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Striking a Balance: Basic Questions About Consumer Protection Law

*Kurt Eggert**

Chapman Law Review's annual symposium, this year entitled "Responsibility and Reform: Striking a Balance in the Marketplace," is focused on an important issue in today's legal landscape: how much and what kinds of protections should be provided to consumers? Central to this issue is how to balance the protection of consumers' persons and pocketbooks with the defense of their autonomy, how to keep consumers from entering into dangerous or disadvantageous transactions without stripping them of the freedom to choose for themselves which products, services, and deals will most benefit them. The panels of speakers for the symposium were focused on four separate but interrelated topics: Predatory Lending, Punitive Damages, Gun and Tobacco Liability, and California's Unfair Trade Practices Act (Business and Professions Code Section 17200).

This Introduction sets forth some of the most important questions raised in the course of the Symposium and describes some answers suggested in the articles that follow. Naturally, the authors often disagree with each other, but my goal is not to prove that one side or the other in any debate is correct but merely to lay out the questions in a methodical manner and direct the reader to the different authors' attempts to respond to these questions.

1. Which Transactions Benefit Consumers?

Normally, consumers are better judges of which transactions benefit them than any state regulator or legislator could be, as consumers have more direct and in depth knowledge of their own preferences. Professor Narveson, in "Consumer's Rights in the Laissez-Faire Economy: How Much Caveat for the Emptor?," states, "Did Consumer make a 'good buy?' That's for Consumer to decide."¹ However, this basic principle has important

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¹ Jan Narveson, *Consumers' Rights in the Laissez-Faire Economy: How Much Caveat for the Emptor?*, 7 CHAP. L. REV. 181, 193 (2004).

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limitations, since to be effective judges of whether a transaction will provide a net benefit to them, consumers must be informed and competent to make the decision at hand, and the transaction must be voluntary.

Most of the disagreement over whether and how much protection to provide consumers stems from conflicting opinions about when consumers' decisions are sufficiently informed, competent, and voluntary. Too little protection leaves consumers vulnerable to abuse. Too much protection leads to a paternalistic restriction of consumers' autonomy. Where exactly to draw the line between protection and paternalism is subject to great dispute. Proponents and opponents of consumer protection disagree on how much information consumers need to make decisions effectively, who is responsible for ensuring they have that information, what decisions consumers are competent to make without help, how often they lack the ability to make good decisions, and how voluntary their agreements are to the terms of various transactions. How these disputes are resolved is central to the design, role, and function of consumer protection law.

2. Should there be a Separate Law of Consumer Protection?

A basic question addressed in this symposium is whether there should be a separate law of consumer protection to begin with, or whether the common law systems of contracts and torts provide consumers with all the protection they need or deserve, or that it is efficient to provide them. In his article "Consumer Law, Class Actions, and the Common Law," Greve lays out (only to attempt to knock down) the normally stated rationales for consumer protection: that buyers have limited information gathering and processing abilities or even limited rationality in their decision-making process which leads them to make errors in their transactions. This information asymmetry and unequal bargaining power between seller and consumer allows merchants to take advantage of the ignorance and lack of bargaining prowess of the less sophisticated buyers.²

Greve argues, however, that each of these arguments proves either too much or too little, since information asymmetries and unequal bargaining powers exist in commercial as well as consumer transactions. Greve is even more concerned about the overlay of a consumer protection system on top of the common law; worried that a duplicative set of systems will decrease,

² Michael S. Greve, *Consumer Law, Class Actions, and the Common Law*, 7 CHAP. L. REV. 155, 157 (2004).

rather than increase, the benefits of those laws to consumers. Professor Harrell, in his article "Basic Choices in the Law of Auto Finance: Contract Versus Regulation," also argues for the primacy of the common law over separate consumer protection law. He states that because contract and tort law depend on case-by-case decision-making by judges, rather than on across-the-board rule-making by a regulatory body, the common law system infringes less on the freedom to contract as it wields a more precise scalpel to cut out inappropriate transactions.³ Harrell also asserts that this system of individual trials is better able to address the infinite variety of fraud, duress, and abuse than a "one size fits all" regulatory scheme. Unlike the common law, which Harrell sees as being based on the usage of market participants, consumer protection law is largely designed by legislators and regulators. Thus, Harrell views consumer protection law as the "top-down" imposition of their own interests and views by an elite few and fundamentally different from the common law, which bubbles up from everyone who participates in commerce.

