Half-a-Cup Better than None: A Pragmatic Approach to Preventing the Abuse of Financial Consumers

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Abstract

The traditional view of corporate law asserts that the corporation serves society via the satisfaction of consumers' revealed preferences, which dictate the ultimate allocation of resources contributed by corporate investors, workers, and managers. Social psychology has long taught, and legal analysts now often concede, that revealed preference is an unreliable guide to social welfare. Human beings have cognitive limits that may be routinely exploited in a variety of ways, including the methods in which decisions are framed. The recognition that there are easily manipulable "bounds" on rationality, self-interest, and free will severely weakens corporate law's familiar claims: if corporations are creating the very preferences they satisfy, the foxes are not only guarding the hen houses, they are running the farm. Still, the problem of bounded consumer rationality continues to be viewed as a matter for external regulation rather than as a reason for rethinking some of the givens of corporate governance. This Article attempts to explain why the Dodd-Frank Act's creation of the Consumer Financial Protection Bureau provides an opportunity to revisit the characterization of bounded consumer rationality as a problem extrinsic to corporate law. The punch line is that the Bureau has both broad regulatory and general educational mandates that could justify a variety of reforms. One such reform recommended in this Article is the creation of a process pursuant to which the providers of at least some financial consumer goods could be certified as subscribing to corporate decisionmaking practices designed to be less injurious to consumer interests than the usual shareholder primacy model historically has dictated.

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April 2013 Vol. 81 No. 3

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INTRODUCTION

Why take out a mortgage you cannot afford?[1] Why borrow money for college from a private lender when lower-cost federal loans

[1] *See* Elizabeth Warren, *Product Safety Regulation as a Model for Financial Services Reg-*

are available?[2] Why accept a loan from a "payday" lender who charges interest in the triple digits?[3] For that matter, why incur debt at all for such items as the latest iteration of the iPad or iPhone when the version you already have still works?

The traditional view of corporate law asserts that the corporation serves society via the satisfaction of consumers' revealed preferences, which dictate the most efficient allocation of resources contributed by corporate investors, workers, and managers.[4] Social psychology has long taught, however, and legal analysts sometimes now concede, that revealed preference is an unreliable guide to social welfare. Human beings have cognitive limits that routinely may be exploited in a variety of ways, including the manner in which decisions are framed.[5] The recognition that there are easily manipulable "bounds" on rationality, self-interest, and free will severely weakens corporate law's familiar claims: if corporations are creating the very preferences they satisfy, the foxes are not only guarding the hen houses, they are running the farm.

Unsurprisingly, corporate America for decades has been paying psychologists and other social scientists and has relied on their insights in devising products and marketing strategies.[6] The result is a marketplace in which a variety of unnecessary and sometimes even harmful products jostle for position before the eyes of a population struggling to make ends meet. In some instances, these products are tangible consumption items. In others, they are the financial vehicles that facilitate consumption.

Still, the problem of bounded consumer rationality continues to be viewed as a matter for external regulation rather than as a reason

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ulation, 42 J. CONSUMER AFF. 452, 452 (2008) (describing the chance of a mortgage "putting your family out on the street" as one in five in 2008).

2 *See* MATTHEW REED ET AL., INST. FOR COLL. ACCESS & SUCCESS, CRITICAL CHOICES: HOW COLLEGES CAN HELP STUDENTS AND FAMILIES MAKE BETTER DECISIONS ABOUT PRIVATE LOANS 2 (2011), http://projectonstudentdebt.org/files/pub/critical_choices.pdf (noting that the majority of undergraduate borrowers do not exhaust lower-cost federal alternatives before turning to private lenders).

3 *See Hearing Your Stories on Payday Lending*, CONSUMER FIN. PROT. BUREAU BLOG (Jan. 19, 2012) http://www.consumerfinance.gov/blog/hearing-your-stories-on-payday-lending/ (noting that the annual percentage rate on some payday loans can exceed 400%).

4 *See infra* notes 83, 132–38 and accompanying text.

5 *See infra* notes 88–102 and accompanying text. Professor David Yosifon argues that even a model recognizing that rationality is bounded falls short of reflecting the situational nature of human cognition and decisionmaking. *See* David G. Yosifon, *The Consumer Interest in Corporate Law*, 43 U.C. DAVIS L. REV. 253, 261–81 (2009); *see also infra* notes 105–09 and accompanying text (expanding on this theme).

6 *See infra* note 101.

for rethinking some of the givens of corporate governance. This conceptualization may well constitute resignation to the often-described race to the bottom by the states that provide corporate charters. In other words, competition for jurisdictionally-specific incorporation business is viewed as inevitably favoring a model of short-term shareholder primacy that as a practical matter liberates managers to engage in self-preferring decisionmaking.[7] On the other hand, because corporations aspiring to any significant size seek consumers nationwide, the same competitive incentive to relax regulation should not necessarily apply to the design of state consumer protection plans, and in no way should apply to the federal design of such a regime.

This Article attempts to explain why the creation of the Consumer Financial Protection Bureau ("CFPB" or "Bureau") by the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 ("Dodd-Frank Act")[8] provides an opportunity to revisit the characterization of bounded consumer rationality as a problem purely extrinsic to corporate law. The punch line is that the Bureau has both broad regulatory and general educational mandates that could justify a variety of reforms. Among other powers, it possesses the authority to prevent unfair, deceptive, or abusive acts or practices directed at financial consumers.[9] The terms "unfair" and "deceptive" previously were used in legislative directives to other regulatory authorities and have a fairly well-developed jurisprudence largely focused on timely and accurate disclosure.[10] The term "abusive" is less well understood, however, and has been declared "puzzling" by the Bureau's new head.[11] Although it easily might be the case that the CFPB's power to prevent abusive practices extends to the regulation of financial products on their merits—at least vis-à-vis some types of consumers—this Article makes a more limited claim: that the CFPB should consider

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7 *See generally* Stephen M. Bainbridge, *Why the North Dakota Publicly Traded Corporations Act Will Fail*, 84 N.D. L. REV. 1043, 1043, 1045 (2008) (noting that adherents to the "race to the bottom" theory argue that, "because . . . corporate managers . . . decide on the state of incorporation," states like "Delaware cater[ ] to management, allowing them to exploit shareholders" and arguing that a North Dakota statute meant to alter that dynamic "will fail").

