Session 3: Emerging issues in consumer protection:
Complementarities and areas of tension

Presentation
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The views expressed are those of the author and do not necessarily reflect the views of UNCTAD.
I. The Roles of Competition Policy and Consumer Protection
Two Inextricably Linked Policies

• Basic Relationship
  – **Competition Policy**: Relies on **supply side** actions that influence the number and size of firms, and how they interact
  – **Consumer Protection**: Focuses on **demand side** actions influence the way consumers purchase goods and services

• Stated more simply
  – Competition creates conditions where consumers have choice
  – Consumer protection protects that choice from being undermined by unfairness and deception
History Illustrates the Relationship

- 1914: FTC started as a competition agency: “Unfair methods of competition”
- 1930s: Deceptive selling distorted markets
  - Competitors either lose sales or use the same sales tactics themselves
  - FTC tried to use competition law, but proof of injury to competition was difficult
- 1938: Congress adds prevention of “unfair and deceptive acts and practices” to FTC mandate
  - The basis of consumer protection at FTC
  - Other aspects of consumer protection left with others
Policy Interdependence

• Lack of competition undermines incentives of firms to:
  – Provide information to consumers
  – Respond to consumer preferences
  – (as well as offer lower prices)

• Unjustified restrictions of non-deceptive information undermines incentives to compete:
  – Firms only innovate if they think they can sell
  – To sell, firms need to be able to promote
  – If restrictions inhibit truthful promotion, less incentive to innovate

• If advertising is not seen as a trustworthy source of consumer information, consumers lose ability to benefit from competition
Cautionary Examples

• Comparative Advertising
  – Once prohibited in U.S.
  – Now recognized as source of valuable consumer information
The Perfect World and the Real World

• In a perfect world, there would be no need for consumer protection. In the long run, competitive markets would:
  – Reward producers who offer what consumers want; and
  – Punish producers who fail to deliver for consumers.
  – And government intervention has costs

• But in the real world, markets don’t always protect consumers
  – Fraud operators have little need for repeat business
  – Deception is not always easy to detect
  – Sometimes it’s too hard to obtain information or to exercise choice

• The short-term cost to consumers of market solutions may be too high, and interests must be balanced
## Four Scenarios for Intervention

<table>
<thead>
<tr>
<th>Scenario</th>
<th>When market structure prevents consumer choice</th>
<th>When regulation prevents consumer choice</th>
<th>When consumers should have choices – but don’t</th>
<th>When consumers have choices – but can’t exercise them effectively</th>
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<tbody>
<tr>
<td><strong>Intervention</strong></td>
<td>“Natural monopolies,” such as water, electricity distribution</td>
<td>“Unnatural monopolies” which exist due to government granted privileges</td>
<td>Cartels, abuse of dominance, or anticompetitive mergers eliminate competition</td>
<td>Credence goods and services -- buyer must rely on seller for information; or where search costs are too high to make choice meaningful</td>
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<td>Sectoral regulation constrains price and quality terms</td>
<td>Competition advocacy seeks market outcomes</td>
<td>Competition law enforcement</td>
<td>Consumer protection enforcement when warranted; Consumer education</td>
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OECD Consumer Policy Toolkit

- Guidance and Framework for Analyzing Consumer Policy
- Information Economics
- Behavioral Economics
Credence Goods and Services

• In many cases, the consumer must trust the seller for information about products
  – Examples: food ingredients, pharmaceuticals, performance data

• Not all credence goods require intervention
  – Sellers depend on repeat business
  – Third party information sources

• Intervention needed in case of fraud or persistent consumer confusion
Search Costs

• Sometimes the information consumers need cannot be readily obtained

• Examples:
  – Inconsistent metrics of comparison
  – Sales under time pressure
  – Infrequent purchases

• Possible solutions:
  – Disclosures (caution: hard to make them effective)
  – Consumer education
  – Allow market to solve problem
  – Balance remedy with costs
  – Beware the law of unintended consequences!
Key Questions

• In deciding whether to intervene or allow the market to solve the problem, how much are we prepared for consumers to endure in the name of allowing competition to function?
• Interventions have cost. Is the cost worth it?
• Factors:
  – What is the harm to consumer?
  – How easily can the consumer avoid the harm?
  – Is the market capable of resolving the problem?
  – Can intervention offer a better solution?
  – What burden are we willing to place on the consumer?
II. Competition and Consumer Protection: Two Sides of the Same Coin
Two Sides of the Same Coin

• Competition is our best protection for consumers
• Consumer protection steps in when markets fail – but does not replace them
• “False dichotomy” that competition and consumer protection are opposed to each other
• Competition and consumer protection are natural partners
Two Sides of the Same Coin

• Sometimes we can use theories that apply both competition and consumer protection principles

• One may be a part of the other
  – Deception can be a means of monopolization
  – Ex. Rambus; Intel

• Or a matter may be reclassified from one type to the other
  – To produce new theories of liability
  – Or new forms of remedy
III. Consumer Protection Supports Competition Policy
Consumer Protection Supports Competition Policy

- Consumer protection helps competition enforcers understand how markets work
- Also helps understand rationales offered to justify restrictions on competition
- Transferred experience with remedies
- Builds public support for market economics
Information Cures Competition Issues

• Cures market power with information – encourages customers to support new entry.

