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## Debiasing Advertising: Balancing Risk, Hope, and Social Welfare

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## DEBIASING ADVERTISING: BALANCING RISK, HOPE, AND SOCIAL WELFARE

*David Adam Friedman\**

### ABSTRACT

*This article explores the nuances of “debiasing through law,” a regulatory approach proposed by Christine Jolls and Cass Sunstein. Proponents have described advertising regulation as a form of debiasing through law. Debiasing approaches regulation through less paternalistic means using strategies that improve consumer decision making. Proponents believe that the improved decision making will gracefully lead to better choices. These debiasing strategies find some of their roots in addressing human cognitive biases and bounded rationality.*

*Although debiasing through law purports to offer an attractive alternative to pure paternalism, this Article demonstrates that the net social welfare effects of this approach can prove difficult to anticipate. An examination of the recent tightening of the regulation of consumer endorsements in advertising illuminates the challenges and nuances of the debiasing approach.*

*This Article attempts to answer a myriad of questions. Does removing the consumer endorsement tool from the marketing arsenal ensure that consumers will make better decisions? The*

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\* B.A., J.D., Yale University. Assistant Professor of Law, Willamette University. Thank you to Michael Abramowicz, Laura Appleman, Richard Birke, Caroline Davidson, Brannon Denning, Chris Jay Hoofnagle, Kristin Madison, Nancy Rapoport, Spencer Weber Waller, and Norman Williams for offering their time to give helpful guidance. Thank you also to the workshop participants at the Cumberland School of Law for comments and insights. The author expresses special gratitude to Christine Jolls for helpful suggestions.

*truthful consumer endorsement can offer other consumers legitimate hope. When netted out, does taking “hope” off the market advance social welfare? Can regulators remove true information from the marketplace and expect to foster an improvement in social welfare? Can regulators preserve real choice while simultaneously improving decisions? Are regulators truly capable of harnessing cognitive and social science to engage in this sort of precision welfare engineering? Consumer-endorsement regulation presents a live proxy for the analytical dissection of debiasing through law.*

*Some scholars have expressed a keen skepticism toward this approach to regulation and toward the whole of behavioral law and economics. This Article presents a cautionary tale about the unpredictability of the net outcomes from deploying debiasing through law.*

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## INTRODUCTION

Jared Fogle not only stumbled across a fantastic way to lose weight, but he also had impeccable timing. The advocate for using Subway sandwiches as a delicious vehicle for weight loss managed to get discovered and signed to a promotional deal in 1997—over a decade before the Federal Trade Commission (FTC) tightened its guidance on “consumer endorsements.”<sup>1</sup> Jared offered a powerful narrative to consumers about his experience consuming Subway products.<sup>2</sup> Even though Jared Fogle’s experience may have been freakish, consumers received the message that at the outer boundary, consumption of Subway products could produce extraordinary weight-loss results.

The FTC’s 2009 revisions to the regulation of consumer endorsements, however, would have smothered in the cradle the welfare-yielding transactions that ultimately resulted from the Jared campaign. Reacting to the strong, psychologically persuasive pull of true information transmitted from a peer,<sup>3</sup> the FTC literally

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<sup>1</sup> See *Nightline: Jared’s Revenge, Eat Fresh Empire* (ABC television broadcast Aug. 14, 2009) (transcript available at 2009 WLNR 15859461) [hereinafter *Jared’s Revenge*]. See also Guides Concerning the Use of Endorsements and Testimonials in Advertising, 16 C.F.R. § 255.2 (2009); *FTC Publishes Final Guides Governing Endorsements, Testimonials*, FEDERAL TRADE COMMISSION (Oct. 5, 2009), <http://www.ftc.gov/opa/2009/10/endortest.shtm>.

<sup>2</sup> See *Advertising and Consumer Protection: Hearing Before the Subcomm. on Consumer Prot., Prod. Safety, & Ins. of the S. Comm. on Commerce, Sci. & Transp.*, 111th Cong. (2009), available at 2009 WLNR 13979468 (statement of Sally Greenberg, Exec. Dir., National Consumers League) [hereinafter *Greenberg Statement*]; *Jared’s Revenge*, *supra* note 1.

<sup>3</sup> See *FTC Requests Public Comments on Endorsement Guides*, FEDERAL TRADE COMMISSION (Jan. 16, 2007), <http://www.ftc.gov/opa/2007/01/fyi0707.shtm> (seeking comment about two empirical studies performed by marketing professors about the implicitly cognitive impact of endorsements on consumers). See also MANOJ HASTAK & MICHAEL B. MAZIS, *THE EFFECT OF CONSUMER TESTIMONIALS AND DISCLOSURES ON AD COMMUNICATION FOR A DIETARY SUPPLEMENT* (Sept. 30, 2003), available at <http://www.ftc.gov/reports/endorsements/study1/report.pdf> [hereinafter HASTAK & MAZIS, *DIETARY SUPPLEMENTS*]; MANOJ HASTAK & MICHAEL B. MAZIS, *EFFECTS OF CONSUMER*

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warns advertisers choosing to use consumer endorsements to prepare for litigation. Specifically, the FTC counsels advertisers to generate and retain empirical data proving that their consumer-endorsement advertisements are non-deceptive. The FTC recommends this practice in order to avoid the initiation of an FTC action.<sup>4</sup> Had Jared Fogle achieved his Subway weight-loss feat today, Subway would have had substantially more risks to weigh in employing his endorsement. Had the threat of FTC action prevented this advertising campaign, Jared and Subway would have suffered welfare losses, but so would consumers who might have benefited from the message.<sup>5</sup>

The revision of the FTC consumer-endorsement guide illustrates some of the complexities of evaluating this particular application of behavioral law and economics in regulation, or as Christine Jolls and Cass Sunstein have deemed it, “debiasing through law.”<sup>6</sup> Debiasing through law purports to bring attractive features to the regulatory arena, achieving welfare-enhancing outcomes without paternalism. The debiasing approach involves influencing human decision making up-front and at the source, and enabling people to make better choices and presumably to enjoy better outcomes.<sup>7</sup> Debiasing proponents wish to avoid the

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TESTIMONIALS IN WEIGHT LOSS, DIETARY SUPPLEMENT AND BUSINESS OPPORTUNITY ADVERTISEMENTS (Sep. 22, 2004), *available at* <http://www.ftc.gov/reports/endorsements/study2/report.pdf> [hereinafter HASTAK & MAZIS, WEIGHT LOSS].

<sup>4</sup> See Guides Concerning the Use of Endorsements and Testimonials in Advertising, 16 C.F.R. § 255.2 (2009).

<sup>5</sup> See *infra* Part III.

<sup>6</sup> Christine Jolls and Cass Sunstein coined this phrase. See generally Christine Jolls & Cass Sunstein, *Debiasing Through Law*, 35 J. LEGAL STUDIES 199 (2006).

<sup>7</sup> This Article will use the “debiasing through law” term formalized by Jolls and Sunstein, as the descriptive term and the associated scholarship provide an elegant and straightforward framework for evaluating the recent regulatory approach taken by the FTC with respect to consumer endorsements. In kind, consumer-endorsement regulation can help inform a broader understanding of debiasing through law. Note that the developing scholarship around this area continues to grow, right along with the broader behavioral economics literature, albeit with different labels. Sunstein and Thaler have also described this regulatory approach as “libertarian paternalism,” selling the notion that

“paternalistic” approach of removing actual choice from the marketplace, while changing the environment to promote improved decision making.<sup>8</sup>

A regulatory approach this delicate and dramatic, hinging on inexact or controversial behavioral science, invites scrutiny.<sup>9</sup> Some

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benevolent interventions can guide people toward making better autonomous decisions that will presumably lead to better outcomes. They have described libertarian paternalism as a “relatively weak, soft, and non-intrusive type of paternalism because choices are not blocked off, fenced off, or significantly burdened.” CASS R. SUNSTEIN & RICHARD H. THALER, *NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH, AND HAPPINESS* 5 (2008) [hereinafter SUNSTEIN & THALER, *NUDGE*]. See generally Cass R. Sunstein & Richard H. Thaler, *Libertarian Paternalism is Not an Oxymoron*, 70 U. CHI. L. REV. 1159 (2003) [hereinafter Thaler & Sunstein, *Not an Oxymoron*]; Richard H. Thaler & Cass R. Sunstein, *Libertarian Paternalism*, 93 AM. ECON. REV. 175 (2003) [hereinafter Thaler & Sunstein, *Libertarian Paternalism*]. Others have laid out the similar concept of “asymmetric” paternalism, dangling it with an ideological spin.

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.

Colin Camerer, Samuel Issachoroff, George Loewenstein, Ted O’Donoghue & Matthew Rabin, *Regulation for Conservatives: Behavioral Economics and the Case for “Asymmetric Paternalism,”* 151 U. PENN. L. REV. 1211, 1212 (2003). Finally, and perhaps most notoriously, Sunstein and Thaler packaged the concept for a broader audience as “nudging.”

A nudge . . . is any aspect of the choice architecture [manipulation of surroundings] that alters people’s behavior in a predictable way without forbidding any options or significantly changing their economic incentives. To count as a mere nudge, the intervention must be easy and cheap to avoid. Nudges are not mandates. [In the context of improving food choices in a cafeteria,] [p]utting the fruit at eye level counts as a nudge. Banning junk food does not. [A ban would be a mandate].

SUNSTEIN & THALER, *NUDGE*, *supra*.

<sup>8</sup> See generally Jolls & Sunstein, *supra* note 6.

<sup>9</sup> Indeed, Jolls and Sunstein anticipate and acknowledge some of this criticism. See *id.* at 226 (acknowledging some of the work of Jeffrey Rachlinski and Robert Rasmussen). See Jeffrey Rachlinski, *The Uncertain Psychological Case for Paternalism*, 97 NW. U. L. REV. 1165, 1206–19 (2003); Robert K Rasmussen, *Behavioral Economics, the Economic Analysis of Bankruptcy Law*,

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scholars have expressed a keen skepticism toward this approach to regulation and toward the whole of behavioral law and economics.<sup>10</sup> This Article presents a cautionary tale about the

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*and the Pricing of Credit*, 51 VAND. L. REV. 1679, 1697–98 (1998).

<sup>10</sup> The debate about the nature and existence of the endowment effect provides but one scholarly battleground in the behavioral law and economics debate. For two robust studies that challenged the well-established status quo, sparking a debate, see generally Charles R. Plott & Kathryn Zeiler, *The Willingness to Pay/Willingness to Accept Gap, the Endowment Effect, Subject Misconceptions and Experimental Procedures for Eliciting Valuations*, 95 AM. ECON. REV. 530 (2004) [hereinafter Plott & Zeiler, *The Willingness Gap*] (employing new experimental tactics, which undermined key assumptions behind the endowment effect) and Charles R. Plott & Kathryn Zeiler, *Exchange Asymmetries Incorrectly Interpreted as Evidence of Endowment Effect Theory and Prospect Theory?*, 97 AM. ECON. REV. 1449 (2007) [hereinafter Plott & Zeiler, *Exchange Asymmetries*] (conjecturing that asymmetries in exchange can be explained through preference theory). Stephen M. Bainbridge urged regulatory caution in the wake of Plott and Zeiler's 2004 findings, which posited that the endowment effect fails to explain the gap between willingness to pay and willingness to accept: "The regulator ought to be confident that (a) the endowment effect is really present; (b) as a result of the endowment effect, an inefficient outcome is proving sticky; (c) that market experience cannot remove the anomaly; and (d) there is a superior regulatory solution." Joshua Wright, *The Endowment Effect's Disappearing Act*, IDEOBLOG (Dec. 24, 2005, 01:53 AM), [http://busmovie.typepad.com/ideoblog/2005/12/the\\_endowment\\_e.html](http://busmovie.typepad.com/ideoblog/2005/12/the_endowment_e.html) (quoting Stephen M. Bainbridge) (Bainbridge's original post to which Wright links is unavailable). For a representative and compelling exchange invoking this counter to the established perspective on the endowment effect see John Carney, *How the Trendiest Economists Got Their Prized Discovery Terribly Wrong*, BUSINESS INSIDER CLUSTERSTOCK (Oct. 5, 2009, 08:58 AM), <http://www.businessinsider.com/john-carney-how-the-trendiest-economists-got-their-prized-discovery-terribly-wrong-2009-10>; Larry E. Ribstein, *The Regulatory Risks of Behavioral Finance*, IDEOBLOG (Oct. 5, 2009, 09:14 AM), <http://busmovie.typepad.com/ideoblog/2009/10/the-regulatory-risks-of-behavioral-finance.html>; Josh Wright, *What's Wrong with the Endowment Effect?*, TRUTH ON THE MARKET (Oct. 6, 2009, 01:22 PM), <http://www.truthonthemarket.com/2009/10/06/whats-wrong-with-the-endowment-effect>; Gordon Smith, *What's Wrong with the "Endowment Effect"?*, THE CONGLOMERATE (Oct. 6, 2009), <http://www.theconglomerate.org/2009/10/whats-wrong-with-the-endowment-effect.html>; Stephen M. Bainbridge, *Mandatory Disclosure and Securities Regulation: A Behavioral Analysis*, PROFESSORBAINBRIDGE.COM (Jan. 29, 2010, 11:00 AM), <http://www.professorbainbridge.com/professorbainbridgecom/2010/01/mandatory-disclosure-and-securities-regulation-a-behavioral-analysis.html>.

unpredictability of the net outcomes from debiasing, using as a vehicle the anticipated effectiveness and potential unintended consequences resulting from the new FTC guide.

Additionally, Jolls and Sunstein posit with specificity that advertising regulation presents an actual pre-existing example of debiasing through law.<sup>11</sup> Advertising regulation usually focuses on purifying or supplementing the flow of information that advertisers use to influence consumer decision making.<sup>12</sup> Though Jolls and Sunstein argue that debiasing through law appears less intrusive and paternalistic,<sup>13</sup> this Article argues that upon closer examination through the lens of a specific form of advertising regulation, the net effects of debiasing can prove difficult to anticipate. Examining the new consumer-endorsement approach in detail can help illuminate the strengths and weaknesses of the claims embodied by Jolls and Sunstein. Are regulators truly capable of this sort of precision welfare engineering? Can regulators preserve real choice while simultaneously improving decisions? Consumer-endorsement regulation presents a live example of debiasing in action.

Although the new approach to consumer endorsements may alter decision making and protect some consumers from entering into social-welfare-destroying transactions, this Article notes that this approach may cause consumers to forgo welfare-creating opportunities as well. Removing true information from the decision-making realm can lead to failed transactions and perhaps other welfare-reducing market distortions.

Moreover, in many scenarios, the consumer endorsement

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<sup>11</sup> Jolls & Sunstein, *supra* note 6, at 216.

<sup>12</sup> See Deborah K. Owen & Joyce E. Plyler, *The Role of Empirical Evidence in the Federal Regulation of Advertising*, 10 J. PUB. POL. & MARKETING 1, 1 (1991) (“The [FTC] is charged with preventing false, unfair, and deceptive advertising . . . . [T]wo . . . questions must be answered . . . [W]hat messages does the advertisement communicate to consumers? . . . [A]re any of these messages materially false or misleading?”). Advertising regulation monitors and polices commercial information as aggregated into “messages.” See generally Richard Craswell, *The Identification of Unfair Acts and Practices by the Federal Trade Commission*, 1981 WISC. L. REV. 107, 108–09 (1981).

<sup>13</sup> See Jolls & Sunstein, *supra* note 6, at 200–03.

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actually comprises part of the substance of the actual offering. The truthful consumer endorsement can offer legitimate hope to the recipient—it presents the upper boundary of an expected range of outcomes from a transaction. When netted out, does “taking hope off the market” advance consumer welfare? Does removing a lonely person’s hope that a dating service might bring them down the course toward marriage advance consumer welfare? Does removing hope that eating healthier sandwiches will induce weight-loss advance consumer welfare?

Sometimes consumers contract for hope and are willing to accept disappointment. They expect to purchase a set of probabilities. This construct might apply to dining at unfamiliar restaurants, buying a new lawnmower, or buying an article of clothing. This might also apply to trying a new diet system, a gym membership, an acne-treatment cream, or a dating service. Consumers may indeed expect an offering to be imperfect or to perform below the highest level, but the information that the offering worked well for someone like them gives them the impetus to try it. As long as that hope is based on a realistic range of expectations, what is inherently wrong with offering that range of expectations?

Ultimately, advocates of debiasing still must wrestle with a core normative problem. What constitutes “good” decision making? What constitutes a “good” outcome? Debiasing through law generally emphasizes promoting the former with a more casual emphasis on the latter. Nonetheless, as the consumer endorsement circumstance demonstrates, in order to answer either question, a view must be formed about the presentation of risk—and the promotion of risk. One person’s risk is another person’s hope, aspiration, or thrill. Debiasing still leaves policymakers with another intrusive, paternalistic judgment call to make.

Part I of this Article describes the overall premise of debiasing through law, including its roots in behavioral law and economics. Then, Part I describes how debiasing works in theory and practice, using a comparison of product-safety regulation to advertising regulation. Focusing further on the underpinnings of advertising regulation, the Article explores the relationship between debiasing and regulatory control over the flow of commercial information to

consumers. Operating within the sphere of advertising regulation, Part II uses the case study of consumer endorsements to illustrate and evaluate this attempt to debias through law. Here, the Article discusses several cognitive biases potentially exploited by consumer endorsements and evaluates how the regulatory changes address them. Part III explores the potential downside to the new regulation, specifically, a reduction in social welfare due to various market distortions, including transactions that fail due to insufficient information and disruptions in pricing. This part also raises a normative question unsolved by debiasing through law—the degree to which risk should be present in the marketplace. Part IV prescribes a recommendation to policymakers that use debiasing techniques, suggesting that debiasing should be applied narrowly to certain markets because sweeping approaches tend to have more unanticipated potential pockets of downside. The Article concludes by reinforcing the notion that regulatory intervention in human decision making can yield positive results, but that the venues for deploying debiasing tactics should be carefully selected.