8 Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, tit. X, 124 Stat. 1375, 1955 (2010).

9 *See infra* Part II.B.

10 *See infra* Part II.B.2.

11 Dave Clarke, *US Abusive Lending Bar Likely Set High—Cordray*, THOMSON REUTERS NEWS & INSIGHT: SECURITIES LAW (Jan. 24, 2012), http://newsandinsight.thomsonreuters.com/Securities/News/2012/01_-_January/US_abusive_lending_bar_likely_set_high-Cordray/ (quoting the CFPB's Director, Richard Cordray, as saying that "an abusive practice . . . would have to be a pretty outrageous practice"); *see also infra* Part II.B.3 (discussing the "abusive" standard).

adopting a process pursuant to which the providers of at least some financial products and services could be certified as subscribing to corporate decisionmaking practices designed to be less injurious to consumer interests than the usual shareholder primacy model historically has dictated. One of these practices would involve calling on the directors of companies providing financial products to declare their individual opinions about the advisability of those products for consumers in certain identified circumstances. At the least, this measure would provide consumers with useful information. At best, it might influence the actual design of some of the products offered.

Although direct federal tinkering in corporate governance has long been troubling in some academic quarters,[12] the proposal advanced above is disclosure-based and thus fits fairly neatly into the limited, but expanding, role claimed by the federal government in recent years. Part I of this Article provides a brief overview of the customary separation of corporate governance and external regulation, as well as of the traditional limitations on the federal role vis-à-vis the former. Part II contains background on the CFPB and its powers. Part III discusses the literature regarding limits on rationality and briefly explores the role of corporate structure in exploiting those limits. Part IV elucidates the proposal that the CFPB involve itself in certifying good governance practices. Part V critiques the proposal from the viewpoints of several schools of legal analysis.

I. Background

A. *Corporate Law v. "Other"*

The concept of "corporate law" generally "sweeps broadly to include any laws significant to the formation or maintenance of the relationships among traditionally recognized corporate stakeholders," as well as the laws preventing at least some of those stakeholders from incurring liability to those outside the corporation.[13] It does not, therefore, "cover subjects such as collective bargaining or employee benefits, simply because, as a matter of tradition," employees are not characterized as stakeholders.[14] The "plethora of laws relating to con-

12 *See infra* Part I.B.

13 Theresa A. Gabaldon, *Feminism, Fairness, and Fiduciary Duty in Corporate and Securities Law*, 5 Tex. J. Women & L. 1, 15–16 (1995) (discussing the division of corporate law topics).

14 *Id.* at 15. *Compare* Jonathan R. Macey, *An Economic Analysis of the Various Rationales for Making Shareholders the Exclusive Beneficiaries of Corporate Fiduciary Duties*, 21 Stetson L. Rev. 23, 26–36 (1991) (describing two arguments for treating shareholders as the sole constituency to which a corporation's directors and officers owe a fiduciary duty), *with* Marleen A. O'Connor, *Restructuring the Corporation's Nexus of Contracts: Recognizing a Fidu-*

sumers, pollution control, etc., [are] excluded for similar reasons."[15] This begs the question whether employees, consumers, trees, or polar bears should be recognized as corporate stakeholders as a normative matter; however, as a descriptive matter, it is clear that they are not.[16]

One consequence of the balkanization of legal subject matters is that arguable contradictions arise. For instance, the late twentieth and early twenty-first centuries have seen both legislative and popular explosions of interest in limits on liability for the owners of businesses as well as for their managers; limits on the fiduciary duties of partners in partnerships and members of limited liability companies thus have matched the development and utilization of new forms of limited liability entities, while the directors of corporations have been protected by statutes and provisions in articles of incorporation exculpating them from monetary liability for a variety of defalcations.[17] What have not matched are developments in a number of laws having significance for the liability of the enterprises themselves. At the state level, these include a wide range of consumer protection devices such as "'plain language' laws," mandatory cooling-off periods, and prohibition of various substantive contractual terms.[18] At the federal level, these developments most recently include the provisions of Dodd-Frank.

B. The Federal Camel and the Corporate Tent

The power to regulate interstate commerce is notoriously broad, and few would find nationwide protection of consumer interests particularly controversial, much less beyond the power of the federal government to adopt.[19] Federal intervention in corporate governance, however, has traditionally struck a different chord. Although the prevailing view appears to be that even comprehensive federalization of

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ciary Duty to Protect Displaced Workers, 69 N.C. L. REV. 1189, 1258–60 (1991) (describing how a lack of fiduciary duty owed to displaced employees could lead to increased regulation and decreased stability).

15 Gabaldon, *supra* note 13, at 16.

16 *But see infra* Part V.B.3 (discussing the team production model of corporate law, which allows directors to consider the inputs of a larger number of stakeholders).

17 *See generally* Theresa Gabaldon, *Experiencing Limited Liability: On Insularity and Inbreeding in Corporate Law*, *in* PROGRESSIVE CORPORATE LAW 111 (Lawrence E. Mitchell ed., 1995) (discussing the contradiction between the twentieth-century developments of limited liability entities and expanding enterprise liability).

18 *Id.* at 116.

19 *See* Jack M. Balkin, *Commerce*, 109 MICH. L. REV. 1, 5–6 (2010) (advocating a broad interpretation of the Commerce Clause in line with the Constitution's structural principles).

corporate law would be legal,[20] there has been extended expostulation at every federal incursion into the territory,[21] up to and including Dodd-Frank's relatively toothless "say on pay" requirements, which permit shareholders of publicly held companies a triennial advisory vote on executive compensation.[22] Opposition to federal involvement in internal corporate affairs is partly justified by enthusiasm for state authority as a general matter, as well as by the argument that state competition for corporate charters will both provide would-be incorporators with choices and lead to the development of more efficient corporate rules.[23] As discussed below, the relatively new school of cultural cognition teaches that reasoned debate is unlikely to resolve what basically are political questions;[24] instead, progress must be based on solutions that appeal to multiple and competing world views.[25] In light of this wisdom, this Article stops short of calling for any full-fledged federal attempt to turn consumers into corporate stakeholders. Rather, it works within the framework of more standard consumer protection devices.

