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Rationality's Reach

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Seduction by Contract: Law, Economics, and Psychology in Consumer Markets. By *Oren Bar-Gill*. Oxford: Oxford University Press. 2012. Pp. xvi, 249. Cloth, $39; paper, $25.

Introduction

Economic analysis and the rational actor model have dominated contracts scholarship for at least a generation.[1] In the past fifteen years or so, however, a group of behaviorists has challenged the ability of the rational choice model to account for consumer behavior.[2] These behaviorists are not trying to dismantle the entire enterprise. They generally accept the fundamentals of economic analysis but argue that the rational actor model can be improved by incorporating evidence of decisionmaking flaws that people exhibit.

Oren Bar-Gill[3] has been one of the foremost and influential proponents of a behaviorist take on contracts, and his recent book, *Seduction by Contract: Law, Economics, and Psychology in Consumer Markets*, is the culmination of these efforts. In the book, he portrays consumers as the targets of temptation. The tempters are credit card, subprime mortgage, and cell phone companies that structure contracts in ways that exploit the behavioral weaknesses of some consumers. They seduce by offering upfront lures like frequent-flier miles, interest-only payments, and ostensibly free cell phones. But these contracts also bury deferred penalties such as escalating interest rates and a bevy of fees. The later costs are a source of regret for consumers and, in Bar-Gill's view, may warrant regulation that can limit this undesirable seduction.

Bar-Gill builds his analysis around a framework that emphasizes the problems with contractual complexity and deferred costs. Complexity can

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1. *See* Eric A. Posner, Essay, *Economic Analysis of Contract Law After Three Decades: Success or Failure?*, 112 Yale L.J. 829, 829 (2003) ("Modern economic analysis of contract law began about thirty years ago and, many scholars would agree, has become the dominant academic style of contract theory.").

2. For some early efforts, see Christine Jolls et al., *A Behavioral Approach to Law and Economics*, 50 Stan. L. Rev. 1471, 1505–08 (1998), which conducts a behavioral analysis of mandatory contract terms, and Russell Korobkin, *Bounded Rationality, Standard Form Contracts, and Unconscionability*, 70 U. Chi. L. Rev. 1203 (2003).

3. Evelyn and Harold Meltzer Professor of Law and Economics, New York University School of Law.

obscure the content of contracts, and consumers may be overly optimistic about what they do not know. This effect, Bar-Gill argues, can lead people to make errors when they assess the value of a bargain (p. 10). Deferred costs, meanwhile, exploit the intense preference that some consumers may have for immediate gratification (pp. 21–23). This myopia leads them to underestimate whether and how often they will fall prey to the deferred fees that many consumer contracts impose.

Throughout the book, Bar-Gill recommends the same salve for both ills. Targeted disclosure, he argues, is a minimally intrusive way to improve consumer-purchasing decisions (pp. 32–43). It can correct optimism by alerting people to the cost of terms that may be buried in contracts, and it can minimize myopia by informing people about typical usage patterns.

In this Review, I contrast Bar-Gill's analysis of complexity and deferred costs with an analysis of these problems that uses a pure rational choice model. My goal is to evaluate which of these approaches fares better at explaining the necessarily limited evidence we have about consumer responses to contractual complexity and deferred costs. As will become clear, I think that what we learn from the behavioral take on myopia tells us more than would a behavioral perspective on contractual complexity. When it comes to dense and complex fine print, there are longstanding rational choice models that predict how people might respond to the high cost of learning what is in a contract. These models predict that people will not read consumer agreements and that contract quality will accordingly be low. I suggest that the problem of rational ignorance of contracts may be a more substantial problem than the misperception that Bar-Gill stresses.

As part of this exercise, I explain my skepticism that the improved disclosure Bar-Gill endorses will be the most effective way to regulate the problems he identifies with consumer contracts.[4] With regard to complexity, this skepticism comes from an argument that the rational choice model may best explain how consumers evaluate form contracts. These models of complexity predict that the failure of consumers to read contracts will substantially degrade the overall quality of contracts. If these models are correct, disclosing that low quality will not do much good.[5] The real culprit here is

4. I am not alone in questioning how effective disclosure will be at improving consumer outcomes. Bar-Gill's occasional coauthor, Omri Ben-Shahar, has written a series of articles and a book with Carl Schneider on the pathologies of disclosure. While Bar-Gill cites this work in passing (p. 33), his case for disclosure would be improved by engaging the Ben-Shahar and Schneider critique in a more substantial way. *See* Omri Ben-Shahar & Carl E. Schneider, More Than You Wanted to Know: The Failure of Mandated Disclosure (forthcoming 2014); Omri Ben-Shahar & Carl E. Schneider, *The Failure of Mandated Disclosure*, 159 U. Pa. L. Rev. 647, 665 (2011) [hereinafter Ben-Shahar & Schneider, *Failure of Mandated Disclosure*] (arguing that mandatory disclosure does not achieve its purported end goal of improving the decisions of consumers); *see also* Daniel E. Ho, *Fudging the Nudge: Information Disclosure and Restaurant Grading*, 122 Yale L.J. 574 (2012) (showing that even simple disclosures like restaurant grades can be inaccurate and subject to manipulation).

5. This argument depends on whether consumers make rational assumptions when they do not know the content of contracts. If they are optimistic or they misperceive the terms of an agreement, as Bar-Gill argues, and disclosure effectively corrects these beliefs, disclosure

the high cost of learning contract terms. After a review of some proposals that follow from the rational choice model,[6] I include my own counterintuitive suggestion that making default rules more seller friendly may be a desirable way to improve outcomes.

When it comes to deferred costs and myopia, Bar-Gill has me convinced that these mistakes occur and that they may have a deleterious effect on welfare. I am not sure, however, how effective disclosure will be as a remedy. This problem is ultimately one of weakness of the will. Consumers know the high costs of making late payments or exceeding their allotted cell phone minutes, but they incorrectly believe that they will be able to exercise enough discipline to avoid these penalties. Given that consumers are able to deceive themselves into thinking that they will behave, I am not necessarily persuaded that telling them that they are likely to misbehave will have much of an effect. Stronger medicine may be necessary to change outcomes.

Before explaining my critiques in more detail, I should emphasize that my goal here is to bring some measured skepticism to parts of the book rather than to refute it in a fundamental way. Bar-Gill stands as one of the handful of distinguished scholars who has forced practitioners of law and economics to take behavioral concerns seriously. The methodical and thorough approach in this book shows why this is the case. Bar-Gill's analysis explores the predictions of the rational actor model and explains how they may fail to account for observed behavior in the consumer markets that he studies. He then assesses whether market-oriented solutions will likely be able to solve the problem, and, where he concludes that they will not, he advocates targeted interventions that may correct for the potential problems that behavioral biases pose. These are hard questions about issues that lack good data. While I disagree with Bar-Gill on some points, his book is likely to remain an important resource for those who want general insight into the application of behavioral concerns to contracts and for those who want a deep understanding of the credit card, mortgage, and cell phone markets that the book covers.

The remainder of this Review explores contractual complexity and deferred costs in separate Parts. In each, I briefly review Bar-Gill's arguments and evidence. I then evaluate those arguments against what a straightforward rational choice model would predict. I end each Part with thoughts about what sorts of remedies may be more effective than disclosure.

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may be able to change contract markets in a way that improves their terms. Pp. 2–5. As one example, if mortgage contracts can succinctly disclose the complex and long-term costs associated with the agreement, the incentive to impose complex and long-term fees may dissipate. P. 176.