In contrast, Michael L. Rustad, in his article "Punitive Damages in Cyberspace: Where in the World is the Consumer?," portrays a bleak fate for consumers who cannot depend on effective consumer protection law in the unregulated, unprotected environment of Internet commerce. In the wild west of cyberspace, consumers face scammers posing as legitimate businesses, "phishing" for credit card numbers and other credit information.⁴ Rustad argues that ordinary damages in tort or contract actions would not provide consumers adequate protection, as the on-line evildoers are too unlikely to be caught. Even when they are caught, rarely can a judgment be collected from "phishers" and Internet scammers.

3. Should Consumer Protection Generally be Enforced by Governmental Agencies, Private Litigation, or Both?

If consumer protection law is to exist, we must still decide whether the dominant means to enforce that law should be governmental regulatory enforcement, either through agency litigation or otherwise, or private litigation. In his article focusing on the firearms industry, "Suing the Firearms Industry: A Case for Federal Reform?," Stephen P. Halbrook argues that

³ Alvin C. Harrell, *Basic Choices in the Law of Auto Finance: Contract Versus Regulation*, 7 CHAP. L. REV. 107, 110-11 (2004).

⁴ Michael L. Rustad, *Punitive Damages in Cyberspace: Where in the World is the Consumer?*, 7 CHAP. L. REV. 39, 40 (2004). "Phishing" is the act of posing as a legitimate business in order to obtain confidential information from another. *Id.* at 40-41.

where legislation has already struck a definite balance and a pervasive set of regulations govern a specific sector of consumer affairs, private litigation that is not authorized by that legislation and regulatory structure is inappropriate, even if it is based on traditional common law causes of action such as public nuisance or other torts.⁵ Greve appears to agree, stating that an obvious means of preventing the underdeterrence of wrongdoing is to “entrust public agencies with the definition and enforcement of prohibitions and injunctions against unfair or fraudulent business practices,” without forcing those agencies to prove the common law elements of any cause of action.⁶ Greve laments that only rarely do federal and state regulations, as enforced by the appropriate agencies, have preclusive effect and preempt private litigation. He says that “[c]ompliance defenses rarely succeed in liability lawsuits over ‘unsafe’ pharmaceutical drugs or automobiles. The risk is not simply confusion or incoherence: it is massive over-deterrence.”⁷

By comparison, and as previously noted, Harrell prefers the individualized decision process of common law trials to the system-wide rulemaking of regulation. Harrell also notes that “public enforcement has exceeded the volume of private litigation” in many areas of federal law.⁸ Moreover, Harrell notes that a significant portion of consumer regulation is federal in nature, and that federal regulation, as opposed to state litigation, benefits large, national enterprises over smaller, local businesses that are less able to bear the burden of complex federal regulation.⁹ Rustad observes that regulatory agencies attempt to track down and punish bad actors in cyberspace, but that these agencies are overwhelmed. “It is as if the FTC is trying to hold back a tidal wave of cyberfraud with a broom.”¹⁰

4. Should Consumer Protection Law Primarily Be Enacted at the State or Federal Level?

A question closely related to the choice between regulatory action and private litigation is whether most consumer protection law should be enacted at the state or federal level. Harrell notes that regulatory action is more often federal, while most private litigation occurs in state courts. He argues this rough division is

⁵ Stephen P. Halbrook, *Suing the Firearms Industry: A Case for Federal Reform?*, 7 CHAP. L. REV. 11, 21-22 (2004).