II. The Consumer Financial Protection Bureau

A. *Creation and Mandate: "And we are going to stand up this bureau and make sure it is doing the right thing for middle-class families all across the country."*[26]

Title X of the Dodd-Frank Act vested the CFPB with the responsibility for regulating consumer financial products[27]—or, as President

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20 *See* E. Norman Veasey, *What Would Madison Think? The Irony of the Twists and Turns of Federalism*, 34 Del. J. Corp. L. 35, 42–43 (2009) (discussing the interaction of federal and state law governing corporations and recognizing that Congress may be able to supplant state corporate law).

21 *See, e.g.*, Lucian A. Bebchuk & Assaf Hamdani, *Federal Corporate Law: Lessons from History*, 106 Colum. L. Rev. 1793, 1827–28 (2006) (discussing and rebutting criticisms of federal intervention into corporate law).

22 Randall S. Thomas, Alan R. Palmiter & James F. Cotter, *Dodd-Frank's Say on Pay: Will It Lead to a Greater Role for Shareholders in Corporate Governance?*, 97 Cornell L. Rev. 1213, 1226–36 (2012) (discussing the debate preceding Dodd-Frank's say on pay provision).

23 *See* Jonathan R. Macey & Geoffrey P. Miller, *Toward an Interest-Group Theory of Delaware Corporate Law*, 65 Tex. L. Rev. 469, 470 (1987) (giving an overview of the "corporate federalist theory").

24 *See infra* Part V.D.

25 *See infra* notes 185–88 and accompanying text.

26 President Barack Obama, Remarks by the President in Nominating Richard Cordray as Director of the Consumer Financial Protection Bureau (July 18, 2011), *available at* http://www.whitehouse.gov/the-press-office/2011/07/18/remarks-president-nominating-richard-cordray-director-consumer-financial.

27 *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1011(a), 124 Stat. 1375, 1964 (2010) (describing the CFPB's duties).

Obama put it, "looking out for people as they interact with the financial system."[28] According to section 1021 of the new legislation, the CFPB is to "implement and, where applicable, enforce Federal consumer financial law consistently for the purpose of ensuring that all consumers have access to markets for consumer financial products and services and that markets for consumer financial products and services are fair, transparent, and competitive."[29] In furtherance of this mandate, many preexisting federal laws relating to the protection of financial consumers were brought under CFPB jurisdiction.[30] In addition, the Bureau was given broad authority to prevent "unfair, deceptive, or abusive act[s] or practice[s] . . . in connection with any transaction with a consumer for a consumer financial product or service."[31]

The Bureau is to engage in "supervision" of many providers of financial products or services to determine both compliance with relevant law and the amount of risk posed by such providers to consumers: subject to certain limits on size, depository and nondepository providers alike are within CFPB supervisory authority.[32] "Supervision" entails both requiring reports and conducting examinations.[33] The Bureau is expected to conduct regular examinations of regulated entities and is empowered to conduct reviews of single or multiple entities focusing on particular issues of concern.[34] It is specifically authorized to collect and make public information from "covered per-

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28 President Barack Obama, Remarks on Signing the Dodd-Frank Wall Street Reform and Consumer Protection Act (July 21, 2010), *available at* http://www.gpo.gov/fdsys/pkg/DCPD-2010 00617/pdf/DCPD-201000617.pdf.

29 Dodd-Frank Act § 1021(a), 124 Stat. at 1979–80.

30 As enumerated in section 1002(12) of the Dodd-Frank Act, these include the Alternative Mortgage Transaction Parity Act of 1982, the Consumer Leasing Act of 1976, the Equal Credit Opportunity Act, the Fair Credit Billing Act, the Home Owners Protection Act of 1998, the Fair Debt Collection Practices Act, the Home Mortgage Disclosure Act of 1975, the Home Ownership and Equity Protection Act of 1994, the Real Estate Settlement Procedures Act of 1974, the S.A.F.E. Mortgage Licensing Act of 2008, the Truth in Lending Act, the Truth in Savings Act, the Interstate Land Sales Full Disclosure Act, most of the Electronic Fund Transfer Act, most of the Fair Credit Reporting Act, and certain portions of the Federal Deposit Insurance Act, of the Gramm-Leach-Bliley Act, and of the Omnibus Appropriations Act of 2009. *Id.* § 1002(12), 124 Stat. at 1957.

31 *Id.* § 1031(a), 124 Stat. at 2005. "Consumer financial product or service" is defined at *id.* §§ 1002(5), (15), 124 Stat. at 1956–60.

32 *Id.* § 1024, 124 Stat. at 1987 (nondepository); *id.* § 1025, 124 Stat. at 1990 (depository institutions with at least $10 billion in assets).

33 *Id.* § 1024(b), 124 Stat. at 1987; *id.* § 1025(b)(1), 124 Stat. at 1990.