6. *See, e.g.*, Avery Katz, *The Strategic Structure of Offer and Acceptance: Game Theory and the Law of Contract Formation*, 89 Mich. L. Rev. 215 (1990); Abraham L. Wickelgren, *Standardization as a Solution to the Reading Costs of Form Contracts*, 167 J. Institutional & Theoretical Econ. 30 (2011).

I. Contractual Complexity

Bar-Gill begins *Seduction by Contract* with a chapter that introduces the methodological tools and assumptions that he will apply throughout his analysis. In his framework, there is a difference between the actual terms of a contract and the perceived terms of a contract (p. 9). The salience of contract terms, he argues, drives the difference between actual terms and perceived terms. If the terms of the contract are salient—that is, they stand out to consumers who properly understand and value those terms—the difference between the actual and perceived terms will be minimal (p. 18). But if the terms are not salient—meaning that they are not prominent and may be difficult to value—the difference between the actual value of the contract terms and the perceived value of the contract terms will be large (p. 25).

A core argument for Bar-Gill is that firms have an incentive to design contracts in a way that increases the wedge between the actual value and the perceived value of the contracts' terms.[7] He argues that firms can draft complex contractual language to make it difficult for consumers to perceive the value of those terms. A rational consumer will infer that the clauses that firms have packed into fine print are likely to favor the seller. Bar-Gill, however, argues that some consumers are irrational. As he puts it, "[I]mperfectly rational consumers will completely ignore the unread or forgotten terms or naively assume that they are favorable" (p. 21).

If consumers miscalculate the value of these terms, it can lead to overconsumption. Bar-Gill cites the complex rules that credit card companies sometimes use as an example.[8] He also marshals some evidence that consumers have difficulty understanding these terms and that this misunderstanding may lead them to price these terms incorrectly.[9] As a consequence, consumers may take on more credit than they should. The behavioral flaw is, in essence, that of consumers being irrationally optimistic about what they do not know.[10] As his technical appendix to the first chapter helpfully shows, those who are optimistic about the terms of contracts will enter into more contracts than is optimal.[11] This effect creates a welfare loss.[12]

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7. *E.g.*, pp. 10, 19, 21. Critics of behavioral law and economics commonly complain that competition should be able to minimize the fallout from biased decisionmaking. At the very least, they assert, competitive markets should fare better than regulated ones. *See, e.g.*, Joshua D. Wright & Douglas H. Ginsburg, *Behavioral Law and Economics: Its Origins, Fatal Flaws, and Implications for Liberty*, 106 Nw. U. L. Rev. 1033 (2012) (arguing that behavioral economics is "libertarian paternalism" that poses a threat to both welfare and liberty).

8. Pp. 66–68 (explaining double-cycle billing and the practice of allocating payments to low-interest balances first).

9. Pp. 79–81 (reviewing studies that show that consumers may not understand the fine print in credit card agreements).

10. Bar-Gill says consumers may ignore the unread terms, p. 21, but I am unsure what this means. To make a purchase decision, a consumer *must* have some belief about the value of unknown terms in the contract.

11. *See* pp. 44–50.

12. *See* pp. 23–26.

Bar-Gill contrasts these behavioral costs with a rational choice account of complex contract terms. But I am not sure that he chooses the right target here. Rather than compare the welfare losses associated with rational choice models of unknown contract terms, he asks a different set of questions. He analyzes whether there could be any welfare-enhancing explanation for the terms that firms bury in the fine print. Unsurprisingly, he finds that double-cycle billing by credit card companies, balloon payments in mortgages, and cell phone penalties are unlikely to add value to contracts.[13]

This comparison asks what a fully informed consumer would think of terms that firms put in complex contracts. The problems created by complexity, however, derive from how consumers will respond to misperceiving or not knowing the terms of contracts. It is this difficulty that creates the welfare loss. The equivalent question under a rational choice framework would ask not how a fully informed consumer would price terms but how an incompletely informed consumer would ascertain the value of a contract and how firms would likely respond to that understanding.[14]

Contrasting the behavioral costs of complexity with a rational choice account of how consumers understand and value contracts poses a harder set of questions. These models predict significant welfare losses, and I suspect that these losses may be more substantial than those created by optimism about complexity. To see why, it is helpful to begin by explaining the reading-cost analysis developed by Avery Katz. This is a pure rational choice model that expects contracts between firms and consumers to be suboptimal.[15] This model has been highly influential, and contract theorists continue to debate and refine the questions the model poses.[16]

13. Pp. 75–78 (credit card fees); pp. 146–56 (mortgage fees); pp. 227–29 (cell phone contract complexity).

14. One might argue that there is a difference between disclosed contractual complexity and fine print. For example, disclosed complexity could refer to information that consumers attempt to understand but misperceive, while fine print could refer to the terms that consumers ignore. Bar-Gill's book draws this distinction, p. 1, and argues that his disclosure regime can minimize the harm from misperception. But one could also frame the issues as similar because both misunderstood and unknown terms affect how consumers place a value on the terms of a contract that they do not know with precision. Whether these two approaches could be united is beyond the scope of this Review, but in the analysis that follows, I examine whether the misperception problem is likely to be larger or smaller than the rational-ignorance problem when it comes to how consumers value contracts.

15. *See* Katz, *supra* note 6, at 294–95 (arguing that, under a strict duty to read, an offeree will not have sufficient incentive to read a form contract and that legal rules could increase bargaining efficiency by limiting the drafting party's freedom to vary the terms of form contracts); Avery Katz, *Your Terms or Mine? The Duty to Read the Fine Print in Contracts*, 21 RAND J. Econ. 518, 518 (1990) [hereinafter Katz, *Your Terms or Mine?*] (arguing that the traditional rule, binding one who accepts a form contract to unread fine print, is "inferior to a rule providing presumptive warranties when negotiation is costly").

16. *See, e.g.*, Wickelgren, *supra* note 6, at 31–32, 36, 41–42 (citing Katz, *Your Terms or Mine?*, *supra* note 15). Bar-Gill does not incorporate the rational choice models of reading costs into his analysis. But, to be fair, he does recognize that one can rationally ignore fine print. *See* pp. 20–21 (noting that rational consumers may not read contracts and will "recognize that unread provisions will generally be pro-seller").

The Katz model asks how firms are likely to structure form contracts if they know that consumers face positive reading costs and that the prevailing rule requires that consumers assume the risk of not reading.[17] The answer to this question is quite elegant, if a bit dispiriting. If consumers read contracts, firms would draft terms that would make a consumer nearly indifferent to the choice between entering into a contract and not entering into it.[18] But consumers will not read contracts because they know that they will have to sink the cost of reading them in return for contracts that do not make them better off.[19] When firms deduce that consumers will not read contracts at all, they will provide even worse contracts than the ones that would make consumers who read indifferent. In this situation, firms know that they compete only on price, and they obtain the lowest prices by dropping quality of terms as much as possible. In equilibrium, no consumers read contracts, and the contracts contain the lowest-quality terms that the law allows.[20]

The welfare losses from these dynamics of the Katz model are potentially very large. In an ideal world of no reading costs, consumers would be perfectly informed. But as a consequence of the structure of form contracts and the reading costs they impose, consumers do not know the content of contracts. Firms respond by decreasing the quality of those terms to minimal levels.[21] This means that there are likely to be higher-quality contract terms that consumers would be willing to pay for, but reading costs stand in the way of parties striking these bargains.

