THE CASE FOR CONSUMER-ORIENTED CORPORATE GOVERNANCE, ACCOUNTABILITY AND DISCLOSURE

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It is legally impossible to offer securities to the public without giving thorough and exhaustive disclosures, allowing potential buyers to compare such securities with competing investment options. But it is legally possible to offer the public any other product under the wide wings of the freedom of commercial speech.

This article calls for corporate informational accountability towards consumers by setting affirmative disclosure standards and requirements on corporations that offer products or services to the public. The article compares product choice to investment allocation, arguing that the choice process, product complexity, and risks are often higher for consumers than for investors. This article also compares the consumer product market to the capital markets, showing that, while investors are aided in their analysis of information by investment advisors and other intermediaries, consumers typically undertake their product research and make their choices unaided. Thus, despite the abundance of commercial speech, markets fail to provide consumers with the requisite information to make an efficient choice, and they overwhelm consumers with an overload of information.

Therefore, this article argues that the informational rights of consumers should be as well protected as the informational rights of investors. Corporate law is established as the doctrinal setting for product disclosures, offering an extension of the scope of current corporate governance by applying stakeholder theory to consumers as corporate members. Finally, corporate law accountability standards are shown to be superior to the current contractarian view towards accountability for product information. Three essential standards for corporate disclosure accountability towards consumers are suggested, including a duty of

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materiality, accessibility, and concise disclosures.

INTRODUCTION

When offering securities to the United States public, corporations must comply with an exclusive informational regime that allows speech only within the uniform boundaries determined by the Securities & Exchange Commission.[1] Corporations must use a standardized method for financial audits and reports, and disclose in plain and simple English any material fact of interest to a potential buyer.[2] But when offering the public other products, corporations are entitled to speak freely to consumers as they wish, under the wide wings of the freedom of commercial speech, constrained only by the ban on misrepresentation and fraud.[3] Why are

1. The Securities Act of 1933 ("the 1933 Act"), 15 U.S.C. § 77a (1982), regulates the public offering and sale of securities in interstate commerce and requires a prospectus designed to provide all material information necessary to investors to fully assess the merits and risks of the purchased security. The Securities Exchange Act of 1934 ("the 1934 Act"), 15 U.S.C. § 78a (1982), requires all registrants to file periodic reports with the Securities Exchange Commission (SEC) in electronic format through the Electronic Data Gathering, Analysis, and Retrieval (EDGAR) system. *See also* JOEL SELIGMAN, THE TRANSFORMATION OF WALL STREET 73-100 (3d ed. 2003) (observing the events and hearings that shaped the development of the early securities acts and markets following the depression); William O. Douglas, *Protecting the Investor*, 23 YALE L. REV. 521, 522 (1934) (criticizing the Securities Act for, among other things, assuming that the public's intake of information will give investors needed protection).

2. Plain English Disclosure, Securities Act Release No. 7497, Exchange Act Release No. 39,593, Investment Company Act Release No. 23,011, 63 Fed. Reg. 6370 (Feb. 6, 1998). The SEC has legal authority to establish financial accounting and reporting standards for publicly held companies under the 1934 Act.

3. The Supreme Court demonstrates an eclectic approach to the protection of commercial speech, subjecting regulation interfering with free advertising to various degrees of constitutional scrutiny. The Supreme Court has upheld such regulation, but has also struck such regulation down based on First Amendment protection. *See, e.g.,* Rubin v. Coors Brewing Co., 514 U.S. 476, 491 (1994) (holding unconstitutional under the First Amendment the Federal Alcohol Administration Act, which prohibited beer labels from displaying alcohol content); City of Cincinnati v. Discovery Networks Inc., 507 U.S. 410, 430-31 (1993) (striking down a ban on the placement of commercial newsracks on city streets and holding that the City had not met its burden of establishing a reasonable fit between its legitimate interests in aesthetics of streets and the means it chose to serve these interests); Edenfield v. Fane, 507 U.S. 761, 774 (1993)(holding unconstitutional under the First Amendment the Florida Board of Accountancy's rule that prohibited accountants from engaging in direct, in-person, uninvited solicitations). The resulting policy differentiates the constitutional protection of commercial speech into two subcategories. The first regards regulation of false or misleading commercial speech, and the second regards regulation of commercial speech in all other cases. The purpose of freedom of commercial speech is to protect the dissemination of truthful commercial information, in an effort to ensure that the public is "intelligent and well informed." Virginia Bd. of Pharmacy v. Virginia Citizens Consumer Council Inc., 425 U.S. 748, 765 (1976). The Supreme Court does not typically extend constitutional protection to restrictions of commercial speech designed to achieve ends other than the dissemination of truthful information. *See, e.g.*, 44 Liquormart Inc. v. Rhode Island, 517 U.S. 484, 489 (1996) (striking down a Rhode Island law that banned advertisement of alcohol prices in an effort to reduce demand for alcohol). While the First Amendment is now considered to protect the dissemination of truthful and non-misleading commercial communications about lawful products and services, the State is authorized to regulate potentially deceptive or overreaching advertising more freely than other forms of

investors better protected than consumers? Why does our legal system choose to provide consumers of investments better information to secure their freedom of choice?

The answers lie in the limited scope of current corporate law. Consumers are not considered corporate stakeholders entitled to informational accountability. Rather, consumers are a weak and voiceless party to a contractual relationship with the corporate seller. The consumer capacity is therefore restricted by the terms of the contract, which is determined unilaterally by the seller. In 2014, corporations offering merchandise or services to the public enjoy the status of small merchants in the archaic marketplace. They need to provide consumers with information only to the extent necessary to render the agreement voluntary, as required under contract law. Consumers of securities, on the other hand, are labeled "investors" and are considered prominent corporate stakeholders. Offering securities to the public invokes an informational regime that requires periodic and immediate uniform disclosures, including all material information in plain English, accompanied by standardized financial audits and reports.[4]

Current corporate law does not acknowledge consumers as legitimate corporate stakeholders and does not impose any duty towards consumers. Corporate accountability is reserved to the shareholders or to the corporation itself as a whole.[5] Board members are agents appointed by

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speech. The resulting constitutional scrutiny standard regarding regulation of such speech is minimal, "less than strict" review. *Id.* at 489 (adopting the "less than strict" standard of review for commercial speech). *See generally* Florida Bar v. Went For It, Inc., 515 U.S. 618, 634-35 (1995) (upholding a state bar rule making lawyers wait thirty days before soliciting legal business from accident victims or their families by direct mail); United States v. Edge Broadcasting Co., 509 U.S. 418, 428-29 (1993) (upholding against a First Amendment challenge a federal statute prohibiting a radio station licensed in North Carolina, a non-lottery state, from broadcasting advertisements to another state's lottery); Posadas de Puerto Rico Associates v. Tourism Co. of Puerto Rico, 478 U.S. 328, 345-56 (1986) (upholding a ban on the advertisement of casino gambling to residents of Puerto Rico, reasoning that the power to regulate such commercial speech was a derivative of the greater power to ban gambling); Virginia State Bd. of Pharmacy, 425 U.S. at 770 (holding a statute that declared it unprofessional conduct for a licensed pharmacist to advertise the prices of prescription drugs as unconstitutional, based on First Amendment protection); Bigelow v. Virginia, 421 U.S. 809, 825-26 (1975) (holding it an error to assume that commercial speech is not entitled to First Amendment Protection or that it lacks value in the marketplace of ideas). *See also* John Paul Stevens, *The Freedom of Speech*, 102 YALE L.J. 1293, 1300 (1993) (noting how First Amendment law has evolved into an elaborate construction of specific judicial decisions). Previously, fraudulent or misleading commercial speech was altogether unprotected by the First Amendment, and therefore its regulation was not subject to constitutional review. *See* Kathleen M. Sullivan, *Cheap Spirits, Cigarettes and Free Speech: The Implications of 44 Liquormart*, 1996 Sup. Ct. Rev. 123, 146 (1996).

4. *See supra* notes 1-2.

5. *See* Guth v. Loft, Inc., 5 A.2d 503, 510 (Del. 1939) ("Corporate officers and

shareholders, and their corporate involvement is focused, and often limited, to the corporation's financial performance.[6] Board members of the corporation typically do not receive information about product disclosures and are not considered to be in charge of the corporation's relationship with its consumers. Indeed, a corporation's board members, who are personally accountable for financial reports under several regimes, often approve disclosures to investors under the federal securities laws.[7] However, direct accountability neither applies to consumers nor accompanies product disclosures.

Regulation favors investors over consumers. For investors, the SEC provides information management services and has established uniform legible standards for disclosure, which are accessible through a Web-based platform for comparing alternative corporate investments.[8] No such regulatory service is available for consumer products. Investors' rights to information are provided *ex ante* to the moment of purchase, whereas consumers' rights to information are generally left to court rulings from cases of misrepresentation, *ex post* to the transaction date.

What distinguishes consumers from investors? Mainly, the purpose of the purchase: consumers shopping for higher returns on their investments are legally protected and secured, whereas consumers shopping for other products or services are left to bargain for information under their contracts of purchase. Indeed, a buyer's status as an investor or as a consumer forms

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directors . . .[,] [w]hile technically not trustees . . . stand in a fiduciary relation to the corporation and its stockholders."); *see also* Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919) (noting that directors are employed and a corporation is organized primarily for the profit of the stockholders).

6. The following information is typically provided to the directors of publicly held companies: monthly, quarterly, and annual financial statements; cash flow, capital and operating budgets; materials on business and financial aspects of major proposed actions such as mergers, sales of securities, or investment in new plants; salary and pension information, in general terms; information on major litigation by or against the corporation; information on labor negotiations; copies of important documents filed with government agencies, and important press releases; an agenda for the Board meeting, with minutes of the past meeting; analyses of the company done by outside sources, and information about the industry; perhaps, manufacturing or marketing data; and tax information.). *Session Four: The Board of Directors' Access to and Use of Information*, 6 J. COMP. BUS. & CAPITAL MARKET L. 243, 252 n.9 (1984) Directors of privately held companies would receive the same sort of information, especially the information in categories (a)-(c). *Id*.

7. *See* Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, 116 Stat. 745 (codified in scattered sections of 11, 15, 18, 28 and 29 U.S.C.) (requiring responsibility for corporate actions in a variety of circumstances, including financial reports).

8. *See Filings & Forms*, U.S. SECURITIES AND EXCHANGE COMMISSION, http://www.sec.gov/edgar.shtml (last visited Sept. 14, 2014) (providing that all companies, foreign and domestic, are required to file registration statements, periodic reports, and other forms electronically through EDGAR).

a clear dichotomy of informational rights. The U.S. Supreme Court has considered requests for product information based on buyers' motivation,[9] but has denied informational rights to consumers who were not categorized as investors and who lacked investment motivation in their purchase. Consumption motivation is our system's justification for denying product information to consumers of real life essentials and for eliminating their freedom of choice.[10]

9. A few cases demonstrate the significance corporate law attaches to investors rather than consumers. In *Securities & Exchange Commission v. W.J. Howey Co.*, the respondent offered units of citrus grove development coupled with a contract for cultivating, marketing and remitting net proceeds to the investor. 328 U.S. 293, 294 (1946). Each customer was offered both a land sales contract and a service contract, after being told that it was not feasible to invest in the grove unless a service contract is made. *Id.* at 295. The land sale contract provided a uniform contract price per acre or fraction thereof, varying in amount only with the number of years the plot had been planted with citrus trees. *Id.* The service contract gave possession over the land to an affiliated party of the seller, where the company was accountable only for an allocation of the net profits based on a check made at the time of picking. *Id.* at 296. The purchasers were, for the most part, non-residents of Florida, predominantly business people who lacked the knowledge and equipment to cultivate citrus groves. *Id.* The Securities Exchange Commission claimed that the transaction constituted an "investment contract" subject to the Securities Act in order to base disclosure requirements on the seller. *Id.* at 297-98. If the transaction was not labeled an investment contract, no disclosure requirement was necessary. *Id.* Likewise, in *United Housing Foundation, Inc. v. Forman*, a housing cooperative in New York City offered apartments through shares of stock that were explicitly tied to the apartment. 421 U.S. 837, 842 (1975). The respondents claimed the Information Bulletin that accompanied the transaction failed to disclose several critical facts. *Id.* at 844. One test applied by the Court of Appeals was the expectation for profits: to be considered for enhanced disclosure requirements, the purchase should be motivated by the prospect of returns on investment rather than the use or consumption of the item purchased. *Id.* at 851-53. The Supreme Court concluded that the investors were attracted solely by the prospect of acquiring a place to live and not by the financial returns of their investment, and hence could not benefit from securities disclosure requirements. *Id.* at 853. Finally, in *Reves v. Ernst & Young*, the Supreme Court rejected the *Howey* approach to determining whether an instrument is "an investment contract," only to adopt the "family resemblance" test of a security, applying the same motivation examination, where courts are required "to assess the motivations that would prompt a reasonable seller and buyer to enter into it." 494 U.S. 56, 64 (1990). The Court stated:

> If the seller's purpose is to raise money for the general use of a business enterprise or to finance substantial investments and the buyer is interested primarily in the profit the note is expected to generate, the instrument is likely to be a "security." If the note is exchanged to facilitate the purchase and sale of a minor asset or consumer good, to correct for the seller's cash-flow difficulties or to advance some other commercial or consumer purpose, on the other hand, the note is less sensibly described as a "security.

Id. at 66. *Howey*, *Forman*, and *Reves* demonstrate an unbearable result from the perspective of this Article. There is no sound justification for excluding consumers from disclosure rights based on their consumption motivations. The court is working under the assumption that only investors should be entitled to information accountability standards.

10. *See W.J. Howey Co.*, 328 U.S. at 300 (explaining that securities laws apply when

Legal literature widely views a corporation as a hierarchy of shareholders, board members, and management, where each layer is serving as an appointed agent of the former layer.[11] Shareholders appoint the members of the board, who in turn appoint a management team to manage the shareholders' assets held by the corporation.[12] Most corporate law scholarship discusses mechanisms to reduce the agency costs accompanying this corporate structure, aiming to increase shareholder value stemming from the corporation: the ultimate purpose of corporate law.[13] A large body of literature focuses on corporate disclosure duties typically imposed in order to enhance shareholder participation and empowerment in the otherwise agent-based management.[14] Most of this

investors "are attracted solely by the prospects of a return on their investment" and that the laws do not apply when purchasers are motivated "to occupy the land or to develop it themselves"); *see also Reves*, 494 U.S. at 64, *aff'd*, Reves v. Ernst & Young, 507 U.S. 170 (1993); Underhill v. Royal, 769 F.2d 1426, 1431 (9th Cir. 1985), *overruled by* Reves v. Ernst & Young, 507 U.S. 170 (1993) (using an approach focusing on investment-like properties, certain promissory notes were classified as securities); Exch. Nat'l Bank of Chi. v. Touche Ross & Co., 544 F.2d 1126, 1137-38 (2d Cir. 1976) (holding that certain notes can be classified as securities within the federal securities laws, relying in part on the commercial-investment dichotomy used in classification).

11. Viewing the shareholder franchise as a key mechanism for keeping boards accountable is an essential and well-established mechanism of corporate law, documented in the literature as well as in court opinions. *See* Blasius Indus., Inc. v. Atlas Corp., 564 A.2d 651, 659 (Del. Ch. 1988) (discussing the "central importance of the [shareholder] franchise to the scheme of corporate governance"); Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 959 (Del. 1985) ("If the stockholders are displeased with the action of their elected representatives, the powers of corporate democracy are at their disposal to turn the board out."). For a leading analysis of the faults of this apparent corporate democracy, see Lucian A. Bebchuk, *The Myth of the Shareholder Franchise*, 93 VA. L. REV. 675 (2007). For a leading discussion of management-board relationships as principal-agent, see Lucian A. Bebchuk & Jesse M. Fried, *Paying for Long-Term Performance*, 158 U. PA. L. REV. 1915 (2010).

12. Shareholders who are displeased with their board can nominate director candidates and then solicit proxies for them. *See* Robert C. Clark, Corporate Law 105 (1986) (outlining statutory authority for shareholder removal of corporate directors); Lucian A. Bebchuk, *The Case for Increasing Shareholder Power*, 118 Harv. L. Rev., 833, 837 (2005) ("In theory, incumbents who fail to initiate a change that shareholders view as value-increasing will be ousted in a proxy contest by a team promising to make the value-enhancing change.").

13. Lucian A. Bebchuk, *Making Directors Accountable*, HARVARD MAG., Nov.-Dec. 2003, at 29.

14. *See e.g.*, Roberta Romano, *Empowering Investors: A Market Approach to Securities Regulation*, 107 YALE L.J. 2359, 2373-80 (1998) (providing a historic perspective and rationale for the disclosure requirement); Roberta Romano, *The Need for Competition in International Securities Regulation*, 2 THEORETICAL INQ. L. 387, 401-07 (2001) (stating that disclosure duties provide protection for investors and discussing the need to establish clear rules for international securities transactions); Merritt B. Fox, *Securities Disclosure in a Globalizing Market: Who Should Regulate Whom*, 95 MICH. L. REV. 2498, 2533-50 (1997) (illustrating the benefits from greater disclosure, including fairness for the investors,

literature focuses on the mandatory nature of disclosure duties towards investors and their underlying justification.[15]

The call for including consumers as corporate stakeholders and for imposing corporate informational accountability towards consumers rests on the observation that investors are not the only group that may provide value to corporate production and thus are not the only group to whom the corporation owes value.[16] Rather than viewing the corporation as property of its shareholders, stakeholder theory views the corporation as a set of relationships between customers, suppliers, employees, financiers (stockholders, bondholders, banks, etc.), and communities.[17] Under the stakeholder approach, the role of the board of directors is to manage and shape those relationships and allocate resources and liabilities among different stakeholder groups.[18] Blair and Stout suggest a "team production" theory of corporate law, wherein corporations are legal entities forming a platform for sharing rights in a joint product created based on the input of all team members: financiers, investors, employees, suppliers, customers and others.[19] Accordingly, the board of directors becomes a "mediating hierarchy," and board members become coordinators of team members'

investment risk reduction, and efficient allocation of resources). *Cf.* Marcel Kahan, *Securities Laws and the Social Costs of "Inaccurate" Stock Prices*, 41 DUKE L.J. 977, 1034-35 (1992) (discussing macroeconomic impact of sudden market corrections after previously undisclosed information goes public); Allen Ferrell, *The Case for Mandatory Disclosure in Securities Regulation Around the World*, 2 BROOK. J. CORP. FIN. & COM. L. 81 (2007) (advocating mandatory, rather than market-based disclosure requirements).

15. *See generally* JAMES D. COX, ROBERT W. HILLMAN & DONALD C. LANGEVOORT, SECURITIES REGULATION: CASES AND MATERIALS 250 (2009) (citing James D. Cox, *Regulatory Duopoly in U.S. Securities Markets,* 99 COLUM. L. REV. 1200, 1230-1232 (1999) (discussing alternative viewpoints on which regulatory bodies are best equipped to set and enforce mandatory disclosure requirements)).

16. *See, e.g.*, R. EDWARD FREEMAN ET AL., STAKEHOLDER THEORY: THE STATE OF THE ART 5-6 (2010) (suggesting relationships between a business and groups affecting or affected by it as unit of analysis); LYNN STOUT, THE SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC 38 (2012) (stating that stakeholders contract with, rather than own, corporations and "corporations own themselves"); Thomas Donaldson & Lee E. Preston, *The Stakeholder Theory of the Corporation: Concepts, Evidence, and Implications*, 20 ACAD. MGMT. REV. 65, 68 (1999) ("Stakeholder analysts argue that *all* persons or groups with legitimate interests participating in an enterprise do so to obtain benefits and that there is no prima facie priority of one set of interests and benefits over another.") (emphasis in original); R. EDWARD FREEMAN, STRATEGIC MANAGEMENT: A STAKEHOLDER APPROACH 46 (1984) (defining stakeholder as one who can "affect or is affected by" an organization).

17. *See* STOUT, *supra* note 16, at 37-38 (stating that shareholders—like debtholders, employees, and suppliers—contracts with corporations).