34 CONSUMER FIN. PROT. BUREAU, SUPERVISION AND EXAMINATION MANUAL Overview 6 (2011), http://www.consumerfinance.gov/wp-content/themes/cfpb_theme/images/supervision_examination_manual_11211.pdf.

sons."[35] A "covered person" is a provider of consumer financial goods or services,[36] but the term also includes affiliates acting as service providers to such persons.[37] An "affiliate" is any person who "controls, is controlled by, or is under common control with another person."[38]

B. The Power to Prevent Unfair, Deceptive, or Abusive Acts or Practices

1. Legislation

As noted above, the CFPB received a grant of authority with respect to unfair, deceptive, or abusive acts or practices (sometimes referred to as "UDAAP"). The precise language permits the CFPB "to prevent a covered person or service provider from committing or engaging in an unfair, deceptive, or abusive act or practice under Federal law in connection with any transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial product or service."[39] The terms "unfair" and "deceptive" derived from preexisting and oft-exercised powers possessed by other authorities, including the Federal Trade Commission ("FTC"),[40] the Federal Reserve Board, the Office of Thrift Supervision, and the National Credit Union Administration.[41] The term "deceptive" evidently was believed to be well enough understood so as to require no legislative gloss.[42] Section 1031(c) does, however, carefully place limits on the CFPB's ability to define an act or practice as "unfair":

> (1) IN GENERAL.—The Bureau shall have no authority under this section to declare an act or practice in connection with a transaction with a consumer for a consumer financial product or service, or the offering of a consumer financial

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35 Dodd-Frank Act § 1022(c)(3)(B), 124 Stat. at 1982 (authorizing the Bureau to make public its reports, subject to privacy exceptions); *id.* § 1022(c)(4), 124 Stat. at 1982 (authorizing the Bureau to gather information from "covered persons and service providers").

36 *Id.* § 1002(6)(A), 124 Stat. at 1956.

37 *Id.* § 1002(6)(B), 124 Stat. at 1956.

38 *Id.* § 1002(1), 124 Stat. at 1955.

39 *Id.* § 1031(a), 124 Stat. at 2005.

40 *See* John E. Villafranco & Kristin A. McPartland, *New Agency, New Authority: An Update on the Consumer Financial Protection Bureau*, ANTITRUST SOURCE, Feb. 2012, at 1, 5 (noting that the CFPB's Supervision and Examination Manual's "guidance on unfair and deceptive acts and practices will be familiar to FTC practitioners").

41 *See* Gail Hillebrand, *The Consumer Financial Protection Bureau: Title X of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010*, 8 BERKELEY BUS. L.J. 219, 221 (2011) (noting that the CFPB borrows some of its statutory standards from these agencies).

42 *See id.* at 223 (noting that "[t]here is no [statutory] definition of deceptive but perhaps we will see some rules that will help to define that").

> product or service, to be unlawful on the grounds that such act or practice is unfair, unless the Bureau has a reasonable basis to conclude that—
>
> (A) the act or practice causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers; and
>
> (B) such substantial injury is not outweighed by countervailing benefits to consumers or to competition.
>
> (2) CONSIDERATION OF PUBLIC POLICIES.—In determining whether an act or practice is unfair, the Bureau may consider established public policies as evidence to be considered with all other evidence. Such public policy considerations may not serve as a primary basis for such determination.[43]

Section 1031(d) expresses the congressional view that the concept of "abusive" also should be subject to constraint:

> (d) ABUSIVE.—The Bureau shall have no authority under this section to declare an act or practice abusive in connection with the provision of a consumer financial product or service, unless the act or practice—
>
> (1) materially interferes with the ability of a consumer to understand a term or condition of a consumer financial product or service; or
>
> (2) takes unreasonable advantage of—
>
> (A) a lack of understanding on the part of the consumer of the material risks, costs, or conditions of the product or service;
>
> (B) the inability of the consumer to protect the interests of the consumer in selecting or using a consumer financial product or service; or
>
> (C) the reasonable reliance by the consumer on a covered person to act in the interests of the consumer.[44]

Even given this constraint, it would appear that Congress believed that it was accomplishing something by granting the Bureau the authority to prevent abusive acts and practices in addition to those that are unfair or deceptive. Exactly what that "something" was is a little less obvious. One would think, after all, that interfering with consumer understanding would be deceptive and that taking unreasonable advantage of consumers would be unfair. The intended contribution of the new term may be informed, however, by an

43 Dodd-Frank Act § 1031(c), 124 Stat. at 2006.

44 *Id.* § 1031(d), 124 Stat. at 2006.

understanding of the traditional (and continuing) constructions of the older terms.

2. *The Traditional (and Continuing) Constructions of "Unfair" and "Deceptive"*

In late 2011 the CFPB published an online "Supervision and Examination Manual" ("Manual").[45] Part Two of the Manual is titled "Examination Procedures" and is divided into subparts dealing with examinations for compliance with each of the various laws within the Bureau's jurisdiction: the Truth in Lending Act, the Fair Credit Reporting Act, and so forth.[46] One of the subparts bears the heading "Unfair, Deceptive or Abusive Acts or Practices" and contains a quantity of useful information straightforwardly borrowed from the FTC's jurisprudence on what constitutes either an "unfair" or a "deceptive" act or practice.[47] There is, however, nothing with respect to "abusive acts or practices" other than the statutory language quoted above and a caution that "[a]lthough abusive acts also may be unfair or deceptive, examiners should be aware that the legal standards for abusive, unfair, and deceptive each are separate."[48]

Unfair Acts or Practices. The statutory definition of unfair acts or practices requires that consumers not be reasonably able to avoid substantial injury.[49] According to the interpretation inherited from the FTC, the inquiry into whether injury from an act or practice is reasonably avoidable turns on whether the act or practice hinders a consumer's decisionmaking or interferes with his or her ability to take action.[50] The Manual assures us that "[n]ormally the marketplace is self-correcting; it is governed by consumer choice and the ability of individual consumers to make their own private decisions without regulatory intervention."[51] Nonetheless, "[i]f material information . . . is modified after, or withheld until after, the consumer has committed to purchasing the product," the not-reasonably-avoidable test will be satisfied.[52] The Manual also takes the position that injury is not reasona-

45 *See generally* CONSUMER FIN. PROT. BUREAU, *supra* note 34 (labeled "first edition" to reflect expectation of ongoing change).

46 *See generally id.* at CFPB Examination Procedures UDAAP 1–Mortgage Servicing 30.

47 *See generally id.* at CFPB Examination Procedures UDAAP 1–10.

48 *Id.* at CFPB Consumer Laws and Regulations UDAAP 9.

