

# DIGITAL REGULATION PROJECT

## Consumer Protection for Online Markets and Large Digital Platforms

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Policy Discussion Paper<sup>†</sup>, No. 1

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<sup>†</sup> The Tobin Center for Economic Policy at Yale hosts the papers of the Digital Regulation Project as a way for some of the world's leading economists and regulatory experts to present policy recommendations based on their relevant research and expertise. The Tobin Center does not take policy positions and therefore the content does not represent the positions of the Tobin Center or Yale University.

# Consumer Protection for Online Markets and Large Digital Platforms<sup>2</sup>

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## Abstract

*Consumer protection law is vital for ensuring that market-based economies work in the economic interest of consumers as well as businesses, and thus to the benefit of civil society. This is the case for online markets just as it is for offline markets. However, despite broad consensus on these points, too little has been done to ensure that the various standards applicable in offline markets are sufficient or adequate to guarantee efficiency and fairness in online markets. This paper outlines eleven key features of online markets that might necessitate standards additional to or different from those that are applicable offline, and provides a menu of possible policies in relation to each. Many of these are general to all online markets, but some are specific to the largest digital platforms. Many if not most of our policy proposals could be enacted through minor changes to existing law or regulation or through decisional law interpreting existing legislation. Some have already been implemented in some jurisdictions. What is needed in all jurisdictions, however, is a regulator or regulators with sufficient expertise around technical issues such as A/B testing and algorithmic decision-making to understand, anticipate, and remedy the myriad ways that online firms can disadvantage consumers.*

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<sup>2</sup> This is the first of several papers prepared by or forthcoming from the Digital Regulation Project, a collaborative effort of experts in economics and regulation in the United States, the UK, and the European Union, who have studied, and are committed to the improvement of, competition in digital markets.

<sup>3</sup> Authors' full titles and conflict disclosures can be found in Appendix 1.

<sup>4</sup> The authors thank Abby Lemert, B.S.E., M.Sc., M.A., Yale Law School Class of 2023 for her expert editing and research assistance.

<sup>5</sup> Omidyar Network and the James S. and James L. Knight Foundation have provided funding and other support for this paper and other forthcoming papers relating to regulation of digital platforms. Amelia Fletcher's work was partly supported by the Economic and Social Research Council [grant number ES/P008976/1]. Omidyar Network employs one of the authors of this paper.

## Introduction

Consumer protection law is vital for ensuring that market-based economies work in the economic interest of consumers as well as businesses, and thus to the benefit of civil society. This is well understood. Across many jurisdictions, consumers are protected by law from unsafe products, fraud, deceptive advertising and a variety of unfair business practices. The United Nations has Guidelines for Consumer Protection, updated in 2015, which outline eleven “legitimate consumer needs.”<sup>6</sup> These in turn build on four core consumer rights embodied within the US Consumer Bill of Rights, as presented by President John F. Kennedy in 1962. In the US, consumers have both public and private rights, under a mixture of national, state, and local law.

One of the 2015 additions to the UN Guidelines was the principle that the “level of protection for consumers using electronic commerce should not be less than that afforded in other forms of commerce.” Clearly, this is critical, as more of the global economy moves online, but what does it mean in practice to ensure that consumers enjoy as much protection online as in traditional markets? What differences do consumers face in an online environment, and what are the implications for consumer protection?

This paper provides an economic perspective and policy thinking on these important questions. It starts by discussing the economic rationale for consumer protection generally, including explaining its key role in protecting against market power and ensuring competitive markets that deliver good consumer outcomes. It goes on to highlight some key differences between online and offline markets, explains what concerns these differences are likely to create for consumers and regulators, and provides a menu of policy proposals for addressing these concerns.

Many of the proposals are intended to be applied to all online firms, both traders and platforms, but some are targeted at the largest online gatekeeper platforms. In providing an economic perspective, the paper does not endeavour to assess the extent to which these concerns are addressed by existing consumer protection legislation, not least because of variation in coverage across US states.<sup>7</sup>

Our focus is on rules relating to the commercial transaction between firm and consumers. We consider that consumer protection law should also apply to markets in which services are ostensibly provided for free, but where consumers pay in the form of data and attention. However, we do not discuss wider detriment that might occur—for example in relation to mental health or democracy—which is typically associated with harmful online content. These issues are important, and it could in principle be argued that products which create

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<sup>6</sup> See U.N. Conf. on Trade and Dev., *Guidelines for Consumer Protection* (2016), [https://unctad.org/system/files/official-document/ditccplpmisc2016d1\\_en.pdf](https://unctad.org/system/files/official-document/ditccplpmisc2016d1_en.pdf).

<sup>7</sup> It is clear there are significant gaps in protection in the US as there is no baseline federal statute. In the EU/UK, the consumer protection regime has to date been set in Brussels and does potentially address some of the concerns discussed in this paper. However, there is still a relative lack of enforcement, which limits firm compliance incentives and also means there is little developed precedent on many core concepts in EU/UK consumer law. Such precedent can provide valuable certainty for both firm compliance and regulatory enforcement.

such detriment are defective, in contravention of consumer protection law.<sup>8</sup> However, this is not our focus in this paper.

This paper presents a menu of regulatory and enforcement options—all of which flow from basic economic principles—that would protect consumers and foster more efficient digital markets. Regulators and legislators might choose to enact some, but not all, of the solutions proposed here depending on the specifics of their regulatory regimes or their desire or mandate for intervention.

In a similar vein, each of the authors of this paper may not endorse every proposal we outline below. Nor is there full consensus among the authors on which of the proposals are most important, or most likely to be effective, in protecting consumers and promoting efficiency. Nonetheless, all authors agree that each of the concerns and proposals this paper identifies is supported by sound, modern economic principles; we offer these proposals based on that consensus.

### **The economic rationale for consumer protection**

In a market economy, it is well understood that we often rely on competition to deliver good outcomes for consumers. What is perhaps less well recognized is the crucial role that effective consumer protection plays in this process, both in facilitating competition and in ensuring that it is directed towards the interests of consumers.

In a standard introductory textbook treatment of markets, consumers know the characteristics of the products available to them (various brands of whole, low-fat, or skim milk, for example), can rank these options in a coherent and consistent (“rational”) fashion according to their preferences, and select their preferred option from among those they can afford. Coupled with a competitive supply and other well-known conditions, such a textbook market generates desirable consumer outcomes in the sense that it is infeasible to make a consumer better off without making someone else worse off.

Even in such an ideal environment, firms have an incentive to limit competition (through cartel behavior, mergers, and monopolization) to increase their profits. Competition policy is designed to protect against such supply-side anticompetitive tactics. By protecting competition, competition enforcement is intended to generate positive consumer outcomes.

In practice, however, this is only true if certain assumptions hold. At a simple level, firms must not be engaging in naked fraud—that is the product they sell must both exist and be

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<sup>8</sup> This and similar theories have been deployed to achieve what might traditionally be seen as social justice, as opposed to efficiency, goals. For example, several survivors of a “conversion therapy” program touted as capable of turning them from gay to straight successfully sued the provider, arguing, among other things, that the services rendered were “unconscionable” in violation of New Jersey consumer protection law. See Erik Eckholm, *In a First, New Jersey Jury Says Group Selling Gay Cure Committed Fraud*, N.Y. TIMES (Jun. 26, 2015), <https://www.nytimes.com/2015/06/26/nyregion/new-jersey-jury-says-group-selling-gay-cure-committed-fraud.html>. Social justice and efficiency concerns are not wholly unrelated, however. Scott Morton et al., (2020), for example, explain how certain features of digital platforms can be addictive or otherwise harmful; how platforms can take advantage of those features and related behavioral biases to extend their market; and that output, which often is deemed a proxy for consumer welfare, cannot serve that analytical role in determining whether platform conduct has harmed consumer welfare. Higher output of something that has the potential to harm consumers – gambling websites, for example – is not always a good thing. Fiona M. Scott Morton et al., *Addictive Technology and its Implications for Antitrust Enforcement*, YALE SCHOOL OF MGMT. (Sept. 2020), <https://som.yale.edu/sites/default/files/Addictive-Technology.pdf>.

what it claims to be. In simple terms, if consumers are unable to distinguish between honest traders and fraudsters, then competition will not deliver good outcomes. Indeed, the incentives of traders to remain honest in a competitive market will be weak, and there is a serious risk that only the fraudsters will survive.<sup>9</sup>

It is well understood that consumer protection has a critical role to play in protecting against such bad market outcomes by preventing fraud, and more generally in providing a level playing field so that firms cannot gain market advantage by offering consumers a bad deal.<sup>10</sup>

Consumer protection also has a more sophisticated role to play, though, even in the absence of all-out fraud. Many of the ideal assumptions set out above do not reflect important aspects of consumer behavior, and this has important implications for competition.<sup>11</sup> Simply put, even with a competitive supply side, markets most effectively deliver good consumer outcomes if consumers make well-informed active choices to buy the products that best suit their needs. This in turn requires them to *attend* to (or engage with) the market in question, *access* relevant information about available products, *assess* that information, and then *act* on that information. These four ‘As’ underpin effective consumer decision-making (Fletcher (2021)).<sup>12</sup>

In practice, real consumers have limited information as well as a limited ability to process information; they face search and switching costs; they have cognitive limitations; and exhibit behavioral biases. They make decisions on the basis of imperfect information; their ranking of options may not be either coherent or consistent; and they may fail to select their preferred option (either by mistake or as a result of misdirection by the seller). In addition, evidence on consumer inertia suggests that consumers procrastinate, either on account of (partially naïve) time-inconsistent preferences or overoptimism regarding future memory or underestimation of future switching costs. They may simply lack self-control or forget to complete the process of finding better suppliers.<sup>13</sup>

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<sup>9</sup> See SICILIANI ET AL., CONSUMER THEORIES OF HARM: AN ECONOMIC APPROACH TO CONSUMER LAW ENFORCEMENT AND POLICY MAKING 114 (2019).

<sup>10</sup> Several chroniclers of Facebook’s rise to monopoly have observed that Facebook engaged in this precise strategy. Before Facebook became dominant, it promised its users strong privacy protections but in fact was building and deploying an extensive tracking program. By contrast, its competitors were keeping their similar promises. Facebook used the data it collected covertly to gain market share to the point that the market began to tip. It was at that point that Facebook formally reneged on its privacy promises, and required users to consent to tracking. See Fiona Scott Morton & David Dinielli, *Roadmap for an Antitrust Case Against Facebook*, OMIDYAR NETWORK (June 2020), <https://www.omidyar.com/wp-content/uploads/2020/06/Roadmap-for-an-Antitrust-Case-Against-Facebook.pdf>; see also Dina Srinivasan, *The Antitrust Case Against Facebook: A Monopolist’s Journey Towards Pervasive Surveillance in Spite of Consumers’ Preference for Privacy*, 16 BERKELEY BUS. L.J. 39, n. 247 (2019).

<sup>11</sup> Our current understanding of the ways in which actual markets differ from “ideal” markets has developed over several decades. An important part of that debate has been the development of a substantial body of behavioral economics research, which includes theoretical work as well as laboratory and field studies. That body of work has advanced our knowledge of “real” consumers and how they differ from ideal ones.