⁶ Greve, *supra* note 2, at 159-60.

⁷ *Id.* at 171 (internal citation omitted).

⁸ Harrell, *supra* note 3 at, 121.

⁹ *Id.* at 121-22.

¹⁰ Rustad, *supra* note 4, at 80.

caused by the fact that most common law is state law and even statutory contract law is primarily state law, whereas most regulatory law, with significant exceptions, is federal law.¹¹ Harrell asserts that state-based common law is more flexible and better able to nourish the development of new and innovative industries, while broad-based federal regulation leads more often to the dominance of large, stable firms.¹²

In his article "Wrong from the Start? North Carolina's 'Predatory Lending' Law and the Practice v. Product Debate," Donald C. Lampe worries that, rather than nurturing new and innovative financial service companies, the state-based laws attempting to prevent predatory lending have created a "regulatory Tower of Babel for multi-state residential mortgage lenders."¹³ Inconsistent state laws, in Lampe's view, fall too heavily on large, multi-state businesses. Halbrook is also concerned that state regulation will lead to an unreasonable burden on interstate commerce, in this case, the interstate sale of firearms.¹⁴

Playing an important role in deciding whether federal or state law will govern consumer issues is the doctrine of preemption, which allows federal laws and regulations to supercede their state counterparts. However, states have their own arsenal of weapons to combat the wholesale preemption of their systems of consumer protection. Lampe notes that states attempt to subvert, stealthily if need be, federal preemption. For example, North Carolina's predatory lending law focused on consumer protection rather than on interest rate limitations as a way to avoid the preemptive effect of the Alternative Mortgage Transaction Parity Act ("AMTPA"), which frees protected lenders from states' usury ceilings.¹⁵ Lampe argues that, to the extent that state law discourages lenders protected by AMTPA from making high cost home loans, the state law can be seen as a "stealth override" of the federal preemption.¹⁶

By comparison, Harrell celebrates the surprising dominance of private state law litigation in the consumer protection arena and the fact that federal regulation has not occupied the field. This, Harrell states, "is surely a testament to the viability of the common law system and should provide a continuing lesson for

¹¹ Harrell, *supra* note 3, at 121-22.

¹² *Id.* at 122.

¹³ Donald C. Lampe, *Wrong From the Start? North Carolina's "Predatory Lending" Law and the Practice vs. Product Debate*, 7 CHAP. L. REV. 135, 148 (2004).

¹⁴ Halbrook, *supra* note 5, at 32.

¹⁵ Lampe, *supra* note 13, at 142.

¹⁶ *Id.* at 143.

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policy makers and advocates on both sides of the consumer law policy debates.”¹⁷

5. What Areas Of Commerce Involving Consumers Should Receive Their Own Sets of Special Rules?

An issue addressed by two of the symposium authors is whether any areas of commerce should be governed by their own sets of special rules. Halbrook argues that trade in firearms should be exempt from some forms of litigation, such as suits for public nuisance, negligence, “negligent design and marketing . . . , strict liability for defective . . . products, and ultra-hazardous activity.”¹⁸ Halbrook argues that the provisions of the Second Amendment to the U.S. Constitution, as well as similar provisions in various state constitutions, should foreclose such private litigation.

By comparison, Rustad argues that the unique characteristics of Internet commerce require special protections for consumers, since few consumers have the technical sophistication “to determine who is tracking their click-streams, unleashing viruses, or sending fraudulent offers.”¹⁹ Many website providers and other Internet businesses have no assets or physical, as opposed to virtual, presence in the United States.²⁰ Even tortfeasors inside the United States may be difficult to locate, as they can falsify the return addresses on their emails and so post defamatory or deceptive messages anonymously.²¹ Rustad argues that these aspects of Internet commerce render ordinary damages an insufficient deterrent for wrongdoing.²²

6. Does Consumer Protection Necessarily or Unduly Limit Consumers’ Autonomy?

Professor Harrell sees an immutable, inevitable trade-off between the autonomy of consumers and their protection, concluding that the two alternatives are (a) party autonomy protected and achieved by the consumers’ ability to freely to enter into contracts and (b) restricted autonomy, caused by regulations that limit the products or services or the terms of consumer transactions.²³ However, I have argued elsewhere that

¹⁷ Harrell, *supra* note 3, at 122.