49 Dodd-Frank Act at § 1031(c)(1)(A), 124 Stat. at 2006.

50 CONSUMER FIN. PROT. BUREAU, *supra* note 34, at CFPB Consumer Laws and Regulations UDAAP 2–3.

51 *Id.* at CFPB Consumer Laws and Regulations UDAAP 2.

52 *Id.*

bly avoidable in instances of transactions occurring without the consumer's knowledge or consent.[53] It cautions, however, that "[a] key question is *not* whether a consumer could have made a better choice. Rather, the question is whether an act or practice hinders a consumer's decision-making."[54] Although this articulation might seem to limit the concept of "unfairness" to instances of inadequate disclosure, the Manual does also state that transactions that are coerced are unfair.[55] In addition—and very importantly—"if almost all market participants engage in a practice, a consumer's incentive to search elsewhere for better terms is reduced, and the practice may not be reasonably avoidable."[56] The examples provided of unfair practices are drawn from the jurisprudence of other agencies and include refusing to release a lien after a mortgage is fully paid, reducing credit limits without notice, and assisting in processing unauthorized checks.[57] Although the Manual tends to frame its analysis of the examples in terms of uninformed decisionmaking,[58] the Manual's earlier references to coercion and to industrywide practice do suggest that lack of disclosure is not the only thing that is unfair.

Deceptive Acts or Practices. As noted above, the Dodd-Frank Act did not define deceptive acts or practices. The Manual, however, endorses and extensively discusses the FTC approach to determining when an act or practice is deceptive.[59] The baseline test is as follows:

> A representation, omission, actor [sic] practice is deceptive when
>
> (1) The representation, omission, act, or practice misleads or is likely to mislead the consumer,
>
> (2) The consumer's interpretation of the representation, omission, act, or practice is reasonable under the circumstances, and
>
> (3) The misleading representation, omission, act, or practice is material.[60]

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53 *Id.*

54 *Id.*

55 *Id.* ("[C]onsumers cannot avoid injury if they are coerced into purchasing unwanted products or services . . . .").

56 *Id.* at CFPB Consumer Laws and Regulations UDAAP 2–3.

57 *Id.* at CFPB Consumer Laws and Regulations UDAAP 3–5.

58 *Id.* at CFPB Consumer Laws and Regulations UDAAP 2 ("[T]he question is whether an act or practice hinders a consumer's decision-making.").

59 *See id.* at CFPB Consumer Laws and Regulations UDAAP 5–7.

60 *Id.* at CFPB Consumer Laws and Regulations UDAAP 5.

Much of the Manual's additional interpretation is a matter of common sense, but there are several points worth noting. One such point is that intent to deceive is not necessary for deception to exist.[61] Another is that claims made with knowledge that they are false are presumed to be material, as are all express claims with respect to a financial product or service.[62] Moreover, evaluations of whether statements or omissions are deceptive are to be contextual[63] and require adopting the perspective of the target audience (such as older Americans, young people, or financially distressed consumers).[64] In addition, it is not necessary that a majority of consumers in the target class would be misled; a "significant minority" will suffice.[65] The examples of deceptive acts or practices drawn from FTC enforcement actions include such matters as the use of unreadable fine print in television ads, and in general suggest that there is latitude for very consumer-friendly interpretations in this area.[66]

3. *The History of "Abusive" Acts and Practices*

In 1994, Congress enacted the Home Ownership and Equity Protection Act ("HOEPA") as an amendment to the Truth in Lending Act.[67] HOEPA regularly is described, both in popular accounts and by various government authorities, as responding to "abusive" lending practices.[68] It specifically prohibits (presumably because they are "abusive") a number of practices in connection with specified high-cost loans, such as prepayment penalties and negative amortization.[69] It also empowered the FTC to prohibit acts or practices in connection

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61 *Id.* at CFPB Consumer Laws and Regulations UDAAP 7 (noting that "[i]mplied claims are presumed to be material when evidence shows that the institution intended to make the claim (even though intent to deceive is not necessary for deception to exist)").

62 *Id.*

63 *Id.* at CFPB Consumer Laws and Regulations UDAAP 5 ("It is necessary to evaluate an individual statement, representation, or omission not in isolation, but rather in the context of the entire advertisement, transaction, or course of dealing, to determine whether the overall net impression is misleading or deceptive.").

64 *Id.* at CFPB Consumer Laws and Regulations UDAAP 6 ("[W]hether an act or practice is deceptive depends on how a reasonable member of the target audience would interpret the representation.").

65 *Id.*

66 *See id.* at CFPB Consumer Laws and Regulations UDAAP 7–8 (giving examples of FTC enforcement actions for deceptive acts or practices).

67 Home Ownership and Equity Protection Act of 1994, Pub. L. 103-325, § 152(d), 108 Stat. 2160, 2191 (codified at 15 U.S.C. § 1639 (2006)) (amending the Truth in Lending Act ("TILA"), 15 U.S.C. §§ 1601–1649, by adding section 129 to TILA).

68 *See, e.g.*, *Legal Resources—Statutes Relating to Consumer Protection Mission*, FED. TRADE COMM'N (June 28, 2012), http://www.ftc.gov/ogc/stat3.shtm.

69 *See* 15 U.S.C. § 1639(c), (f).

with "refinancing of mortgage loans that the Bureau finds to be associated with abusive lending practices, or that are otherwise not in the interest of the borrower."[70] Nonetheless, the term "abusive" was not defined and has never been well understood.[71]

As passed by the House of Representatives, the Dodd-Frank Act limited the CFPB's authority to regulate abusive acts and practices as follows:

> (3) ABUSIVE ACTS OR PRACTICES.—The Director and the Agency may determine that an act or practice is abusive only if the Director finds that—
>
> (A) the act or practice is reasonably likely to result in a consumer's inability to understand the terms and conditions of a financial product or service or to protect their own interests in selecting or using a financial product or service; and
>
> (B) the widespread use of the act or practice is reasonably likely to contribute to instability and greater risk in the financial system.[72]

The systemic risk test called for by part (B) is notably absent from the provision substituted by the Senate and ultimately enacted.[73] Moreover, the final version expands the prerogative of the CFPB from the power to prohibit acts resulting in an inability to understand terms or to protect one's own interests to the power to prohibit interference with the ability to understand terms *and* to prohibit taking unreasonable advantage of a lack of understanding, an inability to self-protect, or reasonable reliance upon a covered person.[74] This change seems to be substantive rather than mere wordsmithing. Most clearly, the CFPB has been given the authority to regulate abuse of trust. More subtly, its ability to prevent acts that result in—that is, *create*—an inability to understand or self-protect has expanded to include prevention of acts that *take advantage* of conditions that evi-

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70 *Id.* § 1639(*l*)(2)(B).