18. FREEMAN ET AL., *supra* note 16.

19. Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 250-51 (1999).

activities and allocators of the resulting production value between different members.[20]

Recent trends in corporate disclosures reflect an increase in corporations' willingness to consider a wider circle of stakeholders. Sustainability reporting, which gives investors information about the non-financial performance of the corporation in different constituencies, is now widely applied and incorporated into corporate filings,[21] and some nations require inclusion of its principles.[22] All but one company listed in the S&P 500 has voluntarily made a sustainability disclosure in a financial filing or linked financial performance to a sustainability initiative.[23] As of 2013, U.K. regulations require that publicly traded, large corporations file "strategic reports," which must include corporate performance indicators, which effectively measure the company's business position and its performance.[24] In India, a 2013 law requires large companies to invest in sustainability initiatives and engage in corporate social responsibility activities with two percent of their average net profits.[25]

This article argues for the inclusion of consumers as corporate stakeholders and for corporate accountability for product information. The argument is structured as follows. Part I compares consumers to investors, showing that consumers are more vulnerable in their relationships with corporate sellers than investors are and thus need greater informational accountability. This article compares the scope of risks per purchase (or investment), the complexity of product choice versus investment allocation, and the right to exit, showing that consumers are at least as vulnerable as investors. The consumer products market is compared to capital markets, and in particular, the role of institutional and investment advisors acting in

20. *Id.* at 250.

21. PETER DESIMONE, INVESTOR RESPONSIBILITY RESEARCH CTR. INST., INTEGRATED FINANCIAL AND SUSTAINABILITY REPORTING IN THE UNITED STATES 1-4 (2013), *available at* http://irrcinstitute.org/pdf/FINAL_Integrated_Financial_Sustain_Reporting_April_2013.pdf; STEVE LYDENBERG, JEAN ROGERS & DAVID WOOD, THE HAUSER CENTER FOR NONPROFIT ORG., FROM TRANSPARENCY TO PERFORMANCE: INDUSTRY-BASED SUSTAINABILITY REPORTING ON KEY ISSUES 2 (2010), available at http://hausercenter.org/iri/wp-content/uploads/2010/05/IRI_Combined_KPI.pdf.

22. *See supra* text accompanying notes 282-286

23. DESIMONE, *supra* note 21, at 5.

24. The Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013, 2013, S.I. 1970 (U.K.). These reports on the company's corporate standing include "information about (i) environmental matters (including the impact of the company's business on the environment) (ii) the company's employees, and (iii) social community and human rights issues . . . ." *Id.* at § 414C(7)(b)(i)-(iii)..

25. Section 135 of the new Act requires that the Board of Directors makes sure that at least two percent of the company's average net profits during the three preceding years is spent on corporate social responsibility policy. For the full version of the law, see The Companies Act, No. 18 of 2013, INDIA CODE (2013).

the investment market is compared to consumer unions acting with the aim of reducing information gathering costs in the consumer products market. Comparing the structural characteristics of the consumer products market to the capital markets leads to the same conclusion: consumers' informational rights are under protected.

Part II analyzes the voluntary commercial speech environments for the consumer products market. The analysis portrays informational practices from three distinct sources: sellers, consumers, and third parties—in particular, consumer organizations. This second part of the article explains why voluntary disclosures are insufficient to create a solid foundation for freedom of consumer choice, due to both market failures in consumers' demand for information and to market failures in the supply of product information. Consumers have both too much and too little information: commercial speech overwhelms informational environments, but, given masses of information overload, it often becomes very costly to find factual information about the material features of the product. At the same time, often the most important and material information is completely unavailable due to insufficient incentives for all three information sources, the inaccessibility of adequate sources of information, and suboptimal mediums for its dissemination. Consider, the following examples: the effective costs of car ownership, the chemical composition and quality of bottled water, and the real savings value compared to future costs of living for pension plans. Consumers' bounded rationality, along with their cognitive limitations, makes them vulnerable to the overloaded commercial speech environment, and given limitations in consumers' capacity to absorb and analyze the overload of information in the consumer products market, leads to failure in the efficient allocation of demand for product information. Sustainability reporting gives little answer to the problem of product information as it is not product specific and not directed at consumers. Market failure is evident on both the demand and supply side of the product information market.

Part III argues for consumers' corporate membership using organizational theories of the corporation. Given that consumer contracts are frequently non-negotiable,[26] but rather subject consumers to the rules determined unilaterally by the seller, the relationship of consumers with

26. Contract obligations are voluntarily assumed: a contract is a legal vehicle for enforcement of mutual assent. In the sale of products or services to the public, one side defines the terms and elements of agreement, and the consumer may merely opt-in or out of the agreement by her decision of purchase. *See* JOHN P. DAWSON, WILLIAM BURNETT HARVEY & STANLEY D. HENDERSON, CONTRACTS: CASES AND COMMENT 511, 420-21 (8th ed. 2003) (discussing the prevalence of standard form contracts in modern business and observing that parties do not negotiate the details of every transaction).

corporate sellers resembles organizational membership. *Securities Exchange Commission v. H. J. Howey Co.*[27] and *United Housing Foundation Inc. v. Forman*[28] create a legal distortion because it is not the purpose of purchase we need to protect, but rather the unilateral relationship and one-sided control of all relevant information, which equally apply to consumers and investors alike.

Part IV compares the doctrinal foundations of corporate law to those currently available to consumers under contract law, showing the merits of the former in setting a disclosure regime for the consumer sector. While theoretical foundations for corporate inclusion of stakeholders are well established, corporate law literature does not offer any model for corporate accountability towards consumers. Part IV suggests three essentials for product information corporate policy. Product information should be required to include all material features and aspects of product ownership and be accessible and concise from a reasonable consumer's point of view. Disclosures should be accessible, easy to understand and read, and be placed prominently on the front of the package. The article suggests standards for product transparency requirements and establishes corporate law as the doctrinal setting for product disclosures, offering an extension of the scope of current corporate governance.

I. COMPARING CONSUMERS TO INVESTORS

Free choice serves as a basic and prominent foundation of capitalistic social ideology and of the respective legal thought regarding the commercial arena. Choice encompasses the moral basis for contracts and their enforcement and is widely considered both a value to be strived for and a basis for responsibility allocation of the agents possessing it. Our legal system goes a long way to protect that meaningful choice process for investors, creating a federal agency that sets exclusive disclosure standards for securities,[29] whereas consumers seem to conduct many of their choices in informational darkness, significantly limiting their ability to exercise informed and rational decision-making.[30] In this part of the article, consumers are compared to investors using several analytic measures. An

27. 328 U.S. 293 (1946).
28. 421 U.S. 837 (1975).
29. *See supra* text accompanying note 1.
30. Informational darkness may be caused by insufficient product information or by an overloaded information environment placing the costs of research on the consumer. In general, freedom of commercial speech applies to all speech regarding products, with the exception of food and drugs. *See* Richard Samp, *Sorrell v. IMS Health: Protecting Free Speech or Resurrecting Lochner?*, 2011 CATO SUP. CT. REV. 129, 140-43 (2011) (discussing FDA regulations on speech).

analysis of the characteristics of the two groups and their applicable markets shows that consumers should be protected at least as much as investors and may in fact require a higher degree of protection than that given to investors regarding informational rights.

A. Consumer Choice Process vs. Investments Allocation Process

Consumers' product choice process is prone to mistakes and confusion. While an investor's typical investment allocation is done in a rational, planned process that uses advisors or mediating institutions, typical consumer choice is spontaneous, irrational and highly affected by personal emotions and cognitive limitations. Corporate sellers strategically avoid information-based marketing and instead strengthen the emotional aspect of consumer decision making because they lack incentives to share product information with the public.[31] Bundling strategies promote the consumers' misperception of products and services, subjecting rational information-based decision making to potential misperceptions.[32] Vague and manipulative presentations place a significant burden on consumers trying to compare and understand the implications of products.[33] Even if

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31. For a sociological analysis of subjective emotional promotions in consumer markets, see JEAN BAUDRILLARD, THE CONSUMER SOCIETY: MYTHS AND STRUCTURES 88-89 (C.T. trans., Sage Publications 1998) (1970); MARTY NEUMEIER, THE BRAND GAP: HOW TO BRIDGE THE DISTANCE BETWEEN BUSINESS STRATEGY AND DESIGN 38-39 (2003). Sellers do have an incentive to treat their clients fairly because repeat buyers consider the reputation of a seller as shown in Lucian A. Bebchuck & Richard A. Posner, *One-Sided Contracts in Competitive Consumer Markets*, 104 MICH. L. REV. 827, 827-28 (2006). However, in a competitive context, information sharing and investment in assistance to consumers in evaluating products' characteristics may prove inefficient and costly for sellers. *See, e.g.*, Howard Beales, Richard Craswell & Steven C. Salop, *The Efficient Regulation of Consumer Information*, 44 J.L. & ECON 491, 503 (1981) (discussing the costs of consumer protection regulation). Consumers' ignorance benefits sellers on average also due to the sub-optimal use of products by ignorant consumers.

32. *See* Oren Bar-Gill, *Bundling and Consumer Misperception*, 73 U. CHI. L. REV. 33, 33-34 (2006) (taking consumer misperception as a given and discussing how sellers employ the bundling strategy in the face of that misperception); Richard Thaler, *Mental Accounting and Consumer Choice*, 4 MARKETING SCI. 199, 208-09 (1985) (discussing bundling in the context of segregate gains); Richard Craswell, *Tying Requirements in Competitive Markets: The Consumer Protection Issues*, 62 B.U. L. REV. 661 (1982) (examining bundling through the lens of tying requirements).

33. This is due to both cognitive and emotional constraints. For a general survey of cognitive constraints, see Angelo DeNisi & Raed Elaydi, *Which Came First, The Irrational Consumer or the Irrational Corporation?*, 6 ROGER WILLIAMS U. L. REV. 33, 35 (2000) (discussing information constraints placed on consumers by organizations); Christine Jolls, Cass R. Sunstein & Richard Thaler, *A Behavioral Approach to Law and Economics*, 50 STAN. L. REV. 1471, 1476-77 (1998) (discussing three limitations of human behavior: bounded rationality, bounded willpower, and bounded self-interest, that cause humans to

sellers provided complete information regarding product characteristics, consumers would be unable to analyze and process the mass of information available to them due to information overload[34] and low literacy levels with respect to corporate documents.[35]

B. Scope of Risks

Typically, investors risk only the capital located in their investment funds. Exceptions occur in structured products, derivatives, and shorts, which often risk additional funds due to higher leverage. In all cases, investors' risk is solely monetary. Consumers, on the other hand, risk much more than the purchase cost. Often, consumer products have health implications. In foods, beverages, toys, clothing, automobiles, cellular devices, and many other products, consumers trust sellers with their health and potentially their lives. Potential risks from products can therefore be much greater than the purchase cost.[36] A higher degree of regulation applies to product safety and quality control.[37] However, quality control only kicks unacceptable products out of the market, without helping consumers choose between remaining acceptable products.[38]

Corporate law does not govern product safety, thus the board of directors is rarely liable for it. Product safety is an engineering staff issue and has less to do with senior managers of the corporation, who are

diverge from economic models); Amos Tversky & Daniel Kahneman, *Judgment Under Uncertainty: Heuristics and Biases*, SCIENCE, Sept. 1974, at 1124 (discussing systematic error in commonly-used heuristics, including representativeness, availability of instances or scenarios, and adjustment from an anchor) [hereinafter Tverksy & Kahneman, *Judgment Under Uncertainty*]. For a general survey of emotional constraints, see Mary Frances Luce et al., *Emotional Decisions: Tradeoff Difficulty and Coping in Consumer Choice*, MONOGRAPHS OF THE J. OF CONSUMER RES., no. 1, 2001 (discussing the role of emotion in decision processes).

34. *See* Shmuel I. Becher, *Behavioral Science and Consumer Standard Form Contracts*, 68 LA. L. REV. 117, 167-77 (2007) (discussing the harmful effects of information overload on contracting).

35. *See generally* Alan M. White & Cathy Lesser Mansfield, *Literacy and Contract*, 13 STAN. L. & POL'Y REV. 233, 234-35 (2002) (reviewing research on consumer literacy and readability of consumer contracts and credit agreements).

36. Consider, for example, baby formula and automobile purchases, in which consumers trust sellers with their lives.

37. This is not always the case. *See* Oren Bar-Gill & Elizabeth Warren, *Making Credit Safer*, 157 U. PA. L. REV. 1, 4 (2008) (observing that although most products sold in the United States pass safety regulations, credit products are relatively less regulated).

38. For example, consider the case of infant car seats. Quality control enforces a minimal safety threshold. Consumers still need to make product choice between the available products, differing in quality and features, beyond the minimal threshold.

typically liable for risks imposed only on investors.[39]

C. Product Attributes and Complexity of Choice

Investments are typically judged by comparing expected rate of return with imposed risk, so prices can reflect the demand and supply curve and signal true value to investors. Products are more complex, and consumers choose products based on a wider spectrum of considerations, features and characteristics. Marketing research shows that, for consumer products, "price is but one of several potentially useful extrinsic cues; brand name or package may be equally or more important, especially in packaged goods. Further, evidence of a generalized price-perceived quality relationship is inconclusive."[40] Thus, while prices can serve as an ultimate signal of value in the investments market, they are less likely to reflect accurately the value to consumers.[41]

D. Intermediaries

Institutional investors and investment advisors are frequent players in the capital markets that have expertise and analytical tools for evaluating different investment strategies based on corporate filings.[42] While investment advisers serve the general investing public with investment advice,[43] institutional investors perform most of the transactions in the capital markets.[44] The Securities Act of 1933[45] and the Securities Exchange

39. *See generally* Francois Brochet and Suraj Srinivasan, *Accountability of Independent Directors - Evidence From Firms Subject to Securities Litigation* (Working Paper, 2013), *available at* http://ssrn.com/abstract=2285776 or http://dx.doi.org/10.2139/ssrn.2285776 (discussing the liability of directors when firms are sued for financial and disclosure related fraud).

40. Valarie A. Zeithaml, *Consumer Perceptions of Price, Quality, and Value: A Means-End Model and Synthesis of Evidence*, 52 J. MARKETING 2, 17 (1988).

41. *See generally* Richard Thaler, *Toward a Positive Theory of Consumer Choice*, 1 J. ECON. BEHAV. & ORG. 39 (1980) (explaining that economic models fail to predict consumer behavior because economic models treat consumers as experts even though the average consumer is not an expert decision-maker).

42. *See* Anita K. Krug, *Institutionalization, Investment Adviser Regulation, and the Hedge Fund Problem*, 63 HASTINGS L.J. 1, 18-20 (2011) (discussing the role of investment advisers). *See generally* Alan R. Palmiter, *Staying Public: Institutional Investors in U.S. Capital Markets*, 3 Brook. J. Corp. Fin. & Com. L. 245 (2009) (discussing the investment practices of major institutional investors in the U.S. capital markets).

43. Krug*, supra* note 42, at 18.

44. *See* Palmiter*, supra* note 42, at 245 (noting that institutional investors "collectively hold more than three-fourths of U.S. capital market investments.").

45. The Securities Act of 1933, 15 U.S.C. § 77a (1982) regulates the public offering and sale of securities in interstate commerce, requiring a prospectus designed to provide all

Act of 1934[46] were enacted during the peak years of the Great Depression with an aim towards protect individual investors. Nowadays, institutions dominate the trading platforms and make most of the U.S. trading volume.[47]

In the consumer product market, consumer unions[48] take on this role. Like analysts and investment advisors, consumer unions exploit economies of scale when evaluating and comparing product information. Unlike individual consumers, consumer unions can devote the resources to conduct a thorough study of the products available by collecting the information, analyzing it, and finally comparing it on a measurable scale.[49] The relationship between consumers and their union may be classified as an agency relationship; the union is authorized to collect product information and test it on behalf of its subscribers. One prominent example is *Consumer Reports*, which is published by Consumers Union, a nonprofit organization established in the 1930s when advertising started flooding the media.[50] For a small fee, consumers in the United States can subscribe to a

material information necessary to investors to fully assess the merits and risks of the purchased security.

46. The Securities Exchange Act of 1934, 15 U.S.C. § 78a (1982) requires all registrants to file periodic reports in electronic format through EDGAR, the Electronic Data Gathering, Analysis, and Retrieval System.

47. Palmiter, *supra* note 42, at 245. In the 1950s, retail investors owned over ninety percent of the stock of U.S. corporations. Alicia Davis Evans, *A Requiem for the Retail Investor?*, 95 VA. L. REV. 1105, 1105 (2009). By 2009, retail investors owned less than thirty percent and represented a very small percentage in U.S. trading volume. *Id.; see also* Donald C. Langevoort, *The SEC, Retail Investors, and the Institutionalization of the Securities Markets*, 95 VA. L. REV. 1025, 1026 (2009) (observing the rapid shift in the last thirty years toward the institutionalization in the financial markets in the United States).

48. In using the term "consumers union" in this article, I mean to refer to any platform that consumers may look to in order to receive information about products and services. Some consumer unions may require subscriptions, such as *Consumer Reports*. *Subscribe*, CONSUMERREPORTS.ORG, https://ec.consumerreports.org/ec/cro/order.htm?INTKEY=I0AHLT4 (last visited, Dec. 23, 2014). Other consumer unions may be free of charge, such as Yelp. YELP, http://www.yelp.com/ (last visited Dec. 23, 2014).

49. *See* CONSUMERREPORTS.ORG, *supra* note 48 (noting that subscribers get "over a thousand ratings, reviews, expert buying advice, product comparisons, consumer user reviews, and product video clips to over 5,000 electronics, appliances, home & garden, baby gear, and food products . . .").

50. Occasionally consumers have additional impartial sources of information provided by third parties giving independent commercial speech. *See, e.g.*, *Energy Bill Savings Start Here!*, USWITCH, http://www.uswitch.com/gas-electricity/ (last visited Oct. 6, 2014) (providing for a comparison of gas, electricity, broadband television, mobile phones, and insurance); *Choose the Right Cell Phone or Plan for You*, MYRATEPLAN, http://www.myrateplan.com/ (last visited Oct. 6, 2014) (providing a comparison of a wide array of consumer needs, including cell-phone plans, television services, credit cards, travel options, and insurance). Interestingly, these free services stay impartial while being frequently sponsored by the reviewed industry. USwitch UK complies with The Confidence

website or magazine that summarizes product information impartially and professionally, and presents its findings in a comparable way.[51] To create its professional product studies, Consumers Union employs more than 600 employees,[52] who make anonymous purchases, test products in equipped laboratories, and publish educational studies for its subscribers.[53]

Consumers Union aims to provide an impartial, independent source of product information that accepts no advertising and runs professional tests on products on behalf of potential consumers.[54] The information output from *Consumer Reports* is impartial, runs ad-free, and is organized and presented systematically.[55] Consumers Union tests products, grades their performance under several chosen criteria, compares them to other products in the same category, and presents the results in a table format that allows for easy comparison and consumer choice. In a typical report, *Consumer Reports* lists the prices of several alternatives and for each gives the overall score and specific grade in each of the tested criteria.

However, this detailed, analytical report of the alternatives is only available for a narrow selection of brands and products.[56] The impartial product review published in *Consumer Reports* refers to a limited number of categories and compares only a few of the available brands for each product surveyed. Other intermediaries acting in the consumer products market may be sponsored by the industry reviewed, impairing the

Code, a voluntary practice that requires unbiased comparisons through independence, impartiality, the fair presentation of tariffs, and the accuracy of information presented, which is managed by the UK energy market regulator Ofgem. *Confidence Code – Code of Practice for Online Domestic Price Comparison Services*, OFGEM (Mar. 18, 2013), https://www.ofgem.gov.uk/ofgem-publications/74615/confidence-code.pdf.

51. Some services, like USwitch U.K., are free of charge, while others, like Consumer Reports, charge membership fees. *Compare Energy Bill Savings Start Here!*, *supra* note 50 (providing product comparisons for free) *with Choose Subscription*, CONSUMERREPORTS.ORG, https://ec.consumerreports.org/ec/cro/order.htm?INTKEY=I0AHLT4 (last visited Oct. 6, 2014) (providing comparison services only if the user becomes a paid subscriber).

52. Employment is funded by revenue generated by subscriptions. *See Mission*, CONSUMERSUNION, http://www.consumersunion.org/about/mission/ (last visited Oct. 6, 2014) (providing information about the Consumers Union staff).