## I. THE PREMISE OF DEBIASING THROUGH LAW

An understanding of the premise of debiasing through law requires a short description of behavioral law and economics because that is where debiasing finds its roots. Pure law and economics assumes that actors will behave rationally and respond predictably to incentives. Any errors that actors make in judgment will, according to the law and economics adherents, balance out in the aggregate and in the long run.<sup>14</sup> Behavioral law and economics emphasizes that human beings are not disposed to behave rationally at all times and in all situations—human rationality is bounded.<sup>15</sup> Delimiting those bounds can generate controversy,

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<sup>14</sup> This has been described as the “rational expectations hypothesis.” See John F. Muth, *Rational Expectations and the Theory of Price Movements*, 29 *ECONOMETRICA* 315, 316–17 (1961).

<sup>15</sup> Economist, policymaker, and controversial former Harvard University President Larry Summers once prefaced an unpublished article attacking the efficient-market and rational expectations hypothesis with the words, “THERE

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particularly when policymakers attempt to incorporate and correct notions of bounded rationality.<sup>16</sup>

People make certain judgment and perception errors consistently and in the same direction. These non-random errors do not “balance out” in the long run. Those who advocate for a debiasing approach suggest that regulators can address these biases and improve human decision making, however defined.

Much of the current regulatory apparatus attempts to ameliorate the *outcomes* that result from bounded rationality, presuming that core human behavior proves highly resistant to external efforts to change it.<sup>17</sup> Most of these traditional regulatory attempts to change behavior aim to “insulate” people from making injurious choices by restricting the choices available for them to make.<sup>18</sup> The new debiasing-through-law approach presumes the

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ARE IDIOTS. Look around.” Ryan Lizza, *Inside the Crisis: Larry Summers and the White House Economic Team*, THE NEW YORKER, Oct. 12, 2009, at 80, available at [http://www.newyorker.com/reporting/2009/10/12/091012fa\\_fact\\_lizza](http://www.newyorker.com/reporting/2009/10/12/091012fa_fact_lizza). Summers was not asserting frustrations with a world less rational than he; he was describing the natural cognitive limitations of all economic actors and decision makers. For more robust and general views of bounded rationality, see generally Christine Jolls, Cass Sunstein & Richard Thaler, *A Behavioral Approach to Law and Economics*, 50 STAN. L. REV. 1471 (1998); Russell Korobkin & Thomas Ulen, *Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics*, 88 CAL. L. REV. 1051 (2000); FRANCESCO PARISI & VERNON SMITH, *THE LAW AND ECONOMICS OF IRRATIONAL BEHAVIOR* (2004).

<sup>16</sup> For example, well-established research supporting the existence of the endowment effect, which predicts that people are reluctant to trade what they already have for an item of equivalent value, has come under some fire. See *supra* note 11. The endowment effect, the initial identification of which largely has been attributed to Richard Thaler, has been a firmament in behavioral law and economics since the early 1980s. See generally Richard Thaler, *Toward a Positive Theory of Consumer Choice*, 1 J. ECON. BEHAV. & ORG. 39 (1980) [hereinafter Thaler, *Toward a Positive Theory*]. See *infra* Part II for a more detailed description of the endowment effect, its implications for the Coase Theorem, and the research that casts doubt on both its existence and the explanation for its existence. See also Plott & Zeiler, *The Willingness Gap*, *supra* note 10; Plott & Zeiler, *Exchange Asymmetries*, *supra* note 10.

<sup>17</sup> Jolls & Sunstein, *supra* note 6, at 200.

<sup>18</sup> *Id.*; Jeffrey Rachlinski, *The Uncertain Psychological Case for Paternalism*, 97 NW. U. L. REV. 1165, 1168 (2003).

persistence of a slew of irrational human-behavioral quirks and modifies rules to accommodate or address these quirks.

Recently, applied behavioral law and economics has aspired to alter the behavior of actors without the harsh paternalism of removing people's ultimate choices from the realm.<sup>19</sup> The new emphasis of behavioral law and economics puts greater weight on improving the quality of individual decision making rather than on mitigating potential bad outcomes resulting from poor choices.<sup>20</sup> The core of the premise rests on the notion that if cognitive psychology affords regulators with knowledge of the consistent cognitive biases of human beings, regulators can counter, de-program, or even leverage these biases.<sup>21</sup> If policymakers know what heuristics or shortcuts people use to make decisions and how these heuristics can lead to error, they can generate awareness of these systematic errors, or counteract them, and improve decision making. Policymakers could employ regulatory tools to neutralize the decision-making "quirk" rather than dictate the outcome.<sup>22</sup>

This Article analyzes a debiasing effort in the advertising regulation realm and assesses the effectiveness of that effort to enable extrapolation of some potential general lessons. This analysis requires an up-front foundational explanation of the mechanics of debiasing through law.

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<sup>19</sup> SUNSTEIN & THALER, *NUDGE*, *supra* note 7, at 4–14.

<sup>20</sup> *See generally id.*; Jolls & Sunstein, *supra* note 6, at 200; Jolls, Sunstein & Thaler, *supra* note 15; Daniel McFadden, *Free Markets and Fettered Consumers*, 96 AM. ECON. REV. 5 (2006).

<sup>21</sup> Much of the cognitive psychology and behavioral economics research into the endowment effect has been performed in human laboratory experiments. For a survey of this research and an overview of the broader reaction to it, see Christopher Curran, *The Endowment Effect*, in 1 BIBLIOGRAPHY OF LAW AND ECONOMICS 819, 819–21 (Boudewijn Bouckaert & Gerrit De Geest eds., 2000). Though the results of the experiments should not be dismissed wholesale, the artificiality and errors of this setting should inject some caution into those who might rely upon them for assessing the effects of policy or tweaking policy.

<sup>22</sup> *See* Jolls & Sunstein, *supra* note 6, at 200–01. *See generally* Camerer et al., *supra* note 7; Sunstein & Thaler, *Not an Oxymoron*, *supra* note 7; Thaler & Sunstein, *Libertarian Paternalism*, *supra* note 7; SUNSTEIN & THALER, *NUDGE*, *supra* note 7.

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*A. One Key Challenge of Debiasing: The Endowment Effect*

A full understanding of the cognitive forces at work in transactional decision making requires exposure to some brief foundational background about the endowment effect. The endowment effect describes a phenomenon where people tend to overvalue wealth or objects with which they are initially endowed. Advertising attempts to induce transactions and the endowment effect may present a force that the advertiser must counter through persuasive tactics. The true power and nature of the endowment effect remains unsettled to some, which concededly complicates the transactional decision equation, but only to a degree.<sup>23</sup>

This section describes the endowment effect debate with the caveat that a bounded understanding of the cognitive biases should perhaps make regulators a bit more cautious when attempting to neutralize or leverage them to improve human decision making.<sup>24</sup> Setting this foundation facilitates exploration of the mechanics of debiasing through law, as applied to product-safety regulation, advertising regulation, and more broadly, control over the flow of information.

The endowment effect may drive an observed behavior where people tend to value something that they own at a higher mark than an equivalent item offered in exchange.<sup>25</sup> This puts a drag on the tendency to exchange or trade. There may be a biological or evolutionary explanation for this phenomenon left over from an epoch when it was considerably more risky to give something up than to retain it.<sup>26</sup> This prehistoric explanation has competed with a

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<sup>23</sup> With or without the weight of an endowment effect, advertisers must and still do tap into long-recognized cognitive biases to induce transactions.

<sup>24</sup> See Stephen M. Bainbridge, *Mandatory Disclosure: A Behavioral Analysis*, 68 U. CIN. L. REV. 1023, 1056 (2000) [hereinafter, Bainbridge, *Mandatory Disclosure*]. Regulators may be prone to the same biases and cognitive errors as those they regulate and protect.

<sup>25</sup> See Thaler, *Toward a Positive Theory*, *supra* note 16. See generally Daniel Kahneman, Jack L. Knetsch & Richard H. Thaler, *Anomalies: The Endowment Effect, Loss Aversion and the Status Quo Bias*, 5 J. ECON. PERSP. 193, 197–99 (1991).

<sup>26</sup> Sarah F. Brosnan & Owen D. Jones, *Law, Biology, and Property: A New Theory of the Endowment Effect*, 49 WM. & MARY L. REV. 1935, 1956–61

purely economic explanation—actors in transactions are more reluctant to part with what they have if they perceive that there is counterparty risk.<sup>27</sup>

The knotty problem of the endowment effect, if not explained away by counterparty risk, presents a basic illustration of conflict between law and economics and behavioral law and economics.<sup>28</sup> For example, the Coase Theorem is premised on the notion that initial allocation of property rights is irrelevant for ultimate efficient allocation of property, and that the sole friction that would prevent this ultimate state from materializing results from transaction costs.<sup>29</sup> If the National Football League allocated tickets to the Superbowl through a random lottery, the Coase Theorem would predict that the recipients of the tickets would trade them to people who had a stronger natural preference to attend the game. Small-scale social experiments have indicated that this would *not* be the likely result. The lottery winners would be much more likely to use the ticket and attend the game because of the endowment effect.<sup>30</sup> Recent research<sup>31</sup> and conjecture have put the significance of that result in doubt, which presents some challenges and urges *some* caution for making policy from this social science.<sup>32</sup>

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(2008). For a brief discussion of the evolutionary background behind decision making, see McFadden, *supra* note 20, at 7–8.

<sup>27</sup> That is, the risk of the other party not fulfilling the commitment. See Carney, *supra* note 10; Wright, *supra* note 10; Smith, *supra* note 10.

<sup>28</sup> Though this Article does not have a mission to litigate the issue, the existence and impact of the endowment effect has been strongly called into question. See, e.g., Plott & Zeiler, *The Willingness Gap*, *supra* note 10; Plott & Zeiler, *Exchange Asymmetries*, *supra* note 10.

<sup>29</sup> Ronald H. Coase, *The Problem of Social Cost*, 3 J. LAW & ECON. 1 (1960).

<sup>30</sup> Daniel Kahneman, Jack L. Knetsch & Richard H. Thaler, *Experimental Tests of the Endowment Effect and the Coase Theorem*, 98 J. POL. ECON. 1325, 1344–45 (1990). Also note, the “status quo” bias may also intersect here. The status quo bias would also support the behavioral attitude to desiring to keep what one already has. Kahneman, Knetsch & Thaler, *supra* note 25, at 197–99.

<sup>31</sup> See, e.g., Plott & Zeiler, *The Willingness Gap*, *supra* note 10; Plott & Zeiler, *Exchange Asymmetries*, *supra* note 10.

<sup>32</sup> See *supra* note 27 and accompanying text (discussing counterparty risk).

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The degree of acceptance of the legitimacy of the endowment effect can be critical to understanding debiasing through law, because marketing and advertising purpose themselves to address it. Marketing and advertising attempt to induce a purchase: to induce consumers to part with wealth in exchange for an offering.<sup>33</sup> If one anticipates a vital endowment effect,<sup>34</sup> one can understand marketers' need and purpose for massive doses of persuasive advertising.<sup>35</sup> In order to drive transactions, marketers must use advertising to enhance the perceived value of an offering,<sup>36</sup> an offering presumably presented at a competitive market price. Some offerings may require more persuasion than others to sell at a viable price for producers, when the brand or offering might be unfamiliar or appear risky to try.

Essentially, marketers and regulators (presumably acting on the behalf of consumers) engage in a tug-of-war over which psychological tactics constitute "fair game" in the inducement of a transaction.<sup>37</sup>

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*See also* David Dunning, George Loewenstein & Leaf Van Boven, *Egocentric Empathy Gaps between Owners and Buyers: Misperceptions of the Endowment Effect*, 79 J. OF PERSONALITY & SOC. PSYCHOL. 66, 73–75 (2000) (raising a new notion that empathy gaps between transactors may drive the endowment effect gap and that this gap may not be easily addressable through debiasing that employs empathetic efforts).

<sup>33</sup> Marketing and advertising aim to move the consumer to part with a dollar to buy a can of soda, but also a specific brand of cola.

<sup>34</sup> And also related prospect theory. *See infra* note 176.

<sup>35</sup> The three leading advertising spenders in the United States in 2009 were companies managing established brands. Procter & Gamble Co. spent \$4.2 billion, Verizon Communications spent \$3.0 billion, and AT&T spent \$2.8 billion. *Marketer Trees: 2010, Database of 100 Leading National Advertisers*, AD AGE (Jun. 21, 2010), <http://adage.com/marketertrees2010/>.

<sup>36</sup> And reduce perceived risks related to the transaction.

<sup>37</sup> Necessarily factoring into this tug-of-war, the First Amendment also restricts regulation of commercial speech. The current doctrine is largely drawn off the line of cases evolving from *Central Hudson Gas & Electric Corp. v. Public Service Commission*, 447 U.S. 557 (1980).

*B. The Mechanics of Debiasing*

The techniques that advertisers use to counteract the endowment effect (or simply to persuade) often rely upon leveraging the optimism bias, the availability heuristic, the framing effect, and a host of other cognitive quirks that they can tap.<sup>38</sup> Advertising regulation purports to make this contest fair, however defined.<sup>39</sup> Though false information certainly cannot be conveyed as part of advertising, misleading information can be trickier to identify and may present the more challenging regulatory dilemmas. Regulators must balance the need to promote conveyance of information and the free flow of welfare-producing transactions against notions of fairness—no small challenge.

Debiasing through law purports to offer a subtle solution. The debiasing premise would dictate that policymakers not ban outright certain types of advertising, which would effectively have the *hard* (as opposed to *soft*) paternalistic<sup>40</sup> result of effectively removing choice from consumers. Certain products may only sell well using certain techniques. This may be for the better or the worse, but if advertising techniques for certain products are eliminated, choice through product availability may diminish, if not completely, almost so.

Debiasing proponents would argue for counter-programming campaigns of sorts that would foster improved consumer decision making about the purchase. As Jolls and Sunstein note:

[T]he law of deceptive advertising is thus a form of debiasing through substantive law; like our proposed approach here, it adopts a middle ground between inaction

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<sup>38</sup> Presumably, they are drawing upon both formal and informal understandings of human cognitive biases. See *infra* Part II for descriptions and illustrations of these cognitive quirks.

<sup>39</sup> Section 5 of the FTC Act “prohibits *unfair* or deceptive acts or practices.” Federal Trade Commission Act, 15 U.S.C.A. § 45(a) (West 2010) (emphasis added). See Craswell, *supra* note 12 for a comprehensive exploration of the conceptual and practical challenges of defining “unfairness.”

<sup>40</sup> See generally Thaddeus Mason Pope, *Counting the Dragon’s Teeth and Claws: The Definition of Hard Paternalism*, 20 GA. ST. U. L. REV. 659, 660–62 (2004) (distinguishing hard paternalism from soft paternalism).

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or naïve informational strategies on one hand, and . . . strategies of heightened liability standards or outright bans, on the other. Of course, the law of deceptive advertising concerns limits on affirmative statements (advertisements) firms choose to undertake, while [debiasing through law] concerns requirements that firms affirmatively provide information in particular ways; but in both cases the underlying attempt is to use law to reduce the severity of consumer error.<sup>41</sup>

Debiasing aims to strike a balance by generating improved consumer decisions in an arena where consumers are bombarded by marketers with both discrete bits and vivid narrative presentations of commercial information.

*1. The Product-Safety Analogy*

Product-safety law provides a stark illustration of the stakes that those who would use debiasing through law for advertising are trying to address, and a helpful bridge to analyzing commercial advertising regulation. Both product-safety regulation and advertising regulation try to control information and product availability while maximizing consumer choice and minimizing consumer risk or danger.<sup>42</sup> Product-safety law may provide some clues about why the FTC may have come up short in their goals with the new regulations for consumer endorsements, when both are viewed through the approach of debiasing through law.<sup>43</sup> (Conversely, an examination of consumer endorsements may ultimately inform a better understanding of debiasing through law.)

With product safety, regulators attempt to inform consumers of the risks of product danger in a manner that overcomes the natural optimism bias.<sup>44</sup> However, a few complications emerge that prevent an enabling of an accurate risk assessment by the consumer:

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<sup>41</sup> Jolls & Sunstein, *supra* note 6, at 216.

<sup>42</sup> In sum, these regulations optimize consumer welfare.

<sup>43</sup> See Jolls & Sunstein, *supra* note 6, at 207.

<sup>44</sup> See *infra* Part II.C.1 for additional discussion of the optimism bias.

Various commentators . . . have emphasized [that] optimism bias may lead many consumers to underestimate their personal risks even if they receive accurate information about average risks—a problem that may arise whenever the key piece of information to be disclosed to individuals is a probability estimate (such as the risk of harm from a product) rather than a certain outcome.<sup>45</sup>

Given these consumer proclivities, what can product-safety regulators do? The options product-safety regulators can consider start with a total *a-paternalistic* (or libertarian / caveat emptor) approach, putting the product on the market and allowing consumers to learn about the product's safety attributes purely through word-of-mouth or direct experience.<sup>46</sup> That is, an absence of regulation that requires no disclosure and no tweaking of the product to make it safer, which would require torts-driven private assessments of risk management.<sup>47</sup> Leaving the calculations entirely to private actors could be costly—and much of our product-safety regimen maintains well-established social and regulatory roots that reflect the notion that the tort system alone cannot promote a desired aggregate level of safety and that prevention of actual harm through regulatory mandates may be required.<sup>48</sup>

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<sup>45</sup> Jolls & Sunstein, *supra* note 6, at 207.