71 *See generally* Frank Salinger, The Short Legislative History of "Abusive" Acts or Practices (or Why Are We Here, Anyway?) (June 5, 2012) (unpublished manuscript), *available at* http://www.masonlec.org/wp-content/uploads/2012/05/GMUAGEPfms52412.pdf (discussing the limited legislative history of the use of the term "abusive" in the Dodd-Frank Act).

72 H.R. 4173, 111th Cong. § 1 (as passed by House of Representatives, Dec. 11, 2009).

73 *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, § 1031(d), 124 Stat. 1376, 2006 (2010). The text of the enacted statute has been reprinted above. *See supra* text accompanying note 44.

74 *See* Dodd-Frank Act § 1031(d), 124 Stat. at 2006. "Covered persons" include providers of financial goods and services and their affiliates. *See supra* notes 36–38 and accompanying text.

dently may preexist. This apparently constitutes a statutory acknowledgment that not all financial consumers start out as perfectly rational and able to self-protect.

In addition to making use of the term "abusive" in its grant of authority to the CFPB, the Dodd-Frank Act used the term in describing the purpose of a provision dealing with the ability to repay a mortgage. Thus, in connection with a safe harbor established for a particular type of "qualified" mortgage, § 1639b(a)(2) states that it is intended "to assure that consumers are offered and receive residential mortgage loans on terms that reasonably reflect their ability to repay the loans and that are understandable and not unfair, deceptive or abusive."[75] This appears to be supplemental evidence that consumers' preexisting conditions—such as ability to repay—can be "abused" notwithstanding their ability to understand what is happening to them.

The statutory use of "abusive" was complemented by some amount of on-the-record muttering by congressional witnesses and statement-making members. For instance, "high fees, incentives for brokers that are harmful to borrowers, and lenders steering consumers to products that are more costly than necessary" were described as "abusive practices,"[76] as was "sell[ing] somebody a reverse mortgage and then becom[ing] his or her investment adviser."[77] On the other hand, at least one member expressed opposition to the Act on the ground that certain terms, including "abusive," were undefined.[78] This lack of comfort seems to be shared by Richard Cordray, the CFPB's new director who, as noted above, has declared the Bureau's power with respect to abusive acts and practices "puzzl[ing]."[79] Cordray went on to say that he did not see the statutory term "abusive" as a weapon that would see frequent use; instead, according to him, "[f]or something to be an abusive practice it would have to be a pretty outrageous practice."[80] According to at least some observers, this perspective means "it is unlikely that the CFPB will be pushing the reach of 'abusive' practices in the near future."[81]

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75 Dodd-Frank Act sec. 1402, § 129B, 124 Stat. at 2139.

76 155 CONG. REC. H14,759 (daily ed. Dec. 11, 2009) (statement of Rep. Schakowsky).

77 155 CONG. REC. H14,759 (daily ed. Dec. 11, 2009) (statement of Rep. Frank).

78 155 CONG. REC. H14,415 (daily ed. Dec. 9, 2009) (statement of Rep. Kingston).

79 Clarke, *supra* note 11.

80 *See id.* (internal quotation marks omitted).

81 Villafranco & McPartland, *supra* note 40, at 6.

4. *Summary and Analysis: The Extent of CFPB Authority with Respect to Unfair, Deceptive, or Abusive Acts or Practices*

Even without its authority to prevent UDAAP, the CFPB's ability to require reports, to examine financial providers, to assess risk to consumers, and to collect and make public information from covered persons probably would suffice to legally justify the type of proposal raised above and fleshed out below. Given its UDAAP powers, such a proposal would seem beyond legal challenge. The power to prevent providers from taking unreasonable advantage of preexisting conditions might well sustain outright bans on supplying certain products to particular types of consumers and certainly would support either voluntary or mandated recommendations with respect to product advisability. If, as is proposed, providers of financial services merely are encouraged to self-identify as subscribing to best practices including product recommendations, consumers' choices presumably would be enhanced, thus addressing the traditional concern that industrywide practices unfairly limit those choices. Moreover, the additional information provided by the directors of electing providers[82] with respect to their views on the advisability of certain products would enhance consumers' understanding, thus reducing the possibility that they might be deceived. Legality aside, the task of the next Section of this Article is to make the case that this proposal is justified as a matter of practical reality.

III. Corporate Law and Rationality

A. *The Rational Consumer*

1. *The Assumption of Rationality*

The law and economics school of legal analysis posits that the corporation is a "nexus of contracts" among capital providers, managers, employees, and others—including consumers—conducting themselves in a manner that is rationally self-interested.[83] Adherents of

[82] Note that directors of "covered persons" also would qualify as "covered persons" subject to CFPB authority under the definition recited above. *See supra* notes 36–38 and accompanying text.

[83] *See* Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure*, 3 J. Fin. Econ. 305, 306–08, 310–11 (1976) (discussing the corporation as a nexus of principal-agent contracts and noting that "[s]ince the specification of rights is generally effected through contracting . . . individual behavior in organizations, including the behavior of managers, will depend upon the nature of these contracts"); *see also* Frank H. Easterbrook & Daniel R. Fischel, The Economic Structure of Corporate Law 16–17 (1991) (discussing the variety of contracts that come together in a corpora-

this school, sometimes known as "contractarians," regard this account as normative, as well as descriptive. Thus, even though it really cannot be claimed that no legal actor ever behaves irrationally, corporate law is said to operate more efficiently if the possibility of irrationality is not just theoretically minimized but indeed is ignored.