• Ex. tying – a dominant firm exploits its market power to force customers to use its own consumable products

• A remedy might require this firm to specify the characteristics of workable aftermarket products
Google Case

• Google Buzz – social networking service
  – Used information of consumers who signed up for Gmail to populate the network
  – Did not adequately communicate that previously private info would be shared publicly by default
  – Made false and misleading representations about the use of account data
  – Other personal info was shared without permission

• Settlement with FTC – agreed to stop deceptive practices
Facebook Case

- Made certain information public without warning users or obtaining approval.
- Promised that only necessary data would be made available to 3rd party apps – in reality almost all data was made available.
- Shared data with advertisers.
- Settlement barred additional misrepresentations and required them to obtain express consent before overriding preferences.
Reframing Competition as Consumer Protection

• Deception of a standard-setting organization (Rambus; Dell)
• Coercing the purchase of a license, by threat of bad-faith litigation (patent extortion)
• Benefits of reframing these as consumer cases
  - Correctly characterizes the method of harm
  - These offenses truly do not need market power
    - Need only the ability to deceive, or to impose costs
  - Thus need to prove market power
    - Although market power is often relevant and helpful
  - Helps us recognize corporations as “consumers” or proxies for consumers
IV. Competition Policy Supports Consumer Protection
Competition Policy Supports Consumer Protection

• Good economics harmonizes consumer and competition policies

• Examples:
  – Comparative advertising
  – Advertising of professionals services
Reframing Consumer Protection as Competition

• State restrictions on the commercial practice of optometry
  – Banned corporate practice, or retail settings
  – State claimed that quality would be lowered, or people misled

• FTC tried to challenge these bans on consumer protection grounds
  – Rebutting the CP theories behind the restrictions
  – Failed in court: the state was not deceiving anyone

• Better to put a case in competition terms
  – These are really restrictions on the set of options
  – State regulatory board is a horizontal agreement
  – Only exempt from antitrust laws if supervised
Intel Case

• Intel stifled competition in market for computer chips – punished its customers (computer manufacturers) for using competitors products.
• Also used deceptive practices to mislead the public – gave impression that other products did not perform well.
• Settlement prevents use of threats to stifle competition, prohibits deception about performance of non-Intel processors, and requires certain disclosures.
Curing a consumer problem by creating more competition

• Disclosures in formats that encourage comparisons and competitive responses
• Appliance energy-use labeling
  – Shows how a product compares with all competitors
  – Helps decision-making
  – Also encourages firms to compete in these terms and create better options
  – Information helps to create market innovation
• Franchise rule
  – Gives information to people who are thinking about buying a franchise
  – Does so in a standard format that encourages comparisons
  – Hope that this will lead to provision of better opportunities
V. Linkages Between Consumer Protection and Competition
Institutional Implications

• Linkages between competition and consumer protection encourage viewing an issue as a market problem
  – Not just as a consumer problem
  – Not just as a competition problem
  – “To a man with a hammer, everything looks like a nail”

• Key linkage: economic analysis informs both
Benefits of Linkages

• Encourages coordination between competition and consumer protection staffs
• Helps each think more clearly by showing how its law fits into the broader “choice” framework
• Provides a richer set of legal theories and remedies
• A plausible midpoint for trans-Atlantic convergence
• Makes it easier to explain actions to the press, the legislature, and the public
Operational Models

Full Integration of consumer protection and competition

- Same staff handles both, chooses competition or consumer remedies as appropriate
- Different skills required
- Risk of distraction by consumer issues with little impact on markets
- Temptation for resources to follow the easy targets

Single agency handles both separately

- Joint policy
- Separate enforcement staffs
- Recognizes need for policy coherence but separate skill sets
- Practical problems of coordination
Operational Models

Separate agencies that build linkages

- Policy linkage by shared views or memorandum of understanding
- Requires shared views by agency leadership
- Linkages can erode with changes in leadership

Complete separation between competition and CP

- Allows each to focus on own priorities
- Risk of policy incoherence
Operational Models Worldwide

• General trend towards consolidating competition and consumer functions
  – Denmark, Ireland, Netherlands, Estonia
  – Financial concerns trump policy issues

• Counter-trend: separation of functions in Iceland