<sup>12</sup> Amelia Fletcher, *Disclosure as a tool for enhancing consumer engagement and competition*, 5(2) BEHAVIOURAL PUB. POLICY 252 (2021).

<sup>13</sup> When ignoring behavioral and attentional constraints, switching costs can explain the prevalence of consumer inertia. Estimates of the necessary switching costs when ignoring behavioral and attentional constraints, however, are often implausibly large. For instance, Handel (2013) concludes that US consumers in his sample lose about \$2000 annually from not changing to a better health insurance plan. Benjamin R. Handel, *Adverse Selection and Inertia in Health Insurance Markets: When Nudging Hurts*, 103(7) AM. ECON. REV. 2643 (2013).

These various factors limit the effectiveness with which consumers *attend to, access, assess,* and *act* on relevant information, and this in turn affects market outcomes. Even “competitive” markets can generate poor consumer outcomes when consumers do not move to choices that provide lower prices, higher quality, or less exploitation. If consumers, for example, ignore an aspect of the product or its price, even competitive firms will exploit this by choosing the neglected dimension to maximize profits (*e.g.*, Gabaix and Laibson (2006)).<sup>14</sup> Similarly, when consumers mispredict future usage—such as being overoptimistic regarding future gym attendance—firms write contracts to benefit from the consumers’ mispredictions of their own behavior (*e.g.*, DellaVigna and Malmendier (2006)).<sup>15</sup>

Unregulated profit-maximizing firms in such settings—knowingly or unknowingly—exploit naïve consumer misperceptions and this can lead to undesirable distributional consequences (*see, e.g.*, Armstrong and Vickers (2012)) as well as a variety of inefficiencies (*see, e.g.*, the discussion in Heidhues and Köszegi (2018) of participation distortions, exploitation distortions, as well as follow-on distortions).<sup>16</sup> Consumer protection when effectively limiting the firms’ ability to exploit such misperceptions can thus lead to more desirable market outcomes.

Furthermore, firms may have an incentive to impede informed consumer decision making so as to exacerbate these issues. For example, firms that do not offer the best deal in the marketplace have a heightened incentive to make product comparisons hard and generate consumer confusion. The inability of consumers to compare products can be a source of profits and oligopoly power, even when there are several suppliers (*see* Scitovsky (1950) and Diamond (1971)).<sup>17</sup> And when markets become more competitive, firms can have incentives (unilateral or shared) to make product comparisons difficult, or otherwise obfuscate, in order

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<sup>14</sup> Xavier Gabaix & David Laibson, *Shrouded Attributes, Consumer Myopia, and Information Suppression in Competitive Markets*, 121(2) *ECON. J.Q.* 505 (2006).

<sup>15</sup> Stefano DellaVigna & Ulrike Malmendier, *Paying Not to Go to the Gym*, 96(3) *AM. ECON. REV.* 694 (2006). Academic studies have established that consumers engage in misperception of firms’ offers or misprediction of their own future use of firms’ service in a variety of markets and investigated how firms’ respond to such behavior. Consumer misperception, and the resulting consumer behavior, has been observed and documented among others in connection with gym contracts; magazine subscriptions (Oster and Scott Morton (2005), mobile phone contracts (Grubb (2009); Grubb & Osborne (2015)), and banking contracts as they related to overdraft fees (Alan et al. (2018)). Sharon Oster & Fiona Scott Morton, *Behavior Biases Meet the Market: The Case of Magazine Subscription Prices*, 5(1) *BEJEAP 1* (2005). Michael D. Grubb, *Selling to Overconfident Consumers*, 99(5) *AM. ECON. REV.* 1770 (2009). Michael D. Grubb & Matthew Osborne, *Cellular Service Demand: Biased Beliefs, Learning and Bill Shock*, 105(1) *AM. ECON. REV.* 234 (2015). Sule Alan, et al., *Unshrouding: Evidence from Bank Overdrafts in Turkey*, 73(2) *J. FIN.* 481 (2018).

<sup>16</sup> Mark Armstrong & John Vickers, *Consumer Protection and Contingent Charges*, 50(2) *J. ECON. LIT.* 477 (2012); PAUL HEIDHUES & BOTOND KÖSZEGI, *HANDBOOK OF BEHAVIOR ECONOMICS – BEHAVIORAL INDUSTRIAL ORGANIZATION* 517 (2018). Participation distortions result if the consumer misestimates either the total price she will pay for the product or the value of the product. In that case she may participate in the market even though the value of product is below its costs. Exploitation distortions arise when firms write contracts that are good at exploiting consumers’ behavioral or attentional bias, but lead to inefficient usage decisions. If consumers underestimate the importance of add-on prices when buying a base product, for example, firms will offer seemingly attractive deals with high add-on prices and low base prices. The high add-on price will induce consumers to inefficiently withhold add-on demand, leading to inefficient usage and thereby to an exploitation distortion. When the exploitation of consumer bias is profitable, a number of follow-on distortions can arise including excess market entry to benefit from these profits (Heidhues et al. (2017)) or firms spending money on inventing new ways to exploit consumer biases (Heidhues et al. (2016)). Paul Heidhues, et al., *Inferior Products and Profitable Deception*, 84 *REV. ECON. STUD.* 323 (2017). Paul Heidhues, et al., *Naïveté-Based Discrimination*, 132(2) *ECON. J.Q.* 1019 (2016).

<sup>17</sup> Tibor Scitovsky, *Ignorance as a source of monopoly power*, 40(2) *AM. ECON. REV.* 48 (1950); Peter Diamond, *A model of price adjustment*, 3(2) *J. ECON. THEORY* 156 (1971).

to avoid the resulting downward pressure on profit margins (*see, e.g.*, Spiegler (2006), Carlin (2009) and Chioveanu and Zhou (2013)).<sup>18</sup> Consumer protection that makes it harder to obfuscate can thus increase the competitiveness of the marketplace to the benefit of consumers.

In the above examples, competition itself is dampened, and market power increased, when consumers make poor choices. In simple terms, if consumers don't search and switch readily to better product offerings, then firms' incentives to offer better deals will be reduced, and it is these incentives that underpin effective competition. Likewise, an established firm will have more market power, and greater incumbency advantage, if it is unlikely to lose its customers to rivals even if the latter offer a theoretically more attractive deal.

Consumer protection can achieve more desirable market outcomes by mandating disclosure of information to consumers, on a clear and prominent basis, thereby increasing their engagement.<sup>19</sup> Importantly, however, it can be both rational and efficient for consumers to choose not to fully inform themselves. If a consumer were always to scrutinize all the terms and conditions of the services they signed up for, they would have little time to do anything else; they instead tend to "click to accept," without giving this "small print" any serious scrutiny.<sup>20</sup>

Regulators can help consumers save time and effort with legislation that protects against unsafe or unfair outcomes. For example, a US consumer who purchases food in a supermarket is not expected to carefully check whether the available food is toxic; they can trust in the ingredient list, the nutrition label, the volume or weight measures, and food safety regulations to protect them from the worst choices.

When consumers are protected in this way from "hidden nasties," they can focus their scarce attention on the salient aspects of the product (*e.g.*, exactly how much sugar) that are likely to result in better choices. Moreover, with such protections, consumers are more likely to have the confidence to try new products or suppliers. Without them, they may be more inclined to buy from established incumbent sellers who may be no better than entrants, but who have earned consumer trust by selling in previous periods. This can clearly increase the market power of such suppliers. Competition can thus be improved by consumer protection law that allows consumers to choose safely between products, including from less well-established

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<sup>18</sup> Ran Spiegler, *Competition over agents with boundedly rational expectations*, 1(2) THEORETICAL ECON. 207 (2006); Bruce Carlin, *Strategic price complexity in retail financial markets*, 91(3) J. FIN. ECON. 278 (2009); Ioana Chioveanu & Jidong Zhou, *Price competition with consumer confusion*, 59(11) MGMT. SCI. 2450 (2013).

<sup>19</sup> Strictly speaking, there may be circumstances in which distortions in consumer behavior can improve market outcomes, because they counterbalance other factors – such as informational problems – which drive competitive markets to deliver poor outcomes. For example, Handel (2013) estimates that if US consumers were to select health insurance plans optimally, the welfare loss from adverse selection effects would double. But even in these cases, rather than relying on consumer confusion and mistakes, regulators should address the underlying adverse-selection problem directly. Handel, *supra* note 13.

<sup>20</sup> Bakos et al. (2014) reviewed the extent to which potential buyers accessed the end-user license agreements of 90 online software companies. They found that only one or two of every 1,000 retail software shoppers access the license agreement and that most of those who do access it read no more than a small portion. Yannis Bakos, et al., *Does Anyone Read the Fine Print? Consumer Attention to Standard-Form Contracts*, 43(1) J. LEGAL STUD. 1 (2014).

sellers, secure in the knowledge that a mistaken choice will not have significant adverse consequences (*see, e.g.*, Heidhues et al., 2021).<sup>21</sup>

Consumer protection law also can help to limit leverage of a market position from a firm's core market into new markets. Where a firm has an existing customer relationship, it has a natural advantage in selling additional products to that customer. However, it can potentially unfairly exploit its advantageous position through selling additional products on a misleading basis. For example, the UK Advertising Standards Authority recently upheld a complaint against Amazon in relation to its advertising of its Amazon Prime service, which is additional or complementary to its core online shopping service.<sup>22</sup> By misleading consumers into taking Prime, Amazon was effectively leveraging its core market position into this additional service, conduct that raises concerns both about Amazon's market power (an "antitrust" concern) and its marketing methods (a "consumer protection" concern).

The above discussion demonstrates that firms can benefit from these consumer limitations and can have an incentive to exacerbate them—for example, through deliberate obfuscation and misleading sales practices. Consumer protection law can help to ameliorate such problems, and thus has a key role to play in limiting market power and ensuring that competition works to the benefit of consumers. As such, effective consumer protection can be seen as a key component of effective competition policy and therefore a natural and central concern of economists.

In enhancing the functioning of markets, consumer protection law plays three core roles:

**First**, consumer protection law *facilitates consumer choice*,<sup>23</sup> for example by mandating disclosure, by mandating measures that aid easy product comparison, by restricting misleading sales practices, or by ensuring that consumers are not unduly inhibited from switching suppliers. Examples include:

- requirements to use standard measurements that facilitate comparing product amounts and effective prices;
- requirements to disclose certain key information prior to purchase, such as the identity of the trader, the main characteristics of the product and the total price payable;
- requirements not to engage in false, misleading or aggressive sales practices;
- requirements not to lock in consumers by making it unduly difficult or costly to switch.

**Second**, consumer protection law comes into play where it proves unrealistic to expect consumers to protect themselves simply by making good and informed choices on all aspects of what they are buying. In such cases consumer protection law acts to *protect consumers*

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<sup>21</sup> Paul Heidhues, et al., *Browsing versus Studying: A Pro-market Case for Regulation*, 88(2) REV. ECON. STUD. 708 (2021).

<sup>22</sup> See Advertising Standards Authority Oct. 30, 2019 G19-1021643, *ASA Ruling on Amazon Europe Core Sarl* (UK), <https://www.asa.org.uk/rulings/amazon-europe-core-sarl-G19-1021643.html>.

<sup>23</sup> Consumer choice can relate to whether to buy at all and how much/often to buy, as well as which product to buy.