¹⁸ Halbrook, *supra* note 5, at 11.

¹⁹ Rustad, *supra* note 4, at 69.

²⁰ *Id.* at 69-70.

²¹ *Id.* at 64.

²² *Id.* at 93.

²³ Harrell, *supra* note 3, at 132.

mere freedom of choice and lack of regulation does not necessarily maximize the autonomy of consumers.²⁴ A consumer unrestricted by consumer protection law may end up with less autonomy if he enters into transactions under the influence of a high-pressure sales agent and without the information or time he needs to decide what he really wants.²⁵ Worse yet, if unprotected by predatory lending regulation, a homeowner who loses her house because of a high cost loan could lose the critical personal autonomy that being a homeowner provides.²⁶ Paradoxically, specific limitations of autonomy, such as absolute freedom to contract, may result in the overall maximization of a consumer's autonomy.²⁷

One specific limitation on consumers' freedom to contract is caused by merchants' use of form contracts of adhesion which consumers have no means of revising or renegotiating. Rustad notes that such contracts dominate Internet commerce, appearing not only as "shrink-wrap" contracts that a buyer purportedly agrees to by opening a product purchased over the Internet, but also as "web-wrap" contracts that spring into effect when one uses a web page.²⁸ Rustad argues that these form agreements force consumers, often unwittingly, not only to waive their rights to punitive damages and other tort remedies, but also to agree to choice of law and choice of forum terms that may severely limit their ability to sue.²⁹

Harrell, on the other hand, asserts that form contracts of adhesion do not significantly limit consumer autonomy. Instead, consumers are not prevented from negotiating the significant terms of their transactions, such as price.³⁰ Furthermore, Harrell argues that at least in consumer credit transactions, consumer form contract terms are mandated by law or by the secondary market, and these standards are designed not only to be consistent but also fair.³¹

7. What Forms of Consumer Protections Should Be Used?

Informational remedies, including the requirement that merchants disclose some information regarding their products, are perhaps the easiest form of consumer protection to defend.

²⁴ Kurt Eggert, *Lashed To The Mast And Crying For Help: How Self-Limitation Of Autonomy Can Protect Elders From Predatory Lending*, 36 LOY. L.A. L. REV. 693 (2002).

²⁵ *Id.* at 732.

²⁶ *Id.*

²⁷ *Id.* at 736.

²⁸ Rustad, *supra* note 4, at 88.

²⁹ *Id.* at 87-90.

³⁰ Harrell, *supra* note 3, at 111.

³¹ *Id.* at 127.

Even Greve, who refers to consumer law “in its modern, disembodied state” as a “bastard regime,”³² agrees that mandatory disclosure requirements can be “efficient in some settings.”³³ Narveson frames the question not so much as whether the merchant should be required to divulge information, but rather how much information is required, how precise that information must be, and how high a level of risk must be before that risk must be disclosed.³⁴ What punishment should the business face if it provides inaccurate information, intentionally or otherwise? The goal, to Narveson, is to ensure that the seller does not significantly increase the amount of risk that a consumer faces involuntarily.³⁵

Restrictions on types or terms of agreements and banning certain abusive practices are less universally popular. Greve argues that merchants, when faced with limitations on some terms—such as the interest rate they can charge—will instead compete “on some other, less transparent margin.”³⁶ Lampe criticizes the effort to restrict particular loan terms and products such as high cost loans, rather than merely attacking abusive sales practices and tightening the requirements to be a mortgage broker.³⁷

