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EC Consumer Protection Law and EC Competition Law: How related are they? A Law and Economics perspective

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Abstract*

EC Consumer Protection Law and EC Competition Law are amongst the most important areas of law, having a deep regulatory impact on the functioning of markets. Their alignment, in terms of goals and approach to the regulation of markets, seems in principle very substantial: both share the benefit of consumers as their most relevant purpose and organizing principle.

However, when one looks deeper into the underlying economic issues that both areas of the Law are more apt at addressing, significant differences become apparent. Monopoly power is the crucial problem for Competition Law in general, and EC Competition Law is no exception to this. Consumer Protection Law however, is not – and should not be – concerned with market power as such, not even in its version of inequality of economic or bargaining power between producer and consumer. The relevant economic phenomenon that justifies in economic terms consumer protection legislation, both at National and European levels, is imperfect information in consumer markets. The focus on informational failures explains the kind of instruments and approaches most common in EC Consumer Law. The divergence in economic rationales, however, is not incompatible with the idea that, in certain circumstances, joint consideration both of competition issues and consumer protection factors appears necessary, but should not lead us to forget the main role of each branch of the Law.

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1. Introduction

Consumer Protection Law and Competition Law count as some of the major branches of the Law dealing with the legal regulation of markets. Their relationship in terms of goals, main issues and structures has not been extensively considered, however, especially in what concerns their role in EC policy and Law. In this paper I will try to offer an analysis of this relationship from the perspective of Law and Economics. Even though neither of them can be understood and operated irrespective of each other, I will attempt to underline how the apparent similarities substantially disappear when one looks at the substantive market imperfections that each of them faces. The emphasis I will place on informational failures as the major rationale for legal activism in consumer markets is fully consistent with the findings of several recent commentators, with a more or less explicit economic propensity in their approach¹. I will also stress what I take to be important lessons for the design and operative functioning of EC Consumer Law.

In section 2, I will deal with the common goal in consumer protection Law and competition Law of promoting the benefit of consumers. In section 3, I present what I deem to be the key factor for a deeper understanding of the proper role of both legal areas: the economic problem that each of them is apt to address adequately. In section 4, I discuss why consumer protection Law is not an efficient instrument for dealing with issues of monopoly and related practices, and how a focus on market power would be misleading and, ultimately, counterproductive for the operation of EC consumer Law. In section 5, I propose a more restricted but, I think, more effective type of approach to consumer protection Law, that permits an increased understanding of its economic strengths and weaknesses. In section 6, I provide a brief and simple example of circumstances in which joint consideration of competition and consumer protection issues seems advisable, and I also conclude.

2. The essential alignment in goals of consumer protection and competition Law

At first glance, of all possible pairings of sectors or areas within a legal system, only a few can claim to be as well aligned in terms of goals and underlying foundations and structural components as consumer protection Law and competition Law. Both areas of the Law, as I

¹ See Gillian K. Hadfield, Robert Howse, and Michael J. Trebilcock, "Information-Based Principles for Rethinking Consumer Protection Policy", 21 *Journal of Consumer Policy* (1998), p. 131; Stefan Grundmann, Wolfgang Kerber, and Stephen Weatherill, "Party Autonomy and the Role of Information in the Internal Market – an Overview", in Stefan Grundmann, Wolfgang Kerber, and Stephen Weatherill (Eds.), *Party Autonomy and the Role of Information in the Internal Market*, Walter de Gruyter, Berlin-New York (2001), p. 7; Stefan Grundmann, "Verbraucherrecht, Unternehmensrecht, Privatrecht – warum sind sich UN-Kaufrecht und EU-Kaufrechts-Richtlinie so ähnlich?", 202 *AcP* (2002), p. 40, specially p. 61.

will attempt to demonstrate in this section, seem to share, in a fundamental way, a core purpose behind their corresponding legal rules, doctrines, and enforcement mechanisms².

To say that the goal of consumer protection Law is to promote the benefit and the interests of consumers is almost tautological. It is true, however, that what constitutes the benefit of consumers is not something that everyone would agree upon, and that it can be understood in different forms and with various emphasis: as economic efficiency and social welfare in consumers' markets, as a re-distributive policy objective favoring consumers, or even as a paternalistic view of what the legal and economic rights of the consumer population should look like³. Probably, the reasons behind all real-world consumer protection legislation in all real-world legal systems combine to a greater or lesser extent, welfare, redistribution, and paternalist threads⁴, rightly or wrongly understood, and EC consumer protection Law is no exception to this. Additionally, the qualifying element of building an effective internal market also for all consumers' goods and services looms large in EC consumer policy and Law. This feature comes as no surprise, given the nature and constraints (particularly the legal constraints posed by articles 153 and 95 EC Treaty) concerning the role of the EC in this field and its law-making powers. But this emphasis on the cross-border and harmonization dimension does not undermine the central purpose of the legislative effort as being one directed to the promotion of the benefit of consumers.

The purpose of competition Law is evidently to preserve and enhance the competitive structure of markets for goods and services. As simple economic theory shows, the big winners from competitive market structures are precisely the consumers of the goods and

² Of course, for those who believe in the coherence and purpose of a legal system, all areas of the Law share a common goal, be it justice, equality, happiness, efficiency, wealth maximization, social welfare, or other imaginable goal. Even though I do think that the whole theoretical and human machinery of the legal system is not a blind enterprise, and that there is a fundamental common purpose in it – albeit instrumental and not self-defined –, what I am referring to in my claim, is narrower than the fundamental ends of the legal system: it is the presence of a more specific and operational affinity in goals, that is not to be found in other areas of the Law – say, Tort Law, or Intellectual Property Law – despite the possible overall encompassing existence of a common goal in the legal system. For an excellent review of fairness or justice-based and human welfare-based conceptions of the goal of a legal system (with a strong bias and forceful arguments in favor of the latter), see Louis Kaplow and Steven Shavell, *Fairness versus Welfare*, Harvard University Press, Cambridge (MA), (2002).

³ For instance, in the Commission's new consumer policy strategy for the period 2002-2006, adopted on 7 May 2002, the bold statement that "...all consumers (across the EU) should benefit from the same high level of protection...", in line with the provisions of articles 95.3 and 153.1 of the EC Treaty, could (although not necessarily "should") be interpreted as an open admission of the fact that achieving a homogeneous high amount of consumer protection is a proper and valuable goal in itself, no matter how much or how diversely different consumers might value the level of protection, and how willing they would be to pay for it. In other terms, that a high level of consumer protection is a "merit good" (one which the political power has decided should be consumed by citizens in a certain amount, no matter how the real demand for it may be) that helps and benefits consumers even if they themselves do not recognize it. I am not implying by this that EC consumer policy has to be understood largely as a paternalistic policy, just that some of its formulations are not inconsistent with this view, and that some amount of it is an ingredient of EC policy.

