to be acting under the Telemarketing and Consumer Fraud and Abuse Prevention Act.[177] When this authority was challenged,[178] Congress stepped in and explicitly ratified the Registry.[179] In addition, the FTC has promulgated rules regarding pay-per-call services[180] ("900" numbers) and children's online privacy,[181] both in response to specific congressional directives.[182] Whether or not it is justified, the FTC's reluctance to aggressively or creatively use its unfairness rulemaking

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'mousetrapping'"). Although the final court order did not use the term "mousetrapping," it did describe the underlying conduct. *See* FTC v. Zuccarini, No. 01-CV-4854, 2002 U.S. Dist. LEXIS 13324, at *3 (E.D. Pa. Apr. 9, 2002).

173. *See* Alan M. White & Cathy Lesser Mansfield, *Literacy and Contract*, 13 STAN. L. & POL'Y REV. 233, 259 (2002) ("The FTC has not issued a substantive consumer-contract regulation since the 1984 Credit Practices Rule. Recent rules tend to emphasize disclosures or the avoidance of misrepresentations and to regulate abusive conduct, rather than regulating substantive terms.").

174. *See* PRIDGEN, *supra* note 6, § 12:13, at 1004–05 (citing the rulemaking in response to the Telephone and Dispute Resolution Act of 1992, the Telemarketing Act in 1994, the Comprehensive National Energy Policy Act of 1992, and amendments to the Fair Packaging and Labeling Act).

175. The FTC Funeral Industry Practices Rule, which became effective in 1984, is one exception. *See* PRIDGEN, *supra* note 6, § 9:14, at 590–91 (discussing 16 C.F.R. § 453.2 (1985)). For an economic analysis of the FTC Funeral Rule, see Fred S. McChesney, *Consumer Ignorance and Consumer Protection Law: Empirical Evidence from the FTC Funeral Rule*, 7 J. L. & POL. 1 (1990).

176. *See* 16 C.F.R. § 310 (2007). For discussions of the administrative and legislative history of the Do Not Call Registry, see Joseph Dean Findley, *The Do-Not-Call Registry and Its Overwhelming Support: This Time Congress Really Means It*, 5 WYO. L. REV. 605 (2005); R. Michael Hoefges, *Telemarketing Regulation and the Commercial Speech Doctrine*, 32 J. LEGIS. 50 (2005); Douglas C. Nelson, *The Do-Not-Call Implementation Act: Legislating the Sound of Silence*, 16 LOY. CONSUMER L. REV. 63 (2003).

177. 15 U.S.C. § 6101 (2000).

178. *See* U.S. Security v. FTC, 282 F. Supp. 2d 1285, 1294 (W.D. Okla. 2003) (holding that the FTC lacked authority to create the Do-Not-Call Registry), *rev'd sub nom.* Mainstream Mktg. Servs., Inc. v. FTC, 358 F.3d 1228, 1251 (10th Cir. 2004), *cert. denied*, 543 U.S. 812 (2004).

179. *See* Act to Ratify the Authority of the Federal Trade Commission to Establish a Do-Not-Call Registry, Pub. L. No. 108-82, 117 Stat. 1006 (2003) (codified at 15 U.S.C. § 6102 (Supp. V 2005)).

180. Trade Regulation Rule Pursuant to the Telephone Disclosure and Dispute Resolution Act of 1992, 16 C.F.R. pt. 308 (2004).

181. Children's Online Privacy Protection Rule, 16 C.F.R. pt. 312 (2004).

182. Telephone Disclosure and Dispute Resolution Act, Pub. L. No. 102-556, 106 Stat. 4181 (1992) (codified in pertinent part at 15 U.S.C. §§ 5711–5724 (2000)); Children's Online Privacy Protection Act, 15 U.S.C. §§ 6501–6506 (2000).

authority, and to proceed through threatened litigation and consent decrees, has led to a remarkable dearth of unfairness case law at the appellate level during the past two decades.[183]

III. BEHAVIORAL LAW AND ECONOMICS AT THE FEDERAL TRADE COMMISSION: POSSIBLE REGULATORY DIRECTIONS

A. Introduction

Thus far, this Article has discussed two conflicting, long-term trends. During the past fifteen years, we have witnessed the rise of behavioral law and economics, which has led to advocacy of a new paternalism or an "anti-antipaternalism."[184] The second trend began in the early 1980s, as the FTC moved towards an economic view of unfairness grounded in a concept of consumer sovereignty—a move that Congress explicitly approved.[185] Former FTC Chairman Timothy J. Muris, an important player (or victor)[186] in the historical drama, summed it up in a 2004 interview: "In 1981, the FTC began to put its faith in markets. We made a conscious shift from being an agency that tried to promulgate rule after rule. We believed back then and continue to believe today that the FTC should be the umpire, not the star player."[187] Given this prevailing ethos, the question emerges as to how the Commission is likely to respond to the new paternalism. The remainder of this Article will address this issue.

B. Deference to Congress and Commission Study

At the outset, it is worthwhile to acknowledge two possible regulatory responses to the new paternalism. First, the FTC could take no special action. The Commission could continue to do what it has been doing for the past several years—assiduously avoiding industry-wide unfairness rulemaking and bringing carefully selected unfairness enforcement actions

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183. In a piece published in 2000, Stephen Calkins made the following observation about the congressional codification of the FTC Unfairness Statement:

> The Supreme Court has not spoken. No new court of appeals has weighed in. No opinion of the Commission addresses FTC Act Section 5(n). The Commission has not based any new Trade Regulation Rule on the unfairness authority. New initiatives and new thinking are reflected only in consent orders and complaints (a couple of which have led to District Court decisions).
>
> In part due to the dearth of binding precedent, the law of FTC unfairness remains indeterminate.

Calkins, *supra* note 77, at 1960 (citations omitted); *see also supra* notes 163–64 and accompanying text (discussing adoption of FTC Act § 5(n)).

184. *See supra* Part I.

185. *See supra* Part I.

186. *See Muris Interview*, *supra* note 142, at 10 ("There really was a Reagan Revolution in antitrust and consumer protection. As I like to say, my side won.").

187. *Id.*

based upon traditional economic doctrine, guided by the strictures of § 45(n).[188] By implication, this would be a policy of deference to Congress; the Commission could sit back and wait for Congress to suggest or mandate action in specific trade or marketing contexts based upon evidence of suboptimal consumer behavior. This cautious approach would be understandable given the history of FTC unfairness policy traced earlier in this Article.

Second, even without traditional regulatory action, such as rulemaking or litigation, the FTC could use its unique position to influence the debate over the new paternalism through economic research. FTC Commissioners appointed by presidents from both political parties have noted that one of the strengths of the FTC is that it is not simply a law enforcement agency, but that it is charged with studying the marketplace and working with industry to develop innovative regulatory solutions to potentially deleterious marketplace phenomena.[189] Robert Pitofsky, Chairman of the FTC from 1995 to 2001, explains:

> Another important change in the Commission's approach to regulation, contributing to its enhanced status, involves the recognition that the FTC was not created solely as a law enforcement agency. Rather, it was established in 1914 to work with the private sector, provide advice about possible violations, anticipate and study economic trends and developments, and anticipate and report to the White House, Congress, and the public likely economic problems. To support this role, the FTC was granted in its enabling statute broader powers of investigation than almost any other department or agency in the federal government. Published reports and studies over the last several years relating to changes in business patterns as a result of global competition, for-profit invasions of individual privacy, strengths and weaknesses of the current patent system, and issues at the intersection of antitrust and intellectual property, among many others, have usefully discharged that function.[190]

Pitofsky's successor, Timothy Muris, echoed this point:

> Just as a high-technology company must research to develop new products, so too must a competition agency expand its knowledge to design law enforcement and other policies to conquer current and anticipated consumer problems. A farsighted feature of Congress's

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188. *See supra* notes 163–64 and accompanying text.
189. *See generally* Symposium, *More Than Law Enforcement: The FTC's Many Tools—A Conversation with Tim Muris and Bob Pitofsky*, 72 ANTITRUST L.J. 773 (2005) (detailing the nonlitigation role of the FTC).
190. Robert Pitofsky, *Past, Present, and Future of Antitrust Enforcement at the Federal Trade Commission*, 72 U. CHI. L. REV. 209, 213–14 (2005) (citations omitted).