<sup>46</sup> In reality, this option does not often exist. Automobile manufacturers, for example, must achieve certain safety thresholds to let their products go to market. Above that minimum standard lies a zone for consumers to trade off price, features, and safety. See Howard Beales, Richard Craswell & Steven C. Salop, *The Efficient Regulation of Consumer Regulation*, 24 J. L. & ECON. 491, 492–93 (1981).

<sup>47</sup> Note that in the absence of regulation, tort law would predict that producers would seek the proper mixture of disclosure, enhanced safety, and acceptable risk. There is a vast literature on product liability law (and associated law and economics) that this Article recognizes but does not have adequate room to address.

<sup>48</sup> For an historic call to action to prevent consumer injury, see generally RALPH NADER, UNSAFE AT ANY SPEED: THE DESIGNED-IN DANGERS OF THE AMERICAN AUTOMOBILE (1965). For an overview of government intervention to promote food and drug safety, see generally PHILIP J. HILTS, PROTECTING AMERICA'S HEALTH: THE FDA, BUSINESS AND ONE HUNDRED YEARS OF

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The next approach on the spectrum could be categorized as “weak-form” debiasing. This approach would be the provision of raw statistical risk information to the consumer, while leaving the product on the market. Under most circumstances, this approach proves somewhat ineffective because consumers make “systemic mistakes in the assessment of probabilities.”<sup>49</sup>

Advocates of the “strong-form” (or the standard) debiasing approach would posit that making available a “concrete instance of the occurrence”<sup>50</sup> would be most effective, while not intrusive, nor completely hands-off.<sup>51</sup> A “truthful narrative[] of harm [would provide] a more modest and measured approach to optimism bias” than approaches that might be more paternalistic or “over-the-top” in their messaging to consumers.<sup>52</sup> These techniques are guided toward improving decision making unobtrusively without the heavy hand of removing choice from the market. Choice generally, and choice to transact, has an inherent value<sup>53</sup> and should not be casually eliminated by regulators if people can consider the choice in a properly informed manner.<sup>54</sup> Long before Milton Friedman

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REGULATION (2004).

<sup>49</sup> Jolls & Sunstein, *supra* note 6, at 210.

<sup>50</sup> *I.e.*, “[I]n the consumer safety context the law might require that *the real life story* of an accident or injury be printed in large type and displayed prominently . . . .” *Id.* at 213 (emphasis added). For example, presenting “truthful narratives of harm.” *Id.* at 215. Presentation of so-called worst-case scenarios can cause consumers to either unduly overreact or simply tune out. *Id.* at 214–15.

<sup>51</sup> *See id.* at 210.

<sup>52</sup> *Id.* at 215. An aggressive approach might be exemplified by the well-known ad where an egg was displayed, with the narrator proclaiming, “This is your brain,” and then after the egg hits a hot frying pan, continuing, “This is your brain on drugs.” Shaila K. Dewan, *The New Public Service Ad: Just Say “Deal with It,”* N.Y. TIMES, Jan. 11, 2004.

<sup>53</sup> For a survey about perceived value of choice, see Sheena S. Iyengar & Mark R. Lepper, *Rethinking the Value of Choice: A Cultural Perspective on Intrinsic Motivation*, 76 J. PERSONALITY & SOC. PSYCHOL. 349, 349–50 (1999).

<sup>54</sup> With product safety, choice can be eliminated by a direct mandate to remove the product from the market entirely, raising disclosure requirements to a level where consumers will almost universally reject the offer (effectively removing choice), or raising safety features to an unreasonably protective level that makes the offering cost-prohibitive (again, effectively removing choice).

and Rose Friedman put the phrase “Free to Choose” into the popular lexicon,<sup>55</sup> Thomas Jefferson noted, “[f]reedom is the right to choose: the right to create for oneself the alternatives of choice. Without the possibility of choice, and the exercise of choice, a man is not a man but a member, an instrument, a thing.”<sup>56</sup> In the consumer-transaction context, freedom can be expressed even through the bountiful variety found in a grocery cart.<sup>57</sup>

Moving along the paternalism spectrum, using product safety as the baseline illustration, regulators can employ “insulating” strategies, which begin to slide toward “hard” paternalism and removal of ultimate choice for the consumer.<sup>58</sup> These strategies aim to protect the consumer from defects by elevating safety standards to burdensome levels. The costs of the insulated product can cause potential transactions to fail because risk has been almost entirely stripped from the offering. This paternalistic approach assumes that consumers should not be permitted to trade off price or other features for risk. The example *reductio ad absurdum* would be if regulators required automobiles to be designed to prevent *all* fatalities, rendering them too expensive for everyday use. Individuals would be prevented from making the “un-insulated,” “risky,” “dangerous” choice of purchasing and owning a car, but would lose the freedom to choose a precious means of transportation.<sup>59</sup>

At the far end of the spectrum, the ultimate strategy that would

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See Jolls & Sunstein, *supra* note 6, at 207–08.

<sup>55</sup> See generally MILTON FRIEDMAN & ROSE D. FRIEDMAN, *FREE TO CHOOSE: A PERSONAL STATEMENT* (1980).

<sup>56</sup> Iyengar & Lepper, *supra* note 53, at 349. This quote has also been attributed to modernist American poet and Librarian of Congress, Archibald MacLeish. See, e.g., DEREK HUMPHRY, *LAWFUL EXIT: THE LIMITS OF FREEDOM FOR HELP IN DYING* 8 (1993); FRANK OBERLE, *FINDING HOME: A WAR CHILD’S JOURNEY TO PEACE* 275 (2004).

<sup>57</sup> But see generally BARRY SCHWARTZ, *THE PARADOX OF CHOICE: WHY MORE IS LESS* (2005) (concluding that an excess of choice can generate unhappiness for the chooser).

<sup>58</sup> Jolls & Sunstein, *supra* note 6, at 207–08.

<sup>59</sup> For a rich discussion of the inevitable tragedies of cost-benefit analysis in a resource-constrained environment, see generally PHILIP BOBBIT & GUIDO CALABRESI, *TRAGIC CHOICES* (1978).

truly eliminate risk exposure for the consumer would be an outright ban of an offering. This ultimate paternalistic approach eliminates all choice for the consumer. It fails to improve consumer transactional decision making and it leaves absolutely no room for absorbing *any* level of acceptable risk.<sup>60</sup>

## 2. *Product Safety Compared with Advertising Regulation*

Product-safety regulation provides a crisp illustration of the regulatory approaches available for protecting consumers—ranging from zero regulatory protection, to enhancement of decision-making through debiasing through law, to reducing choice through insulation from outcomes, to eliminating choice completely. As noted previously, advertising regulation can be treated as a form of debiasing through law. At the very least, advertising regulation provides a unique testing ground for debiasing through law.

Chilling consumer endorsements (or effectively eliminating them), certainly reflects an effort to enhance regulation, to control more tightly the flow of information from the marketer to the consumer.<sup>61</sup> At first glance, a crackdown on consumer endorsements resembles an effort to control information to enhance consumer decision making. It does not resemble an insulation strategy, as the offerings endorsed are not required to change, nor are offerings outright banned. One could look at this effort as a soft, non-intrusive (but still softly paternalistic) means of improving the considerations people mix into decisions to transact—a classic example of debiasing through law.<sup>62</sup>

A second look, one which this Article will explore in greater detail, reveals that a crackdown on consumer endorsements—effectively regulating commercial information flow by removing *true* information from that flow—can certainly have the power to

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<sup>60</sup> See generally Jolls & Sunstein, *supra* note 6, at 207–08.

<sup>61</sup> The changes in consumer-endorsement regulation will be explored in significant detail *infra* Part II.

<sup>62</sup> For better or worse, by removing a tool from the marketer's arsenal, regulators have made it incrementally more difficult for marketers to counter the influence of the endowment effect on consumers.

“improve” the quality of consumer decision making, but can also have other possible side effects that might prove less desirable when considering total social welfare.

For example, there are some products or services that present an arguably “acceptable” amount of consumer risk. As will be discussed, occasionally a consumer endorsement is *designed* to induce the consumer to take a calculated risk, and sometimes the product or service offering is focused around risk *per se*. If regulation of a marketing practice is too heavy-handed and the practice becomes too risky to employ, the practice may disappear entirely. If the practice disappears entirely, certain types of offerings dependent on the practice will disappear. This might increase social welfare with certain transactions<sup>63</sup> and it might subtract with others.<sup>64</sup> If advertising regulation *is* debiasing through law, advertising-regulation initiatives should be closely scrutinized to see if debiasing actually works as intended by proponents.<sup>65</sup>

### *C. Debiasing, Advertising, and Information Flow*

Regulators are concerned with preventing “bad,” social-welfare-destroying transactions from reaching completion. Note that “bad” transactions present themselves affirmatively. Injuries, failed results, and complaints resulting from disappointed

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<sup>63</sup> The FTC’s commissioned studies on the weight-loss industry may demonstrate that the effective elimination of consumer endorsements in that industry, and the subsequent disappearance of the offering, might enhance consumer welfare. HASTAK & MAZIS, *WEIGHT LOSS*, *supra* note 3; HASTAK & MAZIS, *DIETARY SUPPLEMENTS*, *supra* note 3.

<sup>64</sup> The Subway sandwich campaign discussed at length, *infra* Part II, may provide an example of where effectively eliminating consumer endorsements might reduce consumer welfare. On-line dating services that use married couples who met through their service may provide another illustration. The Article later suggests a middle ground where the FTC, instead of leveling a blanket threat, addresses industry-specific behavior under the broader enforcement powers of Section 5 of the FTC Act, or similarly through the Food and Drug Administration.

<sup>65</sup> And again, vice-versa—advertising regulation can inform the broader picture of debiasing, just as the breastfeeding advertising campaign did.

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expectations are tangible to regulators.<sup>66</sup> Therefore, regulators often try to address what they can easily see,<sup>67</sup> or tackle problems related to something dramatically unpleasant that recently happened.<sup>68</sup>

For example, by tightening down on consumer endorsements, the FTC attempted to purify the information flow from producers to consumers in order to create a transactional environment where consumers become less prone to acting on misperceptions and erroneous extrapolations from true individual consumer experiences. As the Article explains, this novel debiasing approach—an approach that involves using information and presentation to improve decision making—can yield imperfect results, illustrations of which are available. The new consumer-endorsement regulations attempt to improve decision making with a seemingly benign design.<sup>69</sup> But the welfare impact of the change

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<sup>66</sup> This applies across the regulatory board. The Food and Drug Administration's drug approval process has at certain junctures been regarded as too cautious. See Robert Pear, *Faster Approval of AIDS Drugs Is Urged*, N.Y. TIMES, Aug. 16, 1990, at B12. The modern process can trace some of its legacy to the thalidomide tragedy in the 1950s. See FRIEDMAN & FRIEDMAN, *supra* note 55, at 202–05; see also generally, Linda Bren, *Frances Oldham Kelsey: FDA Medical Reviewer Leaves Her Mark on History*, 35 FDA CONSUMER MAG., Mar.–Apr. 2001, available at [http://permanent.access.gpo.gov/lps1609/www.fda.gov/fdac/features/2001/201\\_kelsey.html](http://permanent.access.gpo.gov/lps1609/www.fda.gov/fdac/features/2001/201_kelsey.html). Approving a dangerous drug is visible. Libertarians have argued that the social costs of over-caution in drug approval can be less visible, but that over-caution may be just as socially expensive. FRIEDMAN & FRIEDMAN, *supra* note 55, at 204–10; Gary S. Becker, *Get the FDA Out of the Way and Prices Will Drop*, BUSINESSWEEK, Sept. 16, 2002, available at [http://www.businessweek.com/magazine/content/02\\_37/b3799028.htm](http://www.businessweek.com/magazine/content/02_37/b3799028.htm).

<sup>67</sup> See, e.g., Omnipresent advertisements for “free credit reports” that confused consumers resulted in FTC Action. Free Annual File Disclosures Rule: Final Rule and Statement of Basis and Purpose Amending the Rule To Prevent Deceptive Marketing of Free Credit Reports, Pursuant to Section 205 of the Credit Card Accountability Responsibility and Disclosure Act of 2009, 16 C.F.R. § 610 (2010).

<sup>68</sup> See, e.g., Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. 111-203, 124 Stat. 1376 (2010), passed in part “to protect consumers from abusive financial services practices . . .” that revealed themselves in the years just prior to passage of the legislation. *Id.*

<sup>69</sup> *FTC Publishes Final Guides Governing Endorsements, Testimonials*,

may be ambiguous and uneven across markets. From a normative perspective, these regulations may turn out to be more rigidly paternalistic than intended. They may indeed remove choice from the marketplace, more than regulators might anticipate.<sup>70</sup> These results can inform a broader understanding of debiasing through law.

Voluntary transactions in the marketplace generate positive social welfare, net of any externalities, because the assumption is that the parties would not have entered into the trade if each were not put in a better position. The assumption is that the trade represents the best available option for each party to improve its position and that the end result will prove to be Pareto optimal.<sup>71</sup>

Welfare economics finds that regulatory action is justified only when a specific market imperfection is evident and when the benefit from correcting that market imperfection exceeds the cost of properly regulating the market. If a market imperfection is not apparent, or if the benefits of correcting that imperfection are small, then intervention risks causing more harm than good to social welfare.<sup>72</sup>

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*supra* note 1. “Under the revised Guides, advertisements that feature a consumer and convey his or her experience with a product or service as typical when that is not the case will be required to clearly disclose the results that consumers can generally expect.” *Id.* On the surface, this sounds like a means of facilitating commerce fairly, but as this paper explores, more implications must be considered.

<sup>70</sup> For example, if regulators provide consumers with information about the risks of eating chocolate, if the information is too alarming, chocolate will cease to be a real choice. Regulators can scare decision makers away from a choice that then renders the choice extinct, even for others who would choose it in spite of exposure to and true absorption of the information. Other distortions can happen from removing information from the marketplace. For example, if regulators forbid price-based advertising, total prices may rise, which may reduce choice and welfare. *See infra* Part III.

<sup>71</sup> “[A] policy change is socially desirable [and meets the Pareto criterion] if, by the change, everyone can be made better off, or at least some are made better off, while no one is made worse off.” RICHARD E. JUST, DARRELL L. HUETH & ANDREW SCHMITZ, *THE WELFARE ECONOMICS OF PUBLIC POLICY* 14 (2004).

<sup>72</sup> J. Gregory Sidak, *A Consumer-Welfare Approach to Network Neutrality Regulation of the Internet*, 2 *J. COMPETITION, L. & ECON.* 349, 366–67 (2006).

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Debiasing through law describes a type of regulatory intervention, a means of correcting imperfections. Engaging in this type of intervention requires an understanding of the underlying nature of the regulated transactions.

Debiasing should disrupt or improve “bad” transactions. A “bad” transaction can be rooted in contracting norms as well as welfare economics.<sup>73</sup> “Bad” transactions often result from “bad” information polluting the transaction environment, distorting expectations about what will be exchanged.<sup>74</sup> A “bad” transaction could also arise from scenarios where the parties, *ex-ante*, err (or engage in deceit, mild or aggressive) in their valuation of what they are surrendering or receiving.<sup>75</sup>

These *ex-ante* errors are significant because the law of contract is notoriously reluctant to undo or revisit transactions that are merely unbalanced or one-sided. Generally, a party must show that there is something seriously deficient with the process of the formation of the transaction for the agreement to be undone. The defenses of duress,<sup>76</sup> undue influence,<sup>77</sup> and unconscionability,<sup>78</sup> for example, all require inquiries into the transaction process in order for a party to succeed.<sup>79</sup>

For the purposes of this Article, “bad” transactions can be translated into welfare terms. When Party X makes a decision based on a distorted perception from information proffered by Party Y, and the distorted decision devalues transactional outcome for Party X, Party X obviously loses welfare. That creates a social concern. If Party Y is the counterparty and creator of misperception in this exchange, and Party Y gains more in welfare than Party X loses, this exchange might enhance welfare in a one-

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*See, e.g.*, MICHAEL KATZ & HARVEY ROSEN, MICROECONOMICS 398–99 (3d ed. 1998).

<sup>73</sup> *See* Beales et al., *supra* note 46, at 505–06.

<sup>74</sup> *Id.*

<sup>75</sup> *Id.*

<sup>76</sup> RESTATEMENT (SECOND) OF CONTRACTS §§ 175–176 (1981).

<sup>77</sup> *Id.* § 177.

<sup>78</sup> *Id.* § 208 cmt. b.

<sup>79</sup> Improper threats, the exercise of dominion over a party, and “defects” in the bargaining process are threaded throughout these defenses.

round game. But in a multiple round game, the destruction of trust will cast a pall over future transactions, ultimately reducing welfare, as fewer welfare-creating transactions and exchanges will likely result.<sup>80</sup> Regulation of advertising should attempt to maximize social welfare with fairness as the constraint.<sup>81</sup> Over-regulating advertising might have the same welfare-reducing effects as the open permission of bad transactions, if information proves insufficient for consumers to engage heartily in social-welfare-yielding transactions.

### *1. Advertising Regulation and Debiasing*

Before entering the narrower problem of consumer-endorsement regulation, taking a step back to consider advertising regulation more broadly can provide context. Advertising regulation, as embodied in the Federal Trade Commission Act<sup>82</sup> (and “baby” FTC Acts at the state level),<sup>83</sup> focuses broadly on unfair or deceptive practices that generate transactions through the inducement of *ex-ante* errors on the part of the consumer.<sup>84</sup> Presumably, an atmosphere of deception promoted by an advertiser would lead to a “bad” transaction—a failure to yield net instant or long-run social welfare, an unjust redistribution of surplus to the advertiser from the consumer, or perhaps, all of the above.