⁴ See Ian Ramsay, "Consumer protection", in Peter Newman (editor), *The New Palgrave Dictionary of Economics and the Law*, vol. I, MacMillan, London, (1998), p. 410, emphasizing the combined presence of those three rationales, and expressing overall a positive opinion on this plurality of motivations. For reasons that will become clear in section 5 below, I am somewhat skeptical about the appeal of the re-distributive and paternalistic motives in consumer protection Law.

services. Perfect competition ensures that all consumers who value a certain good or service at more than what it would cost for the society to produce the good or provide the service, will obtain it at the price which reflects the exact social cost. Allocative and productive efficiency are simultaneously achieved. Moreover, the surplus generated by the production and provision of goods through the competitive market accrue entirely to consumers, so their position cannot be improved by Government policy or legal rules.

As is widely understood among economists, lawyers and policy-makers, though, the attempt to replicate the conditions for perfect competition⁵ in all markets for goods and services is doomed to failure and it can even be counterproductive. The desire to bring all markets as close as possible to these ideal conditions with the use of legal rules and policies will be futile in many cases, because of unavoidable constraints to the number of producers, level of information, entry costs, and so on. Moreover, it may be overtly inefficient and, therefore, harmful to consumers under several circumstances: when there are increasing returns to scale, a small number of producing firms, even just one firm, might be required for productive efficiency, that is, for producing the good or service at the lowest available cost for society; when informational goods are involved, the need for an incentive to produce the good in the first place may require the award of a temporary monopoly in the distribution of the product⁶.

So, more realistically, the proper economic role of competition Law, and of competition policy more generally, is to avoid the negative efficiency consequences of those market structures that most openly depart, without good reason, from competition, notably those arising from the presence of a single producer or a group of producers acting like a single

⁵ The standard assumptions in economic theory for a perfectly competitive market are the following: atomicity of producers (the number of producers is so large that no single producer has an impact on what others do); product homogeneity (the products by all different producers are perfect substitutes); perfect information (both producers and consumers have perfect knowledge of all relevant variables); equality of producers (all producers have the same technology and cost functions); free and unlimited entry (any producer may enter or exit the market as it wishes). Of course, this set of assumptions clearly shows that perfect competition is a theoretical construct, and that it is not something that we can derive by induction or observation from real-world markets. Still, it is an extremely useful benchmark to evaluate the performance and the possible corrective measures in real life markets.

⁶ The use of patents and copyrights as exclusive rights on the production and distribution of a given informational good (invention, work of literature or art, computer program, etc.) conferring some monopoly power on the right-holder is explained in economic terms by the need to provide dynamic incentives for the creation of informational goods: if these were sold from the start under conditions of perfect competition, and given that the marginal cost of providing an additional access to the informational good (an additional viewer of the film, an additional user of the computer program, for instance) is close to zero, the expected profit for the original producer of the good also approaches zero, so the inventor or creator will not be able to recover the fixed costs of creating the invention or work in the first place. To provide incentives to overcome this problem, the legal system grants temporary exclusive rights, leading to market structures departing, in some cases widely, from the conditions of perfect competition. Needless to say, these exclusive rights pose problems of their own, even some that are of great interest to competition Law (under-dissemination of existing works, abuse of patent and copyright, monopoly leverage). These disadvantages are the reasons used by some to advocate, on economic grounds, the use of other alternatives to provide incentives for the production of new intellectual goods: See Tanguy van Ypersele and Steven Shavell, "Rewards versus Intellectual Property Rights", 44 *Journal of Law and Economics* (2001), p. 525. Nevertheless, the economic case for making an exception, at least to some extent, to the conditions of perfect competition in order to induce a more desirable level of production of informational goods, has firm grounds in economic theory.

producer, that is, monopoly and collusive behavior. Still, this relatively more restricted scope of competition Law does not alter the fact that consumers remain the beneficiaries of curtailing monopoly and collusive behavior of firms.

When a monopolist, or a group of firms behaving like one, restricts output to maximize profit, it causes a raise in price above the competitive level. This will bring about a shift in the ultimate beneficiary of the surplus of the market exchange. A fraction of this surplus (even the whole surplus, under certain conditions) will be transferred from consumers to producers, making the former worse-off and the latter better-off. More importantly in economic terms, the restriction in output will determine that some consumers who value the good or service above the social cost of its provision – but less than the monopoly price – will be deprived of the possibility of its purchase, and will be forced either to do without it, or else to turn to less-preferred –or more costly to produce in social terms– alternative goods. This is the most characteristic economic deadweight loss caused by monopoly and collusion⁷. Its elimination or weakening by competition Law serves primarily the interest of consumers, and benefits them, in very much the same way as consumer protection Law, albeit perhaps in a more indirect and less easily observable manner. Competition Law, however, might pursue, by means of legal rules against monopolistic and collusive behavior, other goals different from the elimination of the efficiency losses that monopoly creates to the detriment of consumers. Some of these alternative goals might also be inspired by the intention to directly benefit consumers (redistribution of market surplus or income, more generally, in favor of consumers) or might be largely independent of consumers' welfare (the promotion and advance of small and medium-sized enterprises instead of large firms⁸, the desire to block the leverage and concentration of the political power of economic interests and groups). I am highly doubtful about the aptitude of any competition Law system to achieve these other “non-economic goals”, but the likelihood of its past, present, or future adoption as goals by a given legal system cannot be entirely disregarded, although it is uncertain whether some of these purposes do play a role in the operation of EC competition Law.

⁷ Other economic inefficiencies have been claimed as arising out of monopoly. One is the wasteful rent-seeking that will be encouraged by the desire to acquire or to maintain the monopoly rents, rent-seeking process that in the extreme would eat up all supra-competitive profits, transforming the shift in consumers' to producers surplus in a net loss. This claim is associated particularly with the Chicago Law and Economics School, most notably, with Richard Posner, “The Social Costs of Monopoly and Regulation”, 83 *Journal of Political Economy* (1978), p. 807. There is also relatively widespread sharing of the idea that monopolistic market structures might be less friendly to innovation and to the development and introduction of new technologies. Although there is sound theoretical support for this claim, at least since Arrow's classic article [Kenneth Arrow, “Economic Welfare and the Allocation of Resources for Inventions”, in Ralph Nelson (editor), *The Rate and Direction of Inventive Activity*, Princeton University Press, Princeton (NJ), (1962)], it is not unlikely that other strategic factors might counteract the disadvantage of monopolistic firms in terms of the pure incentives to innovate, so that the actual relevance of this inefficiency remains unclear: Jean Tirole, *The Theory of Industrial Organization*, MIT Press, Cambridge (MA), (1988), p. 392 and following. Less well-grounded still is the claim that monopoly would lead necessarily to a decrease in the quality of goods and services offered to consumers: Neither in economic theory nor in empirical evidence is there sufficiently strong support for this view. See Oz Shy, *Industrial Organization. Theory and Applications*, MIT Press, Cambridge (MA), (1995), p. 315 and following, and *infra*, p. 7-8.