> institutional design is that it gave the FTC flexible tools to perform the necessary research and development.[191]

The FTC's Bureau of Economics, which is "composed of 70 Ph.D.-level economists, a small cadre of accountants, and 25 other staff who support the FTC's two missions of promoting competition (antitrust) and protecting consumers,"[192] has already taken this type of action on the BLE front. In April 2007, the Bureau of Economics hosted a conference entitled "Behavioral Economics and Consumer Policy," which brought together many prominent academics involved in the debates over the new paternalism.[193] Thus, the FTC has indicated a willingness to use its formidable resources and expertise to study the implications of BLE and the new paternalism. Further study of how BLE applies to different consumer transactions is one possible course of action for the FTC.

C. The New Paternalism and Behavioral Unfairness Claims

In response to the new paternalism, some advocates will press the FTC to go beyond mere study and to bring unfairness actions based upon claims of behavioral exploitation.[194] As this Article has shown, however, any FTC action will take place against the backdrop of established unfairness jurisprudence—a body of law undergirded by the concept of consumer sovereignty, which reflects a historic political accommodation between the FTC and Congress. The remainder of this Article will use three concrete examples—mail-in consumer rebates, supermarket design to induce impulse purchasing, and payday lending—to illustrate the challenges that the FTC faces if the Commission is inclined to bring unfairness actions based on behavioral exploitation—what this Article will term behavioral unfairness claims (BUCs).

1. Behavioral Unfairness Claim Example #1: Consumer Rebates

Although consumer rebate usage has exploded during the past two decades,[195] if one believes press accounts, rebates are despised by

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191. Timothy Muris, *Principles for a Successful Competition Agency*, 72 U. CHI. L. REV. 165, 176 (2005).

192. Michael A. Salinger, Pauline M. Ippolito & Joel L. Schrag, *Economics at the FTC: Pharmaceutical Patents Dispute Settlements and Behavioral Economics*, 31 REV. INDUS. ORG. 85, 85 (2007). The mission of the FTC's Bureau of Economics is outlined at http://www.ftc.gov/be/about.shtm (last visited Apr. 24, 2008).

193. For more information, see http://www.ftc.gov/be/consumerbehavior/ (last visited Apr. 29, 2008). *See also* Salinger et al., *supra* note 192, at 98 (discussing the conference).

194. For the sake of brevity and focus, this Article only deals with the FTC's unfairness authority, though the FTC's prohibition on deceptive practices might also be fertile ground for the new paternalism. *See* Salinger et al., *supra* note 192, at 99–100.

195. *See* Edwards, *Consumer Rebates*, *supra* note 165, at 362–63 (noting that the total rebate offer volume now ranges from four to ten billion dollars per year and describing the important role rebates play in the high-end electronics industry).

U.S. consumers, who view them as a massive scam.[196] However, referring to rebates as a "scam" is misleading because it suggests that there is one problem with rebates, when in reality there are several different categories of consumer rebate complaints, each of which raises different issues. Some aggrieved consumers claim that rebate offerors delay or fail to pay legitimately earned rebate rewards and impose unnecessarily complicated rebate redemption requirements to discourage consumers from completing the rebate redemption process.[197] These complaints about the manner in which particular rebate promotions are managed do not necessarily lead to a view that rebates ought to be outlawed. One can complain about late rebate award payments or onerous redemption requirements while still holding the view that rebate programs could be beneficial for consumers in certain circumstances. Someone with this view might support legislation and regulation to compel rebate offerors to simplify onerous rebate redemption requirements and to promptly pay rebate awards,[198] as well as enforcement actions against rebate offerors who failed to pay consumer rebates within the promised period of time.[199]

This Article, in contrast, will only address the BUC that consumer rebates are inherently exploitive (regardless of how particular rebate programs are administered) and that consumer rebates ought to be considered unfair per se under § 5 of the Federal Trade Commission Act.[200] The basic behavioral argument asserts that consumers fail to redeem their rebates due to a confluence of emotional, psychological, or cognitive factors, even though this behavior does not maximize wealth or utility.[201]

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196. *See id.* at 363 (observing that "despite their popularity, few marketing practices have received as much negative press as rebates").

197. These complaints are examined in greater detail in Edwards, *Consumer Rebates*, *supra* note 165, at 363.

198. For a discussion of various types of state legislation on rebates, see *id.* at 396–98.

199. *See id.* at 399–400 (discussing various FTC enforcement actions against rebate offerors).

200. One might also press a per se unfairness claim against consumer rebates based upon the price discriminating effect of rebates. The argument proceeds as follows: Rebates facilitate price discrimination because rebates allow sellers to sell a good for two prices: the shelf price paid by consumers who do not participate in the rebate offer, and the after rebate strike price, paid by the consumers who do participate in the rebate offer. *See* Yuxin Chen, Sridhar Moorthy & Z. John Zhang, *Price Discrimination After the Purchase: Rebates As State-Dependent Discounts*, 51 MGMT. SCI. 1131, 1131 (2005); Chakravarthi Narasimhan, *A Price Discrimination Theory of Coupons*, 3 MARKETING SCI. 128 (1984) (discussing coupons as price-discrimination devices); *see also* Edwards, *Consumer Rebates*, *supra* note 165, at 376 n.63 ("[O]ne might argue that (1) it is inherently wrong to sell the same good to different consumers at different prices, or (2) the ability of a firm to price discriminate demonstrates that the firm possesses unlawful market power."); Alexei M. Marcoux, *Much Ado About Price Discrimination*, 9 J. MKTS. & MORALITY 57, 58 (2006) (arguing that price discrimination is not inherently unfair). These arguments, while interesting, do not necessarily involve behavioral exploitation, and thus will be bracketed here.

201. This behavioral law and economics of consumer rebates is covered in greater detail in Edwards, *Consumer Rebates*, *supra* note 165, at 376–95. The following treatment is

Rebate offerors, some claim, are not only aware of this suboptimal consumer behavior, but the very point of a rebate offering is to exploit these behavioral glitches, as Jeff Sovern explains:

> When consumers fail to obtain rebates, manufacturers retain the funds involved, making rebates particularly valuable to manufacturers, especially when compared to coupons or sales. Manufacturers apparently employ rebates chiefly because they increase sales by creating an illusion of a lower price, while the transaction costs generated by rebate offers permit manufacturers effectively to charge the unrebated price to most consumers.[202]

Therefore, from this perspective, rebates are "unfair" even when a rebate program is honestly and efficiently managed.[203] To fit this behavioral argument into existing law, however, a per se unfairness challenge to consumer rebates under § 5 of the FTC Act would need to establish that consumer rebates are likely to cause injury that is (1) substantial, (2) not outweighed by any offsetting consumer or competitive benefits that consumer rebates produce, and (3) not reasonably avoidable by consumers.[204] In the case of consumer rebates, all three of these elements require regulators to answer challenging empirical questions and to engage directly with the precepts of behavioral law and economics.

The first requirement in any unfairness action is that the challenged practice cause substantial consumer injury. But who suffers economic or monetary harm due to mail-in rebates? One obvious choice would be consumers who buy a product because of a rebate (rebate-dependent purchasers),[205] but then fail to redeem the rebate[206]—a phenomenon known

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merely used to illustrate the challenges that behavioral issues raise under FTC unfairness law.