53. *Mission*, CONSUMERSUNION.ORG, http://consumersunion.org/about/mission/ (last visited, Dec. 9, 2014)

54. *Id.*

55. *Id.*

56. Most of the products Consumer Union surveys in *Consumer Reports* are for rather large purchases, such as kitchen appliances, automobiles, and expensive baby equipment. Consumers Union does not survey any services or low-cost products, perhaps under the assumption that services require customization and are thus hard to compare on an ultimate social scale, and low-cost items do not stem the drive to research or pay the fee for a collective research source.

impartiality and commitment to the consumer as their ultimate client.[57]

Therefore, consumers unions acting in the consumer product information market are not a sufficient solution to the problems of product information. Unlike analysts and investment advisors acting in capital markets and serving investors, intermediaries acting on behalf of consumers fail to solve market failures in the consumer products market due to both the costs of information and the structural differences between the consumer products and the investment markets.

The discrepancy of information costs between capital and consumer products markets is significant. Due to the disclosure requirements of the federal securities laws, intermediaries acting in capital markets have abundant information available under the uniform requirements of securities regulation and need only to review and analyze well-digested and easily accessible information,[58] while third parties must bear the costs of searching, verifying, analyzing, and occasionally pricing product information.[59]

The cost of obtaining information is significant for the efficient functioning of institutions. Institutions acting in capital markets find mandatory disclosure under securities laws useful and think disclosure provides users "essential information that heavily influences their decisions."[60] The information management mechanisms provided by EDGAR and its plain English form are generally satisfactory to institutions and assist in reducing transaction costs and in facilitating the dissemination of clear information to the market.[61] Institutions are attracted to firms with certain disclosure practices, and some corporate managers adopt disclosure practices to attract such investors.[62] A recent empirical study shows that

57. *See, e.g.*, *WhistleOut Terms of Use*, WHISTLEOUT.COM http://www.whistleout.com.au/Terms-Of-Use (last visited Dec. 9, 2014) (providing consumer comparisons of complex products sponsored through referral commissions of the industries reviewed); YELP.COM, http://www.yelp.com/ (last visited Dec. 9, 2014) (relying on enhanced search results offered to merchants for sponsorship).

58. *See supra* note 1 (identifying the primary statutes that regulate the issuance of securities in the United States).

59. *See How We Test*, CONSUMERREPORTS.ORG, http://www.consumerreports.org/cro/about-us/whats-behind-the-ratings/testing/index.htm (last visited Oct. 6, 2014) (documenting the considerable technical, engineering, and scientific costs of Consumer Reports).

60. Evans, *supra* note 47, at 1108 (citing THE SPECIAL COMM. ON FIN. REPORTING, AM. INST. OF CERTIFIED PUB. ACCT., IMPROVING BUSINESS REPORTING – A CUSTOMER FOCUS: MEETING THE INFORMATIONAL NEEDS OF INVESTORS & CREDITORS (1994), *available at* http://www.aicpa.org/interestareas/frc/accountingfinancialreporting/downloadabledocuments/jenkins%20committee%20report.pdf).

61. *Id.* at 1112.

62. *See* Brian J. Bushee & Christopher F. Noe, *Corporate Disclosure Practices, Institutional Investors, and Stock Return Volatility*, 38 J. ACCT. RES. 171, 200 (2000)

even index funds, which are passive and cost-conscious investors, govern through eliciting disclosure.[63] Indeed, institutional investors appreciate disclosures: they have the capacity to analyze and understand the disclosed texts and the ability to elicit information.[64] A recent work comparing the bond and the loan markets in the U.S. shows that even in the absence of mandatory disclosure, institutional investors obtain significant information about their investments in syndicated loans through private ordering.[65]

In contrast, for the consumer products market, accumulated information of past consumers' experiences is rare. Consider food and beverages as an example – the shared experiences of consumers fail to inform us of the ingredients in, and nutritional value of, what we consume. However, intermediaries will only bear the costs of research if such research efforts would result in profit. Because sellers are the lower cost provider, there is no sense in expecting intermediaries to conduct research that would reverse engineer food in order to decipher ingredients and nutritional value. For complex products that often require extensive research in order to reveal their nature and characteristics, these costs may be significant. Information aggregators and intermediaries are bound to engage in duplicate efforts to reach the same information and uncover it only partially. Mandatory disclosure may lower the cost of information, and may thus be justified as a means to improve and enhance the competition between information aggregators and intermediaries, as well as a means to reduce the entry barriers to the market of information aggregation for the benefit of consumers.[66]

The discrepancy of costs for information traders for investors and for consumers is especially questionable when considering the information gaps between seller corporations and outside information traders seeking to uncover nonpublic information. This is especially true regarding complex products that often require extensive research in order to reveal their nature and characteristics. While regulation lowers the costs of information searching for investors, no such information regulation is available for

("[I]nstitutional investors are attracted to firms with more forthcoming disclosure."); Mark H. Lang and Russell J. Lundholm, *Corporate Disclosure Policy and Analyst Behavior*, 71 ACCT. REV. 467, 490 (1996) ("[M]ore forthcoming disclosure policies . . . attract more analysts . . . .").

63. Jordan Schoenfeld, *Shareholder Governance Through Disclosure* (May 4, 2014) (unpublished manuscript), *available at* http://ssrn.com/abstract=2350181.

64. Elisabeth de Fontenay, *Do the Securities Laws Matter? The Rise of the Leveraged Loan Market*, J. CORP. L. (forthcoming 2014)

65. *Id*.

66. *See generally* Zohar Goshen & Gideon Parchomovsky, *The Essential Role of Securities Regulation*, 55 DUKE L.J. 711, 713-14 (2006) (positing that the role of securities regulation is to create and promote a competitive market for information traders).

consumers, and third parties acting in the consumer product information market are bound to engage in duplicate efforts to reach the same information and only partially uncover it. As the cost of information decreases, the number of third party agents and information traders is expected to increase,[67] and their contribution is expected to be more precise.[68]

Corporate accountability for product disclosures can be justified as a means to improve and enhance the competition between information traders and third party information providers, and as a means to reduce the entry barriers to the market of information trading in the consumer products market. The seller corporation is the low-cost provider of relevant information. More corporate accountability for consumer product disclosures may lead to fewer instances of asymmetric information between consumers and sellers, and contribute to facilitating a competitive market.[69]

In addition to cost, another reason for the discrepancy between institutions in capital markets and intermediaries in the consumer products market is the structural characteristics of both markets. Institutions in capital markets enjoy the benefit of a social policy enforcing the public use of their services. Pension funds and provident funds, for example, present an extraordinary benefit to their clients, who are inclined to use their professional services in order to receive the tax benefits and social assurance that accompanies pension savings.[70] Mutual funds and index funds allow the public saving routes that reduce transaction costs for trading.[71] Financial regulation, however, restricts the occupation of money management to few certified and highly regulated institutions.[72] Because of this, capital markets are prone to have classes of investors represented by

67. *See id.* at 737 (observing that decreased information search, verification, and analysis costs results in an increase in information traders).

68. This argument assumes that mandatory disclosure lowers the effect of noise traders and associated noise risk. *Id.* at 739 (citing Nicholas L. Georgakopoulos, *Why Should Disclosure Rules Subsidize Informed Traders?,* 16 INT'L REV. L. & ECON. 417, 424 (1996)).

69. *Id.* at 740.

70. *See* Sharon Reece & Mary Beth Navin, *Regulating Pension Fund Investments: The Role of Federal Legislation*, 6 B.Y.U. J. PUB. L. 101, 105 (1992) (noting that the tax benefits associated with using pension funds include "exempting pension fund earnings from federal income tax, allowing employed contributions to accrue tax-deferred to the employee and permitting certain kinds of favorable distribution treatment.").

71. *See e.g.*, *Mutual Funds*, OHIO DEFERRED COMPENSATION, *available at* https://www.ohio457.org/iApp/tcm/ohio457/guide/basics/mutualfunds/index.jsp (last visited Dec. 23, 2014) (noting that mutual funds lower transaction costs "[b]ecause of the size and volume of their transactions").

72. *See* Barry P. Barbash & Jai Massari, *The Investment Advisers Act of 1940: Regulation By Accretion*, 39 RUTGERS L.J. 627, 627 (2008) (identifying the Investment Advisers Act of 1940 as "[t]he centerpiece of U.S. regulation of money managers.").

few certified money managers.

Consumers, on the other hand, make their decisions unaided. We rarely shop individually for securities, but we always go grocery shopping without an intermediary by our side. So the case for informed consent, empowerment, and the need of access to knowledge is stronger for consumers than for retail investors. And at the same time, while the market for intermediaries in capital markets prosper thanks to tax incentives and financial regulation, incentives for creating a market of intermediaries in the consumer products market are meager. Providing a database of mandatory information lowers the costs of entry to the information aggregation market and may be required to support its growth.[73]

E. The Right to Exit

Corporations give their members and owners three types of rights: exit, voice, and loyalty.[74] Of relevance to this article is the right to exit. Indeed, investors in public corporations may exit their investments at reasonable costs, by selling their securities on an exchange or over the counter and "cashing out" of their relationship with the corporation. Consumers of mass products and services may find higher barriers to switching their consumption preferences. Costs of exiting may include fees, contractual restrictions, and social and logistical costs that make the right to exit theoretical or very costly for the average consumer.[75] Consider the costs of switching a childcare service provider at a preschool, the costs of switching a bank account service center, and the costs of switching media and cellular providers. In all three examples, exit is very costly and unlikely to serve as a tool of disciplining bad management in striving for its reform, even given high and effective competition in the markets. The costs of exit sometimes arise naturally from the situation, as in the

73. EDGAR is an interesting benchmark for mandatory disclosure for consumers because it succeeds in addressing both the needs of retail investors and the requirements of institutions. Securities disclosures are provided on a single database accessible to all at all times, rather than enclosed to each particular securities transaction. EDGAR provides the interested public information easy to compare and to trace back, without burdening or imposing on the non-interested public. *Company Filings*, U.S. SECURITIES AND EXCHANGE COMMISSION, http://www.sec.gov/edgar/searchedgar/companysearch.html (last visited Oct. 11, 2014).

74. *See generally* ALBERT O. HIRSCHMAN, EXIT, VOICE AND LOYALTY: RESPONSES TO DECLINE IN FIRMS, ORGANIZATIONS, AND STATES 76-77 (1970) (examining a manner of analyzing certain economic processes which can illuminate a wide range of social, political, and moral phenomena).

75. *See* Oren Bar-Gill & Omri Ben-Shahar, *Exit from Contract*, 6 J. LEGAL ANALYSIS 151, 151 (2014) (discussing restrictions on exit rights and noting that "consumers often choose transactions with lock-in provisions, trading off exit rights for other perks.").

childcare example, but are often pre-designed carefully by corporate sellers as a strategic method of preventing profit loss.[76] For example, the costs of switching banking providers could be lowered if consumers were entitled to switch and keep their bank account numbers, payment orders, and records. However, the industry prefers keeping the costs high to preserve its profitability margins.[77]

F. Regulation

Investors' informational interests are strictly protected by the U.S. Securities and Exchange Commission (SEC), a mighty regulatory agency with wide authority to determine the content, form, and timing of disclosure.[78] The elaborate framework of disclosure rules developed by the SEC includes a web-based platform that is easily accessible to all with plain English uniform disclosures.[79]

Consumers' informational interests lie on contractual foundations. Thus, product information is scattered throughout separate sources of various credibility and impact, and is presented in widely different forms and languages. Consumers interested in a product must bear the costs of assembling this information. Corporations, which already have and can easily provide the information, typically choose to engage in commercial speech that creates emotional manipulation and vague branding on the one hand and information overload on the other.[80] No single authority is in position to demand material information for products for the benefit of their users, and consumers are limited to claims of contractual misrepresentation, fraud, and to a lengthy and costly process of legal proceedings to seek remedies while overcoming the burden of the de minimis rule. Since consumers are widely dispersed, pursuing such proceedings is highly unlikely.

Regulation's preference toward investors is beyond ownership status. Shareholders are owners of the corporation, and disclosure to them is easily justifiable as part of their ownership and property rights in the incorporated asset. Creditors, however, receive similar information management services to those granted to shareholders,[81] despite having a contractual

76. *See* Bar-Gill & Ben-Shahar *supra* note 75, at 152 (noting that exit hurts sellers and that some sellers worked to make exit costly through contractual provisions).

77. *See* Bar-Gill & Ben-Shahar *supra* note 75, at 152 (noting that exit hurts sellers and that some sellers work to make exit costly through contractual provisions).

78. *See supra* note 1 (discussing the securities regulation framework established by the Securities Act of 1933 and the Securities Exchange Act of 1934).

79. *See supra* note 73 (discussing the SEC's EDGAR platform).

80. *See* discussion *infra* Part II section B.1.

81. *See* 15 U.S.C. § 77b (2012) (defining a security as "any note," with several

relationship with corporations that is similar to that of consumers. The informational protection of creditors thus shows that the law protects investors as a preferred status. An analysis of the choice process of consumers as compared to the investment allocation process shows that consumers are at least as vulnerable as investors. Comparing the consumer product market to capital markets shows that market forces, regulation, and intermediaries are better protecting investors, and that consumers typically make their product research and choice unaided. In the following part, this article provides an analysis of voluntary disclosures available in the consumer product market to evaluate the degree of informational protection provided to consumers by freedom of commercial speech.

II. WHY IS VOLUNTARY DISCLOSURE NOT ENOUGH?

We are surrounded by vast amounts of product and brand information. This part of the article provides a thorough analysis of product information markets, arguing that what consumers know is not enough and is at the same time too little and too much to affect consumers' choice processes efficiently. The analysis refers to sellers' supply of product information on the one hand, and to consumers' demand for product information on the other. Recent trends of sustainability disclosures are also discussed, showing that they are not a better consumer choice process because of the limited scope, audience, and enforcement incentives.

A. Supply of Product Information

The two main generic groups that supply product information are: (1) sellers and (2) past and present consumers. The social allocation of product information is currently pursued mainly through freedom of speech.[82] Under this model, market forces determine the allocation of information between sellers and consumers – namely what sellers and consumers choose to share with each other voluntarily. Due to incentive disparities between the two groups, sellers typically choose to share more information than consumers; sellers stand to gain from information sharing, which can increase their sales, enhance their reputation, and entrench their market share, while consumers' gain from such information sharing is usually limited to their individual consumption capacity. Commercial speech is

exceptions); 15 U.S.C. § 78c (describing a security as "any note," and proceeding to some exclusions). Any note with a maturity exceeding nine months comes within the statutory definition of a security. *Id.* § 78c (10).

82. *See* U.S. CONST. amend. I ("Congress shall make no law . . . abridging the freedom of speech . . . .").

thus mainly speech for commercial purposes: specifically, the purpose of affecting sales.[83] Below I argue that the marketplace rule of dissemination of product information through commercial speech is resulting in market failure and thus justifies intervention.

1. Consumers' Commercial Speech

Consumers' accumulated experiences are a vast source of product information. Past consumers know almost everything there is to know about a product, including its hidden highlights and most disturbing problems. Had the market for product information been efficient, this vast amount of accumulated information would change hands and be easily forwarded to future consumers, who have yet to make their consumer choice. Alas, a market failure on the supply side of information creates a hurdle for this efficient transaction. Past and present consumers fail to efficiently forward their accumulated experiences to future consumers due to limited incentives, limited accessibility to communication mediums, limited accessibility to the information, and reliability barriers.

a. Limited Incentives for Information Sharing

The product information environment is structured asymmetrically in a way that allows sellers to dominate most content and forms of commercial speech.[84] This asymmetry is intrinsic to the structure of merchandise business in a mass production society: within each market segment, few sellers offer products to many consumers and consumers are dispersed, typically acting separately and independently as individuals or nuclear families. Although sellers have strong incentives to use commercial speech as a means of sales promotion, consumers are much less inclined to use commercial speech simply because their stakes involved with any given product are typically low and bounded by the individual consumption scale. This problem can be conceptualized as a

83. Scanlon defines commercial speech with reference to the participant's intent, stating, "expression by a participant in the market for the purpose of attracting buyers or sellers." Thomas M. Scanlon, *Freedom of Expression and Categories of Expression*, 40 U. PITT. L. REV. 519, 540-41 (1979). I focus on speech for marketing purposes, meant to attract consumers, and more specifically, to persuade and otherwise affect them toward consuming products or services promoting the speaker's interest.

84. Hsiu-Yuan Tsao, Pierre Berthon, Leyland Pitt & Michael Parent, *Brand Signal Quality of Products in an Asymmetric Online Information Environment: An Experimental Study*, 10 J. CONSUMER BEHAV. 169, 169 (2011) (discussing seller strategies for exploiting the information asymmetry in the consumer products market).

problem of high transaction costs for information sharing,[85] as well as a problem of collective action for the consumer community.[86] Since individual consumers are numerous, each having a small stake of investment in any given product purchased, the consumer's costs of commercial speech per given product individually outweigh the expected benefits, even when the accumulated interests of consumers as a group are indicating an opposite result. It is individually rational for a consumer to undertake the costs of commercial speech only when her proportionate share of the expected collective consumers' benefits from doing so exceeds the expected costs.

b. Limited Accessibility to Communication Mediums

These problems were extremely difficult to overcome in the traditional communication environment. Traditionally, a scarce supply of opportunities in mass communication mediums such as newspapers, radio and television contribute to high costs of commercial speech.[87]

85. This is a conventional framing for this problem. Ronald Coase, *The Problem of Social Cost*, 3 J.L. & ECON. 1 (1960). Coase uses the case of environmental pollution to show the economic principle of transaction costs, and to suggest that the harmful costs of pollution should not be seen as externalities. *Id.* Rather, such costs result both from the production process and from people's choice to live near the plant. Rather than resulting from externalities of the factory, pollution is seen as stemming from a large number of acts and omissions on both sides. If the parties were able to bargain with one another – the solution that they jointly prefer – an efficient result can be expected. In theory, steel users (the factory's consumers) and pollution sufferers might agree to share the cost of pollution (for example, through the installation of antipollution equipment). "Transaction costs" are the costs of coming together to reach an agreement, and these costs prevent bargains from occurring. Bargaining is impracticable because of transaction costs, and regulation may be used to overcome the problem of transaction costs and achieve an efficient arrangement.

86. *See generally* RUSSELL HARDIN, COLLECTIVE ACTION (1st ed. 1982) (postulating that people act in their individual interests in making collective decisions); TODD SANDLER, COLLECTIVE ACTION: THEORY AND APPLICATIONS (1992) (synthesizing the latest research on collective action). The resulting disincentive to act is compounded by the free-rider problem: any one consumer may decide to save the costs of information sharing on the belief that others will do so and she will still be able to enjoy the benefits in her next purchases.

87. KYLE BAGWELL, THE ECONOMIC ANALYSIS OF ADVERTISING 69-83 (Columbia Univ. Dep't of Econ. Discussion Paper Series, Paper No. 0506-01, 2005), *available at* http://academiccommons.columbia.edu/catalog/ac:115358. Interestingly, total advertising expenditures have risen in recent years. While 20th century communication mediums were scarce and voiced only corporate commercial speech, new media makes it possible for consumers to voice their opinions in various channels of publicity, including web forums, Facebook, Whatsapp and other social media channels accessible to all. *See* Mercedes Esteban Bravo, José M. Vidal-Sanz & Gökhan Yildirim, *Expenditure Trends in US Advertising: Long-Term Effects and Structural Changes with New Media Introductions*, (Universidad Carlos III de Madrid, Working Paper No. 15, June 2012), *available at*

Accordingly, consumers' inclination to use commercial speech was lower, simply because their accessibility to the communication mediums was scarce and severely limited.[88] Much of what we hear is thus what sellers have spoken directly through promotional business sites and through online advertisements, or indirectly, through other agents and astroturfing.[89] Sellers thus quantitatively dominate the commercial speech arena.

In this asymmetric setting, the Internet created a distinctive revolution by contributing to the democratization of information. On the Internet, unlike in any traditional information medium, all users are free to become creators and suppliers of information, and not merely its end consumers. Thanks to the Internet, becoming a supplier of information, rather than merely its consumer, is cheap, easy, and accessible to all.[90]

The Internet thus helped to democratize the product information market due to the strict equality of its users who are equal not only in access to information, and the equality in the opportunities of its creation and dissemination.[91] Since commercial speech opportunities are distributed

http://ideas.repec.org/p/cte/wbrepe/wb121506.html (a historical analysis of advertisement expenditures in the U.S.).