3. The different underlying economic problems in consumer protection and competition Law

From this community of goals and intended beneficiaries, it would be easy to jump to the conclusion that the fundamental economic questions involved, and the adequate theoretical approach are also the same in both branches of the Law. I will try to show that this view is misleading, and, moreover, that it can prove notably harmful for a proper design and understanding of consumer protection generally, and at the EC level more specifically.

Despite the fact that promoting consumers' welfare can be justly considered the governing purpose of both competition Law and consumer protection Law, the divergence between the economic problems that both sets of legal rules are supposed to address is very substantial. I will argue that consumer protection Law is apt –and, consequently, should be used primarily for this purpose - at redressing the inefficiencies in consumer markets arising from a family of market failures, namely imperfect information, and particularly, at least for the more “contractual” portion of consumer protection Law, asymmetric information between producers and consumers. Competition Law, in turn, is – and should be-, as argued in the previous section, primarily concerned about the inefficiencies derived from monopolistic market structures and related issues (collusive and exclusionary practices)⁹. Using consumer protection Law to deal with issues of monopoly power to the detriment of consumers is not only futile in most instances, but will lead us astray in the appropriate design and implementation of consumer protection Law, and can result in unintended harmful consequences for consumers' welfare.

Let me first illustrate the idea that the negative consequences for consumers of monopolistic structures and practices are typically those that competition Law is precisely supposed to tackle.

As is well known, and was briefly examined in the previous section, when there is only one producing firm (or several firms acting as a cartel) output is restricted and the price of the good or service increases to the detriment of consumers' and society's well-being¹⁰. But no matter how large the market power or the monopoly power of the firm, it usually has no incentive to engage in other types of contractual behavior that are unfair or detrimental to consumers' welfare¹¹. If consumers can observe the relevant variable of the transaction (quality of the good, fairness and adequacy of the rights and obligations from the contract,

⁸ A motivation that might not be totally absent from Directive 2000/35/EC, of 29 June 2000 on combating late payment in commercial transactions.

⁹ As Gillian K. Hadfield, Robert Howse, and Michael J. Trebilcock, “Information-Based Principles for Rethinking Consumer Protection Policy”, 21 *Journal of Consumer Policy* (1998), p. 150 very aptly state it: Antitrust policy focuses on the structure of markets, and consumer protection policy focuses on the structure of consumer transactions.

¹⁰ One should keep in mind the qualifications mentioned in text corresponding to note 6 above.

¹¹ This proposition is true under conditions of perfect information. With imperfect information it does not necessarily hold, and for a monopolistic firm (a competitive firm too, as we will see) market incentives might fail in ways that prove harmful for consumers, but the real issue is, then, the informational problem, and not the monopolistic structure of the market.

accuracy of advertising statements, and so forth) the monopolist will generally have the appropriate incentives to offer the level of quality in the relevant variable that consumers desire¹². If the firm offered a level of quality, say in the rights and obligations in case of breach of contract, lower than the one that consumers would prefer, this would mean that the value of increased quality to consumers would exceed the cost to the firm of providing the additional quality to reach the level preferred by consumers. By definition, the monopolist would not be maximizing profit in this situation, because the firm could raise quality to the consumers' desired level, and raise the contract price an amount that more than compensates the firm for the increased costs of providing the additional quality. Cheating consumers in quality to save production costs will only result in a lower consumer willingness to buy the good or service, and thus, would lead to lower prices and lower profits for the monopolist.

4. The substantial irrelevance of monopoly power –and inequality of bargaining power- for consumer protection Law

In the ordinary understanding of consumer protection legislation, particularly with respect to the contractual sphere, inequality of bargaining power between firms and consumers appears to be one of the bigger, if not the biggest, source of concern and failure in the contracting process, requiring the corrective intervention of legal measures directed to redress the imbalance in contractual power¹³. This is, for instance, the view of the ECJ who, in regard of the Directive in Unfair Terms in Consumer Contracts stated that “...*the system of protection introduced by the Directive is based on the idea that the consumer is in a weak position vis-à-vis the seller or supplier, as regards both the bargaining power and his level of knowledge.*”¹⁴ It is also the one expressed by many legal commentators on contractual consumer protection Law¹⁵. According to the economic substance of the interaction under perfect information,

¹² In more technical terms, this conclusion that the monopolist will offer the socially optimal level of quality in all observable contract variables holds only for a homogeneous population of consumers. When consumers differ in their valuations and preferences for quality (some would be willing to pay a high price for fair contractual rights and obligations, but others largely disregard this aspect), the monopolistic firm would care for the quality preferences of the marginal consumer, and if these are lower or higher than the ones of inframarginal consumers, quality would be too low or too high: A. Michael Spence, “Monopoly, Quality and Regulation”, 6 *Bell Journal of Economics* (1975), p. 417. A presentation of these results in a more lawyer-friendly way, in Richard Craswell, “Passing on the Costs of Legal Rules: Efficiency and Distribution in Buyer-Seller Relationships”, 43 *Stanford Law Review* (1991), p. 361.

¹³The idea that the exercise of economic power over consumers is the major traditional rationale behind consumer protection policy is also present in Gillian K. Hadfield, Robert Howse, and Michael J. Trebilcock, “Information-Based Principles for Rethinking Consumer Protection Policy”, 21 *Journal of Consumer Policy* (1998), p. 133; Pamaria Rekaiti and Roger van den Bergh, “Cooling-Off Periods in the Consumer Laws of the EC Member States: A Comparative Law and Economics Approach”, 23 *Journal of Consumer Policy* (2000), p. 371, at p. 373.

¹⁴ Joined Cases C-240/98 to C-244/98 ECJ, *Océano Grupo Editorial SA v. Rocio Murciano Quintero and others*.