A. *Comparing the Rational and Behavioral Models of Complexity*

To know whether we should prioritize the rational or the behavioral model of fine print, we need to know the magnitude of the welfare losses associated with each approach. This Section analyzes what the theory and evidence associated with each model say about the likely welfare effects.

Before proceeding, however, it is important to be clear about the different nature of the welfare losses under the behavioral and rational models.

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17. Katz analyzes outcomes under one rule that places a duty to read on consumers and under another rule that places a duty to speak on firms. Given a sufficiently high cost of speaking, he finds that both rules will produce an equilibrium where firms offer contracts with minimal quality.

18. Katz, *supra* note 6, at 288–89.

19. *Id.* at 289.

20. There have been several recent refinements to the Katz model. Albert Choi and Yeon-Koo Che evaluate the effect on form contracts when some consumers have low reading costs and some have high reading costs. In this model, some firms will offer high-quality contracts. Yeon-Koo Che & Albert H. Choi, *Shrink Wraps: Who Should Bear the Cost of Communicating Mass-Market Contract Terms?* 13–14 (Univ. of Va. Sch. of Law, John M. Olin Law & Econ. Research Paper Series No. 2009-15, 2009), *available at* http://ssrn.com/abstract=1384682. Wickelgren argues that, as long as firms have the power to increase the length of contracts, and thus increase readings costs, the equilibrium of the Katz model will remain the result. *See* Wickelgren, *supra* note 6.

21. *See* Katz, *supra* note 6, at 288 ("[P]roviding any quality above the minimum possible level is not a rational strategy for sellers . . . .").

Bar-Gill asserts that both the difficulty of evaluating multiple price dimensions and optimism about unknown terms lead to overconsumption by irrational consumers (p. 164). These people pay more than they would if they were correctly informed. The losses anticipated by the rational choice model come from the inability to communicate (pp. 13–14). There is no overconsumption in this case because consumers understand that contracts contain the low-quality terms. The welfare loss comes instead from the inability of firms to provide higher-quality contracts that would make both firms and consumers better off.[22] These losses are not incompatible; there can simultaneously be overconsumption from optimism and forgone contracts due to reading costs. But both problems stem from how much consumers are willing to pay for unknown or costly-to-understand terms. A comparison of these models helps one understand where regulatory priorities should lie.

At a theoretical level, there is a strong reason to believe that the Katz model suggests larger problems than a behavioral approach. The scale of the rational choice analysis encompasses all consumers and all firms. Consumers and firms' collective inability to communicate means that they lose the chance to reach agreement on welfare-enhancing terms. The behavioral model, however, identifies a problem that only applies to a subset of consumers—those who overestimate how favorable some contracts' terms may be (p. 12).

This difference in the affected populations does not necessarily mean that the magnitude of the problem that reading costs cause is larger than that created by incorrect optimism. It could be that reading costs result in relatively few missed bargains: perhaps the average customer would not be willing to pay for more favorable dispute resolution clauses or for enhanced warranties. Alternatively, the degree of optimism that some consumers exhibit may be so large that they enter into contracts that make them far worse off. Nevertheless, the bare fact that the rational choice model creates across-the-board losses suggests that reading costs might be a more effective target of regulation than optimism.

It would be ideal, of course, if it were possible to estimate welfare losses associated with consumer optimism and reading costs.[23] But gauging these costs empirically would likely pose daunting challenges. Take optimism costs. Knowing whether some of the consumers who have entered into a class of contracts are actually optimistic is a methodologically thorny task. Consumers can be optimistic, they can be correct, or they can be pessimistic. And to make things more complicated, a single consumer can be optimistic

22. *See id.* at 291–92 (suggesting that efficiency might be improved by providing implied warranties and refusing to enforce some of the low-quality terms that stem from the cost of communication).

23. Bar-Gill presents some evidence that attempts to ascertain the cost of consumer mistakes. His review of studies on subprime mortgages is, perhaps, the most thorough. *See* pp. 160–64 (reviewing studies that document that cognitive deficiencies may lead consumers to make costly mistakes). But these studies do not tie the problem directly to optimism about the content of complex contracts.

about some terms, correct about others, and pessimistic about yet more terms, all within the same contract.

Imagine a contract between a firm and a consumer that contains the following dispute resolution terms: (1) all disputes will be subject to mandatory arbitration; (2) each side will pay its own costs; and (3) the arbitration will take place in the city where the firm has its headquarters. Consumers who do not take the time to read the contract would have to infer the dispute resolution terms in the agreement. Suppose that a consumer believes that the contract contains a mandatory arbitration clause, that it requires the consumer to pay the firm's costs, and that the arbitration will take place in the city where the consumer lives. In that case, the consumer is correct about arbitration, pessimistic about costs, and optimistic about venue.

What will a consumer with this set of beliefs do? We still do not know because, to make a prediction, one needs to know the relative importance that the consumer attaches to each of these provisions.[24] If the consumer places a significant value on the cost provision and not on the venue provision, the consumer will underestimate the value of the dispute resolution provision. Alternatively, if the consumer places substantial weight on the venue provision and not on the cost provision, the consumer will overestimate the value of the dispute resolution features of the contract. Finally, the consumer could care roughly equally about the cost and venue provisions, which would allow pessimism and optimism to more or less cancel each other out.

This exercise suggests that the empirical challenges here are significant. Some researchers have attempted to determine whether consumers are aware of the content of agreements, although such researchers do not account for the importance that consumers place on each contractual term.[25] Their research shows, perhaps unsurprisingly, that consumers are correct about some terms, optimistic about others, and pessimistic about the remainder.[26]

24. For a recent theoretical investigation of optimism and pessimism that includes some preliminary data, see Ian Ayres & Alan Schwartz, *Remedies for the No Read Problem in Consumer Contracting*, 66 Stan. L. Rev. (forthcoming 2013), *available at* http://www.law.uchicago.edu/files/files/Ayres%20paper.pdf. Ayres and Schwartz note that the presence of optimists creates two inefficiencies: (1) these optimists overpay for their contracts, and (2) the presence of optimists leads sellers to lower the quality of contracts, which in turn creates a negative externality by forcing those with correct and pessimistic beliefs out of the market. *Id.* (manuscript at 24).

25. *See supra* note 23 (discussing Bar-Gill's review of these studies).

26. All-Indus. Research Advisory Council, Public Attitude Monitor 1989: A Survey of Public Attitudes on Auto Insurance Rates, Seat Belts, Attorney Advertising, Homeowner's Insurance, and Insurance Claim Fraud 13–15 (1989) (showing that a majority of homeowners correctly believed that their insurance policies covered theft and vandalism but incorrectly assumed that their policies did not cover riots and did cover flood damage).

To be sure, estimating the welfare losses associated with reading costs is also a difficult task.[27] Doing so would require knowing how much consumers value contract terms of different quality and ascertaining how much it would cost firms to supply those different terms. Estimating supply and demand curves is a difficult and data-intensive task.[28] The task of doing this for the class of transactions covered by form contracts would be daunting.