Consumer protection can be provided not only by giving consumers causes of action not recognized by the common law, but also by increasing the penalties that consumers can seek, including punitive damages for bad behavior by businesses, or by providing remedies, such as disgorgement of profits in addition to or instead of traditional damages.³⁸ While Greve asserts that corporations universally oppose punitive damages,³⁹ Rustad notes that in Internet litigation, punitive damages are a sword typically wielded by large corporations against individuals, such as cybersquatters, spammers, and critics.⁴⁰ Also, Rustad argues that enhanced remedies such as punitive damages are necessary to encourage individual litigants to act as private attorneys general and so protect other consumers.⁴¹

Greve criticizes other tools of consumer protection, such as class actions and laws lessening the common law’s standing

³² Greve, *supra* note 2, at 178.

³³ *Id.* at 156.

³⁴ Narveson, *supra* note 1, at 194-95.

³⁵ *Id.* at 199.

³⁶ Greve, *supra* note 2, at 161.

³⁷ See generally Lampe, *supra* note 13.

³⁸ Greve, *supra* note 2, at 160.

³⁹ *Id.* at 177.

⁴⁰ Rustad, *supra* note 4, at 57-58.

⁴¹ *Id.* at 100.

requirements. Greve asserts that the procedural protections and due process safeguards of class actions “are deadweight at best and an invitation to opportunism at worst”⁴² and he raises the “specter that corporate defendants will cut themselves cheap, collusive settlements with a plaintiffs’ lawyer of their choice.”⁴³ Unfair competition law that does not involve a certified class suffers, Greve argues, from the lack of preclusive effect, thus leaving defendants who win, lose, or settle still subject to suit on the same or similar claims.⁴⁴

Lampe, by comparison, criticizes consumer protection regulations that remove the intent requirement and impose strict liability, for example on loans that trip certain triggers imposing additional regulation on high cost loans.⁴⁵ Such strict liability is even more dangerous, Lampe asserts, when it is framed in “ambiguous, non-standard definitions” and the lender is given only a limited opportunity to cure any mistakes or missteps.⁴⁶

Both Lampe and Harrell are troubled by laws seeking to protect consumers by forcing third parties, such as the assignees of loans, to be liable for the bad actions of the original seller or lender who dealt with the consumer. Lampe views such laws as a “market disruptive”⁴⁷ approach not to mention “esoteric and legally complicated.”⁴⁸ Harrell is especially wary of class action attorneys seeking assignee liability in order to find a deep pocket or a windfall and warns that the resulting litigation costs as well as liability risks to assignees can harm consumers by driving up the cost of doing business.⁴⁹ I have argued, on the other hand, that assignee liability is a crucial weapon in the battle against predatory lending, as it forces secondary markets to police mortgage brokers.⁵⁰ By protecting borrowers from abusive loan practices, assignee liability should lower, rather than increase, the cost of credit.

Conclusion

Consumer protection law is a complex, vibrant body of doctrine and can be examined from many different viewpoints. Chapman’s symposium shows the importance of the questions

⁴² Greve, *supra* note 2, at 166.

⁴³ *Id.* at 167-68.

⁴⁴ *Id.* at 168.

⁴⁵ Lampe, *supra* note 13, at 143.

⁴⁶ *Id.*

⁴⁷ *Id.* at 149.

⁴⁸ *Id.* at 151.

⁴⁹ Harrell, *supra* note 3, at 130.

⁵⁰ Kurt Eggert, *Held Up in Due Course: Predatory Lending, Securitization, and the Holder in Due Course Doctrine*, 35 CREIGHTON L. REV. 503 (2002).

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that arise from this area of law, as well as how the individual authors have chosen to answer them. From the differing and conflicting views that follow should come a richer understanding of the balance that must be struck between protection and paternalism in the design and implementation of consumer protection laws.