¹⁵ See Hugh Beale, “Inequality of Bargaining Power”, 6 *Oxford J. Legal Stud.* (1986), p. 123; Manfred Wolf, “Party Autonomy and Information in the Unfair Contract Term Directive”, in Stefan Grundmann, Wolfgang Kerber, and Stephen Weatherill (Eds.), *Party Autonomy and the Role of Information in the Internal Market*, Walter de Gruyter, Berlin-New York (2001), p. 313, at p. 323; Remiert Tjittes, in Beale, Hartkamp, Kötz, Tallon (editors), *Cases, Materials and Text on Contract Law*, Hart Publishing, Oxford and Portland (OR), (2002), p. 527. Stefan Grundmann, “Verbraucherrecht, Unternehmensrecht, Privatrecht – warum sind

though, this view is largely unfounded, as it equates the issue of quantity restriction (which is, justifiably, associated with monopoly) with that of reduction in quality of the relevant transaction variables, including contractual rights and obligations. The fact that we have a large monopolistic firm contracting with a minuscule (in economic terms) consumer, does not by itself raise concerns and suspicions about the terms of the transaction that consumer protection Law is well-placed to address and eventually to improve upon. Improvements, if such is the case, might come from the side of competition Law, but these will affect price paid and quantity transacted by all consumers, and not the terms of the individual contract.

It is true, though, that there are instances in which a link between monopoly and imperfect information can be traced. Firms enjoying monopoly power might have incentives to exploit, or even create, imperfections in the information available to consumers, especially with the goal of price discriminating between groups of consumers differing in their ability to obtain or process the relevant information¹⁶. This and other related problems do not call for consumer protective measures specifically addressed to monopoly power issues. They can be more fruitfully understood and tackled within the overall setting of the provision of information to consumers in the market, in which the efficiency condition of equality between marginal social benefits and marginal social costs of providing information to consumers are very rarely met, and this regardless of the competitive or monopolistic structure of the underlying product or service market (although inefficiencies arise for different reasons).

There are also circumstances in which an existing imperfection in the available information might induce a monopolistic firm to alter the preferred level of quality in the contract in order to maximize profits. It is not consumers' ignorance about a relevant variable of the transaction that drives this result, but rather the producer's lack of information.

If consumers differ in their valuation of the good or service, the monopolist would maximize profits by sorting them into groups according to their willingness to pay and charging them a different price (price discrimination). If the monopolist could readily observe the type of a given consumer, no changes will be required in the most efficient level of quality of the contract terms. But if the monopolist ignores the type of a given consumer, and if willingness to pay is correlated with some dimension or element in the

sich UN-Kaufrecht und EU-Kaufrechts-Richtlinie so ähnlich?", 202 *AcP* (2002), p. 40, at p. 65 is more dubious about the strength of the belief of European lawyers in the inequality of bargaining power theory. To be fair to lawyers, it must be said that faith in that theory was shared by most economists before the development of the economics of information. Moreover, apart from the issues discussed in this same section, it is true that private information is not unrelated to bargaining power in a bargaining situation or game. Indeed, private information is a big source of bargaining power. Private information, however, is far from being perfectly correlated with size or economic dimension (firm *vis-à-vis* consumer) and, in fact, in many transactions between consumers (used houses or second-hand vehicles) it is indeed pervasive.

¹⁶ Steven Salop, "The Noisy Monopolist: Imperfect Information, Price Dispersion and Price Discrimination", 44 *Review of Economic Studies* (1977), p. 393; Howard Beales, Richard Craswell, and Steven Salop, "The Efficient Regulation of Consumer Information", 24 *Journal of Law and Economics* (1981), p. 507.

contract terms (say, a term contemplating liquidated damages for breach of the contract), the producer will be inclined to introduce¹⁷ a menu of contracts to divide consumers into groups corresponding to their willingness to pay for the good or service: for instance, one contract will include a high damage term together with high price, and the other would include an inefficiently low damage term (the inefficiency is introduced on purpose to prevent high-valuation consumers from choosing the cheap contract) together with a low price¹⁸.

One could think that, if we were able to identify the existence of monopoly power in a setting of heterogeneous consumers and monopolist ignorance of consumers' types, consumer protection legislation should enter the picture imposing a minimum level of quality in the contractual terms, so no inefficient terms are introduced in the contracts offered by the monopolist with the purpose of price discriminating among different types of consumers. The problem with this call to consumer protection Law to redress monopoly evils, is that the impact of its rule in this setting is largely indeterminate and, eventually, might act to the detriment of consumers, for three reasons. Firstly, because if not all relevant terms that might be used by the producer for screening purposes are covered by the minimum standards imposed by consumer legislation, we would simply get a shift in the distortions towards those terms not regulated under the consumer protective measures¹⁹. Second, because it is hard for legislators, regulators or Courts to collect and elaborate all the information required to reasonably determine the optimum floor for all relevant contract terms. Finally, and more importantly, because the legal imposition of levels of quality and contract terms for consumer transactions involving a monopolistic seller might induce not a better serving of all types of consumers but simply a price rise that would leave those groups with a lower willingness to pay excluded from getting access to the product or service²⁰.

¹⁷ In technical terms, the fact that the initiative is on the side of the uninformed party (the producer, in this case), makes the interaction one of screening and not of signaling. See on this, Eric Rasmusen, *Games and Information. An Introduction to Game Theory*, 3rd edition, Blackwell, Oxford, (2001).

¹⁸ This is a well-established result of the economic theory of imperfect information: See Inés Macho-Stadler and David Pérez-Castrillo, *An Introduction to the Economics of Information. Incentives and Contracts*, Oxford University Press, Oxford, (1997), p.... For applications in the Law of contract damages and default terms of contract Law, see Jason Scott Johnston, "Strategic Bargaining and the Economic Theory of Contract Default Rules", 100 *Yale Law Journal* (1990); Ian Ayres and Robert Gertner, "Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules", 99 *Yale Law Journal* (1989), p. 87; Ian Ayres and Robert Gertner, "Strategic Contractual Inefficiency and the Optimal Choice of Legal Rules", 101 *Yale Law Journal* (1992), p. 729. A recent survey of all this literature, in Fernando Gómez, *Previsión del daño, incumplimiento e indemnización*, Civitas, Madrid, (2002).

¹⁹ Alan Schwartz, "An Examination of Nonsubstantive Unconscionability", 63 *Virginia Law Review* (1977), p. 1053.

²⁰ In more technical economic terms, that the legal regulation of terms might not only lead from the original and less efficient separating equilibrium (separating because each consumer type gets a different thing, in this case, each signs a contract with different terms, some of which, as we have seen, are inefficient) to a more efficient pooling equilibrium (pooling because there is no discrimination and all consumers get the same contract terms). The imposed terms might imply that the profit-maximizing strategy for the monopolist is one leading to a separating equilibrium, but one in which separation occurs because price is so high that only consumers with high willingness to pay get the good or service and the rest do not buy. On this result, see Fernando Gómez, *Previsión del daño, incumplimiento e indemnización*, Civitas, Madrid, (2002).