2. *Legal Decision Theory*

Professor Gregory Mitchell has introduced the term "legal decision theorists" to describe the scholars who advocate the behavioral analysis of law.[84] These theorists have sought to apply the insights of social psychology and related fields toward the goal of developing a realistic account of how decisions are made in contexts relevant to law and lawmaking.[85] In evaluating the operation of financial markets and profit-making entities, they frequently have decried assumptions about the rationality of the relevant actors.[86] They have criticized the ability of many such actors to act in accordance with procedural norms of rationality (such as consistency and assimilation of new information), focusing on the predictable cognitive heuristics that permit humans to make decisions or identify their own preferences in light of limits on time, information, and actual ability.[87] Legal decision theorists thus have concluded that "human decisionmaking processes are prone to nonrational, yet systematic, tendencies," resulting in "bounds" on rationality and free will that routinely should be anticipated.[88]

Although decisionmaking may be systematically nonrational, legal decision theorists do not claim that lack of rationality occurs uni-

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tion); Henry N. Butler & Larry E. Ribstein, *The Contract Clause and the Corporation*, 55 BROOK. L. REV. 767, 770 (1989) (characterizing the corporation as a nexus of contracts).

84 Gregory Mitchell, *Why Law and Economics' Perfect Rationality Should Not Be Traded for Behavioral Law and Economics' Equal Incompetence,* 91 GEO. L.J. 67, 78–79 (2002).

85 *See id.* at 69 n.2 (extensively cataloging scholarship in the behavioral analysis of law).

86 Jon D. Hanson & Douglas A. Kysar, *Taking Behavioralism Seriously: The Problem of Market Manipulation*, 74 N.Y.U. L. REV. 630, 634–35 (1999) ("Ultimately, any legal concept that relies in some sense on a notion of reasonableness or that is premised on the existence of a reasonable or rational decisionmaker will need to be reassessed in light of the mounting evidence that a human is a reasoning rather than reasonable animal." (internal quotation marks omitted)).

87 *See* Mitchell, *supra* note 84, at 69 ("[A] fundamental assumption of the new behavioral law and economics movement is that individuals systematically fall prey to a host of 'cognitive illusions' that lead to predictable nonrational behaviors both inside and outside traditional markets. Thus, whereas law and economics treats all legal actors in all situations as if they were perfectly rational, behavioral law and economics treats all legal actors in all situations as if they were equally predisposed to commit errors of judgment and choice." (footnote omitted)).

88 Hanson & Kysar, *supra* note 86, at 633.

formly across all populations and in all situations. For instance, there is evidence supporting the proposition that education is correlated with "better" decisionmaking.[89] Specifically, in the context of selecting mortgage brokers it appears that better educated consumers pay far less for their loans.[90] There also is evidence of quality variance dependent on the decisionmaker's accountability to others.[91]

The prospect of intersubject variation does not, however, undercut the insight that many individuals make nonrational decisions in entirely foreseeable ways. For example, individuals have the tendency to respond predictably to the manner in which a decision is framed. It has, for instance, been fairly well established that decisionmaking is affected by whether an outcome is described in terms of achieving a gain or of avoiding a loss—with decisionmakers generally considering the latter to be more important.[92] Similarly, individuals have a clearly revealed bias in favor of maintaining the status quo. This means, for instance, that if a savings plan is designed as one that an employee affirmatively must select, there will be significantly less participation than if it is a plan in which participation is the default.[93] Legal decision theorists also have made the claim that many individuals do not test hypotheses in logical fashion, instead preferentially soliciting confirming evidence and simply failing to perceive disconfirming evidence.[94] Relatedly, theorists have identified a confirmation bias "in

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89 *See* Mitchell, *supra* note 84, at 87–93 (summarizing a number of studies that demonstrate this point).

90 *See* SUSAN E. WOODWARD, U.S. DEP'T OF HOUS. & URBAN DEV., A STUDY OF CLOSING COSTS FOR FHA MORTGAGES 43–44 (2008), http://www.huduser.org/Publications/pdf/FHA_closing_cost.pdf ("Differences in charges to borrowers in neighborhoods w[h]ere no adults have completed college versus those in neighborhoods w[h]ere all adults completed college are double or triple any race differences measured in these data, and they cannot be explained by differences in defaults, delinquencies, or loan origination success rates.").

91 Mitchell, *supra* note 84, at 110 (calling this the "situational variable with perhaps the most far-reaching effects on judgment and decisionmaking behavior, yet a variable often neglected in experimental studies and in legal decision theorists' analyses of legal decisionmaking").

92 *See* Russell Korobkin, *Libertarian Welfarism*, 97 CALIF. L. REV. 1651, 1658 (2009) (describing this so-called "framing effect").

93 *See id.* at 1663 (observing that "companies that changed the default rule to 'enrollment' . . . reported a significant increase in the number of employees taking advantage of the [employer-sponsored retirement] plans").

94 Hanson & Kysar, *supra* note 86, at 650 ("[T]he confirmatory bias seems to have a self-reinforcing and escalating quality: An individual interprets ambiguous evidence as consistent with her initial hypothesis and then views that evidence, as interpreted, as further confirmation of her hypothesis."); Robert A. Prentice, *The Case of the Irrational Auditor: A Behavioral Insight into Securities Fraud Litigation*, 95 NW. U. L. REV. 133, 145–46 (2000) (noting that "this bias is so

accordance with which exposure to a competing position will not dislodge and may even strengthen the antecedently held position."[95]

It is fairly easy to see how providers of consumer goods or services can and do appeal to these and other heuristics. Professors Hanson and Kysar have described this type of activity in the context of a call for changes in prevailing schemes for product liability.[96] Although Professors Hanson and Kysar do not primarily deal with financial products, their findings can easily be extrapolated: there is no particular reason to believe that consumers faced with puzzling financial products would be capable of, or inclined toward, more rational behavior than would be the case in selecting among tangible product offerings.[97] In fact, studies conducted by academics in the fields of finance and marketing well document the irrationality of financial consumers, noting, for instance, the often-exploited tendency to "round down" from, say, $399 to $300, rather than to "round up" to $400,[98] and investors' tendency to rely on economically irrelevant historic performance measures in making investment decisions.[99] Concomitantly, there is an extensive body of literature dealing with the most effective methods of marketing financial products.[100] This literature notes many examples of decisionmaking tendencies that are

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strong that trained scientists judge research reports that agree with their views to be of higher quality than those that disagree").