202. Jeff Sovern, *Toward a New Model of Consumer Protection: The Problem of Inflated Transaction Costs*, 47 WM. & MARY L. REV. 1635, 1639 (2006) [hereinafter Sovern, *Transaction Costs*].

203. John G. Lynch, Jr. & Gal Zauberman, *When Do You Want It? Time, Decisions, and Public Policy*, 25 J. PUB. POL'Y & MKTG. 67, 71 (2006) ("Some people may believe that knowingly offering a rebate that a substantial percentage of consumers are unlikely to redeem (though they believe otherwise) is an unfair competitive practice. However, the FTC appears to operate under a definition of unfairness that makes this outcome unlikely . . . .").

204. To date, not a single judicial opinion has held that consumer rebates are per se unfair under § 5 of the FTC Act. Just as important, the FTC has never advocated this position (though some consumer rights advocates have gone so far as to suggest that all rebates should be paid at the point of purchase). Nevertheless, even though the concept of unfairness has not been extended in this manner, rebates provide an interesting test of the current FTC unfairness standard. This topic was addressed in Edwards, *Consumer Rebates*, *supra* note 165, at 403–06. The following treatment of this issue is an expansion and refinement of that discussion.

205. *See id.* at 367 (discussing categories of consumers in a rebate promotion).

206. *See* Sovern, *Transaction Costs*, *supra* note 202, at 1684 (concluding that those who intend to redeem but fail to do so "experience a distortion of their demand function").

as "breakage" in the marketing literature.[207] The harm caused by rebates would thus be evidenced by subsequent behavior (non-redemption) that is inconsistent with initial intentions (the desire to redeem at the time of purchase). The problem with defining the injury or harm in this way is that it ignores the fact that the non-redemption, though inconsistent with initial intentions, actually might be wealth-maximizing behavior, depending on the consumer's reservation price, the costs of redemption, and the size of the mail-in rebate. If a consumer's reservation price is met by the pre-rebate shelf price of an item, and redemption is costly (including opportunity costs) while the rebate is small, it would be difficult to say that a purchaser is "harmed" when she fails to redeem, even if this is contrary to her initial intentions. On the other hand, a consumer who intends to redeem and then follows through and indeed redeems her rebate might not consider herself to have suffered harm, but such a decision, though successful in a sense, might not be wealth-maximizing, depending on the costs of redemption and the size of the rebate. In other words, failing to follow through on one's intentions can either maximize utility or diminish utility, depending on the situation.[208] A more fruitful economic way to conceive of the harmed group would be to include those consumers who meet the following three conditions: (1) their reservation prices are not met by the pre-rebate shelf price; (2) they purchase a good because their reservation prices will be met if they redeem the rebate (taking into account the costs of redemption); and (3) they fail to redeem the rebate.[209] These are consumers who, in the final analysis, have paid more than their reservation price for a product. Unless their reservation prices were irrationally determined (which raises a host of other issues), such consumers plainly suffer an economic harm.

This leads, however, to two difficult empirical tasks under current unfairness law. First, we would need to establish, within the context of a particular rebate promotion, the size of this group of economically harmed consumers and the aggregate harm to the group. Second, a per se

207. *See* Edwards, *Consumer Rebates*, *supra* note 165, at 369–70 (elaborating on the concept of breakage).

208. A way around this conclusion is to say that the redeemer in that case enjoys non-pecuniary benefits from redeeming a rebate, such as the satisfaction brought about by the rebate redemption process. Thus, any consumer who is deprived of the pleasure of successfully redeeming a rebate suffers harm. The use of a non-economic measure for consumer harm, however, creates additional utility measurement and comparison problems.

209. Jeff Sovern argues that even successful redeemers incur transaction costs:

> Even consumers who obtain the rebate incur transaction costs that do not benefit society because they must comply with the requirements for the rebate. If the seller simply offered the product at a reduced price, consumers would not have had to fulfill any requirements to obtain the reduced price. Accordingly, the rebate comes at a dearer price than necessary.

Sovern, *Transaction Costs*, *supra* note 202, at 1685.

unfairness claim would require a showing that the economic harm caused by the consumer rebate promotion is not outweighed by the positive economic benefits that it generates. There are two main positive benefits generated by rebates. First, as with any mechanism for seller price discrimination, rebates allow sellers to offer a product at multiple price points, thus opening the market to those who cannot afford the product at the higher single, fixed price.[210] Second, sellers claim that they are able to collect valuable marketing information as part of the rebate reward requests.[211] The issue for regulators is how to determine which rebates are likely to generate sufficient benefits to outweigh the economic injuries to some consumers. Given that consumer reservation prices and redemption opportunity costs are not readily apparent to third parties, these are not simple tasks.[212]

Finally, the FTC Unfairness Policy, as incorporated into § 45(n), requires proof that the injury to consumers is not reasonably avoidable.[213] The Unfairness Policy Statement explicitly ties this element to the concept of consumer sovereignty:

> Normally we expect the marketplace to be self-correcting, and we rely on consumer choice—the ability of individual consumers to make their own private purchasing decisions without regulatory intervention—to govern the market. We anticipate that consumers will survey the available alternatives, choose those that are most desirable, and avoid those that are inadequate or unsatisfactory. However, it has long been recognized that certain types of sales techniques may prevent consumers from effectively making their own decisions, and that corrective action may then become necessary. Most of the Commission's unfairness matters are brought under these circumstances. They are brought, not to second-guess the wisdom of particular consumer decisions, but rather to halt some form of seller behavior that unreasonably creates or takes advantage of an obstacle to the free exercise of consumer decisionmaking.
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> Sellers may adopt a number of practices that unjustifiably hinder such free market decisions. Some may withhold or fail to generate critical

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210. *See* Matthew A. Edwards, *Price and Prejudice: The Case Against Consumer Equality in the Information Age*, 10 LEWIS & CLARK L. REV. 559, 562–70 (2006) (discussing economic price discrimination).

211. *See* Edwards, *Consumer Rebates*, *supra* note 165, at 372–73 (noting that a firm can learn how much consumers spend, which products are purchased together, and shopping patterns from rebates).

212. Presumably other scholars will have different opinions as to who is harmed by rebates; in any event, the discussion serves to show that the concept of consumer injury is not as straightforward in this context as one might presume. Fortunately, the FTC has a staff of expert economists who are far better trained to untangle these issues.

213. *See* FTC Unfairness Policy Statement, *supra* note 123.

> price or performance data, for example, leaving buyers with insufficient information for informed comparisons.[214]

Accordingly, while the Unfairness Policy assumes a self-correcting market based on consumer choice, the FTC will intervene in certain cases:

> Consumers ordinarily protect themselves by choosing among alternative products. For their decisions to be meaningful, however, they must be based on reasonably full and accurate knowledge of the alternatives. This process may be undermined in some instances if sellers either withhold or fail to generate certain material information about their products. When the benefits of providing such information exceed its costs, the Commission is empowered to act to ensure its availability.[215]

To continue with our example, what does it mean for an injury to be "reasonably avoidable" in the case of consumer rebates? By definition, some consumers do successfully redeem their rebates and thus avoid injury.[216] Other consumers decide to patronize sellers and manufacturers that offer regular low prices or instant incentives rather than delayed incentives, such as mail-in rebates. These consumers also avoid injury. But the key to behavioral exploitation (if we concede its existence) is that some consumers are not aware of their own potential future suboptimal or irrational behavior. One could argue that this group of consumers cannot reasonably avoid injury absent regulatory intervention of some sort. From this perspective, the statutory language requiring an injury that is "not reasonably avoidable by consumers themselves"[217] applies not to all consumers, but to those who suffer injurious behavioral or cognitive failings as a result of the challenged practice.[218] The FTC's reasoning in *International Harvester* supports this perspective: "Whether some consequence is 'reasonably avoidable' depends not just on whether people know the physical steps to take in order to prevent it, but also on whether

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214. *Id.* at 1074 (internal citation omitted).