In summary, there does not seem to be any good reasons to engage the machinery of consumer protection Law to directly combat the negative effects of monopoly and monopolistic practices. This should be primarily left to competition Law, or other relevant branches of the Law, such as public regulation of the market²¹. Consumer protection legislation has a comparative advantage, however, in addressing (some of) the deficiencies in the operation of consumer markets arising from a broad and complex range of market failures that can be loosely grouped together under the heading of imperfect information.

5. Consumer protection Law as a set of instruments to reduce information imperfections in consumer markets

In this section I will argue that the economic understanding of imperfections in the information available in consumer market transactions offers the best guide for the definition, scope, boundaries, and instruments, but also the inherent limitations of consumer protection Law. Other alternative principles do not allow for the theoretical coherence and the empirical testability that imperfect information brings to this area of the Law, and, moreover, they result ultimately in a lower level of consumers' preferences, satisfaction and social welfare than the economic understanding makes possible. I will not deal extensively with these alternatives, but, once the monopoly power rationale has been discarded, I will say a few words about redistributive and paternalistic motivations in consumer Law.

Distributional concerns are of great importance for social welfare and, thus, a legitimate concern of the legal system as a whole. But there are, I think, convincing reasons that allow us to think that a strong redistributive concern in favor of consumers and away from firms has no good claims to a proper place in a well-functioning consumer Law. The argument is twofold. First, the redistributive concern will largely be moot due to changes in contract prices: given that typically consumers and producers are in a contractual relationship, the attempt to redistribute through substantive rules favoring consumers will be to a large extent defeated by adjustments in price and other terms that will offset the intended redistribution²².

²¹ In the same sense, in addition to authors cited in note 1 above, Christian Kirchner, "Justifying Limits to Party Autonomy in the Internal Market – Mainly Consumer Protection", in Stefan Grundmann, Wolfgang Kerber, and Stephen Weatherill (Eds.), *Party Autonomy and the Role of Information in the Internal Market*, Walter de Gruyter, Berlin-New York (2001), p. 165, at p. 168.

²² See Richard Craswell, "Passing on the Costs of Legal Rules: Efficiency and Distribution in Buyer-Seller Relationships", 43 *Stanford Law Review* (1991), p. 361; David Weisbach, "Taxes and Torts in the Redistribution of Income", University of Chicago Law School, John M. Olin Program in Law & Economics, Working Paper No. 148 (2002). Not everyone agrees on this, of course: Ian Ramsay, "Consumer protection", in Peter Newman (editor), *The New Palgrave Dictionary of Economics and the Law*, vol. I, MacMillan, London, (1998), p. 413.

Second, even when the redistributive effort is not counteracted by contractual rearrangements, substantive legal rules are a more haphazard and less effective way to achieve this end than the tax and public transfers system²³.

The case for paternalism in consumer protection Law is, at first glance, and somewhat paradoxically, not as unconvincing in economic terms as the one favoring redistribution. Consumer protection Law, and the legal system more generally, can influence individuals' preferences and, thus, can change them in a way that is in the long-term interest of the individuals affected by the preference change. For instance, by imposing a certain level of consumers' information, rights, and protections, EC consumer Law could instill in European consumers a new preference for extended rights and, say, healthier consuming environments that might positively affect the well-being of those consumers in the long run, even if most of them did not have the preference in the beginning and were not willing to pay a price for the rights and protections afforded by the legal rules. From an economic standpoint this paternalistic legal intervention would be viewed favorably, as long as, as we had assumed for the sake of the argument, it increases social welfare. This is, of course, a purely theoretical possibility. Quite a different matter is how likely it is that the paternalistic motivation behind legislators, regulators and Courts in the field of consumer protection will actually be converted into consumers' welfare-enhancing policies and rules. In this respect, the affirmative is much more uncertain.

I am doubtful whether redistributive and paternalistic motivations can be traced in EC consumer protection Law. The grouping together in art. 95.3 EC Treaty of consumers' and workers' rights might be a hint towards the former motivation, and some wording in Directives' preambles and Community programs can also be interpreted as a hint towards the latter. In any case, from an economic perspective none of them provide a sound basis for EC consumer Law.

Imperfect information, on the contrary, constitutes a type of market failure able to provide a reasonable starting point for organizing our knowledge about the optimal role and likely effects of consumer protection legislation. Of course, we should not think that consumers' markets are the only markets in which informational imperfections are likely to loom large. Corporate Law, insurance Law and even general contract Law are areas in which economic

²³ Louis Kaplow and Steven Shavell, "Why the Legal System is Less Efficient Than the Income Tax in Redistributing Income", 23 *Journal of Legal Studies* (1994), p. 667; Louis Kaplow and Steven Shavell, "Should Legal Rules Favor the Poor? Clarifying the Role of Legal Rules and the Income Tax in Redistributing Income", 29 *Journal of Legal Studies* (2000), p. 821. The core of the argument is as follows: the use of taxes and transfers as redistributive mechanisms just creates a distortion, namely in the work-leisure trade-off. Substantive legal rules generate a double distortion: one, the same we have just described for taxes, the other, the inefficiency generated by a legal rule chosen not on its efficiency merits, but on its redistributive effectiveness. Again, some disagree with this gloomy view of legal rules as redistributive instruments: Christine Jolls, "Behavioral Analysis of Redistributive Legal Rules", in Cass Sunstein (editor), *Behavioral Law and Economics*, Cambridge University Press, Cambridge, (2000), p. 288. Su *Economics*, Cambridge University Press, Cambridge, (2000), p. 288; Chris William Sanchirico, "Taxes versus Legal Rules as Instruments for Equity: A More Equitable View", 29 *J. Legal Stud.* (2000), p. 797

models of imperfect information play a crucial role in understanding legal institutions and rules and predicting their relative performance in real-world markets.

On the other hand, we should not think that consumer markets are entirely dominated by imperfect information. Even if we abstract from legal constraints and requirements to this effect, the level of information provided by and at the disposal of market participants in consumers' markets is by no means negligible²⁴.

Consumers acquire information about relevant characteristics and variables affecting the transactions on goods and services by several means. In some cases, by direct observation²⁵. In others, by learning through repeat purchase and consumption²⁶. They can also get information about relevant aspects from third parties, be they people known to them, or independent private and public sources.