*from exploitation* more directly, as well as enhancing their confidence to engage in markets. Existing examples include:

- safety regulations that protect consumers from unsafe products, whether appliances, food, or pharmaceuticals;<sup>24</sup>
- fiduciary duties for financial advisors to act in their clients' best interest when (effectively) making decisions on their behalf;
- standardized contract terms for certain products (and more general unfair contract principles for standard business to consumer contracts) to ensure that firms cannot hide unfair terms and conditions in the fine print.

**Third**, consumer protection law codifies substantive *standards and procedures for dispute resolution* for when things go wrong, for example in relation to rights of return, refunds, or repair.

Another useful distinction, when discussing consumer protection law is the distinction between its more general *preventative* role, in protecting against harmful firm conduct, and its *market design* role, whereby it facilitates or creates tools which are intended to enhance consumer decision making. Although preventative law is more likely to be defined in broad terms, and to apply across firms and sectors, market design measures tend to be more precise and sector-specific. An example of the latter would be the requirement on credit companies to disclose their cost of credit in a tightly designed format (*e.g.*, large font APR) that is designed to facilitate consumer understanding and comparison across products.

The above discussion focuses on the economic rationale for consumer protection, but political and fairness considerations also play an important motivating role. Fairness can relate to the transaction process itself: *Was the consumer in a position to make a free and well-informed choice?* Or it can relate to the substantive outcomes of that process: *Do consumers get a fair deal relative to sellers, or indeed relative to other consumers?* There is broader consensus about the benefits of intervening to protect the former (fair process) than the latter (fair outcomes), but consumer protection law tends to address both in practice, partly because both are well aligned with the economic basis for consumer protection.

Of course, consumer protection law is not always beneficial. Mandating disclosure of relevant information will not improve consumer choice if consumers simply ignore it, and it could even harm consumer decision making if consumers feel overloaded. Likewise, simplified disclosure can be distortionary if the simplification is ill-suited to the choice being made. For example, the use of APRs can lead to worse choices regarding short-term credit options (Bertrand and Morse (2011)).<sup>25</sup> Consumer protection law can also create detriment if,

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<sup>24</sup> Note that in this situation the regulator directly removes choices from the market because they are too harmful to too many consumers.

<sup>25</sup> Marianne Bertrand & Adair Morse, *Information Disclosure, Cognitive Biases and Payday Borrowing*, 66(6) J. FIN. 1865 (2011). See also Duarte and Hastings (2012) for how a simple-fee disclosure regulation in Mexico's privatized social security system backfired because it did not contain all relevant information. Fabián Duarte & Justine Hastings, *Fettered Consumers and Sophisticated Firms: Evidence from Mexico's Privatized Social Security Market*, (Nat'l Bureau of Econ. Rsch., Working Paper No. 18582, 2012),

in protecting the naïve, it inhibits firms from offering products which more sophisticated consumers would both understand and value.

The fact that certain protections can have some negative consequences does not undermine the general need for, and benefits of, consumer protection law; rather, the observation simply demonstrates that regulation of this sort often involves trade-offs. The discussion above provides ample examples of conduct that should be regulated and why we cannot rely on *caveat emptor* (buyer beware). Nonetheless, potential negative consequences should clearly be considered carefully in regulatory design.

### **Consumer protection law for online markets**

This paper asks whether, and if so what, refinements of consumer protection law are needed in online markets, to help ensure that these markets work as much as possible in the interest of consumers.

Of course, many of the consumer protection issues we observe online have analogs in an offline environment. Fraud, obfuscation, and misleading sales behavior are age-old practices, and offline firms are well-versed in trying to persuade consumers to purchase through a variety of activities including the design of their stores, special offers, and different psychological sales techniques.

As a result, there is already an extensive legal framework for consumer protection in place. This paper does not aim to provide a legal assessment of that existing framework, but rather to highlight—in economic terms—what is different in an online environment, the implications for consumer decision making, and how this might be expected to change the consumer protection law that is required.

In taking an economic approach to our analysis, we have not sought to identify whether the issues we highlight imply real gaps in the law. Indeed, it may be that the existing legal framework can address several of the issues that we discuss below. In the US, Section 5(a) of the Federal Trade Commission (FTC) Act imposes a general prohibition on “unfair or deceptive acts or practices in or affecting commerce.” Likewise, in the EU, the Unfair Commercial Practices Directive 2005 generally prohibits “misleading sales practices” that are “contrary to the requirements of professional diligence,” while the EU Unfair Contract Terms Directive 1993 provides general protection for consumers against unfair terms in standard contracts.<sup>26</sup>

Many of the practices highlighted below are likely to be covered by these general regulations or laws (or by common law principles in the US and the UK). Any ambiguity in this regard may potentially be resolved by clarifications, minor amendments or new guidelines. There are, however, some new concerns arising that are more likely to imply a need for more substantial additions or changes to consumer protection law. In particular, although much of the discussion below applies to all online markets, we identify a number of regulations that are specifically intended for the largest online platforms.

We see four main reasons for the differential treatment of these largest online platforms.

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<sup>26</sup> Currently, the EU consumer law applies in the UK too. However, this need not remain the case in future, following the withdrawal of the UK from the EU.

**First**, as critical gatekeepers between business users and consumers, these platforms are in a unique position to change the way in which markets function, through their setting and enforcing of platform rules on their business users. They have access to relevant data and algorithmic design skills that enable more highly automated monitoring and policing of harmful online activity than any third-party regulator could achieve. Their massive scale means that even small changes to enhance consumer protection could benefit millions of consumers.

**Second**, these platforms have immense access to consumer data, and are skilled in deploying machine learning algorithms to mine these data for relevant behavioral patterns, and using A/B testing techniques that effectively industrialize trial and error experimentation to maximize user impact.<sup>27</sup> This advantages them, in particular, as compared to smaller firms with less access to data, in refining their design choices to best influence consumer behavior, whether this be for good or ill.

**Third**, as highlighted above, weak consumer protection can contribute to creating and enhancing market power. Such competition implications are especially problematic in the context of the largest online platforms, given the competition concerns highlighted by a number of recent reports,<sup>28</sup> and the array of other factors tending to impede competition in these markets.<sup>29</sup>

**Fourth**, a key rationale for consumer protection law is the imbalance in power between a firm and its consumers. At the same time, in designing such law, there is always a balance to be struck between protecting consumers and imposing burdens on businesses. Since many small firms have only limited resources and also a limited power imbalance relative to their consumers, any universally applicable legislation will tend to strike this balance by conferring less protection on consumers than would be ideal. In stark contrast, the largest online platforms are huge and benefit from substantial economies of scale, the extent of the imbalance in power between the platforms and individual consumers is dramatic, and the benefits of enhanced consumer protection are likely to massively outweigh any additional burden on the platform. This combination merits stronger regulation than could be justified on a universally applicable basis.

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<sup>27</sup> “A/B testing” refers to the process of comparing two versions of something to see which version performs better. As an example, a website designer might want to test two versions of a “subscribe button,” a small version and a large version. The designer might show the different subscribe buttons to different groups of site visitors and measure which button gets more clicks. A/B testing is not unique to websites or other online settings but has become an especially commonplace tool to assist the design of various online experiences. See Amy Gallo, *A Refresher on A/B Testing*, HARVARD BUSINESS REVIEW (Jun. 28, 2017), <https://hbr.org/2017/06/a-refresher-on-ab-testing>. See also RON KOHAVI ET AL., TRUSTWORTHY ONLINE CONTROLLED EXPERIMENTS: A PRACTICAL GUIDE TO A/B TESTING (2020).

<sup>28</sup> See, e.g., George J. Stigler Center for the Study of the Economy and the State, *Committee for the Study of Digital Platforms Market Structure and Antitrust Subcommittee Report* (Jul. 1, 2019), <https://www.chicagobooth.edu/research/stigler/news-and-media/committee-on-digital-platforms-final-report>; Digital Competition Expert Panel, *Unlocking digital competition* (Mar. 13, 2019), [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/785547/unlocking\\_digital\\_competition\\_furman\\_review\\_web.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/785547/unlocking_digital_competition_furman_review_web.pdf); Jacques Crémer et al., *Competition policy for the digital era* (Apr. 4, 2019), <https://ec.europa.eu/competition/publications/reports/kd0419345enn.pdf>.

<sup>29</sup> Of course, regulation of small firms also can help check the power of large firms by enhancing consumer trust in the products and services offered by the small firms. This in turn increases the likelihood that consumers will switch their purchases from the large to the small firms.

## Key differences between online and offline consumer choice, and implications

In some ways, consumer decision making is easier in an online environment. Finding relevant information about a wide range of products involves a lot less shoe-leather and time than it ever did in an offline environment; indeed, consumers can access new products and sellers that would simply not have been available in their local stores. Consumers are also aided in their choices by a wide range of tools, such as specialist search sites, and access to reviews and ratings from past consumers. These new tools have the potential to improve both consumer and competition outcomes, so long as they work in ways that genuinely enhance consumer decision-making.

The differences between the online and offline environments, however, can also create additional concerns for consumers. In general terms, the online environment allows consumers more easily to compare products and traders (consumers can “click” their way from store to store, for example, rather than walking or driving between them). But this feature of the online environment can in turn give firms incentives to obfuscate price or other features of their offerings to make comparisons more difficult. Obfuscation of this sort creates consumer protection concerns and also limits some of the benefits that the internet can bring.<sup>30</sup> However, there are also more specific differentiating factors between online and offline markets. In each of the sections below, we highlight one of these, explain the concerns that arise, and set out how consumer protections might need to be modernized to address them.<sup>31</sup>

In doing so, we provide a menu of specific policy proposals. Several of these would be suitable for all online firms, whether platforms or traders. However, for the reasons set out above, we also set out a number of proposals that are targeted at the largest online platforms.

The menu is provided in a spirit of “letting a thousand flowers bloom.” They are not inconsistent, but they are also not intended as an “all-or-nothing” package. Many would be valuable even if others were not adopted. All proposals are supported by at least one of the paper’s authors, but not all of the authors fully support every proposal. In some cases, there is greater support for a prohibition if provided for on a “rebuttable presumption” basis, which would allow the firm a right of defence before penalties or other consequences are imposed.

As discussed above, in some cases, the proposals might already be addressed by an overarching principle-based law. Where this is true, the relevant proposals might instead provide useful guidance for interpreting such a prohibition. In several places, we identify safeguards needed to make online sales comparable to offline sales. We note, however, that offline sales also have significant imperfections, and as such we do not restrict our recommendations to those required to achieve parity between these routes to market, but more generally focus on helping consumers and improving outcomes from online interactions.

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<sup>30</sup> See Glenn Ellison & Sara Fisher Ellison, *Search, Obfuscation and Price Elasticities on the Internet*, 77(2) *ECONOMETRICA* 427 (2009).

<sup>31</sup> Of course, there may also be areas of consumer protection legislation that become less important with the move to online commerce. We have not attempted to identify these in this paper.