215. Carol T. Crawford, *Unfairness and Deception at the FTC: Clarifying the Commission's Role and Rules*, 54 ANTITRUST L.J. 303, 308 (1985) (internal citations omitted).

216. The exact percentages are difficult to determine. For a discussion of rebate redemption rates, see Edwards, *Consumer Rebates*, *supra* note 165, at 367–69 (summarizing available data on rebate redemption rates, but cautioning that "reliable rebate redemption rates are difficult to obtain") (internal citation omitted).

217. 15 U.S.C. § 45(n) (2000).

218. *See* Edwards, *Consumer Rebates*, *supra* note 165, at 405 (suggesting that this approach could lead to the argument that even "an honestly and efficiently managed rebate promotion is unlawful" due to "behavioral economics," but acknowledging that "[r]egulators or courts might be skeptical of such a claim since many consumers do indeed redeem rebates and avoid the harm being addressed here"); Lynch & Zauberman, *supra* note 203, at 71–72 ("Consumers who follow the redemption protocol receive the benefit, and they might point out that those who do not could have easily avoided the financial loss. However, it is highly predictable that in the aggregate, consumers will have low redemption rates.") (internal citation omitted).

they understand the necessity of actually taking those steps."[219] In the case of rebates, the wealth-maximizing consumers who redeem or decline to redeem their rebates are not relevant; the focus ought to be on consumers who suffer economic injury due to their suboptimal redemption behavior.

2. Behavioral Unfairness Claim Example #2: Supermarket Impulse Buying

Impulse buying presents another thought-provoking issue for those interested in the regulation of behavioral exploitation. Observers contend that impulse buying is a significant marketplace phenomenon, perhaps accounting "for up to 80% of all purchases in certain product categories."[220] Robert Prentice notes:

> Impulse buying currently constitutes a substantial and growing segment of purchasing behavior, and "compulsive buying" (impulse buying to excess) is on the increase, affecting a substantial percentage of adults. Even items as large as cars and houses are often purchased impulsively. Impulse buying is scarcely rational and "has been linked to postpurchase financial problems, product disappointment, guilt feelings, and social disapproval."[221]

More specifically, the literature indicates that supermarkets use a variety of display and atmospheric tactics to increase impulse purchases or unplanned buying:

> Supermarket techniques for inducing greater consumer purchases, particularly impulse buying, are time-tested and varied. They include item placements, such as shelving milk at the back of the store and arranging soups out of alphabetical order, that force customers to come

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219. Int'l Harvester Co., 104 F.T.C. 949, 1066 (1984) (discussing safety hazards posed by gasoline-powered tractors) (internal citation omitted); *see also* Orkin Exterminating Co. v. FTC, 849 F.2d 1354, 1365 (11th Cir. 1988) (adopting the FTC's position that "'[c]onsumers may act to avoid injury before it occurs if they have reason to anticipate the impending harm and the means to avoid it, or they may seek to mitigate the damage afterward if they are aware of potential avenues toward that end'" (quoting Orkin Exterminating Co. v. FTC, 108 F.T.C. 341, 366 (1986))).

220. Jacqueline J. Kacen & Julie Anne Lee, *The Influence of Culture on Consumer Impulsive Buying Behavior*, 12 J. CONSUMER PSYCHOL. 163, 163 (2002) ("Impulsive consumer buying behavior is a widely recognized phenomenon in the United States . . . . [I]t has been suggested that purchases of new products result more from impulse purchasing than from prior planning."); *see also* Sharon E. Beatty & M. Elizabeth Ferrell, *Impulse Buying: Modeling Its Precursors*, 74 J. RETAILING 169, 169 (1998) (noting that "[i]mpulse buying is a pervasive aspect of consumers' behaviors"); Kathleen D. Vohs & Ronald J. Faber, *Spent Resources: Self-Regulatory Resource Availability Affects Impulse Buying*, 33 J. CONSUMER RES. 537 (2007) (discussing research on impulse buying); Kwon Jung & Clement Lim, *Impulse Buying Behaviors on the Internet* 1–2 (KDI Sch. of Pub. Pol'y & Mgmt., Working Paper No. 06-09, 2006), *available at* http://ssrn.com/abstract=953851 (reviewing literature on impulse buying).

221. Robert A. Prentice, *"Law &" Gratuitous Promises*, 2007 U. ILL. L. REV. 881, 922 (quoting Dennis W. Rook & Robert J. Fisher, *Normative Influences on Impulsive Buying Behavior*, 22 J. CONSUMER RES. 305, 306 (1995)) (internal citations omitted).

> across many products that are not on the customers' shopping lists. They also include putting impulse items like candy at the cash register (as well as judiciously interspersing sugarless gum and trail mix in order to avoid alienating health conscious parents). They extend even to designing aisle width and piping in music that market research has shown to increase customer purchasing.[222]

To borrow Jeff Sovern's terminology, in the case of consumer rebates, the firm is increasing transaction costs to consumers,[223] which unnecessarily imposes additional consumption costs. In the case of supermarket design, firms decrease the costs of consumption. Imagine an unfairness claim based upon this type of supermarket behavioral exploitation. Could a consumer who impulsively purchases a candy bar and a copy of a gossip magazine claim that he has suffered a cognizable injury under the FTC Act? Certainly many would have a visceral reaction that such a cause of action is absurd. In addition, the likelihood of regulatory action based on supermarket exploitation seems slim at best. Nevertheless, this example may help to tease out the boundaries of unfairness and illustrate some problems in defining behavioral exploitation.

With that caveat in mind, assume that a consumer named Ben buys a candy bar and a celebrity gossip magazine at a supermarket checkout counter, and that we can establish that he would not have done so but for the strategic placement of the products. If Ben always regrets such impulsive purchases, then there might be a distinction between what Ben wants and what he likes. The disutility created by Ben's action and the gap between wanting and liking might justify regulatory intervention against the supermarket's insidious shelving tactics:

> The core idea is simple: if there are separate systems for recording liking, expressing wanting, and for learning to want what the brain likes, then paternalism could be justified if the wanting system produces choices that are not later liked, *and* if a paternalistic correction produces

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222. Neil Weinstock Netanel, *Cyberspace 2.0*, 79 TEX. L. REV. 447, 476–77 (2000) (book review) (internal citation omitted); *see also* Robert G. Harris & Thomas M. Jorde, *Antitrust Market Definition: An Integrated Approach*, 72 CAL. L. REV. 1, 27 n.78 (1984) ("[M]any retail enterprises exploit human impulsiveness by . . . designing the arrangement of products in the store to increase the incidence of 'impulse buying.'"); Paula B. Mays, *Determining the Likelihood of Confusion in* Ex parte *Examination: A Trademark Examining Attorney's Perspective*, 89 J. PAT. & TRADEMARK OFF. SOC'Y 207, 211 (2007) ("[M]ost grocers arrange the store aisle to encourage impulse shopping. Candy is placed near the checkout counter along with shocking magazines with such covers as 'Movie Star has alien baby.' Cereal is placed strategically and colorfully displayed in order to attract attention and encourage on-the-spot purchases.").

223. *See* Sovern, *Transaction Costs*, *supra* note 202, at 1638–39 (arguing that "the transaction costs generated by rebate offers permit manufacturers effectively to charge the unrebated price to most consumers," because "instead of simply paying less for the item from the beginning, as would be true with a sale item, consumers must fill out a form, gather proofs of purchase, and send them to the manufacturer").