Producers themselves are major providers of information in consumers' markets. Through labels, product descriptions, and contract information firms communicate significant amounts of information to consumers on goods and services. Of course, advertising plays a key role in transmitting information on the existence, characteristics, prices and other determinants of market transactions. And not only so-called "informative" advertising has this positive informational role. Even advertising apparently devoid of any significant informational content (like celebrity endorsement of a product, say), is able to convey to consumers valuable signals about the level of quality or other important features of the transaction: advertising, and the reputation that is usually associated with it, are extremely powerful market mechanisms to effectively signal consistent levels of quality to consumers, particularly in markets for experience goods²⁷.

More surprisingly, market forces can, under some conditions, induce producers to disclose even unfavorable information to consumers or, more generally, to the other party in a prospective transaction. In what is one of the more striking results of the economics of information, it can be shown that, when the private information in possession of the seller is verifiable (that is, *ex post* it can be determined if disclosure of information was truthful), and the consumer knows that the seller has private information (though not its content, or else it would not be private information of the seller), the seller will voluntarily reveal the information even if it is unfavorable (for instance, that the quality of her product is below

²⁴ A recent review of instruments increasing information available to consumers in Thomas Wein, "Consumer Information Problems – Causes and Consequences", in Stefan Grundmann, Wolfgang Kerber, and Stephen Weatherill (Eds.), *Party Autonomy and the Role of Information in the Internal Market*, Walter de Gruyter, Berlin-New York (2001), p. 80.

²⁵ In these cases, economists speak of search goods or search characteristics, given that search can make consumers informed about them.

²⁶ In these cases, economists speak of experience goods or characteristics, because consumers will become informed after consuming the good. When even after consumption the relevant variables are not ascertainable by the consumer, economists speak of credence goods.

²⁷ On this warranty function of advertising, see Fernando Gomez, "The European Directive on Consumer Sales: An Economic Perspective", in Stefan Grundmann and C. Massimo Bianca (editors), *EU Sales Directive Commentary*, Hart Publishing Company, Oxford and Portland (OR), (2002) (forthcoming), and literature cited therein.

average). This unraveling result stems from the fact that, given the two assumptions just mentioned, consumers expects from all silent sellers the worst possible news concerning the content of the private information. Sellers whose private information is best would voluntarily disclose it, and so would set in motion a continuous process of revelation by the decreasingly good-news sellers, until only that with the worst private information (say, the worst quality) is left alone without disclosure. And consumers would actually observe that their expectations are met: only the worst private information remains undisclosed, and the rest is voluntarily revealed²⁸.

But even if the amount of information provided to consumers through market mechanisms is considerable, it is undeniable that in many circumstances and for many transactions in consumer markets the level of information is far from perfect, and that there is room for improvement in this lack of information through legal rules apt at the correction of informational market failures.

These informational market failures arise out of a broad range of factors: First, some market participants might engage in fraudulent and deceptive practices, inducing inaccurate representations in consumers that cause distortions in their decisions and behavior. Maybe due to the uncontroversial characterization of fraud, misrepresentation and deception as undesirable phenomena, the fact is that the role of consumer protection Law in deterring such inefficient market practices has not been fully appreciated. Probably the unscrupulous fly-by-night producer is the major source of consumers' misinformation and overall harm, and the efforts to deter this type of seller are among the most valuable in the whole enterprise of consumer protection policy²⁹. This explains and justifies the existence of rules against misleading advertising³⁰, as well as strict information and contract formation

²⁸ The unravelling result was developed by Sanford Grossman and Oliver Hart, "Disclosure Laws and Takeover Bids", 35 *Journal of Finance* (1980), p. 323; Paul Milgrom, "Good News and Bad News: Representation Theorems and Applications", 12 *Bell Journal of Economics* (1981), p. 380; and Sanford Grossman, "The Informational Role of Warranties and Private Disclosure of Product Quality", 24 *Journal of Law and Economics* (1981), p. 461. A less technical presentation with applications to various fields of the Law, in Douglas Baird, Robert Gertner and Randall Picker, *Game Theory and the Law*, Harvard University Press, Cambridge (MA), (1994), p. 89 and following; Robert Gertner, "Disclosure and unravelling", in Peter Newman (editor), *The New Palgrave Dictionary of Economics and the Law*, vol. I, MacMillan, London, (1998), p. 605. Empirical studies have found clear evidence of voluntary disclosure and unravelling. For instance, Alan Mathios, "The Impact of Mandatory Disclosure Laws on Product Choices: An Analysis of the Salad Dressing Market", 43 *Journal of Law and Economics* (2000), p. 658-660, shows how the unobservable information (fat content) concerning salad dressings is subject (albeit not completely) to the unraveling effect, by which almost all of the low-fat producers voluntarily disclose the fat content whereas the high-fat ones remain silent.

²⁹ By the way, here we can observe some discrepancy between the conditions and outcomes of competitive market and those of adequate consumer protection: Rogue sellers are more likely to be operating in a market when there are low -or virtually none- barriers to entry, when there are many sellers, and when the rate of entry and exit in the market from the producer's side is high. All these conditions are typical features of a competitive market structure. See Gillian K. Hadfield, Robert Howse, and Michael J. Trebilcock, "Information-Based Principles for Rethinking Consumer Protection Policy", 21 *Journal of Consumer Policy* (1998), p. 153, p. 155.

³⁰ Directive 84/450/EEC of 10 September 1984 on misleading advertisement, and Directive 97/55/EC of 6 October 1997, concerning misleading advertising so as to include comparative advertising. Needless to say, this does not make the determination of when an ad is deceptive or misleading an easy task. Issues such as context, implied claims, heterogeneity of consumers, and existence of more informative

requirements in those consumers' markets and contractual practices more likely to have a high proportion of small and quickly exiting firms, such as door-to-door sales, distance sales, and electronic sales³¹.

Consumers' lack of information can be the result of well documented phenomena³² in consumers' behavior such as bounded rationality (limited capacity to acquire and process information)³³, over optimism, use of cognitive heuristics (hindsight bias, excessive reliance on easily available data, excessive representativeness of small samples, too little weight of future and uncertain events, etc), and rational ignorance (if acquiring information is –even minimally- costly for the consumer, but having the information would not change neither the terms of the transaction nor future use, the consumer may rationally forgo the acquisition of information and prefer to remain ignorant on a relevant variable)³⁴.