There is, however, some empirical evidence that supports the inference that the reading-cost model is accurate. The Katz model predicts an equilibrium in which consumers will not read contracts and contracts will contain terms that are adverse to consumers. The evidence developed by Florencia Marotta-Wurgler and her coauthors suggests that reality is relatively close to this equilibrium. In a study that uses click-stream data to ascertain whether consumers who buy software online read the contracts that govern the sale, the authors find that only "one or two out of every thousand" access the contract and that consumers spend an average of less than a minute reading the agreement.[29] This finding is consistent with the Katz model's prediction that consumers will not read contracts.[30]

The work of Marotta-Wurgler also suggests that form agreements often contain terms that are relatively low in quality.[31] She samples software license agreements and assesses how their terms compare to seventeen of the Article 2 Uniform Commercial Code ("UCC") default rules. She finds that the average agreement has about five terms that are worse than the default rules.[32] Of course, there is no way to know whether this is what the rational

27. It is also important to assess the accuracy of the assumptions in the Katz model. For form contracts that are subject to significant publicity—such as the terms of service for Facebook—there may be a sufficiently large number of people who read the contracts that they can police their content. *See generally* Alan Schwartz & Louis L. Wilde, *Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis*, 127 U. Pa. L. Rev. 630 (1979) (arguing that an informed minority of readers can police the content of agreements). This effect can cause the Katz model to unravel. Similarly, class actions may police the content of fine print in a way that diminishes the welfare loss associated with form contracts. *See, e.g.*, Kinkel v. Cingular Wireless LLC, 857 N.E.2d 250, 263–75 (Ill. 2006) (holding that a class action waiver in a cell phone contract's arbitration clause was substantively unconscionable and unenforceable).

28. *E.g.*, C.-Y. Cynthia Lin, *Estimating Supply and Demand in the World Oil Market*, 34 J. Energy & Dev. 1, 2 (2011) (describing the difficulties in producing satisfactory supply and demand curves for the global oil market).

29. Yannis Bakos, Florencia Marotta-Wurgler & David R. Trossen, *Does Anyone Read the Fine Print? Testing a Law and Economics Approach to Standard Form Contracts* 1 (NYU Ctr. for Law, Econ. & Org., Law & Econ. Research Paper Series Working Paper No. 09-40, 2009), *available at* http://ssrn.com/abstract=1443256.

30. *See* Katz, *supra* note 6, at 289.

31. *E.g.*, Florencia Marotta-Wurgler, *Are "Pay Now, Terms Later" Contracts Worse for Buyers? Evidence from Software License Agreements*, 38 J. Legal Stud. 309 (2009); Florencia Marotta-Wurgler, *What's in a Standard Form Contract? An Empirical Analysis of Software License Agreements*, 4 J. Empirical Legal Stud. 677 (2007) [hereinafter Marotta-Wurgler, *Empirical Analysis*].

32. Marotta-Wurgler, *Empirical Analysis*, *supra* note 31, at 703.

choice approach would predict. The Katz model suggests that firms will supply the lowest-quality terms that are legally permissible when consumers have positive reading costs.[33] It is hard to know what this means in many cases because the contours of the doctrines that provide a floor for contract terms, such as unconscionability[34] and contracts against public policy,[35] are uncertain. Nevertheless, the finding that terms are worse than the defaults provides evidence that is broadly consistent with the Katz model.

To be fair, however, the evidence that reading costs create larger problems than misperception does is not unequivocal. Bar-Gill's book presents a theoretical basis for believing that firms make more money by tailoring their contracts to those who are optimistic or irrational about contract terms. Moreover, there is good reason to believe that optimists will be the ones who actually enter into contracts. Those who are, on balance, pessimistic about terms will place a lower value on contracts. Consequently, they will not be willing to pay much and, all else equal, will be less likely to enter into contracts.[36] It is quite possible that this dynamic occurs and that it accounts for the losses that Bar-Gill attributes to it. But the empirical evidence on this point amounts to surveys that can only show so much. The data showing that people generally do not read contracts and that contract terms are of low quality, in my view, makes a stronger case that reading costs should be a priority. The book would have been strengthened had it engaged that claim in a more direct way.

B. *Regulating Complexity*

Given my concern about reading costs, I have some skepticism that Bar-Gill's proposals for correcting optimism should be a regulatory priority. He advocates thoughtful disclosure to mitigate the effects of consumer optimism (p. 34). What he has in mind are well-designed summaries that can provide an easy-to-understand measure of the salient and nonsalient benefits and costs associated with the purchase of a consumer product (pp. 37–40). As an example, he points to total-benefit-of-ownership ("TBO") and total-cost-of-ownership ("TCO") measures that companies could disclose to consumers before they purchase an agreement (p. 38).

An example that Bar-Gill identifies is the annual percentage rate ("APR") that the Truth in Lending Act requires companies to disclose to consumers who enter into credit agreements such as mortgages and car

33. *See* Katz, *supra* note 6, at 288–89.

34. U.C.C. § 2-302 (2012); Restatement (Second) of Contracts § 208 (1979); Oren Bar-Gill & Elizabeth Warren, *Making Credit Safer*, 157 U. Pa. L. Rev. 1, 71 (2008) ("[The unconscionability] doctrine gives courts broad power to strike down contract terms and entire contracts that shock the conscience and are the product of a flawed bargaining procedure.").

35. *Cf.* Adam B. Badawi, *Harm, Ambiguity, and the Regulation of Illegal Contracts*, 17 Geo. Mason L. Rev. 483 (2010) (describing how the remedies for illegal contracts might take into account the uncertain boundaries of contracts that are against public policy).

36. *See* Ayres & Schwartz, *supra* note 24 (discussing the welfare problems associated with optimistic consumers).

loans (pp. 38–39). The APR purports to condense the various fees and charges associated with consumer credit into a single, easy-to-understand rate (p. 38). But as Bar-Gill recognizes, there "is broad consensus that the APR has not lived up to its great potential" (p. 177). Among the failures of the APR are its late disclosure, its imperfect enforcement, and especially its underinclusiveness with respect to the fees and charges that lenders can impose (pp. 177–78). Consequently, Bar-Gill recommends improving these condensed disclosures by having them incorporate all the various fees that consumers may be charged (pp. 37–40).

A potential problem with these types of disclosures is that they leave contractual complexity in the hands of the firms that supply the form contracts. This structure requires regulators to play an ongoing game of disclosure Whac-A-Mole. Once regulators have issued rules that purport to cover the TBO or TCO for a given contract, firms can try to write their way around these disclosures by devising new fees and charges that are outside the coverage of the rules. Regulators can respond, but unless they are especially nimble and prescient, the control that firms have over the complexity of their contracts may allow them to write around new rules.[37]

But even if regulators are able to keep up with firms' attempts to evade them, what matters most about disclosures is what consumers believe about them. Imagine a consumer confronted with a long, fine-print contract that is accompanied by a simple and brief disclosure that purports to summarize the costs and benefits associated with the agreement. If the consumer believes that the disclosure completely summarizes the costs and benefits associated with the agreement, this type of disclosure may be effective at neutralizing both the problems with overoptimism that concern Bar-Gill and the problems with reading costs that I find more troubling.

If, however, the consumer remains suspicious about what the fine print contains, the welfare losses associated with reading costs reappear. It is quite possible that consumers will assume that, to understand all the costs and benefits associated with the agreement, they need to read the agreement. The need to sink the reading costs before learning the terms starts the cycle anew. Firms may be able to offer the minimally acceptable contract, which means that the consumer will not read the contract, and that will lead to an inference that the terms are low quality. If regulation is to occur, it must, in my view, target the reading costs that are the likely source of the largest welfare losses.