**1. *The lack of direct physical interaction with the trader, and the need for access to contact details, rights of return, and dispute resolution.***

Perhaps the most obvious difference between offline and online is that the consumer has no physical interaction with the trader or the product (if it is a physical product). This can mean that the consumer, in many instances, has no idea who the trader really is or where they really are, they have no ability to try on a product or check it is right for their particular needs, and they have no ability to march into the store and ask for the manager if they are unhappy with the service they have received.<sup>32</sup>

*Specific policy proposals*

Consumer protection law can improve this situation in some very basic ways. Online traders should be required:<sup>33</sup>

- to provide valid and standardized contact details, including geographical address, phone number and email address (or contact form) if such information is not already clear from context;
- to set out clearly and prominently before purchase (i) the main characteristics of the goods or services and (ii) the total price of the goods or services, inclusive of taxes and delivery charges (or if the nature of the goods or services is such that the price cannot reasonably be calculated in advance, the manner in which the price is to be calculated);
- to offer a “no fault” right of return for products—under certain conditions and within a reasonable time frame—which do not turn out to suit the consumers’ needs;
- to set out clearly the process consumers should follow in case of complaints, and to deal with these fairly; and
- to sign up with an online dispute resolution scheme at no or at minimal cost to the consumer (in order to address complaints that are not resolved).

**2. *The lack of clear labeling of advertising or clear demarcation between advertising and organic (or editorial) content.***

In an offline context, consumer protection law typically requires that advertising and marketing be clearly flagged as such and clearly separated from other content.

This makes good sense. Consumers have a good understanding of the nature of advertising and marketing and know how to read the messages conveyed. However, in doing so, they make adjustments to, or caveat, the message that the advertising conveys. Consider a

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<sup>32</sup> Sometimes, the online consumer *does* know who the trader is; a consumer who orders a food processor at Cuisinart.com, for example, can be relatively confident that Cuisinart is the trader. But if that same consumer orders the processor through the Amazon Marketplace, or indeed through a retailer she has found online but hasn’t previously come across, then she may not really know the seller’s identity.

<sup>33</sup> Several of these are provided for in the EU (and currently also the UK) under the EU Consumer Rights Directive.

consumer who sees an ad for a vacuum cleaner in a newspaper that claims it is the best vacuum cleaner yet invented and that it will leave their house cleaner than they could even imagine. That consumer is likely to view this as brand positioning or “mere puffery,” not necessarily truly factual. But if the same consumer reads the same information as news content within a newspaper, she will apply a very different lens, and may well assume that the content is broadly true.

Advertising can thus be effective in winning customers—but is also potentially misleading if it is not clearly labelled as such. In order to prevent consumers from being misled, while also protecting the long-term value of such advertising, it is thus vital that the advertising and news content are clearly distinguished, and this is sometimes provided for by law or within advertising codes of practice.<sup>34</sup>

The situation online is in principle the same: consumers must clearly identify online advertising and marketing if they are not to be misled by it. In practice, however, the labeling of advertising content and demarcation between ads and other content can be far from clear. Even where there is labeling, there seems to be little consistency in how this is done. Common labels include “ad,” “#ad,” “sponsored,” “sp,” “promoted,” or “advertorial,” and sometimes the labels are even less clear, for example “brand partner,” “brought to you by,” or “contribution from.” Ad labels are often tiny—or in a color very similar to the background—such that they are easy to miss. And if ads are mixed up with organic or other non-ad content on a small screen, it can be hard for consumers to distinguish the two in their mind.

Such a lack of clarity may be in the interest of the platform, however. As highlighted above, consumers are more likely to be influenced by advertising or marketing if they don’t identify it as such.<sup>35</sup> This in turn means platform may be able to charge traders more for advertising if it is not clearly labeled. Unless they are restricted from doing so, platforms may thus be incentivised to blur the lines between advertising/marketing and organic and other non-ad content.

### *Specific policy proposals*

- *All advertising and marketing should be clearly and prominently labeled as such.* This labeling should enable consumers readily to identify paid ads/marketing. Advertising and marketing should also be sufficiently well demarcated from organic content that consumers are readily able to identify which is which. Standards should be developed to specify what demarcation is lawful in a variety of settings.
- *Basic guidance and templates should be issued or approved by the regulator on what will be considered suitable labeling online.* Many traders and platforms will not be large enough or want to bear the costs of testing empirically how easily consumers are able to identify their advertising and marketing and will prefer to ensure that they

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<sup>34</sup> For example, this requirement is included in the self-regulatory codes of advertising practice (broadcast and non-broadcast) overseen by the UK Advertising Standards Authority. See Advertising Standards Authority, *Advertising codes* (UK), <https://www.asa.org.uk/codes-and-rulings/advertising-codes.html>.

<sup>35</sup> See Ladder, *Ladder Customer Testimonials*, YouTube (Nov. 5, 2019), <https://www.youtube.com/watch?v=XTQdT1QBH48> (featuring a customer remarking “So, I literally Googled ‘best online life insurance’ and Ladder Life Insurance popped up!”). The top placement in search results often are the result of an ad, not an organic ranking of “best” life insurance, for example.

meet their legal obligations by following simple guidelines, for example in terms of label wording, font size, and color.

The above proposals are intended to be applicable to all online firms. We note, though, that Facebook and Google account, between them, for a very large share of all digital advertising spend in (at least) the US and EU/UK. Given their critical position in relation to advertising media, we consider that a stronger regulatory requirement should be imposed on the largest advertising-funded platforms.

- *Given their critical importance in digital advertising, the largest online advertising platforms should be required to carry out regular empirical testing of their labeling and demarcation of advertising.* The formal rule for these platforms would be no different (to ensure consumers are readily able to identify paid ads/marketing), but the burden would be placed on them to demonstrate that this is the case, rather than the burden sitting with regulator to demonstrate the reverse.

### ***3. The lack of ability to directly examine product quality, and the need for fair and non-misleading online quality indicators***

In an offline environment, a consumer seeking to assess the quality of products or services oftentimes can speak face-to-face with a salesperson, can confer with a shopping companion, and can inspect physical products directly. Online, with the lack of any such physical interaction, consumers have come to rely heavily on a variety of alternative quality indicators. These include peer reviews and ratings, rankings on search sites, and the views of social influencers.

#### *Specific policy proposals*

These quality indicators potentially provide very valuable information but this requires that they should be fair and not misleading. Consumer protection can play a key role in ensuring that this is the case, by requiring the following.

- *Consumer ratings and reviews should be presented fairly and non-selectively.* If consumers are led to believe that they are getting the full picture, then this should be the case—all (genuine and legal) reviews should be shown. If a firm has a policy of removing reviews, it should state clearly and prominently that this is the case, and what the goal is. Any removals should be proportionate to that goal.<sup>36</sup> Where “average” ratings are shown, there should be clarity on the approach being used to construct the averages. Where simple averages are not used, the firm should explain the goal behind the weightings used, and these should be proportionate to that goal.<sup>37</sup>

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<sup>36</sup> For example, in 2016, the UK Competition and Markets authority found that online knitwear retailer, Woolovers, was only selecting positive ratings and reviews. Competition & Markets Authority, *Retailer hosting reviews on its website: improvement of practices*, GOV.UK (Aug. 11, 2016), <https://www.gov.uk/cma-cases/retailer-hosting-reviews-on-its-website-improvement-of-practices>.

<sup>37</sup> Simple averages are not necessarily optimal for consumers. Firms might make adjustments to arithmetic averages based on the informational content of reviews, for example. This practice can actually benefit consumers by placing greater weight on those reviews and ratings that actually have more informational value. See Weijia (Daisy) Dai, Ginger Jin, Jungmin Lee, Michael Luca, *Aggregation of consumer ratings: an application to Yelp.com*, QUANTITATIVE MARKETING AND ECONOMICS, Issue 3/2018 (Dec. 29, 2017), <https://www.springerprofessional.de/en/aggregation-of-consumer-ratings-an-application-to-yelp-com/15418062>.

- *Conditional incentivization of ratings/reviews should also be prohibited.* Given the importance of ratings/reviews, many traders incentivize consumers to write them through special offers of one sort or another. There may be merit in this, so long as consumers are not inhibited from expressing their true view. However, some sellers make such incentives conditional on the consumer writing a 5 star review (or equivalent).<sup>38</sup> This practice is clearly intended to falsely inflate ratings and should be prohibited.
- *Fake reviews and ratings should be illegal, as should the service of selling fake reviews and ratings, and as should the hosting of advertising for such services.* The importance of reviews and ratings has led to some sellers seeking to post fake reviews and ratings, or even to purchase such fake reviews/ratings from third parties. Until recently, services offering fake reviews/ratings were even hosted on eBay, Facebook and Instagram.<sup>39</sup> Such activity undermines the usefulness and credibility of reviews and ratings. Regulators should be empowered to determine whether a review is fake, publicize what factors contribute to a finding that a review is a fake, and prohibit such fake reviews.<sup>40</sup>
- *Social media ‘influencers’ should be transparent about relevant sponsorship or payments when endorsing a product; such hidden advertising should be illegal and social media platforms should have a legal responsibility to prevent it.* Social media influencers are sometimes paid to endorse products, while posing as enthusiasts with no financial interest. Such influencers include bloggers, vloggers, celebrities and social media personalities. Paid-for or sponsored endorsement is effectively advertising and should be labeled as such (see above). This labeling should be sufficiently clear and prominent that consumers are readily able identify the paid ads. Hidden advertising should be illegal and social media platforms should have a legal responsibility to prevent it. This is partly because platforms should not be in a

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<sup>38</sup> A recent investigation by UK consumer organisation found several instances of incentivized ratings on Amazon. See Ellie Hammond, Amazon ‘betraying trust’ of millions of consumers with flawed Amazon’s Choice endorsement, WHICH (Feb. 6, 2020), <https://www.which.co.uk/news/2020/02/amazon-flawed-amazons-choice-endorsement/>.

<sup>39</sup> The UK Competition and Markets Authority has been active in requiring these large online platforms to enhance their systems for identifying, removing and preventing such services. See Competition & Markets Authority, *Fake and misleading online reviews trading*, GOV.UK (Jun. 21, 2019), <https://www.gov.uk/cma-cases/fake-and-misleading-online-reviews>.

<sup>40</sup> We note the new EU ‘Directive on the better enforcement and modernisation of Union consumer protection rules’ (henceforth the ‘EU Consumer Modernization Directive’) is introducing the following requirements: (i) Traders must inform users on their website or application about how they ensure that reviews posted by consumers are authentic reviews from actual consumers who have used or bought the respective product or service. (ii) Traders are prohibited from stating that reviews of a product or service have been submitted by a customer who used or bought the product or service without taking reasonable and proportionate steps to check the accuracy of that statement. (iii) Traders are also prohibited from asking a party to submit false reviews or endorsements, or to misrepresent reviews or social endorsements in order to promote products or services. *Proposal for a directive of the European Parliament and of the Council amending Council Directive 93/13/EEC of 5 April 1993, Directive 98/6/EC of the European Parliament and of the Council, Directive 2005/29/EC of the European Parliament and of the Council and Directive 2011/83/EU of the European Parliament and of the Council as regards better enforcement and modernisation of EU consumer protection rules*, COM (2018) final (Apr. 11, 2018).



position to profit from illegal hidden advertising, but also because they are in the best position to design processes to prevent it.<sup>41</sup>

- *Criteria for rankings and inclusion in “best buy” boxes should be stated clearly and prominently; where traders have paid for higher rankings or better positioning, this constitutes advertising and should be clearly labeled as such.* Given the huge range of products and services available online, consumers can gain great benefit from ranking services and “best buy” boxes which help them to make choices. However, these consumer benefits can be limited if the criteria used to rank products or include them in a “best buy” box are not well aligned with the interests of the consumer. Given the importance of these choice tools, we consider that there should be a general requirement that criteria for ranking/inclusion are stated clearly and prominently. Critically, where traders have paid for ranking/inclusion, this again effectively constitutes advertising and should be labeled as such. Again, this labeling should be sufficiently clear and prominent that consumers are readily able identify the paid ads.<sup>42</sup>

Finally, while the above proposals are applicable to all online firms, we consider that especially strong requirements are needed for the largest online intermediation platforms.