Regulators often focus concern on transactions that are induced

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<sup>80</sup> See generally George A. Akerlof, *The Market for ‘Lemons’: Quality Uncertainty and the Market Mechanism*, 84 Q. J. ECON 488 (1970).

<sup>81</sup> See generally Craswell, *supra* note 12.

<sup>82</sup> Federal Trade Commission Act, 15 U.S.C.A. §§ 41–58 (West 2010).

<sup>83</sup> J. Thomas Rosch, Comm’r, Fed. Trade Comm’n, Speech at the California State Bar: Deceptive and Unfair Acts and Practices Principles: Evolution and Convergence 6–7 (May 18, 2007) (transcript available at <http://www.ftc.gov/speeches/rosch/070518evolutionandconvergence.pdf>) (comparing FTC Act with CAL. BUS. & PROF. CODE § 17200).

<sup>84</sup> In 1981, Richard Craswell surveyed the constitution of “unfair acts or practices,” including “withholding material information” (which has direct applicability to the advertising environment) and “unsubstantiated advertising claims.” See generally Craswell, *supra* note 12, at 107–09. For a contemporaneous analysis of the challenges of defining deceptive advertising, see Beales et al., *supra* note 46, at 495–501, 516–21.

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by one party through the exploitation of a hard-wired predisposition of a consumer to make certain cognitive errors or systematic misjudgments.<sup>85</sup> There are some tactics of psychological manipulation that may unfairly induce transactions. Obviously, the regulation of the information presentation that induces cognitive error must be done with a high level of care, and not just for purposes of compliance with the First Amendment.<sup>86</sup>

When advertising is disaggregated, portions of it will be pure presentation of the product, the price, and availability. These essentials comprise the core of advertising. When these essentials are subtracted from the whole of a piece of advertising, the remaining “residue” is pure persuasion. The attractive people depicted drinking beer on a tropical beach, the happy family depicted playing the board game, the free offer, the call to “buy now because supplies are limited,”<sup>87</sup> all reflect tactics that *persuade*, yet convey almost none of the core substantive information about the product.

Much of advertising regulation and debiasing through law focuses on controlling, managing, or addressing this “residue.”<sup>88</sup> It bears emphasizing again that Jolls and Sunstein contend that debiasing through law aptly describes the approach of advertising regulation.<sup>89</sup> Of paramount importance for protecting consumer decision making is controlling the purity of market information and its presentation. However, if regulatory control over the

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<sup>85</sup> For an example of the multiple sociological and cognitive manipulations involved with so-called “free offer” advertising, see generally David Adam Friedman, *Free Offers: A New Look*, 38 N.M. L. REV. 49 (2008).

<sup>86</sup> See *supra* note 37.

<sup>87</sup> This tactic triggers the scarcity effect. For an empirical demonstration, see generally Akanbi Adewole, Jerry Lee & Stephen Worchel, *Effects of Supply and Demand on Ratings of Object Value*, 32 J. PERSONALITY & SOC. PSYCHOL. 904 (1975).

<sup>88</sup> The use of the term “residue” should not imply that persuasion is unimportant to marketers. Persuasion tactics are extremely important and ingrained in our commercial culture. Entities invest heavily in creating brand identities that attempt to persuade. See Desai R. Desai & Spencer Weber Waller, *Brands, Competition and the Law*, BYU L. REV. (forthcoming) available at <http://ssrn.com/abstract=1545893>.

<sup>89</sup> Jolls & Sunstein, *supra* note 6, at 216.

market information tightens unduly, consumers may also be put in a suboptimal position. Consumers benefit from the unilateral (or occasionally interactive) communications to which advertisers expose them in all media, presuming that the content of these communications is truthful and the persuasive residue “fair.” Availability, price, and differentiation all guide the consumer toward opportunities to make an exchange that could enhance total welfare and make both parties better off.

Nonetheless, “bad” transactions present a real concern and the changes to consumer-endorsement regulation are but one microbe in a broad federal, state, and self-regulatory environment<sup>90</sup> that targets this concern. Although regulation may throw out good transactions with the bad, some of the prevented transactions may well indeed be bad transactions. Studies launched by the FTC have demonstrated that in certain instances, when consumers are presented with a consumer telling the story of an exceptional result from the offering, it raises the expected experience to be above that of the typical experience.<sup>91</sup>

Accordingly, there is a subtle result—a precarious balance—that regulators should seek. Certainly, “bad” transactions should be prevented, but preventing them should be done in the most effective and efficient way. The new regulatory approach does not impose a *de jure* legal prohibition on consumer endorsements, but they are, from their very design, aimed to severely impede them to the point where consumer endorsements might be almost too prohibitive to employ. As this Article describes in Part II, by ratcheting up the costs and raising the risk of legal exposure related to this method of delivering information, the FTC effectively addresses all consumer endorsements in the same manner. All of the “bad” transactions that would have been generated by consumer endorsements would simply not occur. Taken alone, this would be a positive social development.

However, at least two types of “good” transactions that might

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<sup>90</sup> “Private” or self-regulation would include industry norms and third-party groups like the Better Business Bureau and Underwriters Laboratory. *See* Beales et al., *supra* note 46, at 501–02.

<sup>91</sup> *See* HASTAK & MAZIS, WEIGHT LOSS, *supra* note 3; HASTAK & MAZIS, DIETARY SUPPLEMENTS, *supra* note 3.

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be induced through this method would get swept out with the bad: (1) The transactions that required the consumer endorsement “jolt” to boost the consumer incentive to transact, and then put the consumer in a satisfactory position *ex post*; and (2) The transactions that were really about “hope” as much as anything else. Some transactions may fit into both of these typologies.

The second category of transactions (“hope”) presents a difficult category of transactions for regulators to address. Regulators are not in any way taking the offering feature of hope *completely* off the market, but with consumer endorsement restrictions, they are removing the opportunity for producers to use true outcomes from their offerings to present consumers with a hope to which they can aspire.<sup>92</sup> The “hope” in this instance for the consumer would be the possibility of achieving the actual outcome that the consumer endorser experienced.

Concededly, examples of potentially “bad” transactions that use hope and consumer endorsements to induce transactions are commonplace. Weight-loss program offerings and “business-opportunities” programs have potential to magnify the effectiveness of the advertising tactic.<sup>93</sup> With dietary supplements, the FTC produced two empirical studies to demonstrate the potential cognitive distortive effect on expected product results.<sup>94</sup> With so-called “get-rich-quick” business-opportunity offerings, the expectations and results are also easily quantifiable.<sup>95</sup> If the new consumer-endorsement guides merely altered the nature of this particular family of transactions and precisely rebalanced the cognitive playing field within this family, that could be easily justifiable. Other socially-valuable communications, however, could get swept away with a broad, blanketed approach.

For illustration, consider the chiropractor who wishes to induce customers to try controversial chiropractic therapy through her clinic.<sup>96</sup> She publishes a website with true testimonials of

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<sup>92</sup> Because the tactic has become more expensive and riskier to implement, producers are disincentivized from using “hope.”

<sup>93</sup> See HASTAK & MAZIS, WEIGHT LOSS, *supra* note 3.

<sup>94</sup> *Id.*; HASTAK & MAZIS, DIETARY SUPPLEMENTS, *supra* note 3.

<sup>95</sup> See HASTAK & MAZIS, WEIGHT LOSS, *supra* note 3.

<sup>96</sup> Assume that her clinic is on a state border, opening her interstate

exceptional results, designed to lure skeptics to have hope that her services can help. Perhaps this inducement might be able to help someone. Arguably, the new consumer-endorsement guides would help to mitigate any questionable trade practices, but other narrowly-targeted mechanisms exist for that purpose.<sup>97</sup> Questionable trade practices can be addressed with precision rather than through overly-broad regulation.

Or consider an illustration that might be closer to home for readers of a law review article. A law school that showcases “student profiles” on its website, or profiles of recent alumni, may be transmitting experiences that are exceptional, not average. The profiles may indeed present true experiences, but law schools certainly design them to induce the potential applicant to take a closer look at the school, apply, and matriculate if accepted.

Consumer endorsements are certainly not without social value in given situations, but they should nonetheless be monitored. “Bad” transactions can certainly be induced by the presentation of outlier consumer endorsements, and regulators should be on heightened alert when these endorsements are used. However, by implementing the new consumer-endorsement guides, the FTC may have painted with too broad a brush. The FTC could simply have relied on its authority under the FTC Act to commence civil enforcement actions in specific “problem” industries without transmitting a general, strong warning about the tactic.

Perhaps the FTC should apply more scrutiny toward marketers that use this advertising tactic, but should operate with a discretionary stiletto rather than the proverbial hatchet. Some forms of hope have value and are less risky to leave unfettered in the marketplace. Other forms of hope can be quite damaging if expected, then dashed.<sup>98</sup>

## 2. *Regulating Information Flow*

Debiasing through law, when meshed with the consumer

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business to nominal FTC scrutiny.

<sup>97</sup> E.g., actions under section 5 of the FTC Act or state “baby FTC Acts.”

<sup>98</sup> See *infra* Part II.C.1.

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regulatory arena, distills the control of information transmitted through advertising or other disclosures. Depending on the situation and ultimate goal, regulators have mandated the *addition* of information to the flow, the removal or banning of *false* information, but also, interestingly, the *removal* of *true* information from the marketplace.<sup>99</sup> To contextualize properly where consumer-endorsement regulation fits into the consumer law picture, this Article next presents examples of each of these regulatory mandates, starting with mandates to add information into advertising.

*i. Adding Information*

People can make decision errors due to the absence of relevant information that would help them make better choices and debiasing can address this problem.<sup>100</sup> Sometimes adding this information provides raw data for the decision maker to consume, other times this information can be skillfully woven into the fabric of the decision-making process. Adding a narrative about a death resulting from smoking, for example, gives consumers raw information that they likely already have (smoking is hazardous), but also adds the information in a manner that tends to stick.

These decision errors may not necessarily be curable, but providing the information (or mandating its provision) to the decision maker represents a method of debiasing. The Truth in Lending Act,<sup>101</sup> which provides for mandatory, uniform disclosures from lenders, provides an example of a regulatory debiasing mechanism for adding information.<sup>102</sup> Whether these

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<sup>99</sup> Beales et al., sought to define regulatory “information remedies” to solve consumer market failures, categorizing the remedies as “(a) removing restraints on information; (b) correcting misleading information; (c) encouraging additional information.” Beales et al, *supra* note 46, at 513–31. The authors note that “remedying deficiencies in the information market is in some ways a more complex and subtle task than regulating product markets directly.” *Id.* at 514.

<sup>100</sup> Jolls & Sunstein, *supra* note 6, at 207.

<sup>101</sup> Truth in Lending Act, 15 U.S.C.A. § 1601 et. seq. (West 2010).

<sup>102</sup> For a cautionary tale about “glibly” using mandatory disclosure as a panacea in the securities regulation context, see Bainbridge, *Mandatory*

pieces of additional information are heeded by decision makers, or whether they improve decision making, can be a situational question. Over-disclosure can overwhelm consumers with too much information.<sup>103</sup> The marginal information may also prove insufficient to overcome the optimism bias.<sup>104</sup>

Even if the information is absorbed, the additional information may yield lower utility for the recipient. Ignorance can, indeed, be bliss.<sup>105</sup> Mandating disclosure about the FDA's standard for acceptable number of rodent hairs permissible in peanut butter (through a big orange sticker on the jar bearing a picture of a rat) may extinguish a potential transaction that would otherwise create welfare. This would be an inverted restatement of the old saying, "What you don't know won't hurt you."

Mandating disclosure of information to the consumer (adding information) constitutes a classic form of debiasing. Adding information changes how consumers calculate the risks and benefits of a potential transaction and make decisions. The initial

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*Disclosure*, *supra* note 24, at 1058–59 (2000).

<sup>103</sup> See generally Omri Ben-Shahar & Carl E. Schneider, *The Failure of Mandated Disclosure* (Univ. of Chi. Law & Econ., Olin Working Paper No. 516; Univ. of Mich. Law & Econ., Empirical Legal Studies Center Paper No. 10-008, 2010), available at <http://ssrn.com/abstract=1567284> (arguing that widespread mandatory disclosure has failed to protect consumers and may cause harm).

<sup>104</sup> Jolls & Sunstein, *supra* note 6, at 207. See Howard Latin, "Good" Warnings, Bad Products, and Cognitive Limitations, 41 UCLA L. REV. 1193, 1243–44 (1994).

<sup>105</sup> See Christian Turner, *The Burden of Knowledge*, 43 GA. L. REV. 297, 299 (2009):

Sometimes we are better off not knowing things. This near-aphorism is unremarkable when understood as an observation about our everyday lives. Do you really want to know the day, time, and circumstances of your own death? Do you want to know the details of your children's (or parents') love lives? Do you want to know whether your neighbors are scrupulous in paying their taxes? To these, and many questions like them, we answer almost reflexively, "I'd rather not know." We are happier, indeed better off by many measures, if ignorant. . . . Despite the advantages knowledge often confers, ignorance is sometimes preferable because it shields us from unpleasant realities, keeps us from facing difficult choices, or immunizes us against attack by others.

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burden of the costs borne from the added regulatory burden falls on advertisers. Policymakers would hope that the welfare gains from consumer empowerment would exceed any losses created by this extra burden.<sup>106</sup>

*ii. Removing False or Misleading Information*

Section 5 of the FTC Act forms the basic core of advertising regulation at the federal level and speaks to the core mission of the FTC in its control over the information flow.<sup>107</sup> The FTC Act declares unlawful “unfair or deceptive acts or practices in or affecting commerce.”<sup>108</sup> Although this sweeps broadly, this section vests the FTC with the power to compel the removal of certain materially-false bits of information from the marketplace and seek penalties for those who put the information into circulation.<sup>109</sup> Prohibiting advertisers from making false or misleading claims falls into this category.<sup>110</sup>

Removing nakedly false data from the decision-making pool

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<sup>106</sup> In 1981, Richard Craswell described the FTC’s approach toward regulating disclosure measured against the FTC Act’s “unfairness” standard.

[T]he failure to disclose information . . . will be [deemed] unfair if: (1) consumers currently lack the information in question; (2) consumers would choose differently if they had the information, thus facing sellers with a different set of demand curves; and (3) the benefits of better consumer decisions and improved seller performance are not outweighed by the costs of supplying the information.

Craswell, *supra* note 12, at 123. Included in the third category are the costs of collecting and disseminating the additional information, and the risks that disclosure “might [somehow] mislead consumers even further.” *Id.*

<sup>107</sup> “A deceptive claim that constitutes a false statement ‘is clearly at the core of most people’s understanding of deception.’” Beales et al., *supra* note 46, at 496.

<sup>108</sup> Federal Trade Commission Act, 15 U.S.C.A. § 45 (a)(1) (West 2010).

<sup>109</sup> Though as Beales et al. note, this definition of deception proves too narrow as it ignores broader concerns about the effect of other “less patently deceptive” claims on consumer decision making. Beales et al., *supra* note 46, at 495–96.

<sup>110</sup> See Craswell, *supra* note 12, at 123–27 (addressing “unsubstantiated advertising claims”). Sellers must have a reasonable basis for believing all claims they make at the time they make them. *Id.* at 123.

represents an almost pure form of debiasing through law. If advertising regulation and debiasing through law are closely related, this specific portion of the FTC's mandate is the closest cousin. When the advertising practices are patently unfair, an economic rationale undergirds this basic form of consumer protection.<sup>111</sup>

*iii. Removing True Information*

Under the broad auspices of Section 5, "unfair" acts are unlawful. Conceivably, the disclosure of true information could be unfair, thus unlawful. Consumer endorsements might fall into this category, if offered in a way that leads consumers to misleading conclusions.<sup>112</sup>

Certain norms direct suspicion at regulation that removes true information from the marketplace.<sup>113</sup> First Amendment

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<sup>111</sup> Transactions induced by false claims "contribute nothing to consumer welfare." Beales et al., *supra* note 46, at 496. Of interesting note is 15 U.S.C. § 45(a), which enables with specificity regulation of "Made in the U.S.A." labeling. This is a disclosure regulation that protects producers of products of United States origin from false claims of origin by foreign competitors. Consumers would probably not lose utility from use of a product with a falsely-labeled origin if they did not know about it.

<sup>112</sup> Craswell, in his early framework, might have bucketed this problem, the consumer endorsement problem, within a category he deemed, "difficult . . . to analyze," "unfair persuasive techniques." Craswell, *supra* note 12, at 139-51. Specifically, Craswell notes that "one-sided advertising" had been deemed unfair because although the claims were true, they were so overwhelming that they washed over countervailing consumer knowledge. Consumers were not deceived by false information, they were unfairly persuaded. The examples cited were FTC actions involving advertising about cigarettes and food products linked to child nutrition. *Id.* at 147-51. "True, but unfair," could apply to consumer endorsements, but Craswell expresses difficulty in reconciling this bucket. Note that Craswell peers into the future with a plea to social science for some assistance in assessing the fairness of persuasion techniques. "It may eventually be possible to develop a rationale for these cases, by improving our understanding of consumer decision making and the psychological effects of advertising." *Id.* at 150.

<sup>113</sup> Although, seller claims (or affirmative statements lacking a reasonable basis when made that are later even proven true) are vulnerable to be deemed

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jurisprudence reflects that anti-paternalistic norm. As Justice Stevens noted in *44 Liquormart v. Rhode Island*,<sup>114</sup> “[t]he First Amendment directs us to be especially skeptical of regulations that seek to keep people in the dark for what the government perceives to be their own good.”<sup>115</sup> In *44 Liquormart*, the Court struck down two Rhode Island statutes that removed true information from entering the marketplace. The Rhode Island laws prohibited advertising the retail price of alcoholic beverages away from the point of sale.<sup>116</sup> This price information was core offering information, not even persuasive “residue.”