Consumers' ignorance due to all these factors is hard to ameliorate. Firms do have some incentive to educate and inform consumers so that those problems are less acute in many cases. But the market incentives for firms do not reach the level of the socially appropriate incentives to educate and inform consumers. Each single firm would not be able to internalize all the gain from the increased consumers' information, so her incentive to bring it about will be insufficient compared to the social gains from the increase in consumers' information. So the market ³⁵will not by itself provide the optimal amount of education and information to overcome those factors affecting consumers' ignorance.

Consumer Law can to an extent provide partial remedy in some contexts, particularly through disclosure requirements and the creation and imposition of a standardized system

alternatives are relevant to this sort of inquiry. A detailed analysis of these and other issues for advertising regulation, in Richard Craswell, "Interpreting Deceptive Advertising", 65 *Boston University Law Review* (1985), p. 658; Richard Craswell, "Regulating Deceptive Advertising: The Role of Cost-benefit Analysis", 64 *Southern California Law Review* (1991), p. 549.

³¹ Directive 85/577/EEC of 20 December 1985, on contracts negotiated away from business premises; Directive 97/7/EC of 20 May 1997, on the protection of consumers in respect of distance contracts; Directive 2000/31/EC of 8 June 2000, on electronic commerce.

³² See Melvin Aron Eisenberg, "Cognition and contract", in Peter Newman (editor), *The New Palgrave Dictionary of Economics and the Law*, vol. I, MacMillan, London, (1998), p. 282; Cass Sunstein (editor), *Behavioral Law and Economics*, Cambridge University Press, Cambridge, (2000).

³³ Moreover, bounded rationality makes the appeal of deceptive and misleading advertising higher for some producers: see Matthew Nagler, "Rather Bait than Switch: Deceptive Advertising with Bounded Consumer Rationality", 51 *Journal of Public Economics* (1993), p. 359. And surveys of advertisers show that legal constraints are the most important factor influencing decision-making about advertising content and policy: Joel Davis, "Ethics in Advertising Decisionmaking: Implications for Reducing the Incidence of Deceptive Advertising", 28 *Journal of Consumer Affairs* (1994), p. 380.

³⁴ The most notable example of this problem in consumer contracts arises in the context of standard form contracts: reading and understanding the standard terms is costly for the consumer –in time and effort-, and given that the terms are not subject to negotiation, the consumer will usually opt for not even starting to read the forms.

³⁵ By the way, here again a monopoly market structure will arguably approximate better than a competitive one the optimal provision of information, given that the monopolist can internalize more in terms of profits the gains from increased information. The same applies to rational ignorance: competitive firms are more likely to exploit consumers' rational ignorance than monopolists, because competitive pressures can unleash a "race to the bottom" for those variables that the typical consumer rationally decides to ignore.

of measuring and expressing one or more of the variables relevant to the transaction. Probably the best example of this kind of legal intervention is the standardized annual percentage rate that Directive 87/102/EEC of 22 December 1986 on consumer credit (modified by Directives 90/88 and 98/7) imposes as a disclosure requirement for consumer credit contracts. Here, the most (but not the only) relevant element of the transaction needs to be expressly and noticeably communicated in a homogenous and –at least relatively– easily computable and user-friendly way for consumers, so these will be more aware of the relevant variable and the possibility of shopping around for more attractive credit terms is significantly enhanced³⁶. Mandatory and standardized labeling and information disclosure are also common concerning health and safety factors, and experimental and empirical studies have shown them to have had a positive impact on welfare-enhancing consumer choices in the relevant markets³⁷. Additionally, cooling-off periods allowing the consumer to cancel the transaction during a limited period after it was agreed³⁸, can be understood as a way of reducing the impact of bounded rationality and cognitive deficiencies in those consumer transactions in which these problems might seem more serious³⁹.

³⁶ Standardized disclosure obligations might pose some problems of its own, that might have an economic impact: they can induce producers to concentrate quality efforts on the variables included in the standard, at the expense of others left out of it, that may be also important to consumers, and the required disclosure may displace other information that the producer would have conveyed, and might also have been informative to consumers. See, Howard Beales, Richard Craswell, and Steven Salop, “The Efficient Regulation of Consumer Information”, 24 *Journal of Law and Economics* (1981), p. 523 and following. Regarding the specific standardized disclosure requirement in consumer credit contracts, some have criticized this from an economic perspective, stressing the increase in compliance and litigation costs, the negative effects on credit collection terms and customer service (variables not included in the standard disclosure), and the fact that only already well-informed and wealthy borrowers are likely to benefit from it. See Richard Posner, *Economic Analysis of Law*, 5th edition, Aspen Publishers, New York, (1998), p. 408; Richard Hynes and Eric Posner, “The Law and Economics of Consumer Finance”, , 4 *American Law and Economics Review* (2002), p. 194-195. Standardized information on contract terms, however, can also be efficient on account of network externalities (the addition of new users increases the utility derived by existing users).

³⁷ Christine Moorman, “A Quasi Experiment to Assess the Consumer and Informational Determinants of Nutrition Information Processing Activities: The Case of the Nutrition Labeling and Education Act”, 15 *Journal of Public Policy and Marketing* (1996), p. 28; Alan Mathios, “The Impact of Mandatory Disclosure Laws on Product Choices: An Analysis of the Salad Dressing Market”, 43 *Journal of Law and Economics* (2000), p. 660.

³⁸ Directive 85/577/EEC of 20 December 1985, on contracts negotiated away from business premises; Directive 94/47/EC of 26 October 1994, on time-sharing; Directive 97/7/EC of 20 May 1997, on the protection of consumers in respect of distance contracts.

³⁹ Pamaria Rekaiti and Roger van den Bergh, “Cooling-Off Periods in the Consumer Laws of the EC Member States: A Comparative Law and Economics Approach”, 23 *Journal of Consumer Policy* (2000), p. 371, at p. 374 and following, and 385 and following, argue that cooling-off periods, particularly those introduced by EC consumer protection legislation, are potential remedies for irrational behavior, situational monopoly and informational asymmetries. Some, however, doubt the effective impact of those measures, the reason lying in the prediction that few consumers would exercise a right of cancellation that requires them to admit to themselves that they acted as suckers by signing the contract in the first place: See Ian Ramsay, “Consumer protection”, in Peter Newman (editor), *The New Palgrave Dictionary of Economics and the Law*, vol. I, MacMillan, London, (1998), p. 412. Others do not only consider them irrelevant, but criticize them as raising *ex post* opportunism by consumers: Hans-Peter Schwintowski, “Contractual Rules Concerning the Marketing of Goods and Services – Requirements of Form and Content versus Private Autonomy”, in Stefan Grundmann, Wolfgang Kerber, and Stephen Weatherill (Eds.), *Party Autonomy and the Role of Information in the Internal Market*, Walter de Gruyter, Berlin-New York (2001), p.331, at p. 346.