Their critical bottleneck position as a route to market for traders means that there is very real potential for them to both mislead consumers and distort competition through their approach to rankings and “best buy” boxes. While greater clarity around criteria used for ranking/inclusion will help, it is far from obvious that consumers always know how to deal with this additional information. Indeed, if the higher rankings and inclusion in “best buy” boxes didn’t generate additional sales, traders wouldn’t pay for it. At the same time, the complexity of information provided to consumers could risk creating information overload and reducing consumer trust.

We therefore propose that:

- *For the largest online intermediation platforms, given their critical importance as routes to market, payment for rankings and inclusion in “best buy” boxes should be banned completely.* We recognise that this could reduce an important revenue stream for the platforms that they may need to recoup from elsewhere (including by selling ads at the top or along the sides of pages). Nonetheless, it would have a huge benefit in ensuring that rankings and “best buy” boxes on these critical platforms are designed in consumers’ interests and to work as well as possible to aid consumers in their decision-making.

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<sup>41</sup> The UK Competition and Markets Authority has accepted undertakings from several social media influencers to make it clear when they have been paid or otherwise incentivised to endorse a product or service. It has also accepted commitments from Instagram that it will do more to prevent hidden advertising, through both changing its policies and introducing new technological checks. See Competition & Markets Authority, *Social Media Endorsements*, Gov.UK (Aug. 16, 2018), <https://www.gov.uk/cma-cases/social-media-endorsements>.

<sup>42</sup> These requirements will explicitly become law in the EU through implementation of the EU Consumer Modernization Directive. See EU Consumer Modernization Directive, *supra* note 40. Even under existing EU law, the UK Competition and Markets Authority accepted commitments from a number of hotel online booking sites to improve clarity around their rankings and issued principles for the sector. Competition & Markets Authority, *Online hotel booking*, Gov.UK (Oct. 27, 2017), <https://www.gov.uk/cma-cases/online-hotel-booking>.

#### ***4. The importance of interface design/online choice architecture for consumer decision-making, and the potential for it to act against consumers' interests***

A fourth key difference between online and offline relates to the observation that consumer behavior can be strongly influenced by the way in which choices are presented to them. This is also known as “choice architecture,” and it is a key element in online interface design. We know, for example, that consumers exhibit strong “default bias.” An implication is that their choices can be strongly influenced by whether a particular box is initially ticked or unticked. We also note that settings vary and what is appropriate to protect consumers may differ in different cases. We propose general policies below but recommend that the regulator be tasked with studying different cases and adjusting as needed to achieve consumer protection goals.

It is impossible for platforms to avoid providing some form of choice architecture for consumers. And it is difficult to make this architecture entirely “neutral” in terms of leading consumers to replicate exactly the choices they would make if given the necessary time and information (as well as incentives to become informed about the consequences of their choice) to make a careful and deliberate decision. The “neutrality” regulation should not be designed to prevent the platform from helping consumers in their decision-making.

However, there is an obvious incentive for platforms to bias the design of choice architecture in their own interest, or in the interest of their business users, rather than in the interest of consumers. Take the default bias example above and suppose that a particular box commits the consumer to buying an add-on product they don't necessarily want—say flight insurance on an airline ticket. Pre-ticking this box would tend to increase sales of the add-on, because some percentage of consumers will fail to untick the pre-ticked box. They will do this even though they don't need the insurance and would never tick an unticked box. This is a form of “inertia selling” known as “opt-out” selling. It will typically be in sellers' interests but not consumers'.<sup>43</sup>

Where choice architecture is designed to take consumers down pathways that are more in sellers' interests than their own, it is sometimes referred to as containing “dark patterns.” Examples of such misleading conduct that are often highlighted include:

- the creation of a false sense of urgency or scarcity, for example by showing a countdown timer, which in turn puts pressure on consumers and is likely to lead to their making worse decisions; or by showing misleading low stock or high demand

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<sup>43</sup> In theory, such “opt-out” selling of an add-on product could be beneficial for consumers too, if they really need a product and default bias might otherwise lead to under-purchase (too little ticking of an unticked box). An analogous argument was made on appeal against the UK Competition Commission's intervention to prevent payment protection insurance being sold alongside loans. The appellant's argument was that consumers would otherwise not buy an insurance product which was of genuine value to them. The evidence in that case did not support the appellant's claim. See Competition Commission, *Payment protection insurance market investigation: remittal of the point-of-sale prohibition remedy by the Competition Appeal Tribunal – Final report* (Oct. 14, 2010), <https://assets.digital.cabinetoffice.gov.uk/media/5519489040f0b61401000159/report.pdf>. More generally, though, given the incentives of firms to oversell add-ons, it seems right—both economically and ethically—that consumers should make a positive choice when they are making a purchase.

messages like “Just one left at this price” or “Seven people are currently viewing the item”,<sup>44</sup>

- the prominent display of partial price information, with full prices only observed at a late stage of the purchasing process (known as “drip pricing”), or providing prices on a broken-down level with the full price not prominent (known as “partitioned pricing”). Both of these practices have been shown to worsen consumer decision-making and in particular to reduce consumer search (which is in turn likely to lead to worse choices and also harm competition),<sup>45</sup>
- the use of techniques such as brightly colored buttons, pop-ups, prominence, or obfuscatory wording that encourage consumers to sign up for products or services without giving the choice much (if any) attention.<sup>46</sup> While these aspects of interface design are not bad in themselves, and can help consumers to make good choices, they can nonetheless also cross the line into being misleading.

Many of these concepts are also relevant offline, but online platforms are in an especially good position to maximise the impact of their choice architecture. As discussed above, this is due to the combination of three related factors: (i) extensive data about individual consumer behavior; (ii) machine learning algorithms that can mine these data for relevant behavioral patterns; and (iii) A/B testing techniques that are designed to industrialize trial and error experimentation to maximize the choice architecture’s effect on users.

### *Specific policy proposals*

Consumer protection law has an important role to play in ensuring that online choice architecture functions to aid good consumer decision-making, rather than misleading them. It should therefore clearly:

- *Ban the use of defaults that require a consumer to “opt-out” in order to avoid a financial commitment.* This is sometimes known as inertia selling.<sup>47</sup> These often take the form of pre-ticked boxes to enroll, subscribe, or purchase the most expensive

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<sup>44</sup> Messages creating urgency and scarcity were the most common forms of dark pattern found online in a web sweep of 11,000 shopping sites by Mathur et al. (2019). Arunesh Mathur, et al., *Dark Patterns at Scale: Findings from a Crawl of 11K Shopping Websites*, 3 PROC. ACM HUM.-COMPUT. INTERACT. 81 (2019).

<sup>45</sup> For evidence on the detrimental impact of drip pricing and partitioned pricing on consumer decision-making, see Huck and Wallace (2015) and London Economics (2013). However, for an example in which drip pricing did not affect consumer purchase behaviour, see Dertwinkel-Kalt et al. (2020) who also discuss the differences between their conclusions and the prior literature. Steffen Huck & Brian Wallace, *The impact of price frames on consumers decision making: Experimental evidence* (Oct. 15, 2015), <https://www.ucl.ac.uk/~uctpbwa/papers/price-framing.pdf>. London Economics Office of Fair Trading, *Partitioned Pricing Research: A behavioural experiment* (Aug. 2013), [https://webarchive.nationalarchives.gov.uk/20140402165048/http://oft.gov.uk/shared\\_oft/economic\\_research/OFT1501A.pdf](https://webarchive.nationalarchives.gov.uk/20140402165048/http://oft.gov.uk/shared_oft/economic_research/OFT1501A.pdf). Markus Dertwinkel-Kalt, et al., *To buy or not to buy? Price salience in an online shopping field experiment*, 130 EURO. ECON. REV. 103593 (2020).

<sup>46</sup> See, e.g., the Amazon Prime complaint discussed *supra* note 22.

<sup>47</sup> In the EU/UK, the *Unfair Commercial Practices Directive* contains a general prohibition of inertia selling, while the ‘opt out’ selling of add-ons (including through pre-ticked boxes) has now been specifically banned under the *Consumer Rights Directive*.

option but would include any situation in which inactivity on the part of a consumer leads to a purchasing “choice.”<sup>48</sup>

- *Ban the use of messages that create a false sense of urgency or scarcity, which in turn lead consumers to make rushed and pressurized decisions.*<sup>49</sup>
- *Require that prices be displayed prominently upfront and include all unavoidable fees and charges.*<sup>50</sup> Where unavoidable fees and charges can only be calculated at a later stage, they should be included as soon as they are calculable. Any fees and charges that have not been provided before the “checkout” stage of the purchasing process should be cost-reflective.
- *More generally, prohibit interface design which acts to misdirect consumers.* This prohibition would address aspects such as misdirection through brightly coloured buttons, pale wording, or other aspect of interface design.<sup>51</sup>

The focus of the above is ensuring that choice architecture does not mislead consumers. These proposals are applicable to all online firms.

As in previous section, however, we consider that stronger requirements are appropriate for the largest online platforms, given their critical and economy-wide role in consumer decision making.

- *The largest online platforms should be given specific responsibility to ensure that their choice architecture is neutral.* A neutral choice architecture is one that does not present biased selections to the consumers and, to the extent it is possible, allows them to make the same choice that they would make if they had the time and information, as well as incentives, necessary to make a careful and deliberate choice. The largest online platforms should have the resources and capabilities to design such choice architectures and to demonstrate their impact.<sup>52</sup>

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<sup>48</sup> Note that this regulation would not prevent additional products being included as part of a bundle, with the consumer having the potential to make an active choice to remove the option, and so gain a discount. The difference in this case would be that the upfront advertised price of the bundle would be required to include the add-on; in effect, it would not function as an “add-on”, but rather as part of the core product offering.

<sup>49</sup> False scarcity and urgency messages were another element of the recent intervention by The UK Competition and Markets Authority against hotel online booking sites. *See supra* note 42.

<sup>50</sup> The UK Competition and Markets Authority has recently led EU-wide action in relation to the transparency of car rental sites, to ensure that key information is displayed clearly and prominently upfront with no unexpected hidden fees and charges. *See* Press Release, Competition & Markets Authority, CMA leads Europe-wide action on car hire (Mar. 25, 2019), <https://www.gov.uk/government/news/cma-leads-europe-wide-action-on-car-hire>.

<sup>51</sup> In a recent FTC enforcement action, a key finding was that the salient information for consumers was at the bottom of the page (which required scrolling) and was in faint type on a white background. *See* Lesley Fair, *Time for a ROSCA recap: FTC says “risk free trial” was risky – and not free*, Federal Trade Commission (Jul. 3, 2018), <https://www.ftc.gov/news-events/blogs/business-blog/2018/07/time-rosca-recap-ftc-says-risk-free-trial-was-risky-not-free>.