What would a regulatory regime that targets reading costs look like? It is important to recall that reading costs create an effect that is unfortunate

37. One alternative that may mitigate this concern—suggested by Bar-Gill in correspondence—would be to implement a standard that regulators could enforce against firms. The book does not detail what these standards would look like or how enforcement would proceed. Nevertheless, this approach may counter the ability of firms to use fine print to evade the aims of disclosure to a greater degree than the proposals in the book. At the same time, standards are generally more expensive to enforce than the rule-like regulations that Bar-Gill endorses, and it is difficult to know whether the improved accuracy provided by standards would warrant this expense.

from the standpoint of both consumers and firms. Even though there may be high-quality terms that consumers would be willing to pay for and that would still be profitable for firms, contracts do not contain them due to the structural problems posed in the communication of those terms. It is possible that firms might be willing to bear the costs of communicating more consumer-friendly terms. Indeed, one occasionally sees firms do this sort of thing: Discover is currently promoting a credit agreement that forgives a late payment by consumers, and Visa is publicizing a United-branded credit card, offered through Chase, that eliminates the 3 percent surcharge on foreign transactions.[38]

But the practice of firms shouldering some of the costs of communication has its own problems. One difficulty is that it can be expensive to engage in this type of communication. Discover has developed a national television advertising campaign to tout its late-payment forgiveness program. It may be that the costs exceed the gains of this sort of marketing,[39] but a more pressing concern is the lingering presence of fine print. That a contract contains one favorable term does not tell a consumer much about what the rest of the contract says. Barring any compelling evidence to the contrary, it makes sense for consumers to follow the logic that comes with unknown terms that are costly to learn: consumers will assume that they are unlikely to be of high quality.

Given these deep problems with reading costs, it is unsurprising that scholars who have focused on reading costs have recommended stronger medicine than disclosure. Katz, for example, suggests that the way to remedy the situation is to impose standard terms that apply in the absence of express negotiation.[40] But, like many problems of contractual regulation, setting the appropriate level of these terms poses empirical challenges. Because many form contracts are likely to be governed by these terms, there is a particular danger that setting the level too high will put firms in the position of either ensuring that communication takes place or refusing to sell because the terms are not profitable.

Of course, many proposals to regulate contracts go further than those of Bar-Gill and Katz by recommending mandatory contract terms.[41] These approaches are subject to a well-rehearsed set of critiques.[42] Many of these

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38. *Credit Cards & Credit Card Applications*, Discover, https://www.discover.com/credit-cards/index.html?ICMPGN=STL_CC_IT (last visited Nov. 7, 2013) ("No late fee on your first late payment"); *Chase United MileagePlus: Explorer Card*, United, https://www.theexplorercard.com/MPYoureIn30kAFW.aspx (last visited Nov. 7, 2013) ("No foreign transaction fees").

39. To be sure, Discover may have other aims, such as trying to create goodwill with consumers with regard to its general practices.

40. Katz, *supra* note 6, at 276, 291.

41. Margaret Radin's recent book, *Boilerplate: The Fine Print, Vanishing Rights, and the Rule of Law*, advocates mandatory prohibitions on arbitration and argues that similar prohibitions should be considered for the collection of personal information and for the use of intellectual property rights. *See* Margaret Jane Radin, Boilerplate 172, 176, 183 (2013).

42. *See* Ian Ayres, *Regulating Opt-Out: An Economic Theory of Altering Rules*, 121 Yale L.J. 2032, 2084–86 (2012) (advocating for alternatives to mandatory terms); Alan Schwartz &

criticisms hinge on the impediment that mandatory terms pose to the freedom of contract and the private ordering that this freedom permits. Nevertheless, the UCC does contain some mandatory terms, and some of them—such as those that regulate warranties and those that prohibit the waiver of product liability[43]—are not all that controversial. This may be a concession to the reading-cost argument. Given the strong arguments in favor of placing basic product liability on the heads of producers, it must be a symptom of a failure in the contracting process if those provisions do not appear in consumer agreements. The reading-cost argument provides an account of how this failure might occur.

Regulations that target reading costs do not, however, have to use mandatory or implied terms. For example, Abraham Wickelgren proposes that firms have the option to offer standardized form contracts, each of which has a name.[44] The names of these contracts need not be descriptive; Wickelgren uses the example of contracts named after something as arbitrary as colors. A key to this approach is that firms may not deviate from the terms of the designated contracts. Doing so would allow consumers to tell whether firms are offering different types of contracts without having to read them. As he points out, if there are two firms and they both offer the blue contract, consumers can make their purchase decision on the basis of price because they know that the contracts are the same; but if consumers see a blue and an orange contract, they know that firms are offering different contracts.[45] Wickelgren shows that if reading costs are sufficiently low,[46] firms may be able to credibly commit to offering high-quality contracts to those who desire them even though consumers do not actually end up reading the contracts.

Wickelgren's solution is both clever and elegant. As he notes, however, this equilibrium is not unique. Or to put it another way, there is no guarantee that the desirable equilibrium of firms offering high-quality contracts to those who want them will actually occur because the equilibrium requires that the necessary thresholds for reading costs and available contracts be

Robert E. Scott, Review, *Contract Interpretation Redux*, 119 Yale L.J. 926, 930–31 (2010) (noting that mandatory terms undermine private ordering). Omri Ben-Shahar develops a new critique of mandatory terms in his Review of Margaret Radin's book. *See* Omri Ben-Shahar, *Regulation Through Boilerplate: An Apologia*, 112 Mich. L. Rev. 883 (2014) (reviewing Radin, *supra* note 41). He contends that mandatory terms prohibiting arbitration and cost shifting may reflect the preferences of elites who are willing to pay higher prices for their favored dispute resolution terms. This approach may work a regressive cross-subsidy in which the less well-off consumers who are willing to live with these terms for lower prices must pay more to indulge elite preferences. *Id.* at 900–01.

43. *E.g.*, U.C.C. § 2-314 (2012) (implied warranty of merchantability); *id.* § 2-715(2)(b) (consequential damages include injury to person or property stemming from the seller's breach of warranty).

44. Wickelgren, *supra* note 6, at 32–33.

45. *Id.*

46. Wickelgren demonstrates that the threshold for reading costs that will induce some consumers to read depends, among other things, on the quality of the best contract for those consumers who desire high-quality terms. *Id.* at 37–41.

met.[47] As he also points out, it may not be straightforward to develop a regime that punishes firms for labeling a contract as blue when it is not in fact blue, and it is an open question as to who, exactly, would determine the content of the labeled contracts.[48]

I would like to sketch out a counterintuitive approach that goes beyond disclosure but that directly targets reading costs by making default rules more attractive to sellers. Reading costs are a consequence of fine print, and the need to write fine print is often due to the desire of the contract drafter to deviate from the default rules provided by statute. With the UCC, the default rules are quite consumer friendly, and, in some cases, it is difficult to imagine why any firm would not deviate from what the UCC specifies. Examples here include the rules that provide consequential damages as a default and those that stipulate stronger warranties than many firms wish to offer.[49] These rules virtually guarantee the production of fine print and the problems it entails.

If the default rules were more seller friendly, firms might be less eager to contract around them. In a world where the default rules applied more often, consumers might be more familiar with those rules. This situation would allow consumers to know the content of a contract with minimal, or perhaps zero, fine print.[50] Consumers would just need to know the amount of fine print an agreement contained, which they should be able to determine at very low cost.[51] If there were no or very little fine print, consumers could infer that the default rules applied. And if there were fine print, consumers could assume that it contained the bottom-of-the-barrel terms that the Katz model predicts. As long as these seller-friendly terms are better than the bottom of the barrel, consumers might be willing to pay higher prices to the firms that offer them. If some contracts end up being fine-print free, welfare would increase. This improvement would occur because consumers would get some higher-quality contracts and firms would receive higher prices for them. But even if no firms were willing to abandon the contractual flexibility that comes with fine print, the proposal would leave us where

47. *Id.*

48. *Id.* at 42–43.