Nonetheless, the specific situation matters. Removing true information from the marketplace can assist consumers in certain decision-making environments. Of recent note, Professor Elizabeth Warren, in advocating for the establishment of a Consumer Financial Protection Agency (CFPA), argued for mandating simplification and streamlining of disclosures and forms so that consumers would have easier means for comparing financial products. This amounts to removing information to simplify the transactional environment. “Over-disclosure” can occasionally confuse and overwhelm consumers in an information-heavy environment.<sup>117</sup> Warren wrote:

The truth, of course, is that no consumer “chooses” to accept the tricks and traps buried within the legalese of financial products. Rather, consumers must choose among various products with one feature in common: dozens of pages of incomprehensible fine print.

The CFPA will not limit consumer choice. Instead, it will focus on putting consumers in a position to make choices for themselves by streamlining regulations, making disclosures smarter, and making financial products easier to understand and compare. The Agency will promote plain vanilla contracts—short, easy to read mortgages and credit

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“unfair.” *Id.* at 123.

<sup>114</sup> *44 Liquormart v. Rhode Island*, 517 U.S. 484 (1996).

<sup>115</sup> *Id.* at 503.

<sup>116</sup> *Id.* at 489–90.

<sup>117</sup> See generally Ben-Shahar & Schneider, *supra* note 103.

card agreements. The key principle behind the new agency is that disclosure that runs on for pages is not real disclosure—it's just a way to hide more tricks. Real disclosure means that a lender has to be able to explain what it is selling so that the customer can read it and understand it. Once consumers can understand the risk and costs of various products—and can compare those products quickly and cheaply—the market will innovate around their preferences.<sup>118</sup>

Warren's proposal amounts to advocating the removal and resequencing of true information to enhance consumer decision making. The proposal presents another example of debiasing through law.<sup>119</sup>

Of course, consumer-endorsement regulation could be classified as an effort to debias through law by removing true information from the market environment. Unlike the alcohol at issue in *44 Liquormart* or the financial products at issue with the CFPA, however, consumer-endorsement regulation controls a *tactic* that cuts across *all* products and services. Across the board, the FTC has effectively deemed that consumer endorsements have the power to injure consumers, and that true narratives and testimony about a usage experience must be tightly monitored, if not in reality nudged out of the commercial-information sphere. From a policy standpoint, addressing the information problems offering-by-offering might have more appeal. Alcohol, mortgages, and sandwich shops all intersect with advertising differently and all present different types and degrees of transactional risk for the consumer. Why not factor in these differences when addressing the regulatory problem of consumer endorsements rather than firing what effectively amounts to a blanket salvo?

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<sup>118</sup> Elizabeth Warren, *Three Myths About the Consumer Financial Product Agency*, THE BASELINE SCENARIO (Jul. 19, 2010, 06:00 AM), <http://baseline.scenario.com/2009/07/21/three-myths-about-the-consumer-financial-product-agency/>.

<sup>119</sup> See also generally Lauren E. Willis, *Against Financial-Literacy Education*, 94 IOWA L. REV. 197 (2008) (arguing that social detriments of promoting consumer financial literacy could exceed the benefits, implying that removing this information might be helpful to consumers).

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Next, this Article hones in on these recent restrictions on consumer advertising embodied in the 2009 revised consumer-endorsement guides. Examining this case study in detail should illuminate the strengths and weaknesses of the claims embodied by advocates of the debiasing-through-law approach. Are regulators capable of this sort of precision welfare engineering?<sup>120</sup> Can regulators preserve real choice while simultaneously improving decisions? Consumer-endorsement regulation provides an example of debiasing through law in action.

## II. A CASE STUDY FROM ADVERTISING REGULATION

Consumer endorsements have a long history and heritage in advertising in the United States. The power of a real peer, a real product or service user, to induce a transaction has been acknowledged by marketers,<sup>121</sup> regulators,<sup>122</sup> and consumer activists.<sup>123</sup>

Following the statutory mission, the FTC prophylactically seeks to eliminate and prevent unfair and deceptive trade practices and advertising, which it has power to regulate under Section 5 of

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<sup>120</sup> Within the definitional scheme of deceptive advertising regulation that Beales et al. describes, it is challenging, but possible to envision where the new consumer-endorsement regulation would slot in as a cure. Beales et al. largely focus on false claims, production of inaccurate consumer beliefs, and failures to disclose. *See* Beales et al., *supra* note 46, at 496–501. Most likely, they would see this regulation as addressing inaccurate consumer beliefs—and much of their discussion of the remedy for this focuses on improved disclosure. Beales et al. do not focus on the removal of true information as a remedy. As discussed *infra*, consumer endorsements have a complex impact on consumer decision making and social welfare.

<sup>121</sup> *See, e.g.*, Letter from John Feldman & Anthony DiResta, Reed Smith LLP, on Behalf of Ass'n of Nat'l Advertisers, to Office of the Secretary, Fed. Trade Comm'n, 16 C.F.R. § 255 (2009); FTC File No.: P034520 (Mar. 2, 2009), available at <http://www.ftc.gov/os/comments/endorsementguides2/539124-00006.pdf> (reviewing the Guides Concerning the Use of Endorsements and Testimonials in Advertising).

<sup>122</sup> *See* HASTAK & MAZIS, WEIGHT LOSS, *supra* note 3; HASTAK & MAZIS, DIETARY SUPPLEMENTS, *supra* note 3 (demonstrating power of consumer endorsements to create audience recall of message).

<sup>123</sup> *See, e.g.*, Greenberg Statement, *supra* note 2, at 14–20.

the FTC Act.<sup>124</sup> Given that producers aggressively seek to induce transactions against the inertia of the closed human wallet,<sup>125</sup> and then against competing offers of other producers, the advertising arena can be quite fierce tactically.

Virtually all advertising promotes a call to consumer action. The call to action can be pure—a mere dissemination of information about price, qualities, and availability.<sup>126</sup> Questions start to emerge when the call starts to employ devices that move beyond communicating the “pure” component of the call to action—into persuasion. Strategic bundling and pricing of an offer can cause the consumer to value the package differently if laid out one way versus another way. The medium of the message can convey information that does not directly relate to the product. A trusted celebrity endorser or a consumer endorser can add a layer of credibility and identity to the message.

The question is whether adding these extra layers of persuasion to the plain message are unlawfully deceptive or instead a positive addition of useful content. For example, inducing the sale of a food processor by communicating that a free set of steak knives is included, instead of simply offering the processor and the knives together at the same price, may not yield incremental social welfare, but would most probably be lawful.<sup>127</sup> Also, consider that a marketer can lawfully employ a trusted B-list actor to promote a

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<sup>124</sup> Federal Trade Commission Act, 15 U.S.C.A. § 45(a)(2) (West 2010).

<sup>125</sup> See discussion of endowment effect, *supra* Part I. Though the conclusions and implications are now wrapped in some degree of controversy, Kahneman and Tversky demonstrated through classroom laboratory experiments that people value a loss of X greater than an absolute gain of X. See generally Daniel Kahneman & Amos Tversky, *Prospect Theory: An Analysis of Decision under Risk*, 47 *ECONOMETRICA* 263 (1979) [hereinafter Kahneman & Tversky, *Prospect Theory*]. At the front end of a transaction, the implication is that inducing just an even exchange of value requires the marketer to overcome a level of cognitive impulse for the consumer not to part with what they already have. Kahneman and Tversky’s loss aversion work has further implications for analysis of consumer-endorsement regulation, specifically, in assessing the consumer’s reaction to the results of a transaction.

<sup>126</sup> The call to action can also be long-run—the creation of a brand image that communicates a message about the values behind a product.

<sup>127</sup> See 16 C.F.R. § 251.1 (2011). See generally Friedman, *supra* note 85.

safety-alert system for older people.<sup>128</sup> Even if disclosed as a compensated endorser and not a user, the somewhat misplaced trust in the actor is designed to rub off onto the no-name alert system.<sup>129</sup> The former case we may accept because it is practically difficult to control that form of bundling manipulation. The latter case could be troubling on the surface, but what if the offering is an honest one and the target audience needed the comfort of the celebrity endorsement to enter into a “good” transaction?

The consumer endorsement takes advantage of many of the same biases as the rest of advertising. Advertisers count on tapping into an array of consumer biological and cognitive biases to induce transactions, and, in turn, mitigate the biases that inhibit them to act. As noted, the advertising arena, a petri dish for psychological and cognitive games, provides a natural testing ground for debiasing through law. In particular, consumer endorsements have been wide open for debiasing “treatment” and the FTC has, in fact, accorded them this treatment. Section A begins with a description of the power of consumer endorsements, using a well-known advertising campaign as a working example; Section B describes the change in regulatory approach and its potential impact in general terms; and finally, Section C analyzes the various biases that the new approach uses to effectively neutralize the power of consumer endorsements.

#### *A. The Power of Consumer Endorsements*

In 1998, morbidly-obese Indiana University college student Jared Fogle began a journey toward achieving iconic celebrity and cultural-touchstone status.<sup>130</sup> Eating nothing but weight-loss

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<sup>128</sup> This genre and application of celebrity endorsement ad has become so common that actor Sam Waterston spoofed it on Saturday Night Live, pitching “robot insurance” (as a “compensated endorser”) to senior citizens to protect them from “robot attacks.” *Saturday Night Live: Laura Leighton/Rancid* (NBC television broadcast Nov. 18, 1995).

<sup>129</sup> See 16 C.F.R § 255.5 (2011).

<sup>130</sup> Bob Levey, Column, *Q&A with Bob Levey*, WASH. POST (Mar. 18, 2003), [http://discuss.washingtonpost.com/wp-srv/zforum/03/r\\_metro\\_levey\\_031803.htm](http://discuss.washingtonpost.com/wp-srv/zforum/03/r_metro_levey_031803.htm). Fogle has also been spoofed on Saturday Night Live and even in an

friendly Subway<sup>131</sup> sandwiches, Fogle ultimately shed and kept off over two hundred pounds.<sup>132</sup> Two years later, sharp-eyed regional Subway franchise owners received word of Fogle's astonishing achievement and retained him to tell his story in their advertisements. Not long after the regional commercials demonstrated tremendous effectiveness, Subway's corporate headquarters recruited "Jared," as he would come to be known, for a national campaign.<sup>133</sup> Over the next decade, "Jared" lured not just crash dieters, but all kinds of health-conscious consumers through Subway's doors, helping to spur Subway's location presence to equate that of McDonald's, the ultimate food-industry franchising pioneer, by 2009.<sup>134</sup>

Although a number of factors likely drove the astonishing growth of Subway since 2000, the "Jared" campaign, according to CEO Jeff Moody, provided the "absolute cornerstone" for "Subway's success."<sup>135</sup> Moody opined:

I believe the company would have been successful without Jared but not nearly to the degree that we are because he took these healthy products and gave them a face and said something that people could relate to. I mean he's not a celebrity because he set out to be, he's a celebrity [be]cause . . . he resonated with people that had similar issues to him and said, well if that guy can do it, I can do it . . . .<sup>136</sup>

Moody effectively described the power of a peer recommendation or demonstration in the context of a commercial

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episode of South Park. Blair Chancey, *Subway's Savior*, QSR MAG. (Sept. 2008), <http://www.qsrmagazine.com/articles/features/119/subway-1.phtml>.

<sup>131</sup> Subway, Inc. franchised 22,000 sandwich shops in the United States as of 2008. See *Jared's Revenge*, *supra* note 1.

<sup>132</sup> *Id.*

<sup>133</sup> CHIP HEATH & DAN HEATH, MADE TO STICK 218–221 (2007). Heath and Heath offer additional compelling explanations for the Jared campaign's enduring success.

<sup>134</sup> Emily Bryson York, *Subway Set to Overtake McD's in Omnipresence*, ADVERTISING AGE, Sept. 21, 2009, at 3, available at [http://adage.com/Article?Article\\_id=139145](http://adage.com/Article?Article_id=139145).

<sup>135</sup> *Jared's Revenge*, *supra* note 1.

<sup>136</sup> *Id.*

offer. Fogle, at least at the outset of his arrangement with Subway, would qualify as a “consumer endorser” by the FTC.<sup>137</sup> Under the Guides Concerning the Use of Endorsements and Testimonials in Advertising that were in effect until 2009 (“Previous Guides”), Subway could use Fogle’s outlier endorsement, provided that the company disclaimed the endorser’s experience as an atypical result.<sup>138</sup>

Due to the recent changes in the Guides, this highly-effective type of consumer endorsement campaign would be significantly more impractical to launch effectively now. Had Subway wished to launch a consumer-endorsement Jared-style campaign today, under the new guides (“Revised Guides”), the company would have had to choose between two regulatory compliance paths. Subway could either choose to disclose scientifically-derived, empirically-sound, “typical” results alongside Jared’s results, significantly cluttering the message or Subway could simultaneously broadcast an “atypicality” disclaimer, similar to the one previously required but without any accompanying safe-harbor protections. The FTC warns that in this new regime, the disclosure route should also be backed up by empirical evidence that the totality of the advertisement is non-deceptive.<sup>139</sup> This looming threat of

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<sup>137</sup> Arguably, Jared Fogle has now achieved a level of fame that would also subject him to regulation as a *celebrity* endorser for Subway under 16 C.F.R. § 255.5 (2009).

<sup>138</sup> The disclaimer provided a safe harbor. As an alternative, under the Previous Guides, advertisers could present the expected results alongside the exceptional results presented by the consumer endorser.

The Guides are administrative interpretations of the law intended to help advertisers comply with the Federal Trade Commission Act; they are not binding law themselves. In any law enforcement action challenging the allegedly deceptive use of testimonials or endorsements, the Commission would have the burden of proving that the challenged conduct violates the FTC Act.

*FTC Publishes Final Guides Governing Endorsements, Testimonials*, *supra* note 1.

<sup>139</sup> See 16 C.F.R. § 255.2 (2009). The FTC warns advertisers to take significant precautions should they pursue the route of a typicality disclaimer:

The Commission tested the communication of advertisements containing testimonials that clearly and prominently disclosed either

enforcement puts a heavy burden on the prospective use of this tactic. The FTC explicitly advises advertisers to maintain this evidence to avoid the risk of the initiation of an FTC action taken with respect to such an advertisement.<sup>140</sup>

The Revised Guides aim to put a serious brake on the practice of using consumer endorsements, given evidence that consumers unduly raise their expectations about the salutary effects of a good or service after exposure to a peer's true, but exceptional, experience with the offering.<sup>141</sup> Consumer endorsements indeed would be costlier to employ after the revision, given the empirical compliance requirements, and from a regulatory standpoint, would certainly be riskier to use.

At first glance this regulatory approach may seem like a simple, straightforward, common-sense adjustment to the flow of commercial information aimed at consumers. The FTC is charged with protecting consumers from "unfair or deceptive acts or practices,"<sup>142</sup> and clamping down on advertiser presentation of misleading material would certainly be within that authority. If presenting a consumer endorser's true, but atypical, experience

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"Results not typical" or the stronger "These testimonials are based on the experiences of a few people and you are not likely to have similar results." Neither disclosure adequately reduced the communication that the experiences depicted are generally representative. Based upon this research, the Commission believes that similar disclaimers regarding the limited applicability of an endorser's experience to what consumers may generally expect to achieve are unlikely to be effective. Nonetheless, the Commission cannot rule out the possibility that a strong disclaimer of typicality could be effective in the context of a particular advertisement. Although the Commission would have the burden of proof in a law enforcement action, the Commission notes that an advertiser possessing reliable empirical testing demonstrating that the net impression of its advertisement with such a disclaimer is non-deceptive will avoid the risk of the initiation of such an action in the first instance.

*Id.*

<sup>140</sup> *Id.*

<sup>141</sup> Like the consumers in the Hastak & Mazis studies. See HASTAK & MAZIS, WEIGHT LOSS, *supra* note 3; HASTAK & MAZIS, DIETARY SUPPLEMENT, *supra* note 3.

<sup>142</sup> Federal Trade Commission Act, 15 U.S.C.A. § 45(a) (West 2010).

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effectively misleads the public, regulators may choose to debias consumers by drastically restricting or altering the practice.

Here, the FTC has taken a less-common tack in protecting consumers from receiving bits of information that are entirely true, but potentially so powerful in their truth that the dissemination of these bits need to be tightly-controlled.<sup>143</sup> This “you can’t handle the truth”<sup>144</sup> quirk in the regulatory approach opens the door to some serious questions, both in this instance and generally.

Part of the overall question involves determining the nature of the entirety of the commercial offering and what the consumer endorsement intends to convey. In addition to selling healthy sandwiches, is Subway selling the *hope* to consumers (not the promise) that if they transact regularly with Subway they will lose significant amounts of weight? Is hope an appropriate product to sell? Or is Subway merely trying to induce consumer transactions through cognitive error, using a strange, but *true*, story as aspirational bait?

Framed another way, if an internet dating service presents the testimonial of a married couple that met through use of its offering, is the dating service legitimately selling hope, attempting to induce transactions through cognitive error, or both? Another potential way of framing “hope” is to suggest that Subway and the dating service are selling an expected range of outcomes.<sup>145</sup> Perhaps, presenting a product or service in a way that taps into that expected “range of outcomes” presents as an entirely different offering in

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<sup>143</sup> See generally Turner, *supra* note 105. Shielding truthful information to preserve a broader truthful narrative can be important in the jurisprudence of evidence, to purify jury decision making or protect other interests. See, e.g., FED. R. EVID. 407 (subsequent remedial measures); FED. R. EVID. 408 (compromise and offers to compromise); FED. R. EVID. 409 (payment of medical and similar expenses); FED. R. EVID. 411 (liability insurance). In other contexts, people shield the vulnerable from truth when the truth has little value and great detriment.