88. Howard Rheingold, Participatory Media Literacy (2008, retrieved November 2014), available at https://www.socialtext.net/medialiteracy/index.cgi/

89. "Astroturfing" is "the deceptive practice of presenting an orchestrated marketing or public relations campaign in the guise of unsolicited comments from members of the public." *See Astroturfing Definition*, OXFORDDICTIONARIES.COM, http://www.oxforddictionaries.com/us/definition/english/astroturfing (last visited Oct. 27, 2014). European Legislation is an example of the regulation of marketplace rule information mechanism in the case of Internet astroturfing. *See* Eur. Parl. & Council Directive 2005/29, 2005 O.J. (L 149) 22 (EC) (stating that falsely claiming or creating the impression that the trader is not acting for purposes relating to his trade, business, craft or profession, or falsely representing oneself as a consumer is a criminal offence).

90. Unlike the traditional communication mediums, which served mainly to promote commercial speech opportunities of sellers as speakers, the Internet sets a social network for consumer empowerment: it is the first communication medium that gives consumers the opportunity to voice their opinions and review products and sellers. A vast pool of opinions of prior consumers, often rated and aggregated, is available on the Internet. Consumer rating is expanding through the Internet for a variety of services. Many shopping sites include information about the rating previous consumers have given the offered product. For example, Amazon.com presents consumers with the average rating previous readers have given a certain book, including their comments and criticism. Similarly, Tripadvisor.com offers its consumers average ratings and detailed reviews given by experienced consumers who have already used the food and lodging services surveyed by the site. Recently, WellPoint Inc., a prominent health insurer in the U.S., has announced it would team up with Zagat—a purveyor of consumers' restaurant and hotel ratings— to let health-plan members go online to rate and review their experiences with doctors. *See* Vanessa Fuhrmans, *Women to Watch (A Special Report) —- The 50 Women to Watch*, WALL ST. J., Nov. 19, 2007, at R3 (describing the work of female leaders in top Internet companies).

91. Equality – both in terms of access to information and in terms of expression

more equally on the Internet to sellers and consumers alike, the strength of the claim for asymmetry of access to information mediums weakens.[92]

c. *Limited Accessibility to Information*

The asymmetry of information between sellers and consumers is apparent in the allocation of information itself. Sellers control virtually all available information regarding their offered products' characteristics, ingredients, safety, applicability and features, whereas consumers—even as a collective group—hold only the information available from their accumulated experiences. Often, accumulated experience is not enough to discover all there is to know about the product.[93] Sellers choose what to tell consumers and how to tell it, and this choice, channeled through commercial speech, encompasses most of the available product information.

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opportunities – was indeed one of the originally arguments in favor of the Internet. As early of 1996, John Perry Barlow stated that, "We are creating a world that all may enter without privilege or prejudice accorded by race, economic power, military force, or station of birth; We are creating a world where anyone, anywhere may express his or her beliefs, no matter how singular, without fear of being coerced into silence or conformity." John Perry Barlow, *A Declaration of the Independence of Cyberspace*, ELECTRONIC FRONTIER FOUNDATION (Feb. 8, 1996), http://homes.eff.org/~barlow/Declaration-Final.html. Every consumer is free to contribute to public discourse from his experience and to voice his opinions on any seller; and every seller may respond to the criticism through the same venue. Some Internet sites offering consumer reviews, also initiate on-line discussions between consumers and sellers, archived and presented for the benefit of future consumers.

92. This claim requires a disclaimer: despite the democratic structure of Internet accessibility, asserting that the Internet abolishes the informational asymmetries between sellers and consumers would be an overstatement. In fact, Internet users typically rely on few content sites, ultimately granting the owners and editors of such sites an inherent advantage in terms of commercial speech exposure and persuasion power. Obviously, the power of owners and editors of a popular site is asymmetrical to that of an individual consumer criticizing the contents of such a site because the platform for the latter criticism is less popular and gives users less exposure. Given these actual use patterns of consumers, it seems that the Internet is a virtual reflection of the traditional power and capital relations in the society, rather than an equal democracy of opinions. Nonetheless, the Internet does give consumers a platform for documenting their experiences and opinions in an irreversible form that may reach other, future consumers; as such, the Internet gives consumers a larger stage than ever before.

93. The abrupt decline in sales after news of a product scandal, or product recall, best demonstrate the effects of this asymmetry. To illustrate, consider toys that include poisonous lead, putting the children playing with them at risk. Consumers' accumulated experience is not likely to discover such defects efficiently, because each individual consumer has considerable transaction costs to conduct private research. However, the producing seller holds all information about the product's ingredients and safety from the production date, and is in the lowest-cost position to detect and survey the product's voyage through the marketing chain.

Here too, the Internet is revolutionary, allowing accessibility and immediate availability of masses of information, including opinions of previous consumers, to all consumers at any given time. The information accumulated on the Internet is visible to all, and is a shared asset of Internet users throughout the world, crossing nationalities, cultures, and generations. Consumers have much better accessibility to information thanks to the Internet, but they do not know all there is to know.[94]

d. Limited Reliability

The final barrier to information sharing between past and present consumers is overcoming the reliability question and assuring the integrity of the information shared. Suppose all our needs for information were present in customer reviews available online; could we trust these as authentic and reliable? This question is harder to answer because disguised marketing, *e.g.*, astroturfing or undercover marketing,[95] is playing a significant role in the marketing strategies of corporations. Astroturfing is particularly prominent online, as chat rooms and forums for consumers easily mislead their users to perceive everyone as peers. Disguised as authentic consumers who give sincere advice, sellers can affect future consumers and promote their sales while they are protected by the veil of anonymity at a very low cost and with a low risk of liability.[96]

94. Not all the essential information is available on the Internet, and even the available information requires vast resources for processing and analysis. To illustrate, consider a purchase of an automobile: most consumers will want to know the total cost of ownership of the car, a price accumulating the average cost of maintenance as well as the miles per gallon expected utility. Even a thorough investigation of all information sources available on the market would not reveal this information, which is held exclusively by the seller.

95. *See* Eur. Parl. & Council Directive 2005, supra note 89, at 34.

96. A well-known published example of undercover marketing is Sony Ericsson, who used stealth marketing in 2002, hired actors in major cities, and had them ask strangers to take their picture with a brand new picture phone while talking about how cool the new device was. Robert Walker, *The Hidden (in Plain Sight) Persuaders*, N.Y. TIMES MAGAZINE, Dec. 5, 2004, at 68. Undercover marketing can affect encyclopedias, as well as Wikipedia, which is a consumer-updated source of information, an encyclopedia based on the wisdom of the crowds, is, too, subject to manipulation. Subjects of negative consumer reviews can push content below the fold by adding their own content to the top of their Wikipedia page, to push the authentic negative information down, or bury the negative information by masses of positive marketing propaganda to create information overload and noise and to make information retrieval harder for consumers. *See* Jessica Bowman, *What To Do When Your Company Wikipedia Page Goes Bad*, SEARCH ENGINE LAND (June 27, 2007, 9:46 AM), http://searchengineland.com/what-to-do-when-your-company-wikipedia-page-goes-bad-11572 (explaining the breadth of marketing ideas for blurring past consumers' authentic reviews).

2. Sellers' Commercial Speech

Most analyses of sellers' incentives for disclosure assume perfect functioning of the market. Under the assumption that product quality is reflected in prices, a key result in the literature on disclosure states that sellers are likely to voluntarily disclose product information; more specifically, sellers are likely to voluntarily disclose all information that can be verified without cost.[97] In particular, sellers are likely to voluntarily disclose product information as a means of differentiating their own product and/or brand from others available on the market.[98] The intuition behind this result is that if the seller does not disclose product information, he will not be able to charge surplus for the additional quality provided. In the absence of information about product differentiation, consumers are expected to assume similar levels of quality for competing products; hence, sellers of above-average products are incentivized to disclose further information in order to distinguish their products from their lower-quality competitors.[99] Theoretically, this scenario may result in a reversed "lemons" process[100]: if consumers assume non-disclosing sellers are offering lower quality products, more and more sellers would disclose to associate themselves with higher quality products. More sellers would disclose and the process would repeat itself until all types (except the lowest of quality) disclose. Such process is expected to lower the average level of non-disclosing sellers, until every seller discloses.[101] Disclosure is

97. This result is rooted in the assumption of perfect functioning of the marketplace rule. If prices fully reflect quality, sellers have incentive to disclose information about product quality so that they can charge adequate prices for their product. Absent such disclosure consumers will not pay the stated price since they would assume the worst about the product's value. Thus sellers, except those offering the lowest quality, have an incentive to voluntarily disclose information regarding their product. If disclosure is costly, sellers are expected to voluntarily disclose only if their quality exceeds a threshold. *See* W. Kip Viscusi, *A Note on 'Lemons' Markets with Quality Certification*, 9 BELL J. ECON. 277, 277-79 (1978) (discussing quality certification as an option for high-quality sellers in certain markets); Sanford J. Grossman & Oliver D. Hart, *Disclosure Laws and Takeover Bids*, 35 J. FIN. 323, 323-27 (1980) (explaining that sellers will always distinguish themselves if there is no transaction cost).

98. *See* Sanford J. Grossman, *The Informational Role of Warranties and Private Disclosure about Product Quality*, 24 J.L. & ECON. 461, 464-65 (1981) (supporting the proposition that high-quality sellers have an incentive to voluntarily distinguish themselves).

99. *See* Beales, Craswell & Salop, *supra* note 31, at 503-06.

100. *See* Giang Ho & Anthony Pennington-Cross, *The Varying Effects of Predatory Lending Laws on High-Cost Mortgage Applications*, 89 FED. RES. BANK OF ST. LOUIS REV. 39, 43-44 (2007) (putting forth the "reverse lemons" hypothesis in the context of the mortgage market).

101. *See* Grossman, *The Informational Role of Warranties and Private Disclosure about Product Quality*, supra note 97, at 39 (implying that regulatory intervention in disclosure is

considered an effective measure because a key theoretical study predicts that if informed consumers reach a critical mass, sellers in sufficiently competitive markets will have an incentive to cater to the needs of these informed buyers and thus confer benefits to the non-informed consumers as well.[102]

However, product quality is only reflected in prices if the market functions efficiently,[103] and such efficient functioning requires rational, deliberating consumers, who are actively searching, processing and comparing product knowledge, and in turn, can translate their product knowledge into product quality and finally into price. When consumers fall short of this standard and fail to understand sellers' disclosures, disclosure is less likely to occur voluntarily: under such conditions, sellers of higher quality products will not be able to distinguish themselves from sellers of lower quality products, and low-quality sellers will have incentives to hide their quality.[104]

Despite these theoretical assertions, empirical studies show that the predicted theory of voluntary disclosure is not validated in practice. For example, in a study of salad dressing labels conducted in the U.S. prior to the Nutrition Labeling and Education Act's[105] mandatory disclosure requirements, only 9% of firms selling high fat salad dressing chose to disclose fat content on the product's label, whereas all sellers of low fat salad dressing voluntarily disclosed.[106] Sales of high fat dressings eventually declined after regulatory intervention that imposed mandatory disclosure rules.[107] Other empirical studies examined the effects of

completely unnecessary as eventually all sellers would disclose to signal quality). It is also backed up by some empirical works: George Benston, for example, compared the pre- and post-legislation disclosure made by firms prior to the adoption of the 1934 Securities Exchange Act. George J. Benston, *Required Disclosure and the Stock Market: An Evaluation of the Securities Exchange Act of 1934*, 63 AM. ECON. REV. 132, 144-45 (1973) (finding that no significant price effect resulted from the new mandated disclosure and concluding that voluntary disclosure prior to the act was sufficiently efficient).

102. Alan Schwartz & Louis Wilde, *Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis*, 127 U. PA. L. REV. 630 (1979).

103. THOMAS A. DURKIN & GREGORY E. ELLIEHAUSEN, TRUTH IN LENDING: THEORY, HISTORY, AND A WAY FORWARD 27 (2011)

104. This scenario is typically called market for lemons, since the marketplace rule applied here creates a race to the bottom on product quality: no seller has incentives to invest in higher quality products when higher quality cannot translate to higher prices. *See generally* George A. Akerlof, *The Market for 'Lemons': Quality Uncertainty and the Market Mechanism*, 84 Q. J. ECON. 488, 488-500 (1970) (explaining the market for lemons).

105. Nutrition Labeling and Education Act of 1990, Pub. L. No. 101-535, §§ 1-10, 104 Stat. 2353-67 (1990) (current version at 21 U.S.C. § 301 (2014)).

106. Alan D. Mathios, *The Impact of Mandatory Disclosure Laws on Product Choices: An analysis of the Salad Dressing Market*, 43 J.L. & ECON. 651 (2000).

107. *Id.*

informed minorities, showing that only about one in one-thousand online shoppers chose to become informed and read the contract, a number far below the critical mass Schwartz and Wilde seek.[108] These empirical studies also found that increasing contract accessibility does not result in an economically significant increase in readership or a sufficient number of informed consumers to create an informed minority.[109]

Indeed, models that examine how the market functions for product information given to consumers who do not understand disclosures predict that, if the number of informed consumers is insufficient to deter low-quality sellers from disclosing and overcharging, the threat of losing the informed consumers' business is too weak.[110] In the resulting equilibrium, low-quality sellers are expected to charge a price commensurate with high quality sellers. As Fishman and Hagerty state, "with no informed customers, price cannot signal quality."[111] Sellers might not disclose positive or negative product information due to insufficient incentives.[112] A seller is unlikely to disclose positive information relevant to all brands in a certain category because the disclosing seller would both share the benefits of disclosure with its competitors and solely carry the advertisement costs.[113] Likewise, sellers are not likely to disclose negative information

108. A key theoretical result predicts that if informed consumers reach a critical mass, sellers in sufficiently competitive markets will have an incentive to cater to the needs of these informed buyers and thus confer benefits to non-informed consumers. *See* Alan Schwartz & Louis Wilde, *Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis*, 127 U. PA. L. REV. 630, 659-62 (1979) (explaining that information problems in consumer markets raise difficult issues regarding how to determine and fix market imperfections). *See generally* Yannis Bakos, Florencia Marotta-Wurgler & David R. Trossen, *Does Anyone Read the Fine Print? Testing a Law and Economics Approach to Standard Form Contracts*, (N.Y.U Ctr. for Law, Economics and Organization, Research Paper No. 09-40, 2009) (casting doubt on the "informed minority" hypothesis, which holds that in competitive markets, an informed minority of buyers who are term-conscious is sufficient to discipline sellers from using unfavorable boilerplate terms).

109. *See* Mathios, *supra* note 106.

110. *See generally* Michael J. Fishman & Kathleen M. Hagerty, *Mandatory Versus Voluntary Disclosure in Markets with Informed and Uninformed Customers*, 19 J.L. ECON. & ORG. 45, 53 (2003) (analyzing the benefits and disadvantages of rules mandating the disclosure of sellers' information). Understanding a disclosure, in this regard, means understanding its implications. A consumer can be aware that a disclosure has been made, and that the information is available, without comprehending its consequences and implications. For example, a consumer may observe a nutritional food label without comprehending the health consequences associated with consuming the food.

111. Fishman & Hagerty, *supra* note 110, at 45, 53.

112. *See generally* Beales, Craswell, & Salop, *supra* note 31 (examining the complexities of how to properly and efficiently inform consumers and the ways in which the legal system has attempted to solve this issue).

113. Disclosures of category benefits may be beneficial enough to overcome this externality in cases of a monopoly or a large market share.

about a certain brand in a particular product category since such a disclosure would be expected to benefit all substitute suppliers, while no particular seller is likely to internalize the benefits of the disclosure.[114] Sellers are likely to count only their own profits as a benefit, and they do not count the additional profits obtained by other firms and the additional consumer surplus. From the individual seller's perspective, a free-riding externality can be beneficial to society. In determining what information to disclose, a seller is likely to ignore these benefits and balance only its individually attained, internalized benefits against the costs of providing information.[115] The result is undersupply of product information.[116]

The practice of obscuring the available information, often in the form of hidden add-on prices, thrives "even in highly competitive markets, even in markets with costless advertising, and even when the shrouding generates allocational inefficiencies."[117] To illustrate this argument, consider the consumer credit market. Since credit information tends to be complicated, consumers are typically imperfectly informed regarding the credit products they purchase.[118] Sellers, who provide that credit, are in a position to become the cheapest providers of information. Provision of voluntary information could be used to correct mistakes of consumer misperception. But, as Bar-Gill and Warren show,[119] insufficient incentives and the collective action problem are significant obstacles for such voluntary consumer education:

> If seller A reduces this risk and invests in educating consumers about the benefits of her superior product, then seller A will attract a lot of business and make a supracompetitive profit. But

114. *See* Beales, Craswell & Salop, *supra* note 31, at 503-04 (discussing free-rider problems).

115. *See* Beales, Craswell & Salop, *supra* note 31, at 507-09 (explaining that the incentive to disclose optimally can be restored if sellers obtain sufficient market power to capture most of the benefits of the information). Market power can stem "from a monopolistic or oligopolistic market structure or from a perceived monopoly caused by differentiation" of the seller's brand from other competing products." *Id.* at 504. While they supply better incentives for consumer information disclosure, these market structures are imperfectly competitive and inevitably create other imperfections in the performance of the product market. *Id.* at 491-539.

116. *See* Beales, Craswell & Salop, *supra* note 31, at 504 ("The general effect of these externalities [the free-rider problem] is to lead to an undersupply of general information.").

117. Xavier Gabaix & David Laibson, *Shrouded Attributes, Consumer Myopia, and Information Suppression in Competitive Markets*, 121 Q. J. ECON. 505, 505 (2006).

118. Barr-Gill & Warren, *supra* note 37, at 8-11.

119. Barr-Gill & Warren, *supra* note 37, at 11-20. *See also* John Y. Campbell, *Household Finance*, 61 J. FIN. 1553, 1554 (2006) (describing the collective action problem that prevents sellers from educating consumers in the mortgage market).

> this is not an equilibrium. After seller A invests in consumer education, all the other sellers will free-ride on seller A's efforts. They will similarly reduce the product risk and compete away the profit that seller A would have made. Anticipating such a response, seller A will realize that she will not be able to recoup her investment. Seller A will thus be less likely to improve the safety of her product, and instead will continue to offer a higher-risk product.[120]

Board suggests that sellers may choose not to disclose, despite a competitive environment, if disclosure would result in fiercer competition with rivals.[121] If one high quality firm chooses to disclose, others must trade off the increase in competition and resulting fall in price if they also disclose, with the effect on sales and reduced product quality, as perceived by consumers, if they do not disclose.[122] If the sales' effect and perceived decrease in product quality outweigh the increase in competition, the seller will prefer not to disclose.[123] However, when some high quality sellers choose not to disclose, this may generate a positive externality for low quality sellers.[124] These low quality sellers may pool together and take advantage of consumers' misperceptions of quality levels.[125]

Undersupply of product information can also result from the products' public good properties. This occurs when information used by consumers generates an external benefit to uninformed consumers.[126] These uninformed consumers shop randomly and enjoy the higher quality induced by the patronage of informed consumers.[127] This externality implies that not enough information will be produced, even in an otherwise efficient market.[128]

Another market failure in the supply side of product information involves reliability: there is not always sufficient incentive to supply truthful information. False positive claims and/or withholding of negative information can be beneficial to a seller, and thus considered optimal, if

120. Bar-Gill & Warren*, supra* note 37, at 18.

121. Oliver Board, *Competition and Disclosure*, 57 J. INDUS. ECON. 197, 198-99 (2009).

122. *Id.* at 198.

123. *Id.*

124. *Id.*

125. *Id.*

126. *See generally* MURALI PRASAD PRANTA, BUSINESS, CONSUMER AND THE GOVERNMENT: AN ECONOMIC AND LEGAL PERSPECTIVES 25 (2001) (discussing public good properties of information and its under supply amongst consumers)

127. *Id*.