49. *E.g.*, U.C.C. §§ 2-314, 2-715(2) (2012).

50. The assumption that consumers will be aware of default rules may not be correct. While it is difficult to know the degree of consumer knowledge, there is, however, some evidence that consumers are aware of the default content of important rules, such as warranties. *See* Yair Listokin, *The Meaning of Contractual Silence: A Field Experiment*, 2 J. Legal Analysis 397, 399 (2010) (providing "suggestive" evidence that consumers value silent warranties at about the same level as warranties that state the default UCC warranty).

51. Note that a very important caveat to this analysis is that the consumer must be aware whether or not fine print accompanies the contract. The analysis in *ProCD, Inc. v. Zeidenberg*, which held that a software license agreement located inside the product's box was binding as long as the consumer could read the terms and return the product, would be problematic. 86 F.3d 1447 (7th Cir. 1996). At a minimum, for this approach to work, a consumer would need to know whether or not fine print was present at the time of purchase.

we are now. Or put another way, the downside would be no worse than the status quo.

This approach would probably entail a substantial expansion of the content of the default rules. Common law contract doctrines and UCC rules are so general that any firms that want coverage of concerns that are specific to the goods or services they provide will need to use fine print.[52] For this proposal to be feasible, it would probably require default rules that are specific to certain goods and services. Examples might include a default cell phone contract and a default rental car agreement. The expansion of the number of default contracts naturally puts pressure on the assumption that consumers will know the contracts' terms. But if consumers can safely assume that fine-print-free contracts offer them better-than-the-bottom terms, they might not need to know their precise content to be willing to pay a little more. Moreover, certain terms, such as those involving dispute resolution, could be standardized across a large number of products.

Given this setup, the difficult question is how much more seller friendly the default rules would have to be in order to make the proposal palatable to both consumers and firms. As an initial matter, no one knows much about consumer preferences for higher-quality contract terms. If the default dispute resolution clause provided for arbitration in a neutral forum with both sides bearing their own costs, would consumers be willing to pay more for that than for a strongly seller-biased arbitration clause? It is also hard to know how firms might respond. Would some allow for a choice of contracts with and without fine print? Or would most refuse to give up the control and tailoring that comes with boilerplate? It would be an empirical challenge to figure out these matters, but there is at least the prospect of improvement over a world choked with low-quality boilerplate.

Considering default rules that are more seller friendly suggests a few larger points. First, the traditional account of default rules has emphasized the desirability of choosing rules favored by the majority of parties. In doing so, policymakers can minimize the costs of contracting around them.[53] But the costs of poorly chosen default rules can go beyond contracting costs. These rules generate fine print, which in turn increases reading costs. As reading costs increase, the downward spiral that is possible in both the Katz

52. *See* Richard E. Speidel, *Revising UCC Article 2: A View from the Trenches*, 52 Hastings L.J. 607, 614 (2000) ("Article 2 drapes its framework of standards and rules over all contexts where goods are sold. The starting point is the same whether the contract involves natural gas, new cars, or factory equipment.").

53. Robert Cooter & Thomas Ulen, Law & Economics (6th ed. 2011); Eric Maskin, *On the Rationale for Penalty Default Rules*, 33 Fla. St. U. L. Rev. 557 (2006) (arguing that default rules should be based on cost efficiency). *But see* Ian Ayres, *Ya-Huh: There Are and Should Be Penalty Defaults*, 33 Fla. St. U. L. Rev. 589, 589 (2006); Omri Ben-Shahar & John A.E. Pottow, *On the Stickiness of Default Rules*, 33 Fla. St. U. L. Rev. 651 (2006); Neil M. Richards, *The Perils of Social Reading*, 101 Geo. L.J. 689 (2013) (arguing that when default rules implicate intellectual privacy concerns, the choice to share should be a conscious and knowing one).

and Wickelgren models becomes more likely. Consumers will not read contracts, and firms will respond with minimally tolerable provisions. But if majoritarian default rules can avoid fine print, the costs of poorly chosen defaults are larger than just the cost of contracting around them.

A second point relates to how contract interpretation rules can interact with boilerplate. In the current context of consumer-friendly defaults,[54] the rule that ambiguous language will be construed against the drafter seems questionable. The poor souls who generate boilerplate probably respond to this threat by drafting more terms to cover more contingencies in more detail. This effect should increase the length of contracts, resulting in the now-familiar consequences associated with higher reading costs.[55] But in the context of default rules that are more seller friendly, this rule might actually be desirable. The goal of the proposal is to allow consumers to more easily differentiate between higher-quality and lower-quality contracts. The length of the contracts is one way to differentiate between these contracts: short or nonexistent contracts contain the defaults, and longer contracts are highly likely to opt out of the default rules in favor of lower-quality terms. Insofar as this canon makes this differentiation easier, it has some attraction.

II. Myopia and Deferred Costs

While I think that a rational choice approach to contractual complexity provides a more pervasive understanding than a behavioral approach, I find Bar-Gill's arguments about the prevalence of and problems associated with consumer myopia quite compelling. Following a long philosophical and economic tradition, he argues that this behavioral flaw can cause consumer preferences to change when the consumers must make decisions over time.[56] Bar-Gill's innovation here is to examine how firms can design contracts to exploit these preference changes. Firms can do this by stacking benefits of a contract at the beginning of the contract term and leaving the costs for later.[57]

When consumers evaluate agreements with upfront benefits and deferred costs, they may be tempted by the benefits—such as a low introductory interest rate or a subsidized cell phone—while also believing that they will not have to pay the later costs. They may, for example, expect that they will switch credit cards when the higher interest rate kicks in or that they will not go over the minute allotment in their cell phone plan. But they face a similar calculus when the time comes to change cards or to refrain from

54. *E.g.*, Restatement (Second) of Contracts § 206 (1979). Courts often invoke this rule in insurance disputes. *See* Kenneth S. Abraham, *Four Conceptions of Insurance*, 161 U. Pa. L. Rev. 653, 664 (2013) ("The maxim *contra proferentem* directs that ambiguities in a contract be construed against its drafter. Nowhere is this maxim invoked more frequently than in insurance disputes, where the drafter is virtually always the insurer." (footnotes omitted)).

55. *See supra* text accompanying notes 17–21.

56. *See* p. 21 ("Myopic consumers care more about the present and not enough about the future.").

57. *See* pp. 81–87 (explaining these effects in the context of credit cards).

talking to a friend; the immediate benefit trumps the later cost of paying a higher interest rate or an overage charge.

One might consider this myopia a flaw because it results from consumers discounting the future at different rates. Conventional definitions of rationality require a constant discount rate to keep preferences stable. There is a fair amount of evidence that people do not discount the future in this way.[58] For example, if someone who prefers $4 today to $5 tomorrow has a constant discount rate, that person should also prefer $4 in 99 days to $5 in 100 days. But a myopic consumer may prefer $4 today to $5 tomorrow and $5 in 100 days over $4 in 99 days. This is a preference flip because the consumer does not value a difference of a dollar over 24 hours in the same way at different points in time. The consumer has a higher discount rate for the immediate future when compared to the consumer's discount rate for events that are further off.