> choices that are unwanted by an agent but will be liked by her, *or* that are wanted but not liked, *and* if the correction does not cause other harms (or much harm to rational agents).[224]

But let us assume instead that Ben eats the candy bar and finds it to be delicious, and reads the magazine and delights in the stories of celebrity misfortune. A few weeks later, as Ben is recycling the magazine, he sees the candy bar wrapper (which he had used as a bookmark) and berates himself for his lack of self-control, which led him to gain weight and to spend valuable time reading gossip magazines instead of professional journals in his field. Fifty years later, as Ben is on his deathbed surrounded by his loving family, he reflects upon his life and concludes that he would not have changed a thing, even though he suffered from diabetes and never advanced a great deal professionally.

In this hypothetical, it is more challenging to evaluate the utility of Ben's action as we are faced with a "multiple selves" problem[225] because there are multiple Bens with varying preferences and desires that differ across time.[226] Because Ben continued to buy and enjoy candy bars and gossip magazines over the course of many years, what Ben learned (if anything) would not be evident and the difference between what he wanted and what he liked is fuzzy.[227] Calling for regulatory intervention on the basis that the

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224. *See* Camerer, *Wanting, Liking, and Learning*, *supra* note 11, at 91 n.11, 92 (citing Kent C. Berridge & Terry E. Robinson, *Parsing Reward*, 26 TRENDS IN NEUROSCIENCES 507, 510–12 (2003)); *see also* Kent C. Berridge, *Pleasure, Pain, Desire, and Dread: Hidden Core Processes of Emotion*, *in* WELL-BEING: THE FOUNDATIONS OF HEDONIC PSYCHOLOGY 525, 527 (Daniel Kahneman, Ed Diener & Norbert Schwarz eds., 1999) ("If an event was pleasant, it should be remembered as pleasant, expected to be pleasant, and desired again. But it appears that the three types of utility often diverge for outcomes in real life."). Put another way, Ben is experiencing a tension between his experienced utility and his decision utility. *See* Camerer, *Wanting, Liking, and Learning*, *supra* note 10, at 90 (noting four types of utility: "experienced utility (the hedonic sensation at the time of consumption that Jeremy Bentham had in mind); remembered utility; forecasted utility (a forecast of experienced utility); and finally, the familiar notion of decision utility (numbers an observer could use to rank an agent's revealed preferences)") (citing Kahneman et al., *supra* note 57, at 376–77; Daniel Kahneman, *New Challenges to the Rationality Assumption*, 150 J. INSTITUTIONAL & THEORETICAL ECON. 18, 21 (1994)).

225. *See generally* Richard A. Posner, *Are We One Self or Multiple Selves?: Implications for Law and Public Policy*, 3 LEGAL THEORY 23 (1997).

226. *See* Stephen M. Bainbridge, *Precommitment Strategies in Corporate Law: The Case of Dead Hand and No Hand Pills*, 29 J. CORP. L. 1, 5 (2003) ("The . . . phenomenon of multiple selves posits that individuals do not have a single utility function, but rather multiple competing utility functions. Because each self orders preferences differently, there is an ever-present risk that the self predominating at a given moment may make decisions not in the complete individual's best interest."); Korobkin & Ulen*, Rationality Assumption*, *supra* note 7, at 1123 ("Each individual, at any given point of time, might not be the unitary, coherent set of preference orderings imagined by rational choice theory. Rather, each individual may be viewed as a collection of competing preference orderings. If so, then there may be a collective action problem in aggregating the contemporaneous preferences of these multiple selves.").

227. Finally, we should note that even if a consumer is harmed by a form of behavioral exploitation, under current unfairness law the harm must be weighed against everyone who

shelving tactics harmed Ben would implicitly favor the guilty Ben, who regretted his consumption, over the impulse-buying Ben, who enjoyed his consumption, and the deathbed Ben, who had no regrets. But, as Glen Whitman explains, this preference cannot be assumed:

> To take the notion of multiple selves seriously, the analyst must consider both sets of interests or preferences. We should not simply assume that the long-run self's interests somehow supersede those of the short-run self . . . . Thus, adopting policies *solely* on grounds that they advance the interests of the long-run self would be inappropriate.[228]

Accordingly, in cases of conflict between a present self and future selves, regulators must articulate a principle to mediate conflict between multiple selves. Not only might it be hard to elaborate such a principle, but the notion of having regulators choose which of our different selves are making the right choices starts to look a lot like the bad old "hard paternalism" that the new paternalism seeks to avoid. This issue suggests that any unfairness action based upon behavioral exploitation is most likely to be successful where regulators can favor the preferences and desires of consumers' future selves without being forced to elaborate finely-tuned normative principles for evaluating consumption choices.

3. *Behavioral Unfairness Claim Example #3: Payday Loans*

The payday lending market provides another fertile area for exploring the intersection of BLE and the FTC unfairness doctrine.[229] Ronald Mann and Jim Hawkins explain the basics of payday loans as follows:

> In financial terms, the product is a very short-term, single-payment loan, in which the lender extends a loan on one date, in return for a promise (usually evidenced by a postdated check or by automated clearinghouse (ACH) authorization) to repay the amount of the loan plus a standard fee, typically in the range of $15 to $20 per $100 borrowed. Notably, the amount of the fee is usually fixed, without regard to the number of days that will elapse between the date of the loan and the fixed repayment date, which is normally the expected date of the borrower's next paycheck.[230]

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benefited from the practice. In the case of placement of certain goods at checkout and impulse purchases, the harm to consumers who make ill-advised purchases must be weighed against the benefits that convenient product placement makes for other consumers. *See* Camerer, *Wanting, Liking, Learning*, *supra* note 11, at 92 (qualifying the wanting-learning-liking framework's promotion of regulatory paternalism with the precondition that intervention "not cause other harms").

228. *See* Whitman, *supra* note 4, at 4.

229. A lucid, recent survey of the payday lending business can be found in Michael A. Stegman, *Payday Lending*, 21 J. ECON. PERSP. 169, 169–75 (2007).

230. Ronald J. Mann & Jim Hawkins, *Just Until Payday*, 54 UCLA L. REV. 855, 861–62 (2007) (internal citation omitted); *see also* Brian A. Glasser & Eric B. Snyder, *Payday Lending—The Litigation and Legislation That Regulate It*, 1 11TH ANNUAL CONSUMER

In recent years, a vigorous public policy debate has emerged about payday lending.[231] Although this Article will neither fully examine nor take sides in this debate, an understanding of the potential behavioral arguments against payday lending requires a brief summary of two issues that critics of payday loans emphasize: the identity of payday loan borrowers and the high cost of payday loans.

Critics argue that payday lenders target less affluent, elderly and unsophisticated consumers,[232] as well as military families[233] and racial

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FIN. SERV. LITIG. INST. 423, 427 (2006) ("A payday loan is a transaction where a consumer borrows against his or her next paycheck. Typically, the consumer provides a recent pay stub as well as a personal check for the loan amount, plus fees, dated for the next payday, when the loan comes due."); Steven M. Graves & Christopher L. Peterson, *Predatory Lending and the Military: The Law and Geography of "Payday" Loans in Military Towns*, 66 OH. ST. L.J. 653, 660 (2005) (defining payday loans as "high interest rate, rapidly compounding loans meant to tide over cash-short borrowers until their next paycheck").

231. One author sums it up:

> Critics argue that payday lenders target unsophisticated, cash strapped, and vulnerable people, charge outrageous and usurious fees, and often lead to a cycle of renewal that results in massive magnification of a relatively modest loan amount. Proponents counter that the industry provides a necessary and desirable financial service to a disenfranchised segment of the population ignored or underserved by mainstream banks, and that increased fees directly correspond only to the increased risks that arise from lending to borrowers with an unfavorable credit history.