128. *See generally* Steven Salop, *Information and Monopolistic Competition*, 66 Am. Econ. Rev. 240, 240 (1976) (arguing that when consumers have imperfect information, the market structure is not perfect competition, but rather, monopolistic competition).

consumers can sustainably believe them.[129] False advertising as a strategy can be worthwhile, especially for sellers of material products that involve ad hoc purchases and do not require long-term relationships with repeating consumers. Online consumer reviews are one means of mitigating the risk of false advertising because sellers of material products are often rated on retailer websites for their reliability.[130] However, as Bar-Gill and Warren note, this may only be a partial solution since consumers must still subscribe some publications, like *Consumer Reports*, and, most importantly, read the reports.[131]

The difficulty of supplying reliable information poses a significant hurdle when sellers lack a standardized measure or benchmark against which products can be compared. In many cases, sellers' voluntary disclosure means little without a backdrop to compare the underlying product whose features are disclosed. One example is the securities market. A company's statement regarding its expected return on investment is meaningless to a potential investor without a benchmark measure of industry or market performance for comparison.[132] For this reason,

129. Beales, Craswell & Salop, *supra* note 31, at 505-06.

130. eBay is one prominent example. eBay offers consumers the opportunity to rate sellers on four different categories: accuracy of the item description; consumer satisfaction with the seller's communication; shipping time for the item; and reasonableness of the shipping and handling charges. *Seller Ratings*, EBAY.COM, http://pages.ebay.com/help/feedback/detailed-seller-ratings.html Sellers are rated on a five star scale on each of these four categories, with five stars being the highest rating and one star the lowest. *Id.* In addition, consumers leave detailed narratives of their experiences and go into more specific depth. *Id.* Detailed seller ratings are anonymous, and sellers cannot see which buyer gave them a certain rating. *Id.* Consumers are thus free to be open about their buying experiences.

131. Bar-Gill & Warren, *supra* note 37, at 14-15.

132. CLYDE P. STICKNEY, ROMAN L. WEIL, KATHERINE SCHIPPER, & JENNIFER FRANCIS, FINANCIAL ACCOUNTING: AN INTRODUCTION TO CONCEPTS, METHODS, AND USES 244 (9th ed. 2000) (describing how to analyze and use a standard financial statement in order to make informed financial decisions). Stickney et al. explain that a similar argument is made for a uniform accounting standard for investors:

> Readers may have difficulty answering questions about a firm's profitability and risk from the raw information in financial statements. . . . Ratios aid financial statement analysis because they conveniently summarize data . . . [but] [r]atios, by themselves out of context, provide little information. For example, does a rate of return on common shareholders' equity of 8.6 percent indicate satisfactory performance? After calculating the ratios the analyst must compare them with some standard . . . [such as] [t]he corresponding ratio for a similar firm in the same industry . . . [or] [t]he average ratio for other firms in the same industry[.]

Id. at 233-34. *But see*, Sharon Hannes, *Comparisons Among Firms: (When) Do they Justify Mandatory Disclosure?*, 29 J. CORP. L. 699, 703 (2004) (arguing that the comparative securities regulation requires mandatory uniform conventions for financial statements and sees this mandatory uniform convention as central to its purpose[133]

Without mandatory standards of disclosure, every seller would disclose in her own terms, language and format. This would lead to market dynamics in which sellers would have no credible disclosure capacity or technology, as well as insufficient public quality assurances. Under such dynamics, as Akerlof's model of market for lemons suggests, only the average quality of the goods will be considered and fairly priced by consumers, and above average quality products will be driven out of the market.[134]

At the other end, market failures on the supply side of product information create incentives for information overload. Sellers are incentivized to provide and disseminate more information, as long as their own cost in so doing does not exceed their expected gain.[135] Since sellers gain when consumers switch brands, they are expected to provide further information aimed at incentivizing consumers to switch to a different brand, while losses occur for competitors and society as a whole.[136] Under such constraints, the losses to competitors can exceed the consumer surplus from switching brands, and the result is the overprovision of information.[137]

The possibility of information overload is further enhanced by an incentive to use abstract and vague commercial speech. In general, competition is expected to skew toward the easily observable characteristics of products.[138] Sellers are thus incentivized to invest in brands and signals, rather than in technical, detailed descriptions of the product's characteristics, since these are the factors that affect consumer choice.[139] This process is a generalization of a lemon's equilibrium in the markets.[140] If vague and abstract commercial speech is more easily observable and memorable by consumers, sellers have no incentive to

advantage for investors may not always justify mandatory disclosure because firms may voluntarily disclose information to obtain information about other firms).

133. *See* JAMES D. COX ET AL., SECURITIES REGULATION: CASES AND MATERIALS 7-9 (5th ed., 2006), (discussing continuous disclosure and other disclosure provisions).

134. Akerlof, *supra* note 104, at 488-490.

135. Beales, Craswell & Salop, *supra* note 31, at 509

136. *Id*.

137. *Id.* at 508-09.

138. One example is a car dealership that sells used cars. If cleanliness of cars is more easily observable and comparable by potential buyers, cleaner cars are expected to sell at a premium. Therefore, sellers are incentivized to over-invest in cleaning their inventory of cars, rather than investing in hidden, or less observable aspects of their underlying product quality. Beales, Craswell, & Salop, *supra* note 31, at 511.

139. Beales, Craswell & Salop, *supra* note 31, at 510.

140. Beales, Craswell & Salop, *supra* note 31 at 510.

invest in educating consumers regarding the true, detailed nature of their products. As a result, sellers do not invest in educating consumers.[141] This creates an information environment that results in spurious product differentiation and branding premiums, thus raising prices for functionally equivalent brands.[142]

The frequent use of boilerplate terms and standard form contracts in the consumer product market obscures product information through added complexity and information overload. Through the artificial framework of form contracts, sellers create an environment of high transaction costs for informed consumer purchasers.[143] As Gilo and Porat suggest, sellers might achieve several goals through this artificial complexity and informational overload, including: segmentation of consumers and price discrimination;[144] stabilization of cartels and obstruction of competition;[145] a façade of the consumer contract that disguises its true nature from potential consumers and third parties;[146] and a credible signal of non-negotiability, that creates a self inflicted barrier on negotiation.[147]

B. Market Failure in the Demand for Product Information

Empirical evidence suggests that consumers "often fail to make

141. *See generally*, Bar-Gill & Warren, *supra* note 37, at 17-20 (discussing why sellers do not tend to educate consumers).

142. Beales, Crasewell & Salop, *supra* note 31, at 510.

143. *See* David Gilo & Ariel Porat, *The Hidden Roles of Boilerplate and Standard Form Contracts: Strategic Imposition of Transaction Costs, Segmentation of Consumers and Anti Competitive Effects*, 104 MICH. L. REV. 983, 986 (2006) (suggesting that sellers use language as a screening method for unwanted customers and use a complicated contracting process as a means to screen repeated consumers from other consumers, who cannot afford to pay the high transaction costs of contracting, as well as the use of boilerplate terms to create price discrimination when benefits and discount are hidden between the lines of long contract language).

144. *Id*.

145. The complexity of terms creates higher transaction costs for consumers who want to compare similar products by rival sellers. Thus, it leads to "an equilibrium in which competition is less fierce, and profits [are], accordingly, higher." Gilo & Porat, *supra* note 144, at 1006. As Gilo and Porat argue, the use of complex form contracts and boilerplate terms to reduce competition is prominent and sustainable not only in monopolistic markets, but also in oligopolistic ones, if the long-term loss from a price war outweighs the short-term profit from price cutting. *Id*.

146. Gilo and Porat discuss cases where boilerplate terms in form contracts are used to hide salient features of the contract, such as exit possibilities from a services contract or insurance for high-risk products. *Id.* at 1014-15. In these cases, form contracts are used to create a fair impression and thus provide sustainability of their terms for the respective sellers, thereby minimizing the likelihood of a court intervention or negative public impact. *Id.* at 987.

147. *Id.*

rational decisions even within the bounds of the information they have acquired."[148] While rational actors would actively search and process product information and trigger competition that would make for an efficient market, real-life consumers fall short of such ability, creating a market failure on the demand-side of product information. Due to their bounded rationality, bounded will power, and psychological reaction to information overload, consumers often do not create sufficient disclosure incentives for an efficient market of product information. In the following section, I briefly survey some of the reasons for the demand side market failure.

1. Information Overload

In product information, more can often become less. Having the information is not enough: even if all potentially relevant information was theoretically obtainable and verifiable through sufficient research efforts, such availability is likely to have limited social effect. This is because the resources required for comprehensive product research and analysis are greater than the expected individual benefit that is likely to result.[149] The cognitive[150] and emotional[151] burdens placed on the consumer in evaluating

148. Melvin Aron Eisenberg, *The Limits of Cognition and the Limits of Contract*, 47 STAN. L. REV. 211, 216 (1995) (citing evidence).

149. This conclusion follows from rational models of the decision process. For example, according to one model, suggested by Stigler, a consumer is likely to invest in studying the alternatives up to the point where the costs of additional research would be higher than the surplus benefit expected. *See* George J. Stigler, *The Economics of Information*, 69 J. POL. ECON. 213-25 (1961) (analyzing the economic effect on the market of the search and identification of sellers and the discovery of their prices). Another model, introduced by Simon, suggests that the choice between alternatives would be made by the product's compliance with the consumer expectations as defined *ex ante*: the consumer is expected to choose not the best product, but rather the first sufficiently good product; that is, the first available product that complied with her *ex ante* expectation. *See* Herbert A. Simon, ADMINISTRATIVE BEHAVIOR 1-17 (3rd ed. 1976); *see also* Eisenberg, *supra*, note 148, at 211-25 (discussing limits on cognition that prevent consumers from making rational choices).

150. Cognitive limitations are augmented by the complexity of the available information, the varying reliability of the information's sources, and its varying forms of presentation. For a discussion of cognitive limitations, see Shmuel I. Becher, *Behavioral Science and Consumer Standard Form Contracts*, 68 LA. L. REV. 117, 120 (2007) (applying behavioral economic findings of cognitive limitations to challenge assumption of utility maximization in contract law); James R. Bettman, Mary F. Luce & John W. Payne, *Constructive Consumer Choice Processes*, 25 J. CONSUMER RES. 187, 187-217 (1998) (developing framework of constructive choice given consumers' limited processing capacity); DeNisi & Elaydi, *supra* note 33, at 50 (discussing both cognitive biases and lack of complete information in consumer decision-making); Tversky & Kahneman, *Judgment Under Uncertainty*, *supra* note 33, at 1124-31 (explaining generally several cognitive biases

the masses of available information are too heavy to instrument and allow daily investigation of the various product alternatives, each with an increasing number of data regarding complex characteristics schemes. On an individual level, the costs of such analysis per product exceed its expected benefits.[152]

Indeed, empirical research suggests that when available information exceeds the consumer's information processing capacity, the consumer has difficulties in identifying the relevant information,[153] exercises increased selectiveness in processing available information, thereby ignoring a significant portion of it,[154] confronts difficulties in identifying the relationship between details and overall perspective,[155] requires more time to reach a decision,[156] and generally reaches a suboptimal decision that compromises the accuracy of her autonomous choice.[157] The benefits of

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present in individual decision-making and judgment of an outcome's likelihood).

151. Consumers conduct emotional trade-offs when making a choice. *See* Luce, Bettman & Payne, *supra* note 33 (discussing the importance of emotional trade-offs in decision-making and what makes some trade-offs more emotionally difficult than others); Lisa Watson & Mark T. Spence, *Causes and Consequences of Emotions on Consumer Behaviour: A Review and Integrative Cognitive Appraisal Theory*, 41 EUR. J. MARKETING 487 (2007)(explaining how an integrated cognitive appraisal theory can be used to understand the causes of emotions).

152. Empirical literature calls this phenomenon "information overload" and defines it in several ways, all pointing to the masses of available information beyond what an individual subject's cognitive and emotional capacities allow her to process. *See generally*, Paul A. Herbig & Hugh Kramer, *The Effect of Information Overload on the Innovation Choice Process: Innovation Overload*, 11 J. CONSUMER MARKETING 45 (1994) (discussing information overload).

153. Jacob Jacoby, *Information Load and Decision Quality: Some Contested Issues*, 14 J. MARKETING RES. 569 (1977).

154. *See generally*. Herbig & Kramer, *supra* note 153, at 46 (explaining that information overload can have adverse effects on consumers' decision-making abilities); Claudia Klausegger, Rudolf R. Sinkovics & Huan "Joy" Zou, *Information Overload: a Cross-national Investigation of Influence Factors and Effects*, 25 MARKETING INTELLIGENCE & PLAN. 691, 709 (2007) (demonstrating negative correlation of information overload with fulfillment of job responsibilities); Paul R. Sparrow, *Strategy and Cognition: Understanding the Role of Management Knowledge Structures, Organizational Memory and Information Overload*, 8 CREATIVITY & INNOVATION MGMT. 140, 144 (1999) (discussing how, when faced with large volumes of information, managers tend to neglect large portions of information and try to punctuate its flow in predictable ways).

155. Susan C. Schneider, *Information Overload: Causes and Consequences*, 7 HUM. SYS. MGMT. 143, 143-53 (1987).

156. Jacob Jacoby, *Perspectives on Information Overload*, 10 J. CONSUMER RES. 432, 433 (1984).

157. Naresh K. Malhotra, *Information Load and Consumer Decision Making*, 8 J. CONSUMER RES. 419, 427 (1982). *See also* Naresh K. Malhotra, *Reflections on the Information Overload Paradigm in Consumer Decision Making*, 10 J. CONSUMER RES. 436, 436-40 (1984) (showing empirically that consumers can be overloaded and defining limits on the number of alternatives and attributes that consumers can process without

acquiring product information often fail to exceed the costs.[158]

Once information overload is detected, it is interesting to ask why consumers do not demand simple and accessible disclosure. For an individual consumer, the costs of making such a demand outweigh its potential benefit[159], and collective action problems[160] make a public claim hard to achieve. Moreover, voicing a concern about accessible information requires some awareness of the costs and mal-effects of information overload, and such awareness may be present in fewer consumers than those who need informational protection. Optimism and overconfidence make it natural for many consumers to trust their ability to process product information rather than acknowledge that the effort required is not reasonable, even if potentially possible to overcome.[161] Demanding that sellers simplify their information entails an acknowledgement of one's own limitations, imposing a psychological cost on consumers making such a request.[162]

experiencing the dysfunctional consequences of information overload); *see also* Russell Korobkin, *Bounded Rationality, Standard Form Contracts, and Unconscionability*, 70 U. CHI. L. REV. 1203, 1220 (2003) (discussing generally behavioral economic theory of choice). One question arising from this (concise) description of information overload's effects is the definition of accuracy in consumer decision-making. An underlying assumption of the dysfunctional effects of information overload seems to be that the consumer's aim is preconceived and predetermined before she begins to consider her purchase opportunities. This assumption seems to be partially incorrect because consumers do not always know in advance exactly what they want. Recent studies in cognitive psychology show that people's ability to forecast their future happiness (or utility, in economic terms) is contingent and partial. *See* DANIEL TODD GILBERT, STUMBLING ON HAPPINESS 18-19 (2006); Daniel T. Gilbert & Timothy D. Wilson, *Prospection: Experiencing the Future*, 317 SCI. 1351, 1352 (2007) (explaining the various conditions that must be met in order for a person's present hedonic experience to be a reliable predictor of their future hedonic experience). Hence, the accuracy of an actual consumer choice is to be determined in relation with a dynamic model of our preconceived desire, rather than a static preconception of the desired good. Since this dynamic model of desire conception is also affected by the context within which the choice is made, including the information environment, information overload may affect the consumer's perception of the desired good, making the discrepancy between the preconceived desire and the actual choice harder to detect and to measure.

158. *See generally* HOWARD RAIFFA, DECISION ANALYSIS: INTRODUCTORY LECTURES ON CHOICES UNDER UNCERTAINTY 181 (1968) (analyzing formally how costly information is to acquire).

159. *Id.*

160. *See supra* note 86 and accompanying text (discussing the collective action problem in the consumer community).

161. *See supra* Part II.B.2, notes 163-168 and accompanying text.

162. For a detailed explanation of this cost, see *infra* Part II.B.2.

2. Optimism and Overconfidence

Consumers are unrealistically optimistic and systematically fail to accurately evaluate risks and probabilities of success.[163] Nearly ninety percent of drivers believe they drive better than average,[164] while ninety-seven percent of consumers believe that they are either average or above in their ability to avoid accidents with bicycles.[165] Even when consumers are explicitly warned about product risk, they are unlikely to internalize and incorporate such risks in their consumer choices.[166] For example, only three percent of consumers who were informed of the risks associated with bleach and drain cleaner considered their home to present an above-average risk for hand burn and child poisoning from the use of drain cleaner, gas poisoning, or injury to children from the use of bleach; half of the consumers believed their house to pose average risk, while the other half believed their house was lower than average risk.[167] Since consumers fail to understand and internalize products' risks and the likelihood of their occurrence, they are not likely to pay for better, safer products, which is necessary in order to form a competitive market that will create sufficient incentives for suppliers to invest in minimizing the risks.[168]

3. Framing and Rules of Thumb

For efficient functioning of the market for product information, it is necessary to assume invariance—i.e., that a consumer's choice between two options should not depend on how such choice is characterized and

163. This is a well-documented human fallibility. *See, e.g.*, Neil D. Weinstein, *Unrealistic Optimism About Future Life Events*, 39 J. PERSONALITY & SOC. PSYCHOL. 806, 806 (1980) (discussing surveys concerning automobile accidents, crime, and disease that suggest people are unrealistically optimistic about the future).

164. Ola Svenson, *Are We All Less Risky and More Skillful Than Our Fellow Drivers?*, 47 ACTA PSYCHOLOGICA 143, 146 (1981).

165. W. KIP VISCUSI & WESLEY A. MAGAT, LEARNING ABOUT RISK: CONSUMER AND WORKER RESPONSES TO HAZARD INFORMATION 95-106 (1987). Overconfidence and optimism are documented across all aspects of life. For example, people who were about to get married were overconfident about their divorce-related prospects as compared to the rates of the entire population; even when the median of respondents predicted that fifty percent of the population gets divorced, the median of respondents predicted their own chances as zero percent. Lynn A. Baker & Robert E. Emery, *When Every Relationship is Above Average: Perceptions and Expectations of Divorce at the Time of Marriage*, 17 L. & HUM. BEHAV. 439, 443 (1993). In general, most people think they can do better than others and perceive themselves as immune from hazards and risks.

166. *See* VISCUSI AND MAGAT, *supra* note 165, at 93-97.

167. *Id.*

168. *Id.*

presented, or framed.[169] Rational consumers should not be affected by different presentations of the same information; rather they should be able to drill down to the essence of the information, and take all relevant facts into account.[170] Real-life consumers, however, rarely fulfill this criterion.[171]

One example of the framing effect is loss aversion. A series of experiments showed that when something is framed as a loss, it is generally perceived as being more costly than if it were framed as an equivalent absence of gain; this is because rather than assigning specific values to objects, people vary in their value estimation based on the default, or base-line allocation.[172] Other prominent examples of the framing effect are systematic biases, or heuristics, which were identified by Amos Tversky and Daniel Kahneman in the 1970s.[173] Tversky and Kahneman demonstrated that anchoring, availability, and representativeness systemically bias human judgment.[174] Anchors influence consumer choice by suggesting a starting point for the thought process: Tversky and Kahneman show that people's decisions are influenced significantly by the immediate figure, question, or experience preceding the decision-

169. Amos Tversky & Daniel Kahneman, *Rational Choice and the Framing of Decisions, in* CHOICES, VALUES, AND FRAMES 4 (Daniel Kahneman & Amos Tversky eds., 2000) [hereinafter, Tversky & Kahneman, *Rational Choice*].

170. *Id.*

171. Tversky & Kahneman, *Rational Choice*, at 210 (noting that consumers' actual behavior often violates invariance); *see also* Amos Tversky & Daniel Kahneman, *The Framing of Decisions and the Psychology of Choice*, 211 SCI. 453, 453 (1981) (discussing the effects of the different ways of framing problems on preference) [hereinafter Tversky & Kahneman, *Psychology of Choice*].

172. Consider this experiment: a class is randomly divided into two groups. Half the students are given a coffee mug and the other half are instructed to try to trade for their classmates' mugs. Daniel Kahneman, Jack L. Knetsch & Richard H. Thaler, *Experimental Tests of the Endowment Effect and the Coase Theorem*, 98 J. POL. ECON. 1325, 1330-31 (1990). Efficient market functioning and utility theory would predict that mugs would end up spread randomly in the class because the group who gained them as a default would trade with the other group, so that the result would be even distribution of the mugs between these two groups (there is no reason to assume an inherent preference for the mugs within the first group, as the class is divided randomly). However, loss aversion and the framing effect make for a completely different result. *Id.* at 1343. The group that received the mugs requires twice as much as others are willing to pay for it. *Id.* at 1338.