This leads to another source of consumers' lack of information, namely search costs. If search costs are relatively high, consumers will not be informed and so the terms of the transaction (including price, even when the market is competitive) might not be optimal⁴⁰. Disclosure requirements and standardized informative messages, such as the one referred to in the previous paragraph, serve also to reduce search costs in various consumer markets and, thus, to improve the functioning of these markets.

The preceding considerations should not induce us to think that the imperfect information rationale sets an insurmountable boundary to the kind of rules that an economically oriented consumer protection Law would be allowed to use. In particular, the tools of consumer law can include not only information-enhancing measures, but also disclosure and standardization requirements, and prevention of deception and fraud. Additionally, the characteristics of some informational problems may (but only "may") suggest that mandatory regulation of some contractual terms is the best cure for such informational market failures. We have mentioned the case of rational ignorance regarding standard form contracts. Information disclosure and facilitating rules might be insufficient, given the very nature of the lack of information (even a minuscule information cost would make consumers rationally and intelligently decide not to read the fine print). And the race to the bottom in the quality of contract terms that can ensue from this set of conditions might call for legal regulation of a minimum level of quality or bundle of consumer rights. That is precisely what Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts does in Article 3 and the Annex. Of course, it is debatable whether the Directive has achieved an optimal balance in the determination of the required quality of contract terms, and even if any legislator or Court can aspire to it, but economic theory does not in itself exclude the use of mandatory regulation in this type of setting.

Moreover, if the disclosure legally required would lead to complex revelation of information by producers, and this complexity would significantly raise information-processing costs for consumers, an outright ban on a certain product or service may (but only "may") be preferable on efficiency grounds. This would be the case if the reduction in informational costs outweighs the costs that both producers (loss of profit) and consumers (loss of enhanced product choice or variety) incur as a consequence of the prohibition⁴¹.

Similarly, in circumstances in which the asymmetry in information does not affect the consumer, but the seller, a case for mandatory intervention may (but only "may") be made on pure efficiency grounds. Here, it is the consumer who has some piece of private

⁴⁰ For optimality in markets with positive search costs, however, it is not necessary that all buyers shop around. When producers cannot distinguish consumers who have searched for contract terms from those who haven't, and when the proportion of searchers is large enough (but not 100%), the terms will be optimal, because producers would prefer to sell to all consumers rather than only to non-searchers. See Alan Schwartz and Louis Wilde, "Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis", 127 *University of Pennsylvania Law Review* (1979), p. 630; Alan Schwartz and Louis Wilde, "Imperfect Information in Markets for Contract Terms: The Examples of Warranties and Security Interests", 69 *Virginia Law Review* (1983), p. 1387.

⁴¹ See Gillian K. Hadfield, Robert Howse, and Michael J. Trebilcock, "Information-Based Principles for Rethinking Consumer Protection Policy", 21 *Journal of Consumer Policy* (1998), p. 159.

information that the producer cannot observe. This is particularly likely in credit markets, in which the professional creditor cannot usually observe the likelihood or the willingness of the consumer to pay back the credit. Imperfect information may give rise here to the use of harsh contract terms or securities that act as signal of belonging to the “good” credit-worthy type of consumer, and not to the bad type. Even if some of these signals are too crude and undesirable for the joint welfare of market participants, they may persist over time. Legal rules setting limits to those terms (for instance, personal bankruptcy protection, limits to repossession, assets excluded from forfeiture, and the like) may (but only “may”) be efficient under some of these circumstances⁴².

All these matters, however, have been –wisely, in my view– left outside the scope of the Directive on consumer credit (with the partial exception of limits to third-party rights and assignment, which is theoretically akin to the other limits), and referred to the Laws of the Member States. In fact, the set of substantive (that is, not pertaining to increased levels of information) consumer rights under this Directive allows for extensive freedom of the Member States to implement the quite general principles sketched to that effect, in contrast with the detailed regulation of the disclosure requirements that the same Directive contains.

6. The weighing of competitive gains in consumer protection Law

The arguments presented in the previous sections lead support to the substantial independence of the economic function of consumer protection Law from that of competition Law, and to the need to keep distinct the approach of each of these fields of the Law. Despite this, there are cases in which the competitive consequences of consumer protection issues are significant and should receive their due amount of attention. I will now provide an example of what I mean by this joint balance of consumer protection and competitive issues.

The area of advertising is particularly likely to give rise to issues of barriers to entry established by dominant firms in order to deter entry by potential new entrant firms. Heavy advertising expenditures, especially if associated with strong trademarks, serve as goodwill and brand loyalty multipliers, and can constitute barriers that entrants will have difficulty in overcoming. One way in which this may happen is through aggressive advertising campaigns that make use of comparison with the established firm, or stress the advantages of the entrants (in price or in other relevant dimension) over the incumbent. In the enforcement of consumer protection rules in advertising one should take into account that in order to surmount the advertising barriers erected by the incumbent firm, the entrants might need some greater leeway as to the aggressiveness of comparative advertising and to the level of substantiation of the claims contained in their advertisement. In the end, entry by new firms would benefit consumers through increased output and

⁴² A full economic discussion of these measures can be found in Richard Hynes and Eric Posner, “The Law and Economics of Consumer Finance” 4 *American Law and Economics Review* (2002), p. 168.

reduced prices, so it is efficient that in the enforcement of consumer protection rules on advertising, regulators and Courts take into account the future competitive gains of the advertising campaign - especially when it is the incumbent who challenges it on charges of being misleading.

Other examples are possible (for instance, some contract terms like exclusivity clauses and contractual damage clauses might also eventually serve to raise barriers against potential competitors⁴³), but the point is clear. Competitive gains are real social gains, and they should be weighted when one is designing, interpreting and implementing consumer protection Law. But this should not mean that in this process we take a side road and forget what I believe is the proper role and economic rationale for consumer Law, and specially EC consumer protection Law, which is to address the problems of imperfect information in consumer markets. The challenges that EC consumer protection legislation faces in building a consistent framework that would serve to increase efficiency in consumer markets that are still largely (though certainly not always to the same extent) fragmented by national, cultural, and linguistic barriers, are, to be sure, enormous. To burden EC consumer policy with the extra task of increasing the amount of competition in European consumer markets does not seem to me a sound policy prescription. It is a task which this branch of EC Law (in fact, private and public Laws of the Member States also) is ill-equipped to accomplish successfully.

⁴³ Philippe Aghion and Patrick Bolton, "Contracts as Barriers to Entry", 77 *American Economic Review* (1987), p. 388.