Chad A. Cicconi, *A Role for Payday Lenders*, 123 BANKING L.J. 235, 235 (2006) (internal citation omitted); *see also* Michael Bertics, Note, *Fixing Payday Lending: The Potential of Greater Bank Involvement*, 9 N.C. BANKING INST. 133, 134 (2005) (arguing that "[t]he payday lending market is currently functioning at an equilibrium that is harmful to consumers," and that "the entry of banks into the payday lending market could solve this problem by enhancing the competitive market forces within the industry"); Charles A. Bruch, Comment, *Taking the Pay Out of Payday Loans: Putting an End to the Usurious and Unconscionable Interest Rates Charged by Payday Lenders*, 69 U. CIN. L. REV. 1257, 1259 (2001) (contending that "new federal legislation should be enacted to bring interest rates charged by payday lenders into conformance with traditional limits of usury and unconscionability"); Carmen M. Butler & Niloufar A. Park, *Mayday Payday: Can Corporate Social Responsibility Save Payday Lenders?*, 3 RUTGERS U. J.L. & URB. POL'Y 119 (2005); Creola Johnson, *Payday Loans: Shrewd Business or Predatory Lending?*, 87 MINN. L. REV. 1, 25–97 (2002) (surveying numerous deceptive and exploitive payday lending practices); Mann & Hawkins, *supra* note 230, at 857 ("The high interest rates that payday lenders charge have generated a flurry of critical proposals, ranging from calls to end payday lending altogether to proposals for additional disclosures by payday lenders."); Aimee A. Minnich, *Rational Regulation of Payday Lending*, 16 KAN. J.L. & PUB. POL'Y 84 (2006); ELIZABETH RENUART & KATHLEEN E. KEEST, THE COST OF CREDIT § 7.5.5, at 293 n.439 (3d ed. 2005).

232. *See* Pearl Chin, *Payday Loans: The Case for Federal Legislation*, 2004 U. ILL. L. REV. 723, 727 (characterizing typical payday borrowers as "vulnerable customers who do not have access to information or to credit alternatives that would allow comparison shopping"); Scott A. Hefner, *Payday Lending in North Carolina: Now You See It, Now You Don't*, 11 N.C. BANKING INST. 263, 267 (2007) ("The payday lending industry has been charged with targeting minorities, low-income earners, military personnel and the elderly.") (citing Press Release, Office of N.Y. State Att'y Gen., New York Sues to Stop Illegal Payday Lending Scheme (Sept. 24, 2003), http:// www.oag.state.ny.us/press/2003/sep/sep24a_03.html); Johnson, *supra* note 231, at 99 (concluding "that payday loan customers are primarily low-to-moderate income consumers who have personal checking accounts").

233. *See* Graves & Peterson, *supra* note 230, at 657–58. Government intervention took the form of a 36% interest rate cap on loans to military members. *See also* John Warner

minorities.[234] These criticisms have an ominous tone: vulnerable borrowers are not just consumers of credit—they are *targeted*; they are *prey* in a sinister economic hunt. Other commentators dispute the overbroad characterizations of payday borrowers as uneducated and poverty stricken.[235] Regardless of which side is correct,[236] it seems beyond dispute that "[m]ost payday loan customers are highly credit-constrained."[237]

In addition to focusing on the identity of payday loan borrowers, payday lending critics focus on the "high" cost of these loans, which is illustrated by converting payday loan fees into annual percentage rates.[238] One economist notes: "When the fee for a short-term payday loan is translated into an annual percentage rate (APR), the implied annual interest rate ranges between 400 and 1000 percent."[239] The likelihood that borrowers

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National Defense Authorization Act for Fiscal Year 2007, Pub. L. No. 109-364, 120 Stat. 2083 (to be codified at 10 U.S.C. § 987).

234. *See* Renuart & Keest, *supra* note 231, § 7.5.5.1, at 293 n.439 (citing Uriah King et al., *Race Matters: The Concentration of Payday Lenders in African American Neighborhoods in North Carolina*, Ctr. for Responsible Lending (2005), *available at* http://www.responsiblelending.org/pdfs/rr006-Race_Matters_Payday_in_NC-0305.pdf).

235. For reviews of the conflicting demographic data regarding payday borrowers, see Minnich, *supra* note 231, at 88. The controversial study at the heart of these discussions is Gregory Elliehausen & Edward C. Lawrence, CREDIT RESEARCH CTR., PAYDAY ADVANCE CREDIT IN AMERICA: AN ANALYSIS OF CUSTOMER DEMAND (2001), *available at* http://www.cfsa.net/downloads/analysis_customer_demand.pdf. *Cf.* Richard J. Thomas, Note, *Rolling over Borrowers: Preventing Excessive Refinancing and Other Necessary Changes in the Payday Loan Industry*, 48 WM. & MARY L. REV. 2401, 2403–07 (2007) (assessing the study's legitimacy in light of its alleged flaws, which include its sponsorship by one of the industry's trade associations, and a small sample size of clients who all borrowed at the same time of year).

236. One expert on payday lending states:

> Researchers have conducted several surveys of the characteristics of payday loan customers and their findings are broadly consistent. All payday loan customers have bank accounts, for this is what makes them eligible for the service. The vast majority is employed and has a household income between $15,000 and $60,000. The customers tend to be young adults; most are under forty years old. Most have children in the household. A strong majority has a high school education; about half have some higher education. Somewhat more than half are women. About half carry major credit cards.

John P. Caskey, *Fringe Banking and the Rise of Payday Lending*, *in* CREDIT MARKETS FOR THE POOR 17, 18–19 (2005).

237. Stegman, *supra* note 229, at 173.

238. I put "high" in quotation marks because I am not sure how to determine whether a price for something is high, though I suspect that I share the visceral reaction held by many people that these loans are high-cost.

239. Stegman, *supra* note 229, at 170; *see also* Caskey, *supra* note 236, at 18 ("Given the short maturity of the loans and the size of the finance charge relative to the size of the loan, the annual percentage rate on payday loans commonly falls between 350 and 1,000 percent."); Graves & Peterson, *supra* note 230, at 661 (average payday loan rates range from 364% to 550%); Renuart & Keest, *supra* note 231, at 295 (calculating the translation of payday loan fees "into annual percentage rates typically not less than 390% and averaging close to 500%, though advocates and credit code enforcement agencies have noted rates of 1300% to 7300%").

Though loans at these rates seem intuitively outrageous and hard to defend, some commentators argue that it is not fair to express payday loan fees in the form of annual will take out multiple loans within a short period of time or will "roll over" their loans, thus incurring additional fees, exacerbates this cost problem, according to critics.[240]

At this point, we can tell two very different behavioral-economic stories about payday loans: one that supports a BUC against payday lenders and one that does not. Both stories can be seen as a response to the following question: Why would someone choose a loan with a 500% APR?[241] Why would someone pay so much for credit? The first behavioral story blames cognitive limitations or emotional factors for preventing borrowers in the payday lending market from acting as rational, wealth-maximizing, credit-shopping consumers would act.[242] These borrowers, the story goes, fail to compare the costs of payday loans to the costs of other available sources of credit. One of the strongest behavioral arguments is that overoptimistic or overconfident[243] payday loan borrowers overestimate the likelihood that they will be able to pay back their payday loans when their next paychecks arrive, and that they underestimate the likelihood that they will extend, or

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percentage rates. *Compare* Mann & Hawkins, *supra* note 230, at 903–04 (noting that "studies suggest that requiring APR disclosures on payday loans is ineffective" and claiming that "[i]nterest-rate disclosures are misleading because the amount of the fee charged generally does not depend on the number of days until the borrower's payday"), *and* Thomas, *supra* note 235, at 2423 (arguing that "the small, short-term nature of the payday loan makes the APR seem more oppressive than it actually is"), *with* Lynn Drysdale & Kathleen E. Keest, *The Two-Tiered Consumer Financial Services Marketplace: The Fringe Banking System and Its Challenge to Current Thinking About the Role of Usury Laws in Today's Society*, 51 S.C. L. REV. 589, 603 (2000) (arguing that APRs enable consumers to comparison shop for credit), *and* Christopher L. Peterson, *Usury Law, Payday Loans, and Statutory Slight of Hand: Salience Distortion in American Credit Pricing Limits*, MINN. L. REV. (forthcoming 2008) (manuscript at 34–35, http://ssrn.com/abstract=1000041) (explaining why the use of the APR is appropriate for payday loans).