<sup>52</sup> New techniques are being developed that could play a role in enabling platforms to self-assess their choice architecture. *See* Dilip Soman, et al, *Seeing Sludge: Towards a Dashboard to Help Organizations Recognize Impedance to End-User Decisions and Action*, ROTMAN SCHOOL OF MANAGEMENT (Sept. 24, 2019), <https://static1.squarespace.com/static/5d1e3407108c4a0001f99a0f/t/5d8a6fc416577b70f51b896c/1569353670613/BEARxBIOrg-Seeing-Sludge-1.pdf>. A/B testing of outcomes is also likely to be crucial.

## 5. *The greater prevalence online of subscription-based sales and auto-renewing contracts*

With the move online, a growing number of products are offered on the basis of an ongoing subscription-based contract. Where consumers might once have bought a daily newspaper, a weekly cinema ticket, an occasional CD, video game, or audio book, they are now more likely to have a monthly or annual subscription to their favorite newspaper, video streaming service, music streaming services and online gaming service.

Where subscriptions are in the form of fixed-term contracts, these are often set to “auto-renew,” so the service continues unless it is proactively cancelled. Such subscription-based services can be attractive for consumers in smoothing expenditure, and enabling them to try out new music, games, etc. However, they can also result in consumer “lock-in” or inertia, with consumers failing to cancel services they no longer use, or failing to seek out alternative providers that might offer a better service.

Subscription-based sales have long been used in core utility markets, and there is substantial evidence from these markets of consumers’ exhibiting significant inertia in terms of failing to search and switch to better offers. This is concerning partly because consumers are failing to benefit from better deals but also because a lack of search will tend to dampen competition. There is evidence of utility providers gradually raising prices to inactive consumers, creating a substantial “loyalty penalty” relative to the prices they could obtain if they were active.<sup>53</sup> Regulators have made significant efforts to make search and switching as easy as possible in these markets, although this has not proved straightforward.<sup>54</sup>

In an online context, the situation is potentially worsened by the ability of platforms to use their choice architecture in a way that makes signing up very easy (or even hard to avoid) while cancelling or switching is made extremely difficult. Moreover, many subscription services are offered on the basis of a free initial period. While this can be a valuable way of enabling consumers to try a new service, they are not always reminded that they are about to start paying and can find it unduly difficult to cancel the contract.

### *Specific policy proposals*

To ensure that consumers are not unduly locked into long-term subscription-based or auto-renewing contracts, it is vital that consumers are made fully aware of what they are signing up to, kept informed about their commitment through time, and that they can cancel and switch easily and efficiently. More specifically, we propose the following.<sup>55</sup>

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<sup>53</sup> In 2018, the UK Competition and Markets Authority examined five major UK utility markets and estimated a total ‘loyalty penalty’ of £4 billion. See Competition & Markets Authority, *‘Loyalty penalty’ super-complaint*, Gov.UK (Sept. 28, 2018), <https://www.gov.uk/cma-cases/loyalty-penalty-super-complaint>.

<sup>54</sup> See Keith M. Marzilli Ericson, *Consumer Inertia and Firm Pricing in the Medicare Part D Prescription Drug Insurance Exchange*, 6(1) AM. ECON. J. 38 (2014) (finding consumer stickiness in switching Medicare Part D plans); Xiaopeng He & David Reiner, *Why Do More British Consumers Not Switch Energy Suppliers? The Role of Individual Attitudes*, EPRG Working Paper (Sept. 2015), <https://www.eprg.group.cam.ac.uk/wp-content/uploads/2015/09/1515-PDF.pdf> (finding the same for UK energy and gas markets).

<sup>55</sup> We note that many of the following elements are incorporated in the existing Californian Automatic Renewals Law. We also note that the Washington Post is currently subject to a class action under this law for not making it clear that the free offer was for an initial period, and then making it unduly onerous to cancel. See *Washington Post Auto-Renewal Violations California Class Action*, CLASS ACTIONS REPORTER (July 29, 2020), <https://classactionsreporter.com/washington-post-auto-renewal-violations-california-class-action/>.

- *For any sale of subscription-based or auto-renewing service, the price and any minimum contract period or minimum purchase obligation should be set out clearly and prominently upfront.* Where a service is sold on the basis of an initial free period, the price to be paid after this period should be set out clearly and prominently upfront. These terms should also be notified to consumers through a sign-up email.
- *Advance notice should be made of any change in terms.* This should be sent via email and the change in terms should be clear and prominent and flagged within the subject header of the email. When terms change, consumers must be given the chance to cancel and at the same time to continue using the service for a reasonable amount of time while looking for a new supplier. Free trials should not be converted into paid services without specific notice being given, allowing time to cancel.
- *Consumers should be notified of their total ongoing charges from that trader at an appropriate frequency.* Consumers can sometimes stack up a variety of subscriptions, sometimes even duplicative ones, so requiring the trader to notify total charges would help to identify this issue. Guidance would be needed as to what an “appropriate frequency” might be, but it should be infrequent enough to engage the attention of consumers but frequent enough to allow for timely decision-making.
- *There should be a prohibition on the opt-out selling of automatic renewals,* whereby a consumer is defaulted into an auto-renewing contract unless they take a specific action not to allow auto-renewal. Signing up for automatic renewals should require active consent by consumers, not be the result of default bias.<sup>56</sup>
- *It should be possible to cancel a contract via the same medium as it is entered.* That is, there should be no need to phone or write an email or letter to cancel a contract entered online. This obligation could potentially be generalized into a principle-based rule that that it be as easy to cancel a contract online as it is to enter it.
- *There should be no exit fees (i) after any initial minimum contract period or minimum purchase obligation, or (ii) for any contract that has auto-renewed, or (iii) for any contract offered on the basis of a free initial period.* The notice period for any cancellation should not be any longer than 28 days, and thereafter sellers must reimburse *pro rata* any fees paid in advance for any unused service.<sup>57</sup>
- *There should be an easy and efficient mechanism to cancel the service.* This should involve consumers making no more than three clicks. A simple link should be included within the initial sign-up email, and all email notifications thereafter. It may be useful to provide further guidance on what a simple cancellation mechanism might

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<sup>56</sup> There is a possibility that such a prohibition could lead subscription services simply to lengthen the minimum term of a subscription. An online magazine that used to sell one-year subscriptions could decide, for example, to sell only two-year subscriptions. The regulator should monitor for this sort of evasive behavior and be empowered to require shorter renewal periods on a case-by-case basis.

<sup>57</sup> From a behavioural economics perspective, we acknowledge that the ability to cancel at any time risks undesirable consequences. If procrastination is for example driven by naïve hyperbolic discounting, this rule could increase the amount of procrastination. At the same time, it could reduce procrastination deriving from consumers’ overestimating their future likelihood of remembering to do so or underestimating the future hassle cost of doing so. We believe that on average, it is likely to increase the cancellation of contracts with undesirable features.

comprise. For example, a template “cancellation button” (standardized with respect to colour, placement, font, and the like) could usefully be provided; use of this would then act as a safe harbour against liability. Immediate email confirmation of cancellation with date from which on contract is cancelled should also be required.

As in previous sections, although the above proposals are intended to apply to all, we consider that additional requirements are appropriate for the largest online platforms:

- *Where a service involves a regular monetary payment, the platform should be required to contact any user who has not made active use of the service for a year. The regulator should issue guidance as to what constitutes “active use,” which may vary from service to service. If the user does not provide active consent to continuing the service, the platform should be required to terminate the service and cease taking payments.*<sup>58</sup>
- Where considered appropriate, the regulator should have the power to impose a requirement on platforms that consumers be able to port their data to a new provider, on a continuous real-time basis. This will facilitate both one-off switching and ongoing multi-homing.<sup>59</sup> For data portability to work in a safe and secure way, the regulator may also need to accredit or license third-party providers to ensure they meet the standards the government laws down for privacy, security, etc. Clear rules on liability of both the sending and receiving platforms may also be required.

## **6. *The growth in online services that are ostensibly free, but which in practice monetize consumer data and attention***

A sixth difference between online and offline markets is that a greater range of services are provided for no monetary price to consumers and monetized by other means (such as advertising or data collection). In the offline world, consumers always benefited from a number of free radio and TV channels and newspapers, which were advertising funded. Online, such free provision has ballooned, with consumers having free access to a wealth of different services, from social networks, to email, to mapping apps, to games, to audio-visual communications services, etc.

Consumers certainly benefit from these services but they are hardly “free.” Consumers effectively barter for them with their attention and/or their data. As such, there is still a seller-consumer transaction which platforms can abuse, for example, by making it hard for consumers to understand what they are signing up for, by extracting more data than the consumers realize, or by making it difficult for them to switch.

### *Specific policy proposal*

Consumers should thus have the same rights when they receive services in a barter setting as they when they pay money for them. However, existing consumer protection law sometimes

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<sup>58</sup> We note that Netflix has recently adopted this proposal voluntarily as good practice. Eddy Wu, *Helping Members Who Haven't Been Watching Cancel*, NETFLIX (May 21, 2020), <https://about.netflix.com/en/news/helping-members-who-havent-been-watching-cancel>.

<sup>59</sup> In the EU, this is a proposed obligation (Article 6(1)(h)) within the forthcoming Digital Markets Act. *Proposal for a Regulation of the European Parliament and of the Council on Contestable and Fair Markets in the Digital Sector (Digital Markets Act)*, COM (2020) 842 final (Dec. 15, 2020).

refers to “sales practices” or “transactions,” which are terms which might be viewed as implying a monetary payment. Therefore, we consider that:

- *all relevant consumer protection legislation should explicitly apply to digital content and digital services that are provided free of charge but in exchange for personal data, except where such personal data is only used to supply the digital content or service, or to comply with the law.*<sup>60</sup>

## **7. *The greater collection and use online of extensive personal data***

The extent of consumer data which is collected and used by online firms, whether free or paid-for, has ballooned over the past decade and goes well beyond anything observed by way of data collection in the offline world. These data can have a multiplicity of uses. They can act as an input into providing and enhancing the service in question. They can also facilitate in monetizing the service, for example by allowing targeted advertising or sales. Data from one market can also be useful for other activities, not directly related to the service received by the customer, and potentially also monetizable in that wider context.

In agreeing to provide their data for some valuable future use, consumers could be seen as paying “in kind” for the service they receive. However, and unlike the situation with standard prices, it is rarely clear to consumers exactly what data they are providing or how it will be used going forward. Moreover, platforms have an incentive both to obfuscate and to offer defaults that encourage consumers to sign up to maximally extensive data collection and use.

When consumers are informed about the extent of the data they are providing and how it is used, their level of concern tends to increase.<sup>61</sup> At the same time, consumers are not inclined to spend significant time trying to address this issue, as demonstrated by the EU experience of GDPR consent requirements, whereby consumers are given a “take-it-or-leave-it” choice and become “click-happy,” always saying yes.