<sup>144</sup> See A FEW GOOD MEN (Columbia Pictures 1992).

<sup>145</sup> The Commission employed professionals to write two reports to study the effects of consumer endorsements and disclosures. While the reports showed that consumers might expect the demonstrated results in an advertisement to be atypical, the reports did not probe about the *range* of expectations for a set of individual consumers. See HASTAK & MAZIS, DIETARY SUPPLEMENTS, *supra* note 3; HASTAK & MAZIS, WEIGHT LOSS, *supra* note 3.

the marketplace. Consumers may know that experiences vary and may want to be aware of the positive possibilities. They may weigh their expectations optimistically—but is it the feeling of optimism that they are buying? Are these transactions a milder form of a lottery ticket, where the above-average expectation of winning may drive the purchase in spite of disclosed odds, but the thrill of the range of expectations is part of the product?<sup>146</sup> Or is it a less transparent lottery ticket? If Powerball advertised lottery tickets as short-term “Grade D-” bonds instead of presenting the visual narrative of an ordinary person receiving an oversized check, would the perceived *ex-ante* value of a lottery offering be diminished? One would almost have to argue that consumers are buying hope, not a certainty, even if consumer expectations might be prone to optimistic distortion.

If the presentation of a wider range of possible outcomes from a transaction induces more transactions, *some* positive social welfare might be created, simply through exchange. *Ex-ante* hope, based on a truthful experience relayed by a peer consumer, might have innate welfare value, and *ex post* disappointment, though quite real, is something with which consumer transactions in general are rife. Regulators cannot fix all disappointments, however initially induced. A shift in regulatory policy that effectively quashes consumer endorsements may remove some distortions of expectation by smoothing out certain cognitive biases,<sup>147</sup> but not at zero welfare cost. If this holds true, a brief assessment of the impact of the Revised Guides can illuminate the pitfalls of debiasing through law.

## *B. The New Regulatory Approach and Potential Impact*

### *1. Previous Regulatory Approach*

Under the Previous Guides, advertisers could present the

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<sup>146</sup> Gambling on lottery tickets can be destructive after a point, but the common practice has been to showcase winning jackpot tickets, which might have longer odds than finding a spouse on a dating website. For a vibrant view into lottery psychology and sociology, see *LUCKY* (Big Beach Films 2010).

<sup>147</sup> See *infra* Part II.C.

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experiences of consumer endorsers under limited conditions. The most basic requirement was that the consumer endorser, if represented directly or implicitly to be an actual consumer, must have been an actual consumer.<sup>148</sup> Use of a consumer endorsement implies that the advertiser “represent[s] that the endorser’s experience is representative of what consumers will generally achieve with the advertised product in actual, albeit variable, conditions of use.”<sup>149</sup> The Previous Guides required that advertisers possess substantiation that the advertised product’s result would perform at the level the consumer endorser enjoyed, *or* that “the advertisement . . . either clearly and conspicuously disclose[d] what the generally expected performance would be in the depicted circumstances.” The other option, commonly availed, is for the advertiser to “disclose the limited applicability of the endorser’s experience to what consumers may generally expect to achieve.”<sup>150</sup> Quite often, this safe harbor would be employed by the advertiser simply slapping a disclaimer into the advertisement denoting something to the effect of, “Results not typical” or “Results may vary.”

*2. New Approach*

The Revised Guides make this safe-harbor option more impractical for advertisers. If advertisers use consumer endorsers, substantiation must be developed and possessed to support the typicality of the endorser’s experience, and if the endorser’s experience is atypical, the true typical experience must be disclosed. No longer can a marketer promote an endorser who had an outlier experience and cure it magically with a mild disclaimer.

At first blush, the Revised Guides may appear to advance consumer welfare. No longer will consumers be deceived by outlier results. But as this Article discusses, consumers may not *always* be “tricked” by these results. Consumers may know that they are buying the chance to achieve the consumer endorser’s result. That is, consumers may be buying the “hope” that they can

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<sup>148</sup> See, e.g., 16 C.F.R. § 255.2(b) (1980).

<sup>149</sup> See, e.g., 16 C.F.R. § 255.2(a) (1980).

<sup>150</sup> *Id.*

achieve the result—and this purchase may be rational. Consumers do retain protection without the Revised Guides. If an ad is deceptive or unfair, the FTC already has the power to address it.<sup>151</sup>

These recent changes effectively eliminate the consumer option to select hope as a product feature in this context. How does taking hope off the market advance consumer welfare? Does taking away a person's hope that their acne might clear like a peer consumer's did in the television ad advance consumer welfare? Does removing a lonely person's hope that a dating service might bring them down the course toward marriage advance consumer welfare? Some consumer advocates imply that by showcasing a high-end result for consumers, this hope must almost always find its roots in and lead to deception.<sup>152</sup>

This guidance change effectively puts an end to a long-established practice that American consumers have become accustomed to seeing every day, and as a commercial cultural change alone, demands notice. Specifically, this could be the death of campaigns that use consumer endorsers to engage peers with optimism that use of a product or service might have an outlier outcome like that of a Jared Fogle.

When advertisers communicate through consumer endorsers, they are trading on the aspirations of the target consumer to achieve that result. “If *that* person got thin, toned their abdominal muscles, cleared up their skin, found a life partner and was able make \$100,000 per year working from home, or simply get rich, why can't I?”<sup>153</sup> One might interpret the implicit dialogue between advertiser and consumer that way. Or it might be a mere conveyance of information that this is an achievable (but not certain) result from use of the product or service—and that with an associated disclaimer, a consumer should internalize that this true information presented to them presents a possible but not necessarily a probable result. Other scenarios may appear more benign. For example, consumer endorsers can be employed by local restaurants, owners of bed-and-breakfasts, and businesses

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<sup>151</sup> Federal Trade Commission Act, 15 U.S.C.A. § 45 (West 2010).

<sup>152</sup> See Greenberg Statement, *supra* note 2.

<sup>153</sup> Human appearance, mating, and money all seem to present ripe opportunities for the use of a consumer endorsement.

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with lower accessibility to a brand. The consumer endorser can provide information to other consumers about the feel of the user experience.

One common thread woven through all of these consumer-endorsement scenarios is that they involve a marketer attempting to transmit information about a product through the experiences of an actual user. This information at its most pure and benign conveys a true experience and facilitates a transaction to happen with proper expectations on the part of the consumer. At its most nefarious, advertisers can use this approach to seize a true consumer experience and use it to create unrealistic expectations that induce a “bad,” welfare-destroying consumer transaction.

*C. Benefits of the New Approach: Neutralizing Cognitive Biases*

The Revised Guides should effectively eliminate the ability of marketers to exploit a number of cognitive biases to effectuate transactions. Part C explores some of the major biases that consumer endorsements play on and that the Revised Guides address. For consumers, generally, this represents a positive development standing alone, but as this Article explores in Part III, a downside must also be weighed.

*1. Optimism Bias and Hope*

Where hope is commoditized, cognitive psychology must be nearby. Where commerce meets cognitive psychology, behavioral law and economics cannot be avoided. These “Jared-style” consumer-endorsement campaigns exploit the power of a few widely accepted psychological phenomena absorbed by the behavioral law and economics literature, notably optimism bias and the availability heuristic. Optimism bias, famously epitomized by humorist Garrison Keillor as the “Lake Wobegon” syndrome,<sup>154</sup>

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<sup>154</sup> As broadcaster Garrison Keillor famously repeats about his blessed, fictional upper midwestern town, “Lake Wobegon, where all the women are strong, all the men are good-looking and all the children are above average.” 10

refers to the inclination of individuals to believe that there is an above-average chance of good things happening to them and a below-average chance of bad things. The optimism bias drives people to get out of bed in the morning and encourages risk-taking.<sup>155</sup> One study demonstrated that half of consumers believed that their own households carried “below average” risk, with the other half believing that their households were average. Basic arithmetic tells us that result reflects undue optimism in sum.<sup>156</sup>

[P]eople typically think that their chances of a range of bad outcomes, from having an auto accident to contracting a particular disease to getting fired from a job, are significantly lower than the average person’s chances of suffering these misfortunes—although, again, this cannot be true for everyone.<sup>157</sup>

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*Questions for Garrison Keillor*, TIME (Dec. 21, 2009), available at <http://www.time.com/time/magazine/article/0,9171,1946961,00.html> (emphasis added).

<sup>155</sup> For an overview of the optimism bias, see David A. Armor & Shelley E. Taylor, *When Predictions Fail: The Dilemma of Unrealistic Optimism*, in HEURISTICS AND BIASES: THE PSYCHOLOGY OF INTUITIVE JUDGMENT 334–47 (Thomas Gilovich, Dale Griffin & Daniel Kahneman eds., 2002). This cognitive bias can be credited for getting businesses off the ground, despite high rates of start-up failure. See generally Arnold C. Cooper, William C. Dunkelberg & Carolyn Y. Woo, *Entrepreneurs Perceived Chances for Success*, 3 J. BUS. VENTURING 97 (1988).

<sup>156</sup> Jolls & Sunstein, *supra* note 6, at 204; WESLEY A. MAGAT & W. KIP VISCUSI, INFORMATIONAL APPROACHES TO REGULATION 93–95 (1992).

<sup>157</sup> Jolls & Sunstein, *supra* note 6, at 204. See also Christine Jolls, *Behavioral Economics Analysis of Redistributive Legal Rules*, 51 VAND. L. REV. 1653, 1659 (1998) [hereinafter Jolls, *Behavioral Economics Analysis*]. This phenomenon transcends personal judgments and translates even into professional judgments. Another recent study concluded that litigators are prone to routinely overestimate the success of the outcomes of their cases before the fact. See generally Jane Goodman-Delahunty, Pär Anders Granhag, Maria Hartwig & Elizabeth F. Loftus, *Insightful or Wishful: Lawyers’ Ability to Predict Case Outcomes*, 16 PSYCHOL. PUB. POL’Y & L. 133 (2010). Goodman-Delahunty et al. even employed a debiasing technique, exposure of the subject to what Jolls and Sunstein deemed “truthful narratives of harm,” to alter the thought process, as opposed to cold exposure to statistics, or overly-aggressive tactics that turn off reception. See Jolls & Sunstein, *supra* note 6, at 215. Goodman-Delahunty et al. asked some of their lawyer subjects “to generate reasons why they might not achieve their stated goals. This manipulation did not

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Much of this view of the optimism bias can be framed as a relative one. Individuals measure their risk against that of other individuals. Some literature shows that individuals are overly optimistic (or not as pessimistic as they should be) in assessment of stand-alone event probabilities.<sup>158</sup> Jolls and Sunstein summarize numerous studies:

reporting that professional financial experts consistently overestimate likely corporate earnings, while business school students overestimate their likely starting salary and the number of [job] offers they will receive.<sup>159</sup> People also underestimate their own likelihood of being involved in an automobile accident, and their frequent failure to buy insurance for floods and earthquakes is consistent with the view that people are excessively optimistic.<sup>160</sup>

The frame of the optimism bias tells us that consumers may be cognitively wired to view the stated experience and outcome of another consumer as one they can readily attain—even if that stated experience is at the upper boundary of what one could hope to realize from the advertised product or service.<sup>161</sup>

Optimism bias can be applied to this problem in two different ways—first, there are some aspirations induced by advertisers that are not *necessarily* detrimental to consumers. Consumers need to have some level of optimism about the results of a transaction in order for the transaction to be induced. If the information is not unfair or deceptive, this transaction should yield welfare. Communication of the attainability of a result might be the primary purpose for advertising. Fogle transmitted the message that

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improve calibration [with the real outcomes.]” Goodman-Delahunty et al., *supra*, at 133.

<sup>158</sup> Jolls & Sunstein, *supra* note 6, at 204.

<sup>159</sup> *Id.* at 205; Armor & Taylor, *supra* note 155, at 334–35.

<sup>160</sup> Jolls & Sunstein, *supra* note 6, at 205; Jolls, *Behavioral Economics Analysis*, *supra* note 157, at 1660–61.

<sup>161</sup> A brain-imaging study may have shed some light on why this might be. When considering the potential negative outcomes from a decision, the brain may not retain the memory of negative past events as well as it does positive events. See generally Tali Sharot, Alison M. Riccardi, Candace M. Raio & Elizabeth A. Phelps, *Neural Mechanisms Mediating Optimism Bias*, 450 NATURE 102 (Nov. 1, 2007).

consumption of the Subway offering could lead to significant weight loss. According to Subway's management, this message induced millions of additional consumer transactions, presumably creating welfare.

The second application of the optimism bias, which the FTC is at least implicitly concerned about, is the dangerous type of consumer endorsement claim that deliberately induces systemic cognitive errors. The FTC aspires to eliminate advertisements that yield so much unjustified optimism that they deceive the public and result in bad transactions that are ultimately damaging to welfare. If hope, or a range of outcomes, is on the market, welfare-seeking regulators should not want undue optimism to cause people to overvalue systematically the probability that they will receive the higher range of the outcome.

Even though this more nefarious use of the optimism bias likely yields cognitive errors that result in consumer disappointment, the absolute magnitude of the disappointment of the result after the fact compared with expectations before the fact is not well-understood.<sup>162</sup>

If the optimism bias implies that the hard-wired hope of above-average results will be routinely dashed as results regress to the mean, it becomes more important to consider hope—and lost hope. The ancient Greeks held hope out as a sacred value. After Pandora “unleashed the affliction, disease and death upon mankind”<sup>163</sup> from her box, only one thing remained, hope. The import of hope, and the concept that hope would be a cruel thing to dash, has deep roots. The ancients knew that hope had a special value as a force.<sup>164</sup>

Moving to the modern problem of false hope in the commercial context, there is a notion that true information can lead to false hope. Disappointment *per se* can be socially costly, which means that fostering a high level of hope, or hope for a higher-than-

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<sup>162</sup> The FTC-commissioned studies fail to provide this analysis.

<sup>163</sup> ANNA POTAMIANOU, *HOPE: A SHIELD IN THE ECONOMY OF BORDERLINE STATES* 6 (1997).

<sup>164</sup> For a brief discussion of hope and social trust, see GEORGE CVETKOVICH & TIMOTHY C. EARLE, *SOCIAL TRUST: TOWARD A COSMOPOLITAN SOCIETY* 69–75 (1995).

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typical result, can be destructive. If a weight-loss company induces purchase of its program through hope for a certain result, and this result is not obtained, this may lead to lost consumer emotional investment in hope, as well as the more transparent lost financial investment. More than the financial investment would be lost; hope would be lost, too. This can put the consumer in a position where the utility loss exceeds what would normally be expected from squandered value. Kahneman and Tversky famously found that people are cognitively predisposed to assign a heavier value to a loss of X than to the value of a gain of X.<sup>165</sup> Manufacturing and selling hope of an above-typical result and failing to deliver can diminish utility more dramatically than in a transaction where the typical result would be expected.

But again, it is important to note that traditional FTC discretion would be valuable in regulating the sale of hope via consumer endorsements. Certainly, the hope dashed from failing to achieve an above-typical result from an expensive weight-loss company program differs from that of the hope dashed from the Subway program, which consists of a series of continuing, non-obliging transactions. Yet, consumer endorsements for both are deterred by the new regulations.<sup>166</sup> Why would we regulate hope the same way for two very different cases? Subway operates, interacts, markets, and transacts with consumers in a vastly different manner than weight-loss programs. The transactions are serial and smaller, and the program is simple. Weight-loss programs tend to require a longer contractual commitment and a deeper financial investment.<sup>167</sup> The damage levels from the potential betrayal of hope from a Subway program are likely below that of a typical weight-loss program.

If hope is valuable, taking a sweeping approach to forbid firms from creating it and marketing it as an attribute of their product or

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<sup>165</sup> See Kahneman & Tversky, *Prospect Theory*, *supra* note 125.

<sup>166</sup> Subway may be less deterred than a small weight-loss company if it has more resources to defend the advertising in an action.

<sup>167</sup> The websites of two of the leading weight-loss companies at [www.jennycraig.com](http://www.jennycraig.com) and [www.weightwatchers.com](http://www.weightwatchers.com) illustrate the programmatic and extended nature of required consumer commitment in that industry. JENNY CRAIG, [www.jennycraig.com](http://www.jennycraig.com) (last visited Aug. 13, 2010); WEIGHT WATCHERS, [www.weightwatchers.com](http://www.weightwatchers.com) (last visited Aug. 13, 2010).

service should have a downside somewhere. Basic cognitive science behind the optimism bias and consumer human valuation of gains and losses can inform our understanding of the trade-offs of a sweeping change. Assessing the impact of taking hope off the market in this wholesale manner can lead us to a clearer picture of the regulatory impact.

## 2. Availability Bias

Working along with the optimism bias, and perhaps even a subject of greater concern about consumer endorsements, is the availability bias.<sup>168</sup> Put simply, people tend to use the information most readily available to them as a heuristic for what the broader picture looks like. Consumers are deluged with data of all types in the marketplace and must find efficient shortcuts to navigate through them.

Behavioralists often present the availability bias through the example of people overestimating risk and taking disproportionate steps to mitigate or avoid such risk.<sup>169</sup> Fear of domestic terrorism may provide one example of overestimation of risk, as the media coverage after a tragedy on the scale of the terrorist attacks of September 11, 2001, made terrorism risk more “available” to the public.<sup>170</sup> Sunbathing may present a more serious risk to public health, but the information is not nearly as dramatically and graphically available.<sup>171</sup> The public has more access to information about homicide through the media and less access to information about suicides, which leads to a commonly-held, but incorrect conclusion that homicide is more prevalent than suicide.<sup>172</sup> That conclusion could foster the formation of misguided public-health attitudes.