240. *See infra* notes 244–45 and accompanying text.

241. Or, if one believes that APRs are misleading in this context: Who would choose a $235, two-week loan with a $20 fee? Of course, in some cases, factors other than cost might come into play, such as the reputation of the lender, the level of customer service, and other contract terms, such as late payment penalties.

242. Mann and Hawkins explain:

> In sum, the best case against payday lending is that the market is plagued by cognitive failures, unlikely to be well policed by competitive forces, and likely to generate external costs borne by the rest of society. It is simply not plausible, the argument goes, that a person of ordinary capacity would sensibly decide to borrow money at a rate of 400 percent, using a loan that, in most cases, is likely to remain outstanding for months, if not years. In assessing the weight of this problem, it bears noting that those who will be harmed by the market failure are systematically likely to be far from the top of the distribution of income and wealth.

Mann & Hawkins, *supra* note 230, at 884; *see also id.* at 881 ("Like most consumer financial transactions, payday lending transactions tax the cognitive capabilities of the typical customer in ways that lead to market failures of one sort or another.").

243. *See* Edwards, *Consumer Rebates*, *supra* note 165, at 391–92 (suggesting that people fall prey to overconfidence when making predictions about their own abilities to produce desirable outcomes, or engaging in unfamiliar activities).

"roll over," their payday loans.[244] Such rollovers result in a longer loan term and considerably higher fees than borrowers initially anticipated.[245] One author colorfully observes: "The strongest critics say that payday loans are the credit market's equivalent of crack cocaine; a highly addictive source of easy money that hooks the unwary customer into a perpetual cycle of debt."[246] The implication is that borrowers' behavioral flaws allow payday lenders to price their loans far above what their actual risk dictates, which would not be possible in a perfectly competitive market.[247]

The second behavioral-economic story undermines a potential payday lending BUC. The basic story here is that those who are taking out payday loans are unable to obtain unsecured, short-term loans at a lower interest rate than that offered by payday lenders because they are poor or have bad credit.[248] Accordingly, these consumers, many of whom face an urgent

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244. The precise extent of payday loan rollovers is much debated. *See* Mann & Hawkins, *supra* note 230, at 864–65 (discussing competing evidence on this issue).

245. *See* Chin, *supra* note 232, at 729–30 (offering "examples of borrowers who found themselves buried under a mountain of debt because of multiple rollovers" and concluding that "[w]ith multiple rollovers generating the bulk of revenue for payday lenders, the industry has every incentive to keep its customers in a perpetual cycle of debt"); Drysdale & Keest, *supra* note 239, at 605 ("Much of the concern about short-term fringe lending arises over the question of whether it is, at best, a 'debt treadmill' or at worst, a downward spiral."); Aaron Huckstep, *Payday Lending: Do Outrageous Prices Necessarily Mean Outrageous Profits?*, 12 FORDHAM J. CORP. & FIN. L. 203, 207 (2007) ("Payday loan rollovers and renewals nearly always play a role in real-life examples of payday lending gone bad."); Mann & Hawkins, *supra* note 230, at 896 ("Many commentators—and a good number of legislators—operate on the assumption that proof that a substantial number of payday loan customers are frequent users self-evidently demonstrates the impropriety of the business.");

> [B]orrowers, who often find their funds insufficient the next month to cover both their normal expenses and repayment of the payday loan, are forced to refinance, or "roll over," the loan for an additional fee. This cycle may continue until the borrower has refinanced so many times that the total cost of the payday loan far exceeds any late fees or returned check charges that the borrower would have faced had she not taken the loan. This refinancing trap is the most serious consumer interest concern in payday lending.

Thomas, *supra* note 235, at 2409.

246. *See* Stegman, *supra* note 229, at 176.

247. *See* Richard Hynes & Eric A. Posner, *The Law and Economics of Consumer Finance*, 4 AM. L. & ECON. REV. 168, 170 (2002) ("In a perfectly competitive market the interest rate will reflect the time value of money, inflation, and the risk of default."); *see also* Matthew A. Edwards, *supra* note 69, at 205–06 (discussing the traits of an efficient credit market); Jinkook Lee & Jeanne M. Hogarth, *The Price of Money: Consumers' Understanding of APRs and Contract Interest Rates*, 18 J. PUB. POL'Y & MKTG. 66, 66 (1999) ("In a perfectly efficient financial market, the price of a loan is a function of its risk.").

248. *See* Gregory Elliehausen, *Consumers' Use of High-Price Credit Products: Do They Know What They Are Doing?* 20–22 (Networks Fin. Inst., Working Paper No. 2006-WP-02, 2006), *available at* http://ssrn.com/abstract=921909 ("Many high-price credit customers have characteristics that make qualifying for credit difficult.").

need of some sort,[249] are rationally choosing the best possible option from the menu of available credit choices in the so-called "fringe banking sector,"[250] which includes pawnbroker loans, refund anticipation loans, automobile title loans, rent-to-own transactions, and illegal loans from loan sharks.[251] The only other option that such borrowers have is to defer consumption, and while the price of payday loans may seem "high" to consumers with access to less expensive forms of credit, the interest rate and fees being charged accurately reflect the risk that lenders face in this market.[252] Thus, as Gregory Elliehausen concludes in a recent working paper: "The decision to use high-price credit typically is a result of the consumer's situation rather than a lack of knowledge or information."[253]

The FTC seems to be the ideal government actor to consider which payday lending behavioral-economic story appears more persuasive and whether behavioral anomalies are interfering with consumer choice process, leading consumers to choose more expensive forms of credit (without any economic basis), thus driving up the price of available credit above what lender risk ought to dictate.[254] To return to the existing unfairness framework discussed throughout this Article, the payday lending BUC would attempt to establish the following: (1) that payday loans cause a substantial injury to those consumers who pay more for credit than they otherwise would pay in a more efficient market—one with less suboptimal borrower behavior; (2) that paying higher prices for credit than they would pay in a more efficient market confers no net benefit on consumers; and (3) that those who suffer from cognitive or emotional failings cannot

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249. *Id*. at 29 ("Nearly two-thirds of payday loan customers obtained their most recent new advance (not renewal) because of an unexpected expense or shortfall in income. Only 11.9% used a payday loan for a planned expenditure.").

250. Drysdale & Keest, *supra* note 239, at 591 (referring to the subprime consumer credit market as the "'fringe banking' sector").

251. *See id.* (distinguishing the fringe banking sector from the "'prime' consumer credit market," comprised of "purchase money home mortgages and the secondary mortgage market, home equity loans, credit cards, automobile loans and leases that finance the American Dream for most of the middle- and upper-economic quintiles"); Elliehausen, *supra* note 248, at 2–9 (describing types of loans within the fringe banking sector).

252. This was the conclusion of the authors of an FDIC working paper. *See* Mark Flannery & Katherine Samolyk, *Payday Lending: Do the Costs Justify the Price?* 1, 21 (FDIC Ctr. Fin. Res., Working Paper No. 2005-09, 2005), *available at* http://papers.ssrn.com/sol3/papers.cfm? abstract_id=771624 (concluding that "[t]o a great extent, the 'high' APRs implied by payday loan fees can be justified by the fixed costs of keeping the stores open and the relatively high default losses suffered on these loans"); Huckstep, *supra* note 245, at 204 ("[D]espite the common belief, payday lending firms do not always make extraordinary profits.").