This is not unreasonable behavior. As discussed above, life is simply too short to review all of the detailed terms and conditions for the many services for which we all sign up. It is not that consumers are stupid or lazy. Rather, in many circumstances, the details of the terms and conditions make it difficult (in time or expertise) to make a choice. Moreover, the “choice” is not really a choice at all, but effectively a “take-it-or-leave-it” offer, which the consumer needs to accept if you wish to receive the service.<sup>62</sup> Because many of these services hold significant market power or even monopoly power, the situation from the standpoint of the consumer is very different than, say a grocery shopper who easily can choose to purchase a product *without* high fructose corn syrup rather than a similar product *with* it.

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<sup>60</sup> This change is in the process of being implemented in the EU through the EU Consumer Modernization Directive. See EU Consumer Modernization Directive, *supra* note 40.

<sup>61</sup> BRITAIN THINKS, THE PRICE OF ACCURACY: CONSUMER ATTITUDES TO DATA AND INSURANCE (2019), [https://www.abi.org.uk/globalassets/files/publications/public/data/britain\\_thinks\\_consumer\\_data\\_insurance\\_report.pdf](https://www.abi.org.uk/globalassets/files/publications/public/data/britain_thinks_consumer_data_insurance_report.pdf).

<sup>62</sup> In its market study into digital advertising, the UK Competition and Markets Authority found that several social media platforms either gave consumers no real choice about giving up their data and accepting targeted advertising, or even if a choice was formally available, utilised strongly nudges and defaults to achieve the same outcome. See COMPETITION & MARKETS AUTHORITY, ONLINE PLATFORMS AND DIGITAL ADVERTISING MARKET STUDY (2019), <https://www.gov.uk/cma-cases/online-platforms-and-digital-advertising-market-study#final-report>.



There is an analogy to the offline issue of credit. Unless credit offerings are provided in a clear and highly simplified, standardised and easily comparable format, consumers struggle to make good decisions and don't bother to read the small print. As such, the format in which credit information is provided is now highly regulated, even down to the precise calculation methodology for Annual Percentage Rates and the font sizes to be used.<sup>63</sup>

*Specific policy proposals:*

In an online environment, there is equally a need for the regulator to develop or approve a simplified standardized format for disclosing the privacy features of particular services, which consumers can learn and get used to using. This could usefully contain standardised levels of privacy so that a consumer who invested in learning that she is comfortable with Level 2 could select Level 2 the next time she was confronted with a choice. Such a standardized format would be most useful if it applied across all digital services that collect data from consumers. Service providers could then offer different product offerings to consumers, on the basis of different privacy features. Recognising that this is never going to be a straightforward choice, consumers will nonetheless be in a far better position to make reasoned trade-off than they are today.

We therefore recommend the following:

- *The regulator should develop a simplified, standardised way of presenting privacy features and online firms should be mandated to use it.* The regulator should ensure that the choice screen has simple language and graphics so that it is accessible to a large fraction of consumers.<sup>64</sup>
- *Consideration should also be given to enabling this standardized privacy system to allow consumers to set, upfront, limits on the amount and types of personal data that can be gathered. These limits would then become the default limits for that consumer across different apps and services.* The consumer would only be alerted to provide active consent if a particular site offered privacy protections or gathered more or different data than the consumer had chosen as their preferred defaults.
- *Absent this, the regulator should at least develop default standards for the amount and types of personal data that can be collected without requiring active consumer consent.* Firms wishing to collect more or different data than permitted by the default standards would be required to obtain active consumer consent. This would be valuable in overcoming the issue of “click-happy” consumers. This minimum privacy standard should explicitly exclude both the possibility of selling the personal data and the limitation of liability for third party use of data. If this were done, then any privacy notification would signal something out of the ordinary that was genuinely worthy of a consumer's attention. Firms in turn may wish to avoid triggering such a notification, and thus this standard would likely become the industry norm, reducing

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<sup>63</sup> See Truth in Lending (Regulation Z), 12 C.F.R. pt. 1026 (2017) (regulating font size and bold type for consumer credit reporting).

<sup>64</sup> Apple is developing a format that may be a useful basis of such a requirement (but it should also cover Apple's operating system itself). See Brian X. Chen, *What We Learned From Apple's New Privacy Labels*, N.Y. TIMES (Jan. 27, 2021), <https://www.nytimes.com/2021/01/27/technology/personaltech/apple-privacy-labels.html>.

the requirement for consumers to make difficult choices in this area for themselves, while still allowing firms to diverge if they wish.

## **8. *The prevalence of network effects for digital platforms***

Many digital platforms tend to exhibit network effects, in that the value of the platform to any user will increase with the total number of platform users. For example, a person might value Facebook more than Snapchat because far more of their friends are on Facebook. This means that platforms—especially when starting out—have strong incentives to increase their user base through illicit means.

Dating sites provide a good example. In recent years, a firm with several dating sites was found to have cross-registered members across their different sites without the members' knowledge, to have falsified its member numbers, and to have made it hard for people to take down their profiles when they cancelled their subscription.<sup>65</sup> Another dating site was found to have falsified profiles to gain new members.<sup>66</sup> By using such deceptive tactics to suggest a larger number of potentially available dates or partners, dating platforms can keep users engaged and benefit from their willingness to pay for continuing to use the service.

### *Specific policy proposal*

- Membership platforms should be barred from cross-registering members across their services without their active consent, and from creating fake profiles. When people cancel their membership, their profile should be automatically removed unless they explicitly consent otherwise.

## **9. *The need to prevent the use of data to discriminate against vulnerable consumers***

A further implication of the extensive collection of personal data described above is that it can be used by large online firms to make highly personalized offers that depend on details of the consumer circumstances as well as past behavioral and responses. Indeed, through the use of sophisticated machine learning algorithms, these firms may be better able to predict the consumer's future behavior than the consumer herself. Again, although individualization is also observed in an offline world (a clothing salesperson may show an unusually tall person brands or styles that run large, for example), the potential for individualization is far greater online.

Some forms of individualized treatment can be positive for consumers. Many consumers value advertising and sales offers that reflect their particular interests. But individualized treatment can also be detrimental to consumers. For example, it may allow firms to

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<sup>65</sup> Competition & Markets Authority, *Online Dating Giant Vows Clearer Path to Love*, GOV.UK (June 13, 2018), <https://www.gov.uk/government/news/online-dating-giant-vows-clearer-path-to-love>.

<sup>66</sup> Federal Trade Commission, *FTC Sues Owner of Online Dating Service Match.com for Using Fake Love Interest Ads to Trick Consumers into Paying for a Match.com Subscription* (Sep. 25, 2019), <https://www.ftc.gov/news-events/press-releases/2019/09/ftc-sues-owner-online-dating-service-matchcom-using-fake-love>. See also Gieselmann and Rasch (2021) for a discussion of the use of “chat moderators” on a variety of dating apps in Germany. Jana Gieselmann & Alexander Rasch, *Platform Investment Incentives: Dating and Fake Profiles*, UNI. OF DUSSELDORF, 4th Doctoral Workshop on the Economics of Digitization, online event, May 18-19, 2021, [https://www.tse-fr.eu/sites/default/files/TSE/documents/conf/2021/doctoral\\_workshop/gieselmann.pdf](https://www.tse-fr.eu/sites/default/files/TSE/documents/conf/2021/doctoral_workshop/gieselmann.pdf).

successfully extract consumer surplus through personalized pricing or offers (and especially when firms have significant market power).

Individualization is also less likely to be beneficial if it is associated with consumers' biases or weaknesses.<sup>67</sup> Firms can potentially target individual consumers with advertising or sales offers that are designed to exploit their particular fallibility. A particular focus online has been on the marketing of inappropriate products to children. However, the individualization possibilities online expand the traditional notion of "vulnerable consumers" beyond a group characterized by demographics (e.g., the young or the elderly) to a wider set of circumstances. Online examples might include:

- Firms selling overpriced mortgages or other financial products with "exploitative features" to consumers who reveal in some way that they are less likely to find a more suitable product.<sup>68</sup>
- Advertising platforms serving up ads for casinos to individuals searching for advice about problem gambling, or who have or are attempting to stop gambling.<sup>69</sup>
- Ads for fraudulent financial services to individuals searching for high-yield investments.<sup>70</sup>
- Individuals being targeted at a particular moment of weakness, for example when their mood is expected to be low.<sup>71</sup>

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<sup>67</sup> This is true even when markets are competitive. See Heidhues and Köszegi (2017), *supra* note 16.

<sup>68</sup> See Heidhues and Köszegi (2017), *supra* note 16.

<sup>69</sup> See Adam Satarino, *What A Gambling App Knows About You*, N.Y. TIMES (Mar. 24, 2021), <https://www.nytimes.com/2021/03/24/technology/gambling-apps-tracking-sky-bet.html>.

<sup>70</sup> As the UK's Financial Conduct Authority illustrated, Google listed ads for financial scams in response to searches for high-return investment. See Mathew Vincent, *UK Regulator Says Google Not Doing Enough About Scam Ads*, FINANCIAL TIMES (Sep. 24, 2020), <https://www.ft.com/content/ca700726-c48c-4132-953b-8d6a1e57f00c>.

<sup>71</sup> An example might be advertisers using specialists such as Weather Ads to match their Facebook ads to local weather conditions, which in turn affects the consumer's mood and tendency to buy certain products. See WeatherAds, *Facebook Weather Targeting – How to Sync Your Facebook Ads with Weather*, <http://www.weatherads.io/facebook-weather-targeting> (last visited May 14, 2021). This is broadly in line with academic research illustrating that current weather conditions affect purchases behavior (see, e.g., Conlin et al., 2007, Busse et al., 2015, Chang et al., 2018). Michael Conlin et al., *Projection Bias in Catalog Orders*, 97 AM. ECON. REV. 1217 (2007); Meghan R. Busse et al., *The Psychological Effect of Weather on Car Purchases*, 130 Quarterly J. of Econ. 371 (2015); Tom Y. Chang et al., *Something in the Air: Pollution and the Demand for Health Insurance*, 85 REV. OF ECON. STUD. 1609 (2018). We also note concerns that Spotify (which is increasingly moving into advertising) has developed speech-recognition technology which can detect, among other things, emotional state, gender, age and accent. See Mark Savage, *Spotify wants to suggest songs based on your emotions*, BBC.COM (Jan. 28, 2021), <https://www.bbc.com/news/entertainment-arts-55839655>; Access Now, *Spotify, Don't Spy: Global Coalition of 180+ Musicians and Human Rights Groups Take a Stand Against Speech-Recognition Technology* (May 4, 2021), <https://www.accessnow.org/spotify-spy-tech-coalition/>. Furthermore, there are concerns regarding the use of patent Uber applied for identifying drunk or drugged users of the Uber app; see Arwa Mahdawi, *Uber Developing Technology that Would Tell If You're Drunk*, GUARDIAN (June 11, 2018), <https://www.theguardian.com/technology/2018/jun/11/uber-drunk-technology-new-ai-feature-patent>.