Bar-Gill cleverly shows how a firm that faces a market of myopic consumers can exploit this flaw. By providing benefits of a contract immediately or shortly after signing, firms may encounter consumers who discount any future costs quite steeply.[59] Imagine, for example, a consumer who expects to run up a balance on a credit card in six months. If a firm offered frequent-flier miles that it would give after six months of use and an interest rate of 10 percent, the consumer would discount these benefits and costs at roughly the same rate. This may lead the consumer to decline the offer. But if the contract offered the benefit of frequent-flier miles right away, the consumer would apply the steep discount only to the costs six months down the line. This structure may induce the consumer to accept the bargain. It is arguably undesirable for the consumer to do so because the consumer might overconsume credit by making this choice.

Bar-Gill also identifies how per-use fees, such as credit card late-payment charges and cell phone overages, may be an especially effective way to appeal to myopic consumers.[60] At the outset of a contract, consumers may believe that they will only make occasional use of late fees because the benefits of deferred payment or of talking to a friend, as well as the extra fees these actions entail, are all far off in the future. But when the time comes to decide whether to put off payment or to call that friend, the benefits are now immediate and the cost is still delayed. Consumers may overuse these features because they discount the immediate future quite steeply.

As with optimism, Bar-Gill acknowledges that not all consumers are subject to myopia. This observation naturally leads one to question how pervasive the problem is, and Bar-Gill has a strong response. In the chapter

58. P. 156; George Ainslie, *Derivation of "Rational" Economic Behavior from Hyperbolic Discount Curves*, 81 Am. Econ. Rev. 334 (1991); Shane Frederick et al., *Time Discounting and Time Preference: A Critical Review*, 40 J. Econ. Literature 351 (2002).

59. Pp. 53–54 (credit cards); p. 156 (mortgages); p. 185 (cell phones).

60. P. 49 (noting that consumers mistakenly believe that there will never be a benefit from making a late payment); p. 186 (noting that consumers underestimate the chance of incurring overages).

discussing cell phones, Bar-Gill explains a data set that he and Rebecca Stone developed. Using the data set, he makes a convincing case that consumers often fail to choose the plan that best corresponds to their actual usage (p. 219). For all the plans that Bar-Gill and Stone study, at least a quarter of the consumers choose plans that have cheap initial fees but end up costing more than other plans due to the overage fees that these consumers incur (p. 220). Had they picked a more expensive base plan, the transaction would end up costing them less in the long run because they would presumably not have to pay as much in overage fees. This evidence helps show that at least some percentage of people may be paying for the myopia in a way that deviates from what a rational actor model would predict.

The more difficult question is, what should be done about this myopia? Scholars writing about steep discounting of the immediate future have tied the problem to weakness of the will. Indeed, it is hard to find a discussion of myopia that does not mention the story of Ulysses and the Sirens.[61] When the Sirens are far off and the lure of their enchanting songs is not immediate, Ulysses knows that the costs are greater than the benefits. But he also knows that when those benefits become immediate and the costs are still far off, he will succumb to temptation. Accordingly, he recommends a rather extreme measure to prevent the harm that the weakness of his will might cause. He instructs his men to strap him to the ship's mast and not release him under any circumstances.

Bar-Gill does not endorse this sort of strong remedy. Rather, he adheres to disclosure as the most desirable means to remedy consumer myopia (p. 4). There are defensible grounds for taking this position. This light-touch regulation preserves much of the private ordering that makes contracting a socially valuable institution.[62] This approach is also consistent with efforts to "nudge" people into making decisions that will make them better off without invoking heavy-handed paternalism.[63]

I am particularly skeptical, however, that disclosure—and even the nuanced and intelligent disclosure that Bar-Gill recommends—will be an effective guard against myopia. Ulysses asks his men to take away his agency to prevent him from succumbing to the Sirens. Precommitment strategies of this type abound—common examples include Christmas Club savings schemes and heavy penalties on early withdrawal of 401K accounts[64]—but

61. *See, e.g.*, Jon Elster, Ulysses and the Sirens: Studies in Rationality and Irrationality (rev. ed. 1984); Nava Ashraf et al., *Tying Odysseus to the Mast: Evidence from a Commitment Savings Product in the Philippines*, 121 Q.J. Econ. 635 (2006).

62. As Bar-Gill acknowledges, disclosure does not completely eliminate paternalism. Disclosure will inevitably reflect the priorities of legislators, and the features that get disclosed can alter markets because firms compete over the disclosed features. Pp. 42–43.

63. Richard H. Thaler & Cass R. Sunstein, Nudge: Improving Decisions About Health, Welfare, and Happiness (rev. & expanded ed., Penguin Books 2009) (2008); Cass R. Sunstein & Richard H. Thaler, *Libertarian Paternalism Is Not an Oxymoron*, 70 U. Chi. L. Rev. 1159 (2003).

64. A Christmas Club is a special savings account at a bank where the customer deposits money throughout the year. The account rules either forbid or penalize the withdrawal of

they generally require restrictions that go beyond disclosure. As Jon Elster identifies, to counteract myopia, one needs to alter the magnitude of the costs and benefits that come with decisions or change the timing associated with these costs and benefits.[65] Improved disclosure does not have these effects.[66]

Bar-Gill rightly points out that firms themselves are unlikely to offer much to minimize the costs associated with myopia (pp. 30–32). Cell phone companies could, for example, disallow nonemergency calls once consumers reach their monthly quota. Credit card companies could, similarly, restrict purchases once teaser rates expire. But firms have little incentive to take these measures. They make more money when they can charge higher rates, and, as long as they do not lose many customers by catering to myopia, they should not be expected to provide myopia-limiting products.

Regulatory solutions that alter the cost structure associated with myopic choices are, however, more controversial. One aggressive technique is an outright prohibition on certain types of contract terms. Many states have laws that restrict the interest rates that creditors can charge, and the Credit CARD Act of 2009 prohibits practices such as the use of double-cycle billing.[67] As Paul Heidhues and Botond Köszegi show, when some consumers have a preference for immediate gratification, these types of prohibitions can increase welfare.[68] The regulation they analyze would prohibit terms that impose large penalties for deferring small amounts of payments.[69] They argue that these sorts of restrictions are likely to be palatable because they benefit the unsophisticated consumers—those who overborrow and must

money prior to the holiday season. *See* Jon Elster, *Don't Burn Your Bridge Before You Come to It: Some Ambiguities and Complexities of Precommitment*, 81 Tex. L. Rev. 1751, 1759 (2003) ("People who want to force themselves to save can join a Christmas Club, which will be deaf to any demands for withdrawal of the funds before December 15."); Jolls et al., *supra* note 2, at 1479 (discussing bonded willpower regarding pension plans).

65. Jon Elster, Ulysses Unbound: Studies in Rationality, Precommitment, and Constraints 29–31 (2000).

66. To be fair, Bar-Gill's claim is that providing improved disclosure may allow people to act more like Ulysses. If that supposition is correct, disclosure may be preferable to the stronger rules, such as those prohibiting terms that exploit myopia, because disclosure allows for more private ordering. But the degree to which disclosure will have this effect is not known, and the book could do more to substantiate this claim. This is especially so in light of evidence that people engage in a lot of activities that have short-term benefits and long-term costs—such as smoking and bad eating habits—even though the long-term costs of these activities are well known.