253. Elliehausen, *supra* note 248, at 34.

254. *See* Stegman, *supra* note 229, at 176 (counseling that "the preferred policy choices will vary according to whether payday loans are viewed as a tolerable high-cost form of emergency short-term credit, or whether they are viewed as a loan at triple-digit annual interest rates").

engage in sufficient or effective credit shopping to avoid this harm absent government intervention of some sort.[255]

The harm analysis in a payday lending BUC presents less empirical complexity than that of BUCs in other consumer contexts for two reasons. First, the credit market is a forum in which it is relatively safe to assume a consumer goal of wealth-maximization:[256] most people want to pay as little as they can for a loan. Second, consumer choices in the payday lending arena are unlikely to generate irreconcilable conflict between our present self and our future selves. All of our selves ought to want to obtain the lowest-priced credit available (although the initial decision to borrow to consume in the present might create a serious conflict between present and future selves). Thus, unlike the supermarket impulse-buying context discussed earlier, regulators investigating payday loans do not need to determine how to balance the competing interests of our multiple selves, thus eliminating one major objection to paternalistic governmental intervention.

Finally, one benefit of stating the behavioral issues that arise in payday lending in terms of the FTC's unfairness test is that it allows regulators and scholars to distinguish behavioral claims from other possible arguments against payday lending. Three such claims will be mentioned here to highlight the distinctiveness of the behavioral claim. First, the behavioral claim against payday loans is not based upon the notion that it is inherently immoral, unjust, or unethical for a lender to charge high prices for short-term credit. Even someone who has a great deal of faith in the concept of consumer sovereignty and is dubious about claims that prices are too high when consumers are able to pay these prices could accept the behavioral claim. Second, the behavioral claim is not a macro-economic claim that payday loans are bad for the economy as a whole or that they lead to deleterious effects, such as increased bankruptcies.[257] One can support the behavioral argument in its pure form even in the absence of such negative effects. Third, the behavioral claim can stand independent of arguments that payday lenders routinely violate existing usury, debt collection, and

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255. It is well beyond the scope of this Article to review possible solutions for payday lending abuses. The payday lending literature has many suggestions. *See, e.g.*, Mann & Hawkins, *supra* note 230, at 905–10 (proposing simplified payday loan disclosures and measures to encourage participation in the market by large and reputable lenders).

256. *See* Lee & Hogarth, *supra* note 247, at 66 (noting the difficulty of accounting for "price-quality trade-offs" when analyzing the pricing of other products does not exist in "the credit arena, in which the 'product' is money").

257. *See* Butler & Park, *supra* note 231, at 123 (detailing social costs of the payday lending business, including "bad credit ratings, lower savings rates, less home ownership, bankruptcies, an increase in the number of people depending on welfare, and the costs of preventing and deterring criminal behavior"); Mann & Hawkins, *supra* note 230, at 884 (discussing effects of individuals' financial distress on society as a whole).

mandatory disclosure laws.[258] Even payday lenders who adhere scrupulously to the existing consumer protection laws are open to the charge that consumers' behavioral shortcomings contribute to credit prices that are out of line with lender risk.[259] Accordingly, social critics or consumers' rights advocates might press moral or macroeconomic critiques against payday lending that are distinct from the behavioral claims discussed in this Article.

CONCLUSION

During the past decade, scholars associated with the burgeoning field of behavioral law and economics have attacked the precepts of rational choice theory, questioned the notion of consumer sovereignty, and called for various "soft" forms of paternalistic government intervention. Given its regulatory authority and economic expertise, the Federal Trade Commission is in an ideal position to consider how the new behavioral law and economics approach can most successfully influence the regulation of consumer markets. This Article has shown, however, that the FTC is likely to be reluctant to fully embrace the new paternalism due to the unique history of the Commission's unfairness authority. Over approximately the past twenty-five years, the legal standard of unfairness has moved from a concept of marketplace morality to an economic concept rooted in consumer sovereignty. This change, which reflects a political resolution to an institutionally damaging conflict between the FTC and Congress, has become a part of the Commission's DNA. Right or wrong, this deeply rooted ethos will not easily be shaken by the claims of the new paternalists. The FTC has fought this war before, so the teachings of BLE are unlikely to inspire a full reconsideration of the basic notion of consumer sovereignty.[260] It is far more likely that the Commission will use its formidable resources to study the impact of BLE in particular contexts. As

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258. *See* Johnson, *supra* note 231, at 25 (identifying "payday lending practices that deceive and exploit consumers by means that are quintessentially unfair to consumers and also often illegal"); Mann & Hawkins, *supra* note 230, at 866 (noting the possibility that "mom-and-pop" payday loan providers "operate under the radar in more or less chronic violation of applicable laws governing usury and debt collection"); *id.* at 870 (stating that fraud and illegal lending are also common in the Internet payday lending sector).

259. Although clearly, a failure to adhere to the Truth in Lending Act's mandatory disclosure provisions could exacerbate any cognitive or emotional impediments to effective comparison shopping for credit. *See* Butler & Park, *supra* note 231, at 123 (discussing how failure to disclose material payday loan terms impedes comparison shopping); Johnson, *supra* note 231, at 37–48 (discussing payday lender violations of the Truth in Lending Act).

260. In his comments on an earlier draft of this Article, Jeff Sovern noted that the issue seems to be a "burden of proof" question—how sure must the FTC be before it decides to regulate based upon BLE? I think that Sovern's observation hits a key issue on the head, and this Article has aimed to show that the FTC's institutional history of unfairness theory is likely to make the burden of proof steeper than an uninformed observer would guess. I leave it to others to determine whether this ought to be the case.

a recent paper co-authored by several FTC insiders noted: "The challenge is to find policy approaches that facilitate that learning, and discipline the worst abuses of consumer psychological limitations, without unduly limiting consumer choice and without imposing large costs on the taxpayer, on markets, or on consumers who are not subject to the foible."[261]

Nevertheless, some new paternalists will argue that the FTC ought to bring unfairness actions based on behavioral exploitation as a way of vindicating, rather than displacing, the FTC's consumer sovereignty norm. This Article has used the examples of consumer rebates, supermarket impulse buying, and payday loans to show the empirical challenges raised by such claims under current unfairness law. Courts and regulators that consider behavioral unfairness claims must both weigh the uncertain costs and benefits of complex marketplace phenomena and address what it means for a harm to be "reasonably avoidable" in cases of purported consumer irrationality. Moreover, behavioral unfairness claims that require a decisionmaker to mediate intertemporal "multiple selves" disputes face an additional layer of empirical and normative complexity. It may be, then, that unfairness claims will be most suitable for situations where we can safely assume a consumer goal of wealth-maximization, and where there is little empirical dispute over the disutility of a particular consumer choice. If such restrictions on behavioral unfairness actions fail to satisfy consumer rights advocates or devotees of the new paternalism, then the next course of action will be an asymmetrically paternalistic state or federal legislation. Given the FTC's unfairness history, the Commission is likely to be comfortable deferring to congressional policymaking based upon behavioral law and economics, rather than attempting rulemaking proceedings on its own, inspired by the new paternalism.

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261. *See* Salinger et al., *supra* note 192, at 103. Michael A. Salinger was the director of the Bureau of Economics (BE) from 2005–2007. *See also* Press Release, FTC, Economics Director Michael Salinger to Leave FTC: Michael P. Baye Named New Director of the Bureau of Economics (June 28, 2007), http://www.ftc.gov/opa/2007/06/bedirect.shtm. Pauline Ippolito is currently a deputy director at the BE; Diagram, FTC, Federal Trade Commission: Bureau of Economics, http://www.ftc.gov/be/be-org-chart.pdf. Joel L. Schrag is an economist at the BE; FTC, Bureau of Economics, Conference on Behavioral Economics and Consumer Policy: Participant Biographies, http://www.ftc.gov/be/consumerbehavior/docs/bios.pdf. Of course, the paper bears the usual caveat that the "views expressed . . . do not necessarily reflect those of the Federal Trade Commission or any individual Commissioner."