### *Specific policy proposals*

- *Platforms should not be permitted (through algorithms or direct targeting) to discriminate against consumers based on their membership in any (in the US) protected class (race, religion, gender, etc.) or any group identified by the regulator/government to be vulnerable to particular sales practices or services.* High-paying job ads should not be shown primarily to men, for example, or high mortgage interest rates to Black consumers, or financial scams to the elderly.
- *Traders should be required to inform consumers when a price is personalized on the basis of automated decision-making<sup>72</sup> They should also set out the criteria on which the personalization is based.<sup>73</sup> This would help to provide a reputational check against forms of price personalization that are considered socially egregious. As an example, Uber has been accused of charging higher prices to users whose cell phone batteries were low and the consumers were thus less likely to take the time to search for a lower price. Uber has denied this practice but has accepted that this would be technologically feasible.<sup>74</sup> We presume that its main reason for not engaging in such a pricing strategy is reputational.*
- *Clarify the law in order to explicitly permit reverse engineering for research or policy purposes.* Currently, algorithmic discrimination is most often proven through reverse engineering algorithms and reviewing their outcomes. However, such activity is potentially in breach of the law relating to data scraping, and academics working in this area, typically in the public interest, are fearful of prosecution. Clarification that the law allows this use would help to support such socially useful research.<sup>75</sup>

As in previous sections, we consider that the largest online platforms merit additional requirements.

- *For the largest online platforms, personalised rankings and targeting (whether of advertising or sales offers) should not be permitted to be based on characteristics designed to predict vulnerability.* The regulator would be required to provide guidance on what is meant by vulnerability for the purpose of this provision. A test could be devised that is similar to the neutrality test above.
- *The largest online platforms should be required to set out publicly their approach to targeting, and how they ensure that their systems do not result in inappropriate targeting of vulnerable consumers.* This transparency measure would help in

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<sup>72</sup> This will be introduced in the EU as part of the EU Consumer Modernization Directive. EU Consumer Modernization Directive, *supra* note 40.

<sup>73</sup> The benefits of public explanation of personalized pricing are discussed in Lyons and Sugden (2021). Bruce Lyons & Robert Sugden, *Transactional Fairness and Pricing Practices in Consumer Markets* (Centre for Competition Policy, Working Paper No. 21-03, 2021).

<sup>74</sup> See Jessica Lindsay, *Does Uber Charge More If Your Battery is Lower?*, METRO (Sep. 27, 2019), <https://metro.co.uk/2019/09/27/uber-charge-battery-lower-10778303/>.

<sup>75</sup> We note that data scraping imposes a cost on websites, but websites can overcome this by providing open APIs to allow direct data download. If data scraping were clearly legal, sites would have more incentives to open up their data for research in this way.

incentivising good conduct by the platforms as well as providing valuable information for the regulator for monitoring and enforcement of the previous requirement.

#### ***10. The need to ensure that participants in C2C transactions are adequately protected***

Another key difference between online and offline markets is that individuals are far better able to participate on the supply-side as well as the demand-side. The extent of C2C (customer-to-customer) trading on platforms such as eBay, Craigslist, and Airbnb is far greater than was ever observed through classified ads in an offline environment. Such C2C trading is valuable in allowing the optimal use and re-use of resources, and it brings huge benefits. However, consumer protection law typically only protects consumers when acting on the demand-side of any trade. Moreover, it only protects consumers against poor treatment by business sellers, and it is not always obvious to consumers whether they are dealing with a business or a consumer seller.

The success of the main C2C platforms partly reflects the investment they have made in finding alternative routes for protection of their customers, on both sides of the platform, which has earned many of them a substantial degree of trust. However, this form of “self-regulation” has been imperfect and customers often complain that they find out too late that they were purchasing from an individual, not a business, and thus have no recourse under consumer protection law.

#### *Specific policy proposals*

There is thus a need to complement the valuable consumer protection measures introduced by C2C platforms themselves, if consumer trust is to be enhanced and justified.

- C2C platforms should require sellers to state whether they are a business or an individual.<sup>76</sup>
- C2C platforms are themselves sellers of services to their trader customers. Where these are individuals, standard consumer protection law should apply to the intermediation service sold by the platform to the trader, even though the traders are formally a seller rather than a consumer. Effectively, such individuals should be viewed as consumers of the platform’s intermediation service.

We note that, beyond individual traders, there is an argument that small traders have important similarities to end consumers, in terms of their fragmentation and their lack of bargaining power against the large digital platforms. As such, some elements of consumer protection, for example relating to transparency, could usefully be extended to them too. We have not sought to cover the treatment of small traders in this paper, but we note that in the EU/UK, the “Platform-to-Business” Regulation goes some way towards this, and the Digital Markets Act introduces some additional protections for business users of the largest online platforms.

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<sup>76</sup> This requirement is currently being introduced in the EU as part of the EU Consumer Modernization Directive. EU Consumer Modernization Directive, *supra* note 40.

## ***11. The largest gatekeeper platforms are in a unique position to “police” the third-party business users of their platforms***

A final important characteristic of large digital platforms is that they play two relevant roles. The focus of the discussion above has been on ways in which digital platforms might create or exploit ineffective consumer choice directly themselves. However, many digital platforms also act as critical routes to market for business users, either as sales intermediaries or as advertising media. They are therefore a key medium through which these third parties are able to act to treat consumers poorly or fraudulently. Moreover, in some cases their conduct can exacerbate this harm, as shown by the fraudulent financial services example above.

In respect of this “intermediation” role, platforms are in a unique position to monitor and restrict such activity by business users, to ensure that it is neither fraudulent nor otherwise in breach of consumer protection rules.

Given that platforms earn money from being a conduit, it could be argued that the platforms already have a responsibility to do this. Indeed, some already do, to greater or lesser extents. For example, we assume that Amazon has strong incentives to protect consumers against the sale of fake goods, not least because its own approach to inventory management means that the goods of different traders are often combined and consumers can’t rely on getting their goods sold from the precise trader they have chosen. Likewise, during the early phase of the COVID-19 pandemic, Amazon was active in preventing the sale of fake cures.

Platforms do not always have the right incentives to play this role, however, both due to the associated loss of revenue and because the process of effective monitoring and enforcement can be costly. Investigations and enforcement actions in various jurisdictions suggest that travel sites have failed to make clear that hotels impose resort fees, that a concert ticket aggregator has obfuscated service charges, and that a home rental service has failed adequately to disclose hosts’ fees.<sup>77</sup> These examples demonstrate not just that platforms acting as intermediaries don’t always have the right incentives, but that platforms actually have acted on these mis-aligned incentives, to the detriment of consumers.

### *Specific policy proposals*

- *The largest gatekeeper platforms should be made responsible for taking all reasonable steps to prevent third party business users from engaging in illegal sales practices that breach consumer protection law via their platforms. If they fail to take all reasonable steps – as defined by ex ante standards that prescribe the required*

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<sup>77</sup> See, e.g., Press Release, Federal Trade Commission, FTC Warns Hotel Operators that Price Quotes that Exclude 'Resort Fees' and Other Mandatory Surcharges May Be Deceptive (Nov. 28, 2012), <https://www.ftc.gov/news-events/press-releases/2012/11/ftc-warns-hotel-operators-price-quotes-exclude-resort-fees-other>; Federal Trade Commission, *Online Event Tickets Workshop* (Jun. 11, 2019), <https://www.ftc.gov/news-events/events-calendar/2019/03/online-event-tickets-workshop>. Johnen and Somogyi (2019) argue theoretically that platforms can have an incentive to allow sellers to use intransparent fees and discuss a number of consumer protection cases concerned with such intransparent fees. Johannes Johnen & Robert Somogyi, *Deceptive Products on Platforms* 10-13 (NET Institute, Working Paper No. 19-13, 2019).

“reasonable steps” – they should be liable as if they had engaged in the violations themselves.<sup>78</sup>

- *The largest online platforms should be required to set out publicly their approach to the previous requirement and also publish KPIs:* This transparency measure would help in incentivising good conduct by the platforms as well as providing valuable information for the regulator for monitoring and enforcement of the previous requirement.

## Regulatory powers

For all of the policy proposals above, a further issue is how an enforcer can assure itself that platforms are abiding by the requirements. For most online firms, it may be sufficient to rely on a combination of complaints about breaches to public enforcers with the ability to gather information and impose significant sanctions, and private litigation rights.

For the largest gatekeeper platforms, however, in light of their outsize importance, we recommend a more proactive regulatory approach, including:

- Requiring the platforms to report, on request, details of their **A/B testing** in particular areas.
- Requiring the platforms carry out **A/B testing** to check the impact of their activities, and that they make the results of this A/B testing available to the relevant public body.<sup>79</sup>
- Requiring the platforms to **make data available** (in properly anonymized form) either directly or indirectly via regulators to academics doing research, so they can identify misleading patterns.
- Requiring the platforms to adopt fair and transparent **complaint procedures**, and also that terms of use do not contain any prohibition against users making a complaint to the regulator or any other relevant public body.
- The regulator itself should establish **whistleblower** procedures that permit platform employees to provide relevant public bodies with information about breaches of the consumer protection requirements, on a confidential basis, and potentially even receive compensation (for example, part of any eventual fine).
- **Large sanctions** are likely to be required if these platforms are to take the regulations seriously.

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<sup>78</sup> We note that the forthcoming EU Digital Services Act will introduce some responsibility in this area. See *Proposal for a Regulation of the European Parliament and of the Council on a Single Market For Digital Services and amending Directive 2000/31/EC (Digital Services Act)*, COM (2020) 825 final (Dec. 15, 2020).

<sup>79</sup> The regulator should exercise such power with great caution. A/B testing by its nature can make some consumers worse off than they would have been but for the test, either in an absolute sense or relative to other consumers.

## Conclusion

If markets are to function efficiently and in the interest of consumers and businesses, an authority must be empowered to enforce an effective regime of consumer protection rules applicable to those markets. This is the case for online markets just as it is for offline markets. In addition to this efficiency-based justification for consumer protection, we also know that consumers have the right not to be defrauded or misled. Consumer protection law ought to protect that right regardless of whether the consumer is transacting online or offline. Despite these points of consensus—that consumer protection is necessary to promote efficiency and to protect consumer rights online—too little has been done to ensure that the various standards applicable in *offline* markets are sufficient or adequate to guarantee efficiency and fairness in *online* markets.

This paper has outlined eleven key features of online markets that might necessitate standards additional to or different from those that are applicable offline. In online markets, for example, consumers generally do not interact face-to-face with sellers. This suggests that online sellers should be required to disclose more information about themselves (location and contact information, for example) than offline sellers. Similarly, online consumers generally are unable physically to evaluate products before purchase. This suggests that online quality indicators (product reviews and ratings, for example) take on heightened importance online and ought to be policed with heightened scrutiny.

As a general matter, however, and despite that this paper recommends a number of specific policy proposals for each key difference between online and offline markets, we do not think it necessary that every jurisdiction adopt an entirely new or separate regulatory regime for online markets. Many if not most of our proposals could be enacted through minor changes to existing law or regulation or through decisional law interpreting existing standards of conduct. Some have already been implemented in some jurisdictions. What *is* needed in *all* jurisdictions, however, is a regulator or regulators with sufficient expertise around technical issues such as A/B testing and algorithmic decision-making that they can understand, anticipate, and remedy the myriad ways that online firms can disadvantage consumers.

We also advocate that authorities in various jurisdictions think *systematically* about how to calibrate their consumer protection regimes to ensure that they foster efficiency and protect consumer rights online. The proposals set forth in this paper provide a menu of options—all of which are supported by basic economic principles—specifically designed for authorities engaged in such an undertaking.

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## **Appendix 1 – Author Conflict of Interest Disclosures**

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