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<sup>168</sup> See generally Daniel Kahneman & Amos Tversky, *Availability: A Heuristic for Judging Frequency and Probability*, 5 *COGNITIVE PSYCHOL.* 207 (1973); Timur Kuran & Cass R. Sunstein, *Availability Cascades and Risk Regulation*, 51 *STAN. L. REV.* 683 (1999).

<sup>169</sup> See SUNSTEIN & THALER, *NUDGE*, *supra* note 7, at 24–26.

<sup>170</sup> *Id.* at 25.

<sup>171</sup> *Id.*

<sup>172</sup> *Id.*

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Also undergirding the availability bias is “salience,”<sup>173</sup> which strongly relates to consumer-endorsement regulation. A salient experience will prove much more available when assessing the probability that an event or result will occur. For example, directly experiencing an earthquake will cause a person to have a more accessible data point when assessing the risks of experiencing a future earthquake.<sup>174</sup> “Vivid and easily imagined” risks like dying in a plane crash are over-weighted in comparison to other risks like death by asphyxiation from choking on food.<sup>175</sup> The consumer endorsement is employed to make a positive outcome both the most accessible piece of information and the most *vivid* one.

If presented with a strong consumer endorsement, the availability bias predicts that the consumer will heed that information because the advertiser has centered it right in front of them. The question still remains whether they will discount the more spectacular claims made by consumer endorsers as a *possible* result, rather than a probable result (on a spectrum of results). Much of this depends on the total pool of information that is available and competing with the consumer’s attention in a given environment.

Where consumer endorsements are the centerpiece of an advertisement, they become the available focus of the consumer. The Revised Guides remove consumer endorsements from that centerpiece, potentially neutralizing errors attributable to the availability bias.

*3. Framing Effect*

Prospect theory, promoted by Kahneman and Tversky,<sup>176</sup> contends that humans evaluate the impact of decisions based on “an initial reference point, rather than on the basis of the nature of the outcome itself.”<sup>177</sup> Tied closely into prospect theory is the

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<sup>173</sup> *Id.*

<sup>174</sup> *Id.*

<sup>175</sup> *Id.*

<sup>176</sup> See generally Daniel Kahneman & Amos Tversky, *Prospect Theory*, *supra* note 125.

<sup>177</sup> Jolls & Sunstein, *supra* note 6, at 205.

endowment effect and loss aversion. These theories and observations reinforce the notion that people value losses heavier than gains.<sup>178</sup>

From a practical perspective, the related “framing effect” demonstrates that perceptions and decision processes can be manipulated by framing certain outcomes as losses and others as gains.<sup>179</sup> Advertisers and policymakers put the framing effect to work constantly.

Jolls and Sunstein identified a fairly recent controversy that emerged in the public-health arena involving framing and the use of advertising to promote behavioral changes.<sup>180</sup> Breastfeeding advocates tangled with the baby formula industry over a public-service advertising campaign that graphically emphasized the risks of choosing not to breastfeed.<sup>181</sup> The risks presented in the campaign included a higher incidence of leukemia and childhood asthma.<sup>182</sup> One ad supported by the activists presented images of pregnant women roller-skating with a voiceover: “You’d never take risks while you’re pregnant. Why start when the baby is born?”<sup>183</sup> Representatives from the baby-formula industry blanched at this tactic and urged that the campaign present a message that emphasized the positive benefits of breastfeeding, rather than a parade of potentially terrible consequences.<sup>184</sup> Indeed, the breastfeeding advocates were trying to emphasize downside risks (losses), which people tend to value more highly, while the baby formula industry, in pushing for a softer touch, wished to emphasize the benefits, which people tend to value lower.<sup>185</sup> The

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<sup>178</sup> This path of thinking, constructed around bounded rationality, creates outcomes that are different from what one would anticipate from traditional expected utility theory. *Id.*

<sup>179</sup> See generally Amos Tversky & Daniel Kahneman, *The Framing of Decisions and the Psychology of Choice*, 211 *SCIENCE* 453 (1981).

<sup>180</sup> Jolls & Sunstein, *supra* note 6, at 206.

<sup>181</sup> Melody Petersen, *Breastfeeding Ads Delayed by a Dispute over Content*, *N.Y. TIMES*, Dec. 4, 2003, <http://www.nytimes.com/2003/12/04/business/media-business-advertising-breastfeeding-ads-delayed-dispute-over-content.html?scp=1&sq=%22breastfeeding%20ads%20delayed%22&st=cse>.

<sup>182</sup> *Id.*

<sup>183</sup> *Id.*

<sup>184</sup> *Id.*

<sup>185</sup> Jolls & Sunstein, *supra* note 6, at 206.

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two interest groups were sparring over the framing of the consequences of the decision to breastfeed.

With the Revised Guides, the FTC has implicitly recognized that “truthful narratives” are quite powerful in this consumer endorsement context as well.<sup>186</sup> Truthful narratives, like the one deployed by the breast-feeding advocates, perform a debiasing function, a non-intrusive means of guiding choices, but debiasing advocates generally think of these narratives as a positive interventional tool.<sup>187</sup> With consumer endorsements, a different view of the “truthful narrative” is presented—one where the truthful narrative could be harmful to the consumer. In fact, this view even offers a few commissioned studies to attempt to prove the harm.<sup>188</sup>

The truthful narrative in this instance communicates a remarkable story to consumers about the results that one of their peers has achieved from using a product or service. Jared Fogle told the world his story. His narrative (Subway’s narrative) was about how an obese but otherwise ordinary young man from Indiana achieved weight loss (in what appears to be a less painful way than conventional dieting) with the disciplined consumption of savory Subway products.

From a debiasing perspective, *removing* information from the marketplace and specifically, information packaged in this narrative form, demonstrates the power of a narrative in the negative. The narrative produces the framing in a vivid way, and the new regulation silences that narrative and erases the outlier reference point.

With the Revised Guides, at least in the first round of the game, no choices have been paternalistically removed from the consumer’s menu. All that has been removed is a tactic that regulators purport misleads consumers into making cognitive errors, engaging in “bad” transactions by latching on to compelling narratives. As this Article will explore further in Part III, a broad

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<sup>186</sup> *Id.* at 215.

<sup>187</sup> See generally Jolls & Sunstein, *supra* note 6; SUNSTEIN & THALER, NUDGE, *supra* note 7.

<sup>188</sup> See HASTAK & MAZIS, DIETARY SUPPLEMENTS, *supra* note 3; HASTAK & MAZIS, WEIGHT LOSS, *supra* note 3.

stroke such as this one that removes this information might constitute “overshooting,”<sup>189</sup> to use the parlance of Jolls and Sunstein. Removal of consumer endorsements might prevent “good,” social-welfare-accreting transactions from occurring. Additionally, the consumption of some goods and services yields value through the actual risk of the consumption experience *per se*. There might be something valuable to knowing that a dating service merely *could* lead to a match ending in marriage, for example. Risk is purchased everywhere. Consumers have ranges of expected outcomes for their experiences and quite often they are purchasing this range.

The broad-stroke regulatory deterrence of consumer endorsements might at best have an ambiguous impact. Framing is a tool that marketers may use to induce transactions, and certainly consumer endorsements pin the consumer around the reference point of the endorser. It does not logically follow and there is no available proof, however,<sup>190</sup> that in the *aggregate*, framing tactics by advertisers in this manner reduces social welfare. Debiasing this particular effect is of unproven social value and unknown social risk.

#### 4. Representativeness Bias

Representativeness bias presents another cognitive quirk that the Revised Guides would seem to neutralize.<sup>191</sup> People have great difficulty comprehending that certain events that may seem to occur in a cluster are actually occurring randomly.<sup>192</sup> Classic examples of this are studies of the misperception of “hot hands” in

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<sup>189</sup> See Jolls & Sunstein, *supra* note 6, at 230–31.

<sup>190</sup> The Hastak and Mazis studies were narrowly limited to three offerings, weight-loss programs, dietary supplements, and money-making opportunities. HASTAK & MAZIS, WEIGHT LOSS, *supra* note 3; HASTAK & MAZIS, DIETARY SUPPLEMENTS, *supra* note 3.

<sup>191</sup> See generally Shane Frederick & Daniel Kahneman, *Representativeness Revisited: Attribute Substitution in Intuitive Judgement*, in *HEURISTICS AND BIASES: THE PSYCHOLOGY OF INTUITIVE JUDGMENT* 49 (Thomas Gilovich, Dale Griffin & Daniel Kahneman eds., 2002).

<sup>192</sup> See SUNSTEIN & THALER, NUDGE, *supra* note 7, at 27.

basketball free throws,<sup>193</sup> the misperception of precision targeting of bombings during air-raid campaigns,<sup>194</sup> and from epidemiology, the misperception of the formation of local cancer clusters.<sup>195</sup> The human brain subconsciously makes sense of a random sample through a larger extrapolation that is part of a greater scheme. Much of stereotyping is the product of this phenomenon.

If consumer endorsers present the real, but exceptional, results that they have enjoyed with an offering, the recipients of the message may be prone to the distortions of the representativeness bias. The real, but outlier, results may be the genuine product of randomness. Presented alone, consumers may extrapolate from them the conclusion that they are more typical of the set of experiences that people will have with the offering. By chilling consumer endorsements, the Revised Guides make it difficult for advertisers to highlight the outliers, which may neutralize this bias from working in this circumstance.

### 5. Confirmation Bias

The confirmation bias describes the natural tendency of people to seek and to accept information that confirms previous perceptions and to eschew other information.

If one were to attempt to identify a single problematic aspect of human reasoning that deserves attention above all others, the *confirmation bias* would have to be among the candidates for consideration. Many have written about this bias, and it appears to be sufficiently strong and pervasive that one is led to wonder whether the bias, by itself, might

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<sup>193</sup> See generally Thomas Gilovich, Amos Tversky & Robert Villone, *The Hot Hand in Basketball: On the Misperception of Random Sequences*, 17 COGNITIVE PSYCHOL. 295 (1985); Caryn Conley & Jay Koehler, *The "Hot Hand" Myth in Professional Basketball*, 25 J. SPORT & EXERCISE PSYCHOL. 253 (2003).

<sup>194</sup> THOMAS GILOVICH, HOW WE KNOW WHAT ISN'T SO: THE FALLIBILITY OF HUMAN REASON IN EVERYDAY LIFE 19 (1991).

<sup>195</sup> SUNSTEIN & THALER, NUDGE, *supra* note 7, at 31. See also *Cancer Clusters: CDC Activities: Fact Sheet*, CENTERS FOR DISEASE CONTROL AND PREVENTION, <http://www.cdc.gov/nceh/clusters/factsheet.htm> (last visited July 30, 2010).

account for a significant fraction of the disputes, altercations, and misunderstandings that occur among individuals, groups, and nations.<sup>196</sup>

Wishful thinking pervades human decision making, and hope springs as eternal in the consumer transactional context as it does anywhere else. Cognitively, humans are predisposed to seek information that confirms or reinforces preconceived notions about their worldview.<sup>197</sup>

Consumers seeking a desirable result may grasp on to that result as the likely outcome from a certain course of action, simply because it might confirm a belief that there is a cheap, easy means to achieving a result. If a person wishes to lose weight, and an advertiser presents him with a narrative about an easy system for losing weight, along with an extremely positive actual outcome, confirmation bias should influence the person. The information that confirms the result that the weight-loss seeker wishes to be true will be accorded more heft.

Put differently, people have demonstrated that they will maintain a high evidentiary standard for acceptance of ideas or conclusions that they have a predisposition to dislike and a lower standard of proof for ideas or conclusions that they prefer. The revised approach toward consumer endorsements removes from the information sphere one of the many tools that advertisers can use to trigger the confirmation bias. Simply showing through a consumer endorsement that an offering might solve a problem or meet a need can induce a transaction—if the consumer falls prone to seeking confirmation that there is a way to solve a certain problem or meet a certain need.

Generally, debiasing through law, or in this case, through advertising regulation, can disarm a host of potentially distortive cognitive triggers, including but not limited to the ones mentioned here. However benign the regulatory intention, some negative spillover effects can result from this disarming, which this Article addresses in Part III. Any drag on the flow of information can change how players act in the marketplace. With consumer

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<sup>196</sup> Raymond S. Nickerson, *Confirmation Bias: An Ubiquitous Phenomenon in Many Guises*, 2 REV. GEN. PSYCHOL. 175, 175 (1998).

<sup>197</sup> See generally *id.* (exploring in detail the entirety of confirmation bias).

endorsements, a seemingly well-intended policy change may present some other side effects. These side effects may well be tolerable, just like a medication's side effects. But just as with medication, awareness of these side effects is necessary for evaluating whether the prescription is appropriate.

### III. POTENTIAL COSTS AND FAILURES OF THE NEW APPROACH

As noted, the removal of true information from the marketplace provides an illustration of how debiasing can lead to unanticipated results, and hints that debiasing techniques should be targeted narrowly and cautiously. Having noted the salutary effects of the consumer-endorsement debiasing effort, this section will explore three primary areas of concern, all of which have a common thread.

First, consumer endorsements effectively remove the presentation of "hope" in the marketplace and some offerings *are* hope. Removing "hope" or any offering from the marketplace runs the risk of reducing social welfare and removing choice from the marketplace. Closely related, the hard paternalism that debiasing through law tries to avoid rears its head if the elimination of consumer choice proves to be the practical result.

When the commercial information flow is chilled, particularly the flow of true information, welfare-creating, Pareto-efficient transactions that may have occurred, might fail to occur. Forcing an offering entirely out of the marketplace can create such a loss, but so can consumer uncertainty caused by a restricted flow of data. The cost of transactions lost in this manner must be considered.

Another potential effect that may result from the restriction of information in the market may be higher prices and deadweight loss. Although the impact from chilling consumer endorsements is uncertain, other restrictions in consumer markets, like a ban on disclosing price of alcoholic beverages away from the point of sale, have resulted in higher consumer prices and market disruption. Debiasing through law, toying with the information flow, and trying to improve consumer decision-making processes

can have secondary impacts of this sort. Again, this should guide the policymaker toward more cautious approaches when deploying debiasing strategies. “Nudging” requires a soft touch.

Finally, debiasing is not well equipped to address several related normative problems. Defining “good” decision making and defining “good” social outcomes will be matters for policy debate that transcend the debiasing through law toolkit. Nonetheless, to create policy, paternalistic judgments must be made about what is “good.”

With consumer endorsements, a view must be formed about the presentation and promotion of risk. Risk is naturally associated with a downside or potential losses. But risk can also embody something positive. As noted earlier, one person’s risk is another person’s hope, aspiration, or thrill. Policymakers still must make a potentially paternalistic judgment call on this dimension.

#### *A. Removing “Hope” from the Market*

The tighter regulation of consumer endorsements may remove a set of hope-based offerings from the market. The core offering may remain on the market, but without the consumer endorsement attached, the “hope” component of the offering may need to be eliminated. With a new, looming threat of civil enforcement, the costs and risks of using the consumer-endorsement marketing tactic make the approach riskier and costlier for an advertiser to deploy. This can destroy welfare if the underlying potential transaction would create welfare.

An illustration distills this point. Consider the example of a dating service. A dating service may use consumer endorsements to emphasize the number of successful matches the service has facilitated—and perhaps even the number of marriages that it has enabled. This could be effectively done through the presentation of a beautiful (or accessible) newlywed couple describing the narrative of how the site enabled their marital bliss.

This sort of presentation would deliver to the consumer a compelling narrative about the uppermost boundary of the range of outcomes sought by someone using this service to find a life partner. The range of results comprises this offering—ranging

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from mere entertainment from browsing the site to an ultimate goal (finding a date or mate). Part of the offering might be the excitement about having access to this range of outcomes. Promoting the boundaries highlights this excitement and promotes hope. Hope is part of this product. If regulation removes hope from the market, the market transaction for that hope obviously cannot occur. Less “hope” will be produced and consumed, and less welfare accordingly created.

All offerings present a range of expected outcomes from consumption or use of the offering. Some ranges are tighter than others. An offering comprised of a can of a strongly-branded popular beverage would present a very tight range of expected outcome for consumers. A new four-star restaurant might present a much broader range of expected outcomes—and this might be part of the draw for potential consumers. The thrill of the risk of trying something novel and the hope that it will surpass expectations might be part of the restaurant experience. With a chain restaurant, consumers are not purchasing the thrill of a broad range, they are purchasing a comparatively narrow range of outcome. Consumers seek more certainty rather than hopes or thrills in this instance.

If an offering in this circumstance was entirely centered on hope, and depended heavily on consumer endorsements to promote that hope, the entirety of the offering may disappear. This might be a positive social development, if the promoted offering is of dubious value, like a “make-money-from-home” system that offers outlier testimonials. If the offering retains value and transactions can yield social welfare, the effective elimination of the offering would prove socially costly. A conceivable example might lie in an *effective* weight-loss program that can only sell at scale through the use of consumer-endorsement marketing tactics.

Taking hope “off the market”—with hope embedded in part of an offering or the entirety of an offering—will eliminate some welfare-producing transactions. Chilling the practice of describing hope through the narrative of a consumer endorsement can lead to that result. Broadly debiasing through law can similarly yield to results of concern. Addressing this particular problem in a more targeted way may prove more socially valuable, though the regulatory enforcement effort may be more complex and

challenging. This type of regulatory brain surgery must be performed with care because the consequences can prove unpredictable.

The consumer-endorsement restrictions also put downward pressure on social welfare simply by removing information from the marketplace. As the next section explains, when true information is removed from the marketplace, uncertainty looms, parties are less likely to transact, and transactions fail.

### *B. The Cost of Failed Transactions*

Any regulatory intervention that removes true information from the marketplace should anticipate that the market will put a damper on the communications that enable transactions to happen. Debiasing through law may seem more nuanced, but tampering with information in a broad way to improve consumer decision making may have repercussions in the marketplace.