67. 12 U.S.C. § 86 (2012) (imposing a penalty for taking usurious interest); 15 U.S.C. § 1637(j)(1) (2012) (prohibiting double-cycle billing).

68. Paul Heidhues & Botond Köszegi, *Exploiting Naïvete About Self-Control in the Credit Market*, 100 Am. Econ. Rev. 2279, 2285–86 (2010) (explaining restrictions that can be welfare enhancing).

69. More specifically, they endorse a restriction that prohibits later interest rates from increasing in a convex way as opposed to, say, in a linear way. *Id.* at 2290–91.

pay these penalties—and have no effect on sophisticated consumers who would not have to pay these penalties in any event.[70]

But any restriction on terms needs to be done cautiously. There are potentially welfare-enhancing reasons why firms might want to offer low introductory rates that increase substantially after a set period of time. For example, if there are switching costs associated with moving from one credit card to another or from one cell phone service provider to another, firms may need to compensate consumers for the inconvenience associated with these switches.[71] Offering an initially low interest rate or subsidizing the up-front cost of a cell phone is an important way that firms can help offset the costs of switching.[72]

A prohibition on the ability of firms to tantalize consumers with low introductory offers may harm the welfare of rational, nonmyopic consumers. These consumers may be unwilling to switch unless they receive some sort of compensation from their new provider. Regulation that bans this practice can hinder competition, much in the same way that Bar-Gill worries that behavioral biases may limit competition (pp. 24–25). Knowing whether and how to regulate a consumer market that includes sophisticated and nonsophisticated consumers poses difficulties. As I have highlighted elsewhere in this Review, gathering the correct data is likely to be a demanding task that will not always yield clear answers. Indeed, Alan Schwartz argues that whether rationality or myopia dominates a market can be hard to determine.[73]

The difficulty of ascertaining whether regulation is likely to increase consumers' welfare may be part of what makes intervention such a contested issue. When it comes to myopia, there are theoretical reasons to believe that it leads to harmful overconsumption. But the cure may be worse than the disease, and obtaining an adequate diagnosis is likely to be very difficult. What is the better policy choice in this circumstance? As I have articulated here, and others have explained elsewhere, disclosure may not change much

70. *Id.* Their analysis puts aside the potential for strategic interactions between firms. As below, the potential for competition between customers may provide a very good reason for firms to subsidize switching costs.

71. Guy Arie & Paul L.E. Grieco, *Who Pays for Switching Consumers?*, Pa. State Dep't of Econ. 1 (Oct. 2013), http://www.econ.psu.edu/~plg15/Switching_Oct2013.pdf ("[For the customers of competing firms, switching costs] are like a tax and the firm's short-term incentive is to set a lower price that partially compensates the cost of switching.").

72. The size of switching costs can be difficult to measure. With respect to credit cards, Bar-Gill suggests that robust competition at the issuing level may mean that switching costs are low, but he counters that "psychological switching costs and simple inertia" may restrict actual switches. Pp. 64–65.

73. *See* Alan Schwartz, *The Rationality Assumption in Consumer Protection Law*, Ctr. for Law & Econ. (Mar. 2013), http://www.lawecon.ethz.ch/education/lawecon/education/lawecon/readings/consumer_regulation.pdf.

actual behavior.[74] I find it much more appealing to target the low-hanging fruit with forceful prohibitions.[75]

The double-cycle billing prohibited by the CARD Act is a nice illustration of this low-hanging fruit.[76] This practice can increase the size of credit card balances for consumers who vary their balance substantially over the course of time.[77] Double-cycle billing has several hallmarks of a problematic practice: It is complex and thus likely to be buried in fine print that consumers neither read nor comprehend. It has the potential to reduce the welfare of myopic consumers because those who find themselves carrying larger balances than they expected will have to make higher interest payments. And, finally, it is difficult to imagine how this practice could benefit more rational consumers. It does not, for example, compensate them for switching from one credit card to another. When a practice has these characteristics, it strikes me as a relatively easy case to adopt a prohibition against it.

But a lot of practices that potentially implicate myopia are hard cases. Do we have to ban the pervasive practice of offering no payments for the first few months of a credit purchase? A behaviorist might see these marketing techniques as a temptation to overconsume, while a pure rationalist might see them as an attempt to induce an informed switch. For those of us who are skeptical of what disclosure can accomplish, how do we know what to do when theory can justify both intervention and the free market status quo? I suspect that, for some, the answer has more to do with their prior views about the desirability of regulation. This lack of clear answers suggests that, when it comes to consumer protection, perhaps the most pressing need is for data that can discern whether rationality or myopia predominates.

Conclusion

In much of *Seduction by Contract*, Bar-Gill shows how best to combat the orthodox model of economic rationality. He discusses evidence of how people may deviate from the rational actor model, he builds a theory of how

74. Ben-Shahar & Schneider, *Failure of Mandated Disclosure*, *supra* note 4, at 665; Florencia Marotta-Wurgler, *Does Contract Disclosure Matter?*, 168 J. Institutional & Theoretical Econ. 94, 111 (2012) ("But even if sellers are constrained by reputation, it remains the case that mandating contract disclosure will not change consumer behavior."). Note, however, that the disclosure Marotta-Wurgler examines is disclosure of the terms rather than the targeted disclosure that Bar-Gill advocates.

75. Support for this intuition comes from a recent analysis of the impact of the CARD Act. Agarwal et al. analyze the effects of both the hard restrictions on fees required by the CARD Act and the softer regulations, such as those that require disclosure of the interest rate savings associated with paying off a balance in thirty-six months rather than making minimum payments. The authors find that the fee restrictions produced $20.8 billion in savings for consumers while the interest rate disclosure saved only $71 million. *See* Sumit Agarwal et al., *Regulating Consumer Financial Products: Evidence from Credit Cards*, Soc. Sci. Research Network 4–5 (Oct. 3, 2013), *available at* http://ssrn.com/abstract=2330942.

76. 15 U.S.C. § 1637(j)(1) (2012) (prohibiting double-cycle billing).

77. *See* Mary Beth Matthews, *The Credit CARD Act of 2009—What Is It, and What Does It Do?*, 2010 Ark. L. Notes 65, 68–69.

firms might exploit the model's flaws, he analyzes whether a rational model can account for observed behavior, and he proposes a regulatory regime tailored to the problems he identifies. The critiques in this Review focus only on the last two steps. Bar-Gill's framework for contractual complexity would be more persuasive if it wrestled with the leading rational choice models of contract comprehension. Doing so would not inherently undermine his arguments—indeed, it may even allow for a unified framework of consumer misperception and reading costs. But engaging these claims would almost certainly make his arguments more convincing to committed rationalists.

As for his proposals to remedy the ills he identifies through disclosure, I share the skepticism of others. If reading costs lead consumers to believe that contract terms will be of low quality, disclosing what they already believe may have limited effect. Moreover, if disclosure still allows firms to wield fine print, regulators will need to be particularly deft to keep up the fight. Perhaps this is within their power, but Bar-Gill's book does not detail how and why regulators might be able to do so. A similar critique applies to Bar-Gill's advocacy of disclosure to remedy consumer myopia. Under a standard model of weakness of the will, some form of precommitment is often necessary to prevent succumbing to temptation. While disclosure might nudge people into making better decisions, stronger tonics might be more effective cures for myopia. Both rationalists and behaviorists would benefit from conducting these sorts of relative inquiries in the future.