173. *See* Amos Tversky & Daniel Kahneman, *Availability: A Heuristic for Judging Frequency and Probability*, 5 COGNITIVE PSYCHOL. 207, 208-09 (1973) [hereinafter Tversky & Kahneman, *Availability*] (discussing the subjective biases that result through the use of an availability heuristic); Tversky & Kahneman, *supra* note 33 (discussing systematic error in commonly-used heuristics, including representativeness, availability of instances or scenarios, and adjustment from an anchor).

174. *See* Tversky & Kahneman, *Availability*, *supra* note 173, at 208-09 (providing an overview of a study showing the impact of anchoring, availability, and representativeness on human judgment).

making.[175] Human judgment in general, including consumer choice, is considerably influenced by the comparable data and scenarios available to the memory or imagination.[176] Finally, Tversky and Kahneman show that people tend to base decisions on some subset of data they judge to be representative, leading to systematic erroneous judgments.[177] In the product markets, the subset of the relevant data that is used as a shortcut to a comprehensive search for the facts is often the brand name.

These works show that, rather than making independent decisions that are isolated from their context, humans use rules of thumb for their decision-making, subjecting the resulting choice to deep influence by ways in which alternatives are framed. Therefore, framing plays a meaningful role in consumer markets. In a variety of consumer contexts, sellers use framing effects to increase prices and reduce efficiency and consumer welfare. To illustrate, consider the effects of "add-on" pricing practices: sellers artificially divide products to several different charges, advertising a base price for a product and then offer additional "add-ons" at the time of sale.[178] Even in e-commerce involving search engines, which can be expected to be highly competitive, sellers create artificial complexity and obfuscate product information so as to increase sales based on consumers'

175. *See* Tversky & Kahneman, *Judgment Under Uncertainty*, *supra* note 33, at 1128-29 (discussing anchoring effects)..To illustrate, consider this experiment: subjects were asked two questions: (a) How happy are you? (b) How often are you dating? When asked in this order, the correlation between the responses for these two questions was quite low, but when the question order was reversed, so that the dating question preceded the happiness question the correlation jumped significantly (from 0.12 to 0.66). Fritz Strack, Leonard L. Martin & Norbert Schwarz, *Priming and Communication: Social Determinants of Information Use in Judgments of Life Satisfaction*, 18 EUR. J. SOC. PSYCHOL. 429, 437 (1988).

176. *See* Taversky & Kahneman, *Availability supra* note 173, at 207-09 (discussing the availability heuristic. The availability heuristic is commonly demonstrated by decisions to buy insurance: the spatial and temporal proximity of disasters is most influential in that regard, such that consumers typically choose to hedge, or buy insurance, against familiar and easily accessible risks. *See* Tversky & Kahneman, *Judgment Under Uncertainty*, *supra* note 33, at 1128 (discussing how the ability to imagine a future event impacts and risk-taking).

177. *See* Taversky & Kahneman, *Judgment Under Uncertainty*, *supra* note 33, at 1124-27 (providing a general discussion about representativeness). Representativeness is the tendency to judge the likelihood of an event based on its similarity to a present event, while ignoring other relevant facts; or, the tendency to judge characteristics of an object based on its similarity to an image or stereotype. *See* Daniel Kahneman & Shane Frederick, *Representativeness Revisited: Attribute Substitution in Intuitive Judgment*, *in* HEURISTICS AND BIASES: THE PSYCHOLOGY OF INTUITIVE JUDGMENT 49, 49-50 (Thomas Gilovich, Dale Griffin & Daniel Kahneman eds., 2002).

178. Consider examples such as: a printer and ink, a hotel and Internet connection, and a flight and airport taxes. *See* Glenn Ellison, *A Model of Add-On Pricing*, 120 Q.J. ECON. 585 (2005) (discussing various examples of firms using add-ons).

confusion and bounded rationality.[179] Spiegler shows that, in general, sellers respond to the bounded rationality of consumers with an increased effort to obfuscate, rather than with more competitive pricing.[180]

The result is that the surrounding narrative of a product sales point significantly influences consumer choice, thereby creating a market failure on the demand side of product information. Sellers, in turn, have incentives to create a manipulative environment during the selling experience, using the framing effects and heuristics in branding techniques in order to influence consumer choice, rather than providing consumers with legible and easily comprehendible product information, as rational consumers would require.

4. Bounded Will-Power

Market failure on the demand side of product information often occurs despite consumers' awareness of their interests—due to psychological, rather than cognitive, limitations. Real-life consumers often make choices that the rational consumer would avoid because their will-power does not suffice for better decisions, which would require actively searching for and comparing the alternatives.[181] This occurs when consumers mindlessly choose products, follow the herd in their purchases, or fail to alter the situation and prefer the default option they are using.[182]

Rational consumers would always prefer more options.[183] Real-life consumers are, however, often made worse off by a multitude of alternatives because they cannot resist the temptation to consume products that are readily available, or immediately satisfactory, while being harmful

179. *See* Glenn Ellison & Sara Fisher Ellison, *Search, Obfuscation, and Price Elasticities on the Internet*, 77 ECONOMETRICA 427, 438 (2009) (discussing obfuscation and the possibility that many firms use intentionally confusing websites in order to trick consumers who use search engines).

180. Ran Spiegler, *Competition Over Agents With Boundedly Rational Expectations*, 1 THEORETICAL ECON. 207, 219-220 (2006).

181. *See* Bar-Gill & Warren, *supra* note 37, at 12 (explaining that imperfectly rational consumers might not seek out information because they do not think that they need more information or because they think the unknown information is "trivial, irrelevant, or insufficiently important to justify the cost of its acquisition.").

182. *See generally* Bar-Gill & Warren, *supra* note 37, at 12 (positing reasons for why consumers may remain uninformed about products).

183. This conclusion follows from rational models of the decision process, *see supra* note 149 and accompanying text; *see also* Sheena Sethi-Iyengar, Gur Huberman & Wei Jiang, *How Much Choice is Too Much? Contributions to 401(k) Retirement Plans*, *in* PENSION DESIGN AND STRUCTURE: NEW LESSONS FROM BEHAVIORAL FINANCE, 83, 84 (Olivia S. Mitchell & Stephen P. Utkus eds., 2004) (discussing the historical presumption that consumers perceive more choice as better).

in the longer term.[184] Empirical works repeatedly show that humans systematically fail to self-regulate their consumption when tempted or manipulated by suppliers.[185] Psychologists distinguish between two processing systems, which correspond to intuition and reason.[186] These two-system models of processing are mostly referred to as System 1 and System 2.[187] Decisions relying on System 1 processes often rely on a spontaneous, automatic, un-conscious process and correspond to intuition.[188] Decisions relying on System 2 processes are deliberate, controlled, skillful, and correspond to intellectual reasoning.[189] It is System 1 that we seek to restrain in order to fulfill our longer-term goals.[190]

Consumers often make decisions mindlessly, without allocating sufficient processing resources to access cognitions related to System One. For example, in one study, respondents chose between two alternatives: a chocolate cake, "associated with more intense positive affect but less favorable cognitions," versus a fruit salad, "associated with less favorable

184. A classic example for such a need is that of Ulysses, who instructed his crew to tie him to the mast so that he could listen for himself but be restrained from submitting to the temptation to steer the ship closer. HOMER, THE ODDYSSEY 275 (Robert Fagles trans., 1997).

185. Food is a good illustration of the difficulty of resisting temptation: otherwise, obesity would not have occurred so frequently in the Western world. Consider, for example, the following experiment: subjects were given free buckets of stale popcorn in a movie theatre. Half the subjects received big buckets, while the other half received medium-sized buckets. Recipients of the bigger bucket ate 53% more stale popcorn. *See* BRIAN WANSINK, MINDLESS EATING: WHY WE EAT MORE THAN WE THINK 16-18 (2010) (showing the lack of will-power when presented with stale popcorn). People tend to eat what is readily available rather than deliberate on the food's merits. For a general discussion of obesity and market manipulation, see Adam Benforado, Jon Hanson & David Yosifon, *Broken Scales: Obesity and Justice in America*, 53 EMORY L.J. 1647 (2004).

186. Kahneman & Frederick, *supra* note 177, at 51.

187. *See* Kahneman & Frederick, *supra* note 177, at 51.

188. Kahneman & Frederick, *supra* note 177, at 51 tbl. 2.1.

189. Kahneman & Frederick, *supra* note 177, at 51 tbl. 2.1.

190. Or, in order to fulfill our autonomous desires. A key concept that requires deliberation here is that of autonomy. Since both System 1 and System 2 decisions stem from the same subject, it is philosophically important to justify our preference for one over the other. One way to define autonomy is as a *relationship* between individuals' actions and their preferences, and between individuals' preferences and their selves. Essentially, autonomy is defined here as a consistency between one's self (as accorded by her desired preferences) and one's behavior. Note that the underlying assumption here is that the set of preferences is separate from the "self." Essentially, this view defines autonomy as consistency between two layers of the "self," the core self and a set of preferences that is presumably detached from that core. This assumption was severely criticized as artificial and farfetched. *See, e.g.*, Susan Wolf, *Sanity and the Metaphysics of Responsibility*, *in* RESPONSIBILITY, CHARACTER, AND THE EMOTIONS: NEW ESSAYS IN MORAL PSYCHOLOGY, 48-50 (Ferdinand Schoeman ed., 1987) (discussing theoretical view of agency that utilize this assumption and proposing an alternative theoretical view of agency – "the deep self view").

affect but more favorable cognitions."[191] Findings from such experiments suggest that if processing resources are limited, spontaneously evoked affective reactions, rather than cognitions, tend to have a greater impact on choice.[192] As a result, the consumer is more likely to choose the alternative that is superior on the affective dimension, but inferior on the cognitive dimension (e.g., chocolate cake).[193]

5. Status-quo Bias and Short-sightedness

Making decisions is costly: it is time consuming, and requires cognitive effort and deliberative energy. Thus, most people tend either to stick with the current situation or to prefer their original choice over and over again.[194] For some choices, such as a breakfast menu or running trail, sticking to the original choice makes sense. For others though, inability to change and preference to the current may turn very costly.[195] Because consumers lack the energy to change their decisions, sellers have incentives to create honey traps that are structured aggressively as great bargains for the short term and that require high opt out costs.[196] Consumers' preference for the status quo is related to their shortsightedness in evaluating the alternatives they are offered. Thinking of the longer term costs of product maintenance requires complex calculation and cognitive effort. Sellers have incentives to structure their product as a great bargain, offering a lower purchase-price to hide the high maintenance and usage costs.[197] By the time consumers become aware of the actual cost of the product, the costs consumers incur to change their usage habits ultimately deter the

191. Baba Shiv & Alexander Fedorikhin, *Heart and Mind in Conflict: The Interplay of Affect and Cognition in Consumer Decision Making*, 26 J. CONSUMER RES. 278, 288 (1999).

192. *Id.* at 288.

193. *Id.* at 278.

194. This effect is commonly referred to as the "status quo bias." *See, e.g.*, William Samuelson & Richard J. Zeckhauser, *Status Quo Bias in Decision Making*, 1 J. RISK & UNCERTAINTY 7, 8 (1988) (documenting empirically the "status quo bias").

195. A good illustration for the costs of inertia is failure to update the investment portfolio of pension plans throughout a career, so that the investments for the pension retain the default contribution rate and fund allocation. Brigitte C. Madrian & Dennis F. Shea, *The Power of Suggestion: Inertia in 401(k) Participation and Savings Behavior*, 116 Q.J. ECON. 1149, 1184–86 (2001).

196. This strategy is commonly used in many industries. Credit cards offer a first year free of annual fees, magazines offer great bargains for the first few months, cell phones are offered as great bargains if consumers commit to stay as customers for 3 years, during which the seller has sole discretion to change the fees.

197. *See, e.g.*, Jim Rendon, *Much More Than Just 'Maintenance*,*'* N.Y. TIMES (Jan. 12, 2012), http://www.nytimes.com/2012/01/15/realestate/getting-started-much-more-than-just-maintenance.html?pagewanted=all (noting that the costs of condos in New York are often accompanied by high monthly maintenance fees).

consumer from changing products; as a result, the seller may reap higher prices.[198] Legal intervention may be justified as a means to overcome this bias, inform consumers of the total costs of ownership, and of the temporal alteration options, as well as to set efficient defaults for complex product choices.

C. *Sustainability Reporting*

Recent trends in corporate governance reflect an abundance of corporate "sustainability" reporting – in addition to the established financial reports based on accounting standards – that focus on the corporation's environmental and social impact. A study by the Investor Responsibility Research Center Institute (IRRCI) suggests that 499 of the 500 corporations in the S&P 500 made sustainability disclosures in a financial filing, or linked financial performance to a sustainability initiative.[199] This indicates that corporations may be willing to communicate voluntarily with investors on a variety of topics – including more than those required for disclosure in compliance with the federal securities laws.

Sustainability reporting is significant because it creates a wider scope of information for investors that includes benchmarking and assessment of non-financial performance measured by a uniform format developed by the Global Reporting Initiative (GRI)[200] and voluntarily adopted by many corporations.[201] However, even close adherence to the GRI standards of disclosure would not promote consumers' freedom of choice or the efficiency of the consumer products market. Sustainability reporting is made for investors rather than consumers because it is not product-specific and does not compare the material information about products offered by

198. This strategy is commonly used in software sales. Software is often sold at a bargain or given free with high costs for technical support and service, so that the total costs of ownership are much higher than the apparent purchase price. *See* Raj Sabhlok, *Open Source Software: The Hidden Cost of Free*, FORBES (July 18, 2013, 10:00am), *available at* http://www.forbes.com/sites/rajsabhlok/2013/07/18/open-source-software-the-hidden-cost-of-free/ (noting that free open-source software may be cost-effective, but has "ongoing maintenance and support [costs] as well as the up-front development [costs]").

199. PETER DESIMONE, INVESTOR RESPONSIBILITY RESEARCH INSTITUTE, SUSTAINABLE INVESTMENTS INST., INTEGRATED FINANCIAL AND SUSTAINABILITY REPORTING IN THE UNITED STATES 5 (2013), *available at* http://irrcinstitute.org/pdf/FINAL_Integrated_Financial_Sustain_Reporting_April_2013.pdf.

200. *Mission and Vision*, GLOBAL REPORTING INITIATIVE, https://www.globalreporting.org/Pages /default.aspx (last visited Oct. 14, 2014).

201. *See, e.g.*, DESIMONE, *supra* note 199, at 109 (noting that Southwest Airlines' 10-K stated that the company "undertakes voluntary investigation or remediation of soil or groundwater contamination at several airport sites." (internal citations omitted)).

material categories.[202] Therefore, sustainability reporting's materiality stops at the investor reporting level. Sustainability reporting is a significant step in the development of corporations as good citizens, but has no impact on their role as sellers in real life.

D. Third Parties' Commercial Speech

Product information cannot be sufficiently supplied by third party information providers, such as consumers' unions, because of the nature of product information as a natural monopoly, which creates a free rider externality.[203] Since information collected and generated by professional third parties can be disseminated at low marginal cost (i.e., a natural monopoly), and consumers can redistribute purchased information to other free rider consumers, economic theory predicts a professional third party is expected to produce less than efficient amounts of information, as its profits will not enable internalization of the real demand to its information processing service.[204]

In reality, as in economic theory, third parties and consumer unions do not seem to sufficiently address the difficulty of informational darkness in the consumer products market. The impartial product review published by Consumer Reports is a partial solution, but it only considers a limited number of categories of products and it compares only a few of the available brands for each product surveyed.[205] While providing a significant service, third parties are not a thorough solution to the problems of product information.

Third parties that provide information must bear the costs of the information search, verification, and analysis (and, occasionally, pricing). Regulation may be justified as a means to reduce these costs. As these costs decrease, the number of third party agents and information traders is

202. *See* Jeff Civins & Mary Mendoza, *Corporate Sustainability and Social Responsibility: A Legal Perspective*, 71 TEX. B.J. 368, 369 (2008) (noting that corporations' sustainability programs typically include "strategic planning; corporate policy and goals and procedures to implement them; infrastructure; a code of conduct; standards, manuals, and guides; stakeholder communication, including dialogue and reporting; performance and appraisal metrics; and line responsibilities.").

203. *See* Beales, Craswell & Salop, *supra* note 31, at 503 (discussing the costs of consumer protection regulation). Consumers' ignorance benefits sellers on average also due to the sub-optimal use of products by ignorant consumers); *see also supra* notes 114-116 and accompanying text (discussing the how the free-rider problem leads to a dearth of information for consumers).

204. Beales, Craswell & Salop, *supra* note 31, at 503.

205. *See* Beales, Craswell & Salop, *supra* note 31, at 504 (discussing a speech of third parties and Consumer Reports). Business initiatives such as Kamaze and the like may be an exception to this rule.

expected to increase,[206] and their contribution is expected to be more precise.[207] The cost of obtaining product information is minimal for the corporation that creates it, but it is very expensive for the information trader who is an outsider seeking to uncover nonpublic information. This is especially true with regard to complex products that often require extensive research in order to reveal their true nature and characteristics. Without mandatory disclosure, information traders are bound to engage in duplicate efforts to reach the same information and uncover it only partially. Mandatory disclosure may be justified as a means to lower and subsidize these costs.

Uniform disclosure duties can be justified as a means to improve and enhance the competition between information traders and third party information providers, and as a means to reduce the entry barriers to the market of information trading in the products market. Requiring corporations to disclosure product information to their consumers can effectively subsidize search costs for consumers, facilitate a competitive market for information traders of product information, who may offer similar services to those offered by *Consumer Reports*, and enhance consumer market efficiency and consumers' freedom.

III. CONSUMERS' CORPORATE MEMBERSHIP

A. Consumer Organizational Membership

Corporations should be accountable to consumers for their products' information because of the nature of their relationship with their consumers. Most consumer contracts are constructed very similarly to organizations[208]: consumers purchasing a cell phone, entering a health insurance program, signing up for a daily paper, or ordering cable television are each signing a form contract, but simultaneously subjecting themselves to the rules and procedures of the seller's corporate organization. It is a long and well-established truth that consumers do not really negotiate agreements with corporate providers.[209] Instead, consumers

206. Goshen & Parchomovsky, *supra* note 66, at 741–43.

207. This argument is assuming that mandatory disclosure lowers the effect of noise traders and associated noise risk. *See id.* at 738–39 (discussing the risk of estimating undiscoverable undisclosed information).

208. Menachem Mautner, *Judicial Intervention in the Contents of Contracts and the Question of the Future Development of Israeli Contract Law*, 29 TEL AVIV U. L. REV. 17, 30-35, nn. 28, 38 (2005).

209. RESTATEMENT (SECOND) OF CONTRACTS § 17 (1981); Friedrich Kessler, *Contracts of Adhesion—Some Thoughts About Freedom of Contract*, 43 COLUM. L. REV. 629, 631–32 (1943); Todd D. Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96 HARV. L.

simply choose to enter into a contractual relationship governed completely by the terms of the corporate entity, and during the term of the contract, corporate providers often control all aspects of the relationship.[210]

Corporations are for-profit organizations formed by their shareholders who seek to maximize earnings while isolating the risks through their limited liability status. Scholars of Organizational Behavior often define an organization as a social system of collaboration that strives to maintain or achieve a common goal or objective.[211] Since corporations constantly change their business activity and goals over time, it has been suggested that the organizational goal is simply one of continued survival and perpetuation.[212] In general, organizations are distinct from other social entities.[213] First, organizations are formally recognized by a governmental agency.[214] Often the organization is created by official documents, such as charters, articles of association, bylaws or statutes that are filed with the state's bureaucracies.[215] Second, organizations are distinct in their *boundaries*.[216] Members of the organization may choose to *enter* an organization, and may choose to *exit* it.[217] While contracted with it, though, they are subject to its rules and regulations, as well as to its culture and ethics base.[218] Boundaries are a key element of organizational culture, and often significant resources are devoted to their maintenance and

REV. 1174, 1224–25 (1983).