In the basic advertising scenario, banning deceptive or misleading information from the marketplace should prevent resource misallocation. Before an advertisement-influenced transaction, consumers would be willing to transact and part with something of value for something else to which they assign greater subjective value.<sup>198</sup> If an advertisement conveys misleading or false information or makes misrepresentations, this false conveyance tampers with the consumer's pre-transaction subjective valuation. If the transaction happens, the consumer will receive less than what was expected. This leads to a resource

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<sup>198</sup> Adam Smith wrote:

Whoever offers to another a bargain of any kind, proposes to do this: Give me that which I want, and you shall have this which you want, is the meaning of every such offer; and it is in this manner that we obtain from one another the far greater part of those good offices which we stand in need of. It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our own necessities but of their advantages.

ADAM SMITH, *THE WEALTH OF NATIONS* 18 (The Univ. of Chicago Press 1976) (1904).

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misallocation, deadweight loss, diminished social welfare, and unjust outcomes.

A regime with no regulation of advertising, that of pure caveat emptor or lax enforcement of current laws and regulations, would prove economically chaotic. Transactions costs would rise, as consumers would need to perform more due diligence on those with whom they transact.<sup>199</sup> Brand identity and professional licensing would matter more—even more than they do currently—in markets as consumers would seek heuristics for counterparty trustworthiness.<sup>200</sup> In an environment of increased uncertainty about the validity of claims, one would expect consumers to change their purchase equation. Consumers would not be willing to pay as much for an offering made with uncertain representations. The uncertain representations would translate into a lower expected subjective value by the consumer for the offering.

Generally, the transactions costs would rise because of the consumer uncertainty—and because of the extra information gathering required to build trust in the offering. The current system of policing advertising aims to reduce these transactions costs by purifying information. The FTC, the states, other advertising regulators like the Food and Drug Administration (FDA), and private enforcement mechanisms<sup>201</sup> work together toward this goal—reducing social costs by addressing dishonesty.

George Akerlof's renowned article, *The Market for*

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<sup>199</sup> Permitting claims to float in the market without the confidence of a degree of substantiation would prove socially expensive. “[T]he concern with unsubstantiated claims is that they force consumers to bear the risk . . . . Consumers must either verify the claim themselves—which will be prohibitively expensive—or else purchase the product without knowing whether the unsubstantiated claim is reliable or not.” Craswell, *supra* note 12, at 123.

<sup>200</sup> Akerlof, *supra* note 80, at 499–500. For a brief discussion of the role of brand, see Beales et al., *supra* note 46, at 502.

<sup>201</sup> E.g., through civil remedies afforded by the Lanham Act, Section 43(a)(1)(B). Softer private-enforcement mechanisms also include industry self-regulation and codes, though these mechanisms have limited public benefit. See generally Herbert J. Rotfeld, *Power and Limitation of Media Clearance Practices and Advertising Self-Regulation*, 11 J. PUB. POL'Y & MARKETING 87 (1992). See also generally Jean J. Boddewyn, *Advertising Self-Regulation: True Purpose and Limits*, 18 J. ADVERTISING 19 (1989).

“Lemons,”<sup>202</sup> presented a “structure . . . for determining the economic costs of dishonesty.”<sup>203</sup> Akerlof held out the individual used car market<sup>204</sup> as an example of a market where transactions fail due to perceived information asymmetry. Sellers have the best information about the true value of their own used cars. The sellers know more about the true condition, history, and performance of their own vehicles. Buyers do not have access to that information and therefore will discount the price that they will be willing to pay for the used car, because they do not have complete trust in sellers. Sellers expect the “true” value for the car, but buyers, in their uncertainty, won’t pay that value. Often, this gap yields a transactional failure, as the parties cannot reach agreement on price.<sup>205</sup>

Given that wealth and utility are created when parties successfully exchange goods, this “lemon” phenomenon points toward a common scenario where an information gap obstructs welfare from being created. When applied to advertising regulation, Akerlof’s findings have multiple implications. Eradicating deception from advertising leads to economic certainty, efficiency, and just results. Goods and services are exchanged at their stated qualities and subjective expectations from the exchange are met. Further, confidence and trust in the system at large is restored, furthering an environment hospitable for exchange.

However, as would be the case with most regulatory activity, overzealous or overbroad rulemaking and enforcement in combat

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<sup>202</sup> See Akerlof, *supra* note 80, at 488 (examining the costs incurred as a result of mistrust and information asymmetry).

<sup>203</sup> *Id.* at 488.

<sup>204</sup> Long before entities like CarFax emerged to bridge the information gap in this industry by detailing the title records of all automobiles. See CARFAX, [www.carfax.com](http://www.carfax.com) (last visited Dec. 27, 2010). For a brief history of CarFax, see Lisa Wade McCormick, *CARFAX History*, CONSUMER AFFAIRS.COM (Oct. 10, 2006), [http://www.consumeraffairs.com/news04/2006/10/carfax\\_history.html](http://www.consumeraffairs.com/news04/2006/10/carfax_history.html).

<sup>205</sup> See Akerlof, *supra* note 80, at 204 (exemplifying the model by utilizing automobiles as an example). Note also that certified, pre-owned auto dealer offerings and third-party warranties have emerged to bridge or effectively discount the trust gap. See *Certified Pre-Owned Vehicles Programs*, EDMUNDS.COM, <http://www.edmunds.com/certified-cars/certified-pre-owned-vehicle-programs.html> (last visited Jan. 26, 2011).

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of deceptive advertising would potentially produce deleterious effects just as economically damaging as under-enforcement. When providers of products and services are compelled to disclose less information—or banned from disclosing true information—because of the risk that they may run afoul of new and aggressive regulation, consumer uncertainty about the nature of the offering rises. When consumers know less about an offering, they may be less likely to transact. Consumers would adjust downward the value that they are willing to exchange for the offering. Producers would supply less as a result of a diminished expected return. Deadweight loss would increase.

The chilling of information exchange reduces the ability of the buying and selling parties to communicate at a distance about the offering, thereby reducing the potential for exchange. If the information is truly false and deceives, the exchange should not take place. However, the risk of punishment for stepping over the line may prevent advertisers from treading anywhere near the acceptable line to ensure compliance. Larger, established entities may preserve their competitive position at the expense of smaller entities in this environment. Those with established reputations should prevail under the notion of trust.<sup>206</sup> Even though debiasing through law may appear to be relatively unobtrusive and oriented toward improving individual decision making, *in this particular instance* the secondary effects may hit the market more broadly, leaving the welfare impact open to question. Removing true information can remove a true avenue of valuable commercial communication.

*C. Unintended Consequences: Price Effects*

Debiasing through law, advertising regulation, and specifically, the removal of true information from the marketplace, can have an upside in correcting consumer biases. Potential downsides lurk,

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<sup>206</sup> Note how entities tend to disclose when they were established as a means of presenting durability and trustworthiness. For instance, the author's law school's website advertises that the institution was established in 1883. COLLEGE OF LAW – WILLAMETTE UNIVERSITY, <http://www.willamette.edu/wucl/> (last visited Jan. 25, 2011).

however, with debiasing, just as they would with traditional paternalistic regulation that directly eliminates consumer choices.

Here, this Article briefly discusses the subtle price distortions that could result from the implementation of the Revised Guides. Enhanced regulation of advertising could simply lead to less advertising because of the increased cost of advertising *per se*. If consumer endorsements are the preferred route to marketing an offering, eliminating that tactic will force the advertiser to use a second-best approach. This second-best approach will likely be less effective, all things being equal, and therefore, more expensive. If all marketers had to play by the same rules, consumers may bear some of this burden. Generally, “if . . . [increased] advertising regulation also succeeded in reducing the extent of advertising by raising the cost of advertising, firms in many industries might have an incentive to seek such regulation because it would result in less competition and higher retail prices.”<sup>207</sup> The resulting decrease in social welfare and increase in deadweight loss could provide yet another example of an unanticipated secondary effect from debiasing.

Further, economists have observed in several studies that “the prices of goods and services in places that restrict advertising tend to be higher than those in places that do not restrict advertising.”<sup>208</sup> These linkage studies between advertising and pricing have ranged across consumer goods, from eyeglasses and drugs to alcohol.<sup>209</sup> Restrictions on information in the marketplace “often tend to inhibit competition, with consequent efficiency losses.”<sup>210</sup>

Though it may be difficult to predict what will happen to retail

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<sup>207</sup> Zeynep K. Hansen & Marc T. Law, *The Political Economy of Truth-in-Advertising Regulation During the Progressive Era*, 51 J.L. & ECON. 251, 256 (2008).

<sup>208</sup> *Id.* at 255.

<sup>209</sup> See, e.g., *id.*; Jeffrey Milyo & Joel Waldfogel, *The Effect of Advertising on Prices: Evidence in the Wake of 44 Liquormart*, 85 AM. ECON. REV. 1081 (1999); John E. Kwoka, *Advertising and the Price and Quality of Optometric Services*, 74 AM. ECON. REV. 211 (1984); Lee K. Benham, *The Effect of Advertising on the Price of Eyeglasses*, 15 J.L. & ECON. 337 (1972); John F. Cady, *An Estimate of the Price Effects of Restrictions on Drug Price Advertising*, 14 ECON. INQUIRY 493 (1976).

<sup>210</sup> Beales et al., *supra* note 46, at 514.

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pricing in the industries heavily affected by the Revised Guides, an empirical trail heightens suspicion that the restriction of information may yield unanticipated changes. The new consumer-endorsement approach does not restrict display of *prices* but it does effectively restrict a major form of information from reaching the marketplace. Debiasing may seem non-intrusive and “soft” but the impact can be unpredictable and not always positive for social welfare.

*D. The Stubborn Normative Question*

Advocates of debiasing through law claim the approach to be comparatively unintrusive to traditional regulation, less paternalistic, and protective of ultimate consumer choice. To have meaning, these expressed values must be colored by the real goals of any debiasing effort, which by and large, appear to be about minimizing risk or tightening the range of expected transactional outcomes. Generalizing this approach across the broad range of commercial transactions can be normatively challenging—the risks involved with different types of transactions are situationally unique.

Is it always correct to minimize risk through disclosure or restriction of information? As noted, somewhere in every consumer transaction, hope itself is for sale. In routine transactions, the result rarely diverges from the expected range. In some transactions (tickets to a new Broadway mystery musical, for example), the range of expected results might be part of the sought experience. Minimizing risk and closing the range of expectations through a mandatory disclosure about the mystery ending of the mystery musical may prove socially destructive, though it would in some sense protect consumers from seeing something unwanted.

As modern American political strategists are deftly aware, if “hope” can be credibly attached to a political purchase, voters might just buy it.<sup>211</sup> Do voters expect that all of their hopes will

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<sup>211</sup> Governor Bill Clinton of Arkansas closed his 1992 Democratic Presidential Nomination speech by declaring (in a wrap-around reference to his birthplace of Hope, Arkansas) that he “still believe[d] in a place called Hope.” Bill Clinton, Governor, Acceptance Speech to the Democratic National

truly be realized? Lotteries market themselves this way.<sup>212</sup> In the gambling and lottery instances, *rational* consumers would know that “the house” will win, on average, but they are often buying the thrill.

Sometimes consumers contract for hope and are willing to accept a certain amount of disappointment. They are expecting to purchase a set of probabilities. This applies to staying at unfamiliar hotels, buying a new lawnmower, or buying an article of clothing. Consumers may know that goods and services are not perfect but the information that it worked for someone like them gives them the hope to try it. What is normatively wrong with offering that range of expectations? Advocates of debiasing still must wrestle with the questions that old-fashioned regulators must answer—namely, which risks are acceptable to expose to consumers and which are not? Debiasing addresses this question by intervening in the decision-making process and paternalistic regulation addresses this question by directly removing the risky choices from the marketplace.

This is not to say that regulators should surrender in their efforts to match appropriate venues and approaches for managing consumer risk. Consumers demonstrate emotional discomfort with the risks associated with certain transactions, particularly high-stakes transactions. This can diminish the willingness to transact.<sup>213</sup> As noted through the implications of Akerlof’s work, and in the discussion of social welfare, promoting Pareto-superior transactions should be a policy goal. Policymakers need to sort through these risk-involved scenarios on a granular level but must be careful not to develop a sweeping view that seeks to mitigate all risk—because not all risks are the same.

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Convention (Jul. 16, 1992) (transcript *available at* <http://www.4president.org/speeches/billclinton1992acceptance.htm>).

<sup>212</sup> See, e.g., MEGA MILLIONS, <http://www.megamillions.com> (last visited Aug. 13, 2010) (promoting the lottery with a “Your Dream Here” theme).

<sup>213</sup> Daniel McFadden, Free Markets and Fettered Consumers, AEA Presidential Address (Jan. 7, 2006), at 4–6 (transcript *available at* <http://elsa.berkeley.edu/~mcfadden/aea/presidentialaddress.pdf>).

## IV. RECOMMENDATION TO POLICYMAKERS

Policymakers must be selective and careful when they intervene and engage in debiasing through law. Advertising provides the perfect backdrop for assessment of debiasing techniques.

The new approach to consumer-endorsement regulation, as put forth in the Revised Guides, provides an enlightening case study. A sweeping approach toward concealing true information about consumer experiences could have a different impact across different consumer markets. Consumer-endorsement regulation, though controlling a narrow information tactic, could be tightened to address certain industries more carefully.

Industry-targeted regulation of information presentation might be most sharply demonstrated with the pharmaceuticals markets. For example, the FDA accorded special attention to direct-to-consumer advertising of pharmaceuticals, as spending on this form of advertising in this market grew from \$12 million in 1989 to \$2.38 billion in 2001.<sup>214</sup> A broad array of guidelines and rules were adopted prior to and during this period, specific to direct-to-consumer pharmaceuticals advertising because of the unique risks presented by the products in this marketplace.<sup>215</sup> The products are complex, confusing, and present large consequences resulting from the user experience. Information about the products may be entering from a variety of authoritative avenues, like physicians and pharmacists. This is a market where we would want risk to be minimized by enabling people to use the products in an informed manner. Finding clear answers proves difficult. But comparatively, pharmaceuticals may prove to be an area more worthy of debiasing attention than the sandwiches Jared Fogle promoted for Subway.

Consumer-endorsement regulation shows us that some industries require more attention than others and that overregulation of consumer endorsements in certain industries can

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<sup>214</sup> C. Daniel Mullins & Francis B. Palumbo, *The Development of Direct-to-Consumer Prescription Drug Advertising Regulation*, 57 FOOD & DRUG L. J. 423, 423 (2002).

<sup>215</sup> See generally *id.*

be welfare-destroying.<sup>216</sup> This provides a lesson more broadly for regulators who intend to use the new tools highlighted in the popular book, *Nudge*,<sup>217</sup> and who intend to apply the concepts of debiasing. Selectively deploying debiasing strategies proves key.<sup>218</sup> This type of informational intervention should be performed with caution and elegance, given the intersections between the uncertainties of markets and human behavior.

## V. CONCLUSION

Debiasing through law can be a powerful and creative approach toward regulation and increasing consumer welfare, but application requires care. The revised FTC approach to consumer-endorsement regulation provides a cautionary tale about a seemingly benign regulation that may ultimately prove to sweep too broadly.<sup>219</sup> If regulators had attempted to pursue specific industries or markets, rather than chilling an entire tactic, total welfare—and consumer welfare—could potentially have been further enhanced.

Debiasing approximates much of the law of advertising regulation, as Jolls and Sunstein note. The regulation, as reflected in the Revised Guides, illustrates an approach where debiasing could have been effected more artfully, either through an industry or product-oriented approach. Though the FTC seemed to be

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<sup>216</sup> Treating consumer endorsements monolithically ignores the notion that some consumer endorsements may be more deceptive than others. Craswell “has suggested that the laws against deceptive advertising could best be understood as applying a form of cost-benefit analysis to the interpretation of advertisements.” Richard Craswell, *Regulating Deceptive Advertising: The Role of Cost-Benefit Analysis*, 64 S. CAL. L. REV. 549, 550 (1985). Craswell advocates applying a case-specific approach toward advertising regulation, inquiring into the “total injury” that an advertisement might cause, and whether the advertiser could have taken affirmative steps to prevent the injury. Craswell describes his approach as similar to the “Learned Hand test.” *See generally id.*

<sup>217</sup> SUNSTEIN & THALER, *NUDGE*, *supra* note 7.

<sup>218</sup> Fortunately, the FTC has retained enforcement discretion, but unfortunately, the warning shot from the Revised Guides was broadcast without discrimination.

<sup>219</sup> The Revised Guides are still very new. This Article can only speculate about the future potential impact with the tools available.

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aiming to eliminate or heavily burden a tactic, in an effort to improve consumer decision making, it effectively may have taken products off the market by “overshooting.” Consumer welfare in this instance could have been maximized with a more careful approach, one driven by typical cases, not the worst cases like the weight-loss industry.

This Article can draw several conclusions from the revised consumer-endorsement regulation that can be applied more generally to the underlying principles of debiasing through law. The revised consumer-endorsement regulations will likely increase the cost of inducing transactions in the arenas where this advertising is most commonly used, reducing welfare in some markets. In industries or markets that require a bit more protection for the consumer, like pharmaceuticals, the restriction of true information provided by real consumers about their experience might be welfare-enhancing. If laid down broadly, regulations such as these could have a mixed impact on social welfare, depending on how the regulation affects the variety of transactions that lead consumers to expect a range of results.

The key lesson for policymakers from the consumer endorsements example is that great care should be taken when tampering with the market information flow. Debiasing through law focuses on using information to enhance decision-making, which can certainly happen. But the potential downsides and side-effects are as real as the downsides of traditional, paternalistic regulation, and should not be discounted.