210. *See* Rakoff, *supra* note 209, at 1224 (noting that firms "do not want to negotiate individualized contracts because doing so entails bearing not only the costs of the particular negotiations, but also the economic and institutional costs of modifying an organizational structure geared to the standardized terms.").

211. However, the goal pursuit definition is incomplete as many members of the organization do not share the ultimate goal that the organization was formed to achieve. Corporations are typically formed for profit maximization, but many of their stakeholder members, including consumers and employees, do not share that original goal and are not committed to it. JERALD GREENBERG, MANAGING BEHAVIOR IN ORGANIZATIONS 9 (2010); JEFFREY PFEFFER, NEW DIRECTIONS FOR ORGANIZATION THEORY: PROBLEMS AND PROSPECTS 7 (1997) [hereinafter PFEFFER, NEW DIRECTIONS]; JEFFREY PFEFFER, ORGANIZATIONS AND ORGANIZATION THEORY 125-26 (1982) [hereinafter PFEFFER, ORGANIZATIONS]; W. RICHARD SCOTT, ORGANIZATIONS: RATIONAL, NATURAL, AND OPEN SYSTEMS 23-24 (1992).

212. *See* Pfeffer, NEW DIRECTIONS *supra* note 211, at 7.

213. Pfeffer, NEW DIRECTIONS, *supra* note 211, at 7.

214. Pfeffer, NEW DIRECTIONS, *supra* note 211, at 7.

215. *See, e.g.*, DEL. CODE. ANN. tit. 8, § 101(a) ("Any . . . corporation . . . may incorporate . . . under this chapter by filing with the Division of Corporations in the Department of State a certificate of incorporation. . . .").

216. Pfeffer, NEW DIRECTIONS, *supra* note 211, at 9.

217. *See* Pfeffer, NEW DIRECTIONS, *supra* note 211, at 9 (stating that "maintenance and demarcation" of boundaries are important in organizations).

218. *See* Pfeffer, NEW DIRECTIONS, *supra* note 211, at 9 (noting that, while "organizational boundaries are clearly permeable . . . permeability is to some degree under the control of the organization.").

demarcation, as membership with the organization is an indicator of class and social status.

The typical nature of the corporate relationship with its consumers resembles corporate organizational membership more than it does a contract, and this suggests that corporate law is the more appropriate legal platform for protecting consumer rights. Mautner suggests that consumer contracts resemble organizations in three key manners[219]: first, as members of a corporation, consumers choose to *enter* into their relationships with the seller; second, as members of a corporation, consumers choose to *exit* their relationships with the seller when they end the consumer contract;[220] and third, as members of a corporation, consumers are not able to negotiate the terms of engagement with the seller, but rather subject themselves during the contract period to the seller's complex web of rules and regulations of social control.[221]

Consumers are often subjected to corporate rules and regulations during the term of their contract. Consider, for example, a parent's contract with his or her daughter's preschool. While the parent opts into the agreement voluntarily, once contracted, the entire relationship is set through the preschool's management, which often sets careful procedures to manage the content and form of the daughter's daily life and to manage the parent's ability to opt out and end the relationship. Most technological products set similar boundaries for their consumers, who can choose to purchase and use the product as pre-programmed by the corporate provider, but are not allowed to amend any of its features. Even a standard contract with a health insurer is typically so overloaded with information and includes so many fine-print details that the outcome is the same: the consumer can choose either to purchase or not to purchase the coverage offered, but its terms are unilaterally set by the corporate insurer in its sole discretion and may include any number of exclusions.[222]

While contracts are conceived of as arrangements supposedly

219. Mautner, *supra* note 208, at 30-35, nn. 28, 38.

220. Mautner, *supra* note 208, at 30-35 nn.28, 38. Interestingly, commentators note that corporations often impose a capital lock in provision on their investors. Margaret M. Blair, *Locking in Capital: What Corporate Law Achieved for Business Organizers in the Nineteenth Century*, 51 U.C.L.A. L. REV., 387, 388-89 (2003). Lynn A. Stout argues that the nature of the corporation can be better understood by focusing on its capacity to lock in equity investors' initial capital contributions by making it far more difficult for those investors to subsequently withdraw assets from the firm. A corporation is much easier for equity investors to get into than to get out of. *See* Lynn A. Stout, *On the Nature of Corporations*, U. ILL. L. REV. 253, 253-67 (2005).

221. Mautner, *supra* note 208, at 30-35 nn.28, 38.

222. *See, e.g.*, *Cigna Healthcare Policies*, CIGNA, *available at* http://www.cigna.com /cigna-healthcare-policies (last visited, Dec. 9, 2014) (providing an extensive list of policies, each with its own paragraph description).

mutually agreed to by all parties, organizations have preconceived constructs that are typically prefixed at the moment of a particular agent's entry and are harder for the member to change or affect otherwise.[223] The rules and culture of the organization are a means to achieve social control and coordination between its members. Given that consumers are rarely negotiating parties in control of the details of their arrangement with the seller, their relationship with sellers resembles organizational membership more than it resembles classical contracts: by purchasing the product, consumers choose to consume the product under a detailed set of terms and conditions prefixed by the corporate seller. At the moment of purchase, the consumer does not mutually agree to the terms of the consumer contract, but rather subjects herself to the corporate seller's organizational culture, rules, and procedures in providing the service or product hoped for.

B. Stakeholder Theory

Corporate accountability towards consumers is based on the premise that corporations are established to create social value rather than merely profit for shareholders.[224] Although the conventional analysis of corporate law is focused on reducing agency costs created from the divergence between management, owners, and controlling and non-controlling owners, stakeholder theory refuses to see shareholders as the ultimate beneficiaries of corporate law, but instead sees them as owners of a residual interest in its profits.[225] A stakeholder approach to business defines the corporate purpose as creating as much value as possible for all stakeholders,[226] classically defined as "any group or individual who can affect or is affected by the achievement of the organization's objectives."[227] Under the

223. Mautner, *supra* note 208, at 30-35, nn. 28, 38.

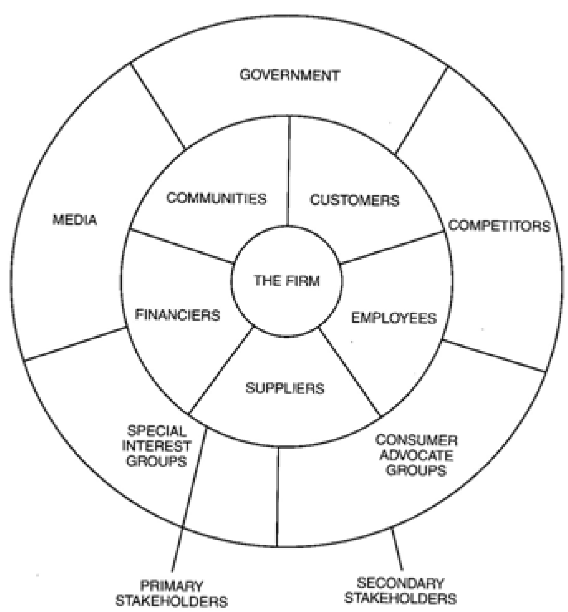
224. Charles Handy, *What's a Business For?*, 80 HARV. BUS. REV. 49, 51-52 (2002).

225. *See, e.g.*, Blair & Stout, *supra* note 19, at 260 (explaining how some economists define the firm as a bundle of assets under common ownership where control is delineated *ex ante* to hired inputs by explicit contracts, while the owners retain residual control and profits).

226. One recurring theme in stakeholder theory literature is the definition of a stakeholder. The Stanford Research Institute (SRI) refers to the group without whose support the organization would cease to exist (including shareowners, employees, customers, suppliers, lenders and society). *See* R. F. Stewart, J.K. Allen & J.M. Cavender, *The Strategic Plan*, Research Report 168, Stanford Research Institute, Long Range Planning Service, Industrial Economics Division (1963). Slinger holds that the term refers to all those who have a "stake" in the corporate enterprise and contribute to the success of its business. *See* G. Slinger, Essays on Stakeholding (1999) (Ph.D. dissertation, University of Cambridge), *quoted in* R. EDWARD FREEMAN ET AL., STAKEHOLDER THEORY: THE STATE OF THE ART 47 (2010).

227. FREEMAN, *supra* note 16, at 46; R. EDWARD FREEMAN & JOHN MCVEA, A

stakeholder mindset, business is seen as a set of relationships between groups that have a stake in the activities of the organization. Accordingly, the stakeholder approach evaluates a corporate seller based on more than just profit maximization to its shareholders; rather, it is evaluated based on how consumers, suppliers, employees, financers (including bondholders and banks), communities, and shareholders interact to create integral value together.[228] The role of management is to shape and manage these relationships and to balance divergent interests for the firm's benefit.[229] Two famous diagrams demonstrate the juggling of management between different stakeholder constituencies.

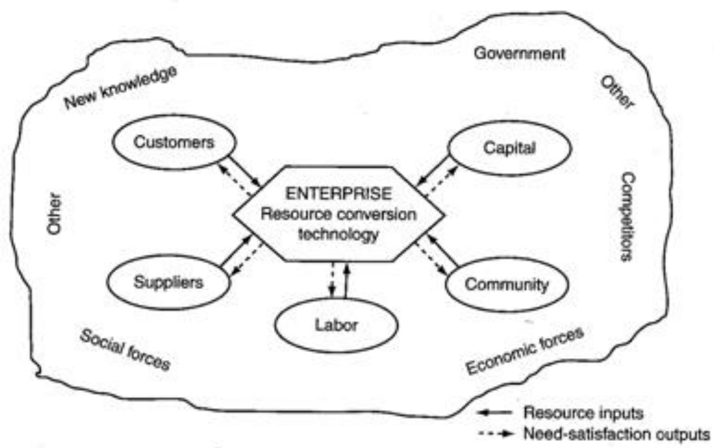


Creating value for stakeholders
Source: R. Edward Freeman, Jeffrey S. Harrison, and Andrew C. Wicks 2007. *Managing for Stakeholders: Survival, Reputation, and Success.* New Haven: Yale University Press. Originally from a conversation with Robert Phillips.

STAKEHOLDER APPROACH TO STRATEGIC MANAGEMENT 189 (Michael A. Hitt et al. eds, 2001).

228. *See* Donaldson & Preston, *supra* note 16, at 68 (noting that stakeholder analysts focus on "*all* persons or groups with legitimate interests participating in an enterprise" (emphasis original)).

229. Donaldson & Preston, *supra* note 16, at 79.



Generalized contributor group interaction between the firm and its environment
Source: W. H. Newman 1979. Commentary. In D. E. Schendel and C. W. Hofer, *Strategic Management: A New View of Business Policy and Planning*. Boston: Little, Brown. 45.

Blair and Stout view a corporation as a team of participants who enter into a complex agreement to work together for mutual gain.[230] The corporation is a coalition of members seeking a premium on its opportunity costs through collaboration with the team.[231] Corporate law is the default set of rules for such cooperation, reducing transaction costs for ad hoc contracting between various members.[232] Stakeholder members of the corporation are thus yielding power over key outputs and inputs to the shared body of cooperation, delegating authority for dispute resolution and for allocation of assets and liabilities to a board of directors acting as trustees of different stakeholders, and aiming to maintain a productive and efficient coalition despite diverging interests between the various groups.[233] Blair and Stout support their view with the language and procedures of corporate law, under which the board of directors owes a fiduciary duty to the firm, a fictional personality, rather than to the shareholders.[234] Under U.S. case law, directors are generally subject to liability only for conduct that harms not only the shareholders but other stakeholders as well.[235] Since U.S. based public corporations typically have no controlling shareholder, but rather are owned by dispersed shareholders, many boards of U.S. public corporations are independent; thus, Blair and Stout limit

230. *See* Blair & Stout, *supra* note 19, at 285-87 (noting how the mediating hierarchy model suggests that shareholders of public companies give up control in hopes of sharing in the benefits that can come from team production).
231. *Id.* at 285.
232. *Id.* at 289 n.90.
233. *Id.* at 285.
234. *Id.* at 298.
235. *Id.* at 299.

their argument to public corporations, while private corporations may adhere to the principal-agent conventional analysis of corporate law.[236]

Stakeholder accountability theory is rooted in ideas about corporate social responsibility that emerged in Europe in the inter-war period (1918-1939) when few large stock corporations dominated the economies of the west. The rise of managerial agents as prominent organs of the corporation, whose owners are passive and widely dispersed, raised the question of managerial agents' accountability. In a series of public correspondences between Adolf Berle and American corporate lawyer E. Merrick Dodd published in the early 1930s, Berle argued that the fiduciary duties of managers should be enhanced to prevent the preference of controlling groups of shareholders over minority groups.[237] Dodd suggested that once the corporation is an independent entity separate from its owners, rather than an aggregate of stockholders, "[t]hose through whom [a corporation] acts may therefore employ its funds in a manner appropriate to a person practising a profession and imbued with a sense of social responsibility without thereby being guilty of a breach of trust[,]" suggesting a view of the corporation not as a purely private enterprise but as a wider organization with social responsibilities and obligations.[238] By the 1950s, shareholder primacy was seen as "slightly old fashioned,"[239] and managers were conceived of as in charge of balancing the interests of different groups connected with the "soulful," socially responsible corporation.[240] In the 1960s, corporate managers were described as "administrators of a community system," explicitly rejecting shareholder primacy.[241] Shareholder primacy returned to dominance with the rise of neoliberal ideology in the financial markets of the 1980s and 1990s.[242]

236. *Id.* at 281.

237. Adolf Berle, Note, *For Whom Corporate Managers are Trustees*, 45 HARV. L. REV. 1365 (1932).

238. E. Merrick Dodd, *For Whom are Corporate Managers Trustees?*, 45 HARV. L. REV 1145, 1161 (1932); E. Merrick Dodd, *Is the Effective Enforcement of the Fiduciary Duties of Corporate Managers Predictable?*, 2 U. CHI. L. REV. 194, 194-207 (1935).

239. L.C.B. Gower, *Shareholder Democracy: A Broader Outlook for Corporations*, 68 HARV. L. REV. 922, 927 (1955) (book review).

240. Carl Kaysen, *The Social Significance of the Modern Corporation*, 47 AM. ECON. REV. 311, 313-14 (1957).

241. BRYAN HORRIGAN, CORPORATE SOCIAL RESPONSIBILITY IN THE 21ST CENTURY: DEBATES, MODELS AND PRACTICES ACROSS GOVERNMENT, LAW AND BUSINESS 89 (2010) (citing Adolf A. Berle, *The Corporation in a Democratic Society*, *in* MANAGEMENT AND CORPORATIONS 1985 63, 68 (M. Anshen and G. Bach eds., 1975)); *cf.* Wilber G. Katz, *Responsibility and the Modern Corporation*, 3 J.L. & ECON. 75, 82 (1960) (countering that the "only statutes and cases which suggest any departure from [shareholder primacy] are those relating to gifts [that] provide no basis for Professor Berle's general assertion that [directors are] . . . 'administrators of a community system.'").

242. Paddy Ireland & Renginee G. Pillay, *Corporate Social Responsibility in a*

Fiercely believing in the forces of the market as efficient and as the primary facilitator of wealth, neoliberals acted toward the goal of deregulation in order to free the forces of the free market from governmental intervention.[243] Shareholders in this period were less dispersed and were represented by few institutional investors, and claims for shareholder activism and shareholder value got stronger.[244]

While shareholders of large corporations in the eighteenth and early nineteenth century were often personally involved in managing or monitoring the corporation, at the beginning of the twentieth century owners of corporations' stocks became typically uninvolved in management or production, assuming a passive role and becoming widely dispersed, taking little interest in the daily management of the business.[245] In the twenty-first century, corporations are not only owned by dispersed owners, but also have a larger global impact than governments, with consumer communities dispersed between various nations and lands. Nothing in the contractual relationship between consumers and sellers resembles the nineteenth century negotiation of a consumer with a small merchant at the town marketplace. The seller is now not owned by an individual, and the buyer is not asking any questions or making any requests. But the law for provision of consumer product information remains the same. The radical reconceptualization of the corporation as a public institution, which suggests that directors owe duties to employees, consumers, creditors, and society as a whole, as well as to shareholders, may not be so radical when considering this historical change.[246]

One significant hurdle that stakeholder theory needs to overcome to become legally applicable is providing a concrete methodology for balancing competing stakeholder interests. The business judgment rule protects board decisions from judicial second-guessing when acting in good faith, with due care, and in a manner it reasonably believes is in the company's best interests.[247] However, protecting consumers' informational interests may inherently conflict with shareholder value. A 2010 Delaware Chancery Court decision in *Ebay Domestic Holdings, Inc. v. Newmark* suggests board accountability standards in for-profit corporations include

Neoliberal Age, *in* CORPORATE SOCIAL RESPONSIBILITY AND REGULATORY GOVERNANCE: TOWARDS INCLUSIVE DEVELOPMENT? 78 (Peter Utting & Jose Carlos Marques eds., 2010).

243. Ireland & Pillay, *supra* note 242, at 85.

244. DOUG HENWOOD, WALL STREET: HOW IT WORKS AND FOR WHOM 286-91 (1997).

245. Ireland & Pillay, *supra* note 242, at 77, 80.

246. Ireland & Pillay, *supra* note 242, at 77, 80.

247. Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971). Boards may not pursue corporate policies that are untethered from the corporation's business interests—revenues, profit, equity value and related matters concerning relationships with customers, suppliers, employees and other stakeholders. *See id.* (noting that board decisions will not be interfered with as long as they can be attributed to any rational business purpose).

acting to promote the value of the corporation for the benefit of its stockholders, which, in that case, involved striking down a "poison pill" designed by the board to preserve organizational culture.[248] Indeed, the concept of a for-profit corporation implies a deeper accountability to shareholder value.

Viewing the corporation as a nexus of contracts implies a need for an evaluation model for stakeholder interests and their strength. In perfectly efficient markets, both principals and agents are able to enter and exit organizational contracts at will if we assume an infinite number of contractual alternatives.[249] But in our imperfectly efficient reality, often agents are not able to enter and exit freely their contractual commitments.[250] This results in power differentials between agents due to unequal corporate dependence between the parties.[251] In balancing between conflicting interests of stakeholders, board members may assess the flexibility of the corporate organizational boundaries.[252] In efficient markets, easy entry into the organizational relationship and smooth exit from it seem to require a lesser degree of corporate accountability. Entry and exit barriers that make the market inefficient, however, seem to call for accountability towards the relevant group of stakeholders.[253] Interestingly, under this power differential model shareholders in publicly traded corporations are actually the least in need of regulatory protection because they can easily exit their relationship with the corporation by selling their stock. In contrast, corporate accountability to consumers, should be required to be higher than corporate accountability to investors, as consumers are often bound by form contracts that have lock-in periods or other high exit barriers.[254]

Stakeholder theory implies accountability only towards contractual parties to the corporation.[255] It is thus significant to note its distinction from corporate social responsibility, which calls for enhancement of corporate accountability towards external parties that are foreign to the

248. 16 A.3d 1 (Del. Ch. 2010) (stating that in this case preserving corporate culture is in directors' self-interest).

249. Charles W. Hill & Thomas M. Jones, *Stakeholder-Agency Theory,* 29 J. OF MGMT. STUD. 131, 135 (1992)

250. Hill & Jones, *supra* note 249, at 135.

251. Hill & Jones, *supra* note 249, at 135.

252. *See* Hill & Jones, *supra* note 249, at 146-47 (suggesting ways for corporate boards to reduce the concentration of stakeholder power).

253. *See* Hill & Jones, *supra* note 249, at 134-35 (noting that power differentials created by inefficient markets "materially affect both the content of principal-agent contracts and the structure of governance mechanisms policing those contracts.").

254. See discussion of exit barriers, *supra* Part I.E.

255. *See* Donaldson & Preston, *supra* note 16, at 68 (stating that stakeholder theory is concerned with those who are involved in the enterprise).

corporation's business.[256] Like the Once-ler in "The Lorax" who rationalizes his corporation's destruction of the environment by stating "How ba-a-a-ad can I be? . . . a portion of proceeds goes to charity,"[257] corporate social responsibility provides corporations with a narrative of societal consciousness that allows them to rationalize harmful corporate behavior. Indeed, under this trend, corporations fail to return their debts to creditors on the one hand, while giving charity donations on the other. Corporate social responsibility allows tax deductions for the—often minor— expense and provides great public relations value. "All the customers are buying," tells us the Once-ler, representing the evil in capitalism, "and the PR people are lying."[258]

Stakeholder theory, on the other hand, is a methodology of corporate accountability towards specific groups deeply involved with the corporation and its activity, including its investors as well as its employees, suppliers, and consumers.[259] Stakeholder theory rejects a soft law approach and calls for specific normative implications. Typically, the corporate moral hazard takes the form of a set of voluntary standards imposed by corporations as an ethical code of principles published by the management and self regulated by the corporation in question.[260] Integrating social and environmental concerns in corporate business operations on a voluntary basis creates limited incentives for legal compliance and thereby often remains a tool of marketing with limited effect on actual performance.[261] For example, the Christian Aid Report, *Behind the Mask: The Real Face of Corporate Social Responsibility*, lists a string of transgressions by international business lobbies that "vigorously oppose" their corporate

256. *See* Alexandra R. Harrington, *Corporate Social Responsibility, Globalization, The Multinational Corporation, and Labor: An Unlikely Alliance*, 75 Alb. L. Rev. 483, 489-90 (2012) (discussing how corporate social responsibility entails responsibility to a broad range of subjects).

257. DR. SEUSS' THE LORAX (Universal Pictures 2012).

258. *Id.*

259. *See* Donaldson & Preston, *supra* note 16, at 68 (noting that stakeholder analysts focus on "*all* persons or groups with legitimate interests participating in an enterprise" (emphasis original)).

260. *See, e.g.*, *Code of Business Conduct*, THE COCA-COLA COMPANY, (April 2009), *available at* http://assets.coca-colacompany.com/45/59/f85d53a84ec597f74c754003450c/COBC_English.pdf (providing Coca-Cola's official code of business that includes topics such as: acting with integrity around the globe, integrity in the company, integrity in dealing with others); *see also* Colin Crouch, *Modeling the Firm in its Market and Organizational Environment: Methodologies for Studying Corporate Social Responsibility*, 27 ORG. STUD. 1533, 1542 (2006)(arguing that corporations have an incentive to manipulate stakeholder theory and corporate social responsibility to achieve their own ends).

261. *See* Ireland & Pillay, *supra* note 242 at 94 ("CSR is often treated by corporations as little more than a public relations or window dressing exercise").

social responsibility commitments,[262] including: Shell Corporation, who officially strives to be a good neighbor but "fails to quickly clean up oil spills that ruin villages"; British American Tobacco, who stresses its commitment to high standards of health and safety but is reported to have "chronic ill-health related to tobacco cultivation"; and Coca-Cola, who states that it uses "natural resources responsibly" but is claimed to have "a wholly owned subsidiary in India [being] accused of depleting village wells in an area where water is notoriously scarce."[263]

The challenge of making corporations accountable to their stakeholders is wrapped up in the issue of how to make accountability meaningful, measurable, and enforceable, bringing the value of free choice back to the consumer shopping experience. In *Individual and Corporate Social Responsibility*,[264] Roland Bénabou and Jean Tirole discuss three alternative visions of corporate social responsibility. Vision 1 is the "win-win" approach, under which the incentive for corporate social responsibility stems naturally and inherently from the promotion of shareholders' interests in profits.[265] When firms fail to accommodate corporate social responsibility, they in fact reduce shareholder value by focusing on the short term.[266] For example, Bénabou and Tirole bring up a firm that may reduce costs by reneging on a contract with its labor or suppliers so as to reduce costs, thereby damaging the long-term goodwill of the different constituencies, making it more difficult to attract motivated employees in the future, or induce suppliers to make long-term investments.[267] Corporate social responsibility under this first vision is in fact a means by which a corporation can maximize profits and enhance shareholder value in the long run.[268]

Bénabou and Tirole label Vision 2 "delegated philanthropy."[269] Under this view, a firm is a channel for expression of different constituencies, and the corporation's management caters to demand by supplying the stakeholders' need in charity while maximizing profit.[270] As Bénabou and Tirole point out, one needs to explain why the corporation is

262. CHRISTIAN AID, *BEHIND THE MASK: THE REAL FACE OF CORPORATE SOCIAL RESPONSIBILITY*, 20 (2007), *available at* http://baierle.files.wordpress.com/2007/11/behind-mask.pdf.
263. *Id.* at 2.
264. Roland Bénabou & Jean Tirole, *Individual and Corporate Social Responsibility*, 77 ECONOMICA 1 (2010).
265. *Id.* at 9.
266. *Id.* at 10.
267. *Id.* at 9-10.
268. *Id.* at 10.
269. *Id.* at 10.
270. *Id.* at 11.

the adequate social vehicle for this philanthropy.[271] As an alternative, for example, Starbucks' consumers could send the workers in a coffee plantation some donations through a charitable organization.[272] The explanation Bénabou and Tirole suggest is transaction cost savings.[273] Since the corporation is already involved in the transaction with the workers, it will be much cheaper for it to forward them the donation.[274] Vision 3 is labeled by Bénabou and Tirole as "insider-initiated corporate philanthropy," and it reflects management's personal need or willingness to contribute money to a good cause, using "others' money" for that purpose.[275]

This article advocates for corporate accountability to product information by considering the corporation in its role as a provider of products or services to the public. Rather than a platform of delegated philanthropy, or a means to enhance value for shareholders or managers, the corporation is a legal institution that is granted legal privileges of incorporation with limited liability, and against such privileges it should incur accountability towards its consumers and not solely towards its investors. If corporations are to be considered social institutions of importance, and not simply assets of their owners, and if managers are to be seen as more than agents of the shareholders, corporate governance must be used as a mechanism for enhancing the voice of stakeholders and

271. *Id.* at 13.

272. *Id.* at 10.

273. *Id.*

274. Obviously, there is some circularity in this answer. There is no doubt that the corporation can deal with the workers more efficiently and for less transaction costs, but the real question is why do we use the corporate vehicle as a social means for charity to begin with. Why do we find the corporate relationship we have with other stakeholder constituencies to raise a justification for charity to begin with? In theory, if consumer citizens are bothered by work conditions in Africa, they can collect and send money to the group in need even if not directly in a relationship with them (one can assume workers for Dunkin Donuts coffee enjoy no better terms of employment, and from a human rights standpoint, there is no justification for why we should support only the workers working directly on our personal cup of latte). The apparent answer is that we find a need to support those in relationship to our actual lives, even if indirectly and through the channel of a for-profit organization.

275. *Id.* at 11. This vision is easily objectionable on corporate governance grounds. *See* Milton Friedman, *The Social Responsibility of Business is to Increase its Profits*, N.Y. TIMES MAGAZINE, Sept. 13, 1970, at 122. Recently, following the U.S. Supreme Court decision in *Citizens United v. Federal Election Commission*, 558 U.S. 310 (2010), much academic ado is credited to the issue of political donations conducted by corporations, giving rise to questions of agency costs and management's personal political agendas promoted at the shareholders' expense.. *See* Lucian A. Bebchuk & Robert J. Jackson, Jr., *Corporate Political Speech: Who Decides?* 124 HARV. L. REV. 83, 87-89 (2010) (noting that corporate political spending is treated similar to ordinary business decisions and is delegated to management).

mitigating conflicts of interests between various groups that arise within the corporate structure. In particular, corporate governance should impose a standard of corporate accountability to product information that would initiate adequate disclosure to consumers based on the power differential test suggested above.

Not all consumers should be treated alike, however. Applying the power differential test for corporate informational accountability implies an organizational assessment of corporate boundaries and consumers' exit barriers from the relationship with the corporate seller.[276] Exit barriers may be contractual, as in cellular packages or utilities contracts, or natural, as in preschool enrollment. Exit barriers are also highly correlated with product risk: the higher the product's risk, the higher the probability the consumer would be affected by its consumption for a long term. Consumption that entails a long-term relationship with the seller should be accompanied by higher informational accountability provided to consumers.

IV. MEDIATING HIERARCHY APPLIED: CORPORATE INFORMATIONAL ACCOUNTABILITY TOWARDS CONSUMERS

Having established that consumers are legitimate corporate members in need of better product information, this article proceeds to sketch normative foundations for such corporate disclosure. Current informational accountability under contract law applies freedom of commercial speech, accompanied by liability imposed *ex post* by courts in cases of fraud and misrepresentation. This *ex post* liability is insufficient. This part of the article sketches a proposal for accountability standards that match the challenge of corporations offering products or services to the public.

A. Doctrinal Foundations: Comparing Corporate Law and Consumer Contracts

Under current law, the relationship between consumers and corporate sellers is categorized as contractual.[277] Like small merchants in the archaic marketplace, multinational corporations offering the public services or products may design their commercial speech according to their commercial interests, providing information only to the extent where contract law would render the agreement involuntary.

276. *See* Charles W. Hill and Thomas M. Jones, Stakeholder-Agency Theory, 29 J. MGMT. STUD. 131, 134 (1992).

277. *See supra* Part I.F.

There are several reasons why this contractual categorization is problematic: as discussed above in Parts I and II, the legal preference toward investors is not justified by the factual characteristics of consumers versus investors as a group, and freedom of commercial speech results in an information environment that does not do enough to support freedom of consumer choice. Contract law's basic assumption is that horizontal scheme exists between contracting parties that are in a mutual relationship, however, the consumer-seller relationship is anything but mutual.[278] Consumers are dispersed and the contractual categorization separates them into separate individual relationships, despite the unified legal platform used by corporations through form contracts.[279] The institution for dispute resolution in contractual relationships is the court, accompanied by *ex post* resolutions coming at a high expense, which makes only class actions plausible.

In considering the appropriate legal paradigm to set informational accountability standards of corporations to consumers, it is useful to consider the major differences between the legal disciplines of contract law and corporate law. While both laws set rules for private parties acting in a free market, they create distinct legal arrangements.

Under a corporate law regime, accountability brings about settlement of the dispute at an earlier time because discussion of adequate product disclosures is conducted prior to the sale, taking into account the interests of consumers and their rights for informed choice. Rather than waiting for consumers to sue based on the contract law claims of fraud or misrepresentation, and apply the precedents *ex post*, corporate law offers an *ex ante* policy to be adapted by the board of directors, an institution balancing the need and interests of consumers with other stakeholder groups, within the organization and given its specific circumstances.

While claims of fraud and misrepresentation under contract law are standards interpreted by the court after the sale, corporate policy for product disclosures set by the board of directors resembles rules: it is specific and accurate, and its normative content is given prior to the sale of the underlying product. Setting a product information policy by the board of directors in advance may be preferable and more efficient. The board of

278. *See* 1 SAMUEL WILLISTON & RICHARD A. LORD, A TREATISE ON THE LAW OF CONTRACTS § 1.1 (4th ed. 1993 & Supp. 1999) (noting that courts "generally continue[] to stress the classic concept of contract requiring two or more parties with capacity, consideration, mutual assent, and a lawful subject matter," but observing that this "classic concept of contract" is "generally inapplicable to formal contracts or contracts under seal.").

279. For all practical purposes, these form contracts may be considered contracts of adhesion. *See* BLACK'S LAW DICTIONARY 159 (4th Pocket ed. 2009) (defining adhesion contract as " a standard-form contract prepared by one party, to be signed by another party in a weaker position, usu. a consumer, who adheres to the contract with little choice about the terms.").

directors is an internal institutional organ possessing a broad view of the business performance of the corporation on the one hand, and possessing vast data on the product or service, on the other hand. The board of directors has much cheaper access to information about the various features, characteristics, and risks posed by products, as well as information about other stakeholders' interests and considerations regarding such potential disclosures. No court of law would ever be able to delve into these specific considerations as effectively as the board of directors. The variety of products sold by most corporations also suggests that the proper institution to address issues of product information should be the board of directors rather than the court, which is not suitable for frequent similar decisions.[280] Letting the board of directors fulfill its role as a mediating hierarchy allows better communication based on a common language shared between various stakeholder groups, leading to higher certainty about the rights and duties of each of the stakeholder groups and better organizational cooperation.[281]

Typically, boards are considered to be accountable to the company, to the shareholders, or to both.[282] Recent trends in international corporate governance, however, suggest dilution of the shareholder primacy norm, making way for other stakeholder concerns. For example, the U.K., once an established kingdom of the shareholder primacy norm, enacted new regulations in 2013 under its 2006 Companies Act that require corporations to include annual reviews about key performance indicators of their business, including with regard to employment and environmental matters.[283] In 2013, India enacted a new corporate law that mandates that public corporations establish a stakeholder relationship committee on the board, requiring independent board members to "safeguard the interests of all stakeholders."[284] The Canadian Supreme Court has ruled that board members owe a fiduciary duty to the corporation rather than its

280. *See* Louis Kaplow, *General Characteristics of Rules*, *in* 5 ENCYCLOPEDIA OF LAW AND ECONOMICS 502, 510 (Boudewijn Bouckaert & Gerrit De Geest eds., Edward Elgar 2000) (expounding that rules are preferable as a normative methodology when frequent policy decisions are required).

281. This argument resembles Schauer's argument for rules over standards, due to the function of rules as a semantic means of communication between the rule maker and the public. *See* Frederick Schauer, PLAYING BY THE RULES: A PHILOSOPHICAL EXAMINATION OF RULE-BASED DECISION MAKING IN LAW AND IN LIFE 53-64(1992)(explaining that the role of rules is to communicate expected behavior to the intended audience).

282. *See* Blair & Stout, *supra* note 19, at 298 (discussing the fiduciary duties of directors).

283. The Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013, 2013, S.I. 2013/1970 (U.K.), *available at* http://www.legislation.gov.uk/uksi/2013/1970/pdfs/uksi_20131970_en.pdf.

284. The Companies Act, 2013, No. 18, Acts of Parliament, 2013 (India), *available at* http://www.mca.gov.in/Ministry/pdf/CompaniesAct2013.pdf.

shareholders, in order to balance the interests of different constituencies.[285] Chinese corporate law requires corporations to "observe social morals" and to "assume social responsibility."[286] The prerogative of shareholders remains to appoint members of the boards of directors[287]—occasionally given limitations on professional qualifications (as in the case of independent directors). But the accountability of the board of directors should be extended towards additional stakeholders. Fiduciary duties of board members encompass the duty of loyalty, the duty of care, and the obligation of good faith.[288] Product information disclosure in the suggested corporate pattern may be rooted in the duty of care and in the obligation of good faith towards consumers as corporate stakeholders.

Timing is also of essence, and the board of directors is expected to establish product information policy in advance, *ex ante* to the moment of purchase, whereas the use of contract law postpones the time of dispute resolution for *ex post* court discussions.

The following is a table summarizing the main differences between contract law and corporate law, demonstrating why corporate law is more suitable for imposing product information accountability.

285. BCE Inc. v. 1976 Debentureholders, [2008] 3 S.C.R. 560, 618 (Can.).

286. *See* Zhonghua Renmin Gongheguo Gongsi Fa (全国人民代表大会常务委员会) [Companies Law of the People's Republic of China] (promulgated by the Standing Comm. Nat'l People's Cong., Oct. 27, 2005, effective Jan. 1, 2006), *available at* http://www.npc.gov.cn/englishnpc/Law/2007-12/13/content_1384124.htm.

287. *See* Julian Velasco, *Taking Shareholder Rights Seriously*, 41 U.C. DAVIS L. REV. 605, 609 (2007) (identifying voting to elect directors as one of the rights of shareholders).

288. *See* Leo E. Strine Jr. et al., *Loyalty's Core Demand: The Defining Role of Good Faith in Corporation Law*, 98 GEO. L.J. 629, 631 (2010) (citing *Cede & Co. v. Technicolor, Inc.* 634 A.2d 345, 361 (Del. 1993) to introduce and explain the duty of good faith, related to the traditional duties of loyalty and care, owed by directors).

A COMPARATIVE VIEW OF CONTRACT AND CORPORATE LAW

	Contract Law	**Corporate Law**
Schematic Description of Relationship Between Parties	Horizontal	Vertical
Consumer Dispersion	Dispersed consumers, separated by numerous individual form contracts	Uniform relationship with consumers, on a single legal platform
Ethical foundation	Mutual assent and freedom of will	Stakeholder theory and consumer corporate membership
Institution for dispute resolution	Court of law	Board of Directors
Timing of Dispute resolution	*Ex post*	*Ex ante*
Liability foundations	Fraud/misrepresentation	Adequate and reasonable disclosure
Remedy standard	Damages, rescission and/or restitution	Damages under private enforcement or public enforcement as applied in securities laws and regulations
Organizational allocation of responsibility for product disclosures	Management and Marketing staff	Board of Directors

B. Essentials of Suggested Product Disclosure

To redefine the informational relationship between corporate sellers and consumers, a profound amendment of disclosure practices is required. Avoiding fraud and misrepresentation is not enough. Product information that is disclosed should become accessible, accurate, comprehensive, and timely, and should allow consumers to fairly compare material product features to those of competing products available on the market. Under these guidelines, corporate sellers that offer or distribute products and services to the public should be the individuals to disclose the product information. Corporate law should be extended to include mandatory disclosure duties of product information following the essentials of materiality, accessibility and concise information. Disclosing the information is not enough; corporations should ensure that information is given concisely and includes all material aspects required for a reasonable consumer to make her decision. Below, some guidelines are suggested for product information policy, considering legibility of information disclosed by the corporation, load of information available regarding the product, lock-in provisions, the ease of exit from the consumer contract, and the long-term costs of the purchase.

Further analysis is required to determine how to create incentives for corporations to comply. Such research should compare patterns of private enforcement tools, such as those available to investors securing accurate filings and statements under the federal securities laws, and public enforcement by a governmental agency in charge of product information management similar to the SEC. Public enforcement may have the advantage of setting a uniform scale and ranking system that would allow easy comparison of products offered, as well as enforcing consistent methodology of disclosure and location of information display. Consumers, or the public agency on their behalf, should be able to sue a corporation for inadequate product disclosure under corporate law even when there is no contractual claim for fraud or misrepresentation, if the disclosure provided for a particular product or service was not adequate given the product qualification.

Based on the analysis of failures in current product information markets given in Part II above, I provide three essentials for product information disclosure below. Corporations selling products to the public should be accountable for product information disclosure, including all material information accessible and to the consumers' public, in addition to their liability currently holding under contract law for fraud and misrepresentation.

(1) Materiality
Product information disclosed must include all significant information for consumers' usage. Information disclosed should be comprehensive and timely. A range of methodologies may be used to determine the significance of features and data for the materiality test. One possible approach is adopting GRI standards[289] for materiality as applied for consumers, taking into account the reasonable estimates of impact on consumers' product use and the products' impact on the consumer's life. Materiality should include long-term costs of purchase and any lock-in periods imposed on consumers.

(2) Accessibility
Product information must be disclosed in an accessible manner on the front of the product's package and in any other prominent source of commercial speech given on behalf of the corporation, in plain English and with no cost, allowing potential consumers to evaluate their purchase prior to payment. Corporations should consider the legibility of product information in assessment of its accessibility. Information disclosed should be legible to the least sophisticated consumer of the product, and accessible to all consumers and potential consumers with no costs.

(3) Conciseness
Due to information overload environments, product information disclosed should be succinct and sharp. Vague statements and masses of information provided in intense commercial speech environments should not be considered adequate disclosure. Product disclosure should be succinct and concise, simple and easy to understand. Simplicity and visual clarity should convey all material information that reasonable consumers need.

CONCLUSION

This article makes the case for the inclusion of consumers as legitimate corporate stakeholders entitled to product informational rights. Comparing consumers to investors shows that they have more in common than the law recognizes. Consumers need at least as much informational assistance as investors do, as shown by a comparison of the consumer

289. Global Reporting Initiative, *supra* note 200.

choice process and the investment allocation process, the scope of risks, the complexity of choice and its structural market settings, such as intermediaries and regulation. This article analyzes voluntary commercial speech environments and comes to the conclusion that the current market for product information fails to provide consumers a meaningful framework for efficient consumer choice. When consumers are considered corporate members under an organizational analysis of stakeholder theory, corporations will be considered accountable to product disclosure. Under the suggested doctrinal outcome, corporate law would impose mandatory disclosure duties of product information, applied to corporations that offer services and products to the public. Consumers would be entitled to reasonable and accessible disclosure of material product data provided by the corporation in simple, easy-to-understand language. As compared to the current contractarian view towards accountability for product information disclosures, a corporate law view of accountability proves superior.