95 Cass R. Sunstein, *Deliberative Trouble? Why Groups Go to Extremes*, 110 YALE L.J. 71, 115 (2000).

96 Jon D. Hanson & Douglas A. Kysar, *Taking Behavioralism Seriously: Some Evidence of Market Manipulation*, 112 HARV. L. REV. 1420, 1427–28 (1999) (examining "case studies of apparently innocuous consumer markets" to find "sustained and deliberate efforts by manufacturers and retailers to manipulate consumer product perceptions" and using this research as a basis to argue for increased enterprise liability).

97 *See, e.g.*, Warren, *supra* note 1, at 454 (quoting memo from banking consultant to corporate executives noting that "most bank products are 'too complex for the average consumer to understand'"); Nicholas Wonder, Wendy Wilhelm & David Fewings, *The Financial Rationality of Consumer Loan Choices: Revealed Preferences Concerning Interest Rates, Down Payments, Contract Length, and Rebates*, 42 J. CONSUMER AFF. 243, 244 (2008) (summarizing literature on "[c]onsumer confusion in the face of complex, multidimensional price information such as auto loan financing").

98 *See, e.g.*, Eric T. Anderson & Duncan I. Simester, *Effects of $9 Price Endings on Retail Sales: Evidence from Field Experiments*, 1 QUANTITATIVE MARKETING & ECON. 93, 105 (2003) (noting that "customers round prices down and essentially ignore the right-most digits. For example $59.99 might be coded as $59 or, in an extreme case, as $50." (citations omitted)); Wonder, Wilhelm & Fewings, *supra* note 97, at 267 (observing the same phenomenon).

99 *See, e.g.*, Joseph Johnson & Gerard J. Tellis, *Blowing Bubbles: Heuristics and Biases in the Run-Up of Stock Prices*, 33 J. ACAD. MARKETING SCI. 486, 486–87 (2005) (proposing that "consumers typically do not ignore past information about products, even when they should").

100 A great deal of this research is summarized in Tae Jun Lee, The Role of Financial Services Advertising on Investors' Decision-Making 43–65 (May 2011) (unpublished Ph.D. disserta-

available for exploitation, detailing, for instance, ways in which impulsivity can be increased.[101]

3. *Critical Realists*

Legal decision theory sometimes is viewed as the product of a group of scholars practicing "behavioral law and economics."[102] This group has both noted the importance of the various phenomena identified above and written broadly on various corporate law subjects; its possible views on the proposal in this Article are discussed in more detail below.[103] There is, however, another recent school making interesting contributions to legal decision theory that are highly relevant to matters of consumer choice. "Critical realists" identify shortcomings in law and behavioral economics, advancing the argument that any conversation about rationality, bounded or otherwise, underestimates the importance of situational influence on behavior.[104] Systematic failure to attend to situation is said to promote "dispositionist discourse," in which purported "common sense" prompts attribution of behavior to individual "disposition" or choice, rather than to such realities as biological response to manipulated products and environments.[105] In illustrating their views, critical realists make quite a convincing case that it is situational manipulation, rather than poor personal choices, that has led to America's obesity epidemic.[106] Although not yet extending their insights to the financial transactions that facilitate consumption—whether of Big Macs, shelter, or other

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tion, University of Tennessee, Knoxville), *available at* http://trace.tennessee.edu/cgi/viewcontent.cgi?article=2090&context=utk_graddiss.

101 *Id.* at 143 (observing that "transformational ads and ads without disclosures may enable people with high impulsiveness . . . to choose financial option [sic] on impulse or without self-control").

102 Gregory Mitchell, *Taking Behavioralism Too Seriously? The Unwarranted Pessimism of the New Behavioral Analysis of Law*, 43 WM. & MARY L. REV. 1907, 1913–16 & n.12 (2002).

103 *See infra* Part V.B.1.

104 *See* Jon Hanson & David Yosifon, *The Situation: An Introduction to the Situational Character, Critical Realism, Power Economics, and Deep Capture*, 152 U. PA. L. REV. 129, 136–37, 179–88 (2003).

105 *See* David G. Yosifon, *Legal Theoretic Inadequacy and Obesity Epidemic Analysis*, 15 GEO. MASON L. REV. 681, 684–685, 731 (2008) ("[I]f we resolve to see others and ourselves not by the flare of intuition alone, but more fully in the light of social science, among the first things that we learn is that our intuitions and common sense often betray us. They do so in particular with respect to our assessment of the sources of our own and others' behavior." (footnote omitted)).

106 Adam Benforado, Jon Hanson & David Yosifon, *Broken Scales: Obesity and Justice in America*, 53 EMORY L.J. 1645, 1797 (2004) ("How much free choice do urban families have when the nearest supermarket is two bus rides away, and the Popeye's is across the street? How much free choice do we really have regarding the options available at restaurants . . . ?").

items—there is no reason to believe that such an extension would be inapt.

4. Contractarians Redux

Neither legal decision theory nor critical realism has driven contractarian analysis from the field. It has been suggested that many legal decision theorists have not carefully distinguished experimental and survey empiricism and have failed to reckon with the latter.[107] Although there does not appear to have been exhaustive study of the field, limited survey empiricism is said to demonstrate that the model of law and behavioral economics has no more predictive power with respect to the studied consumer borrowing choices than a stricter law and economics model premised on classic rationality.[108] Moreover, strict law and economics analysts emphasize that legal decision theory (and, presumably, critical realism) tends to support paternalist government intervention, and that paternalism has costs. These include "lessen[ing] the incentive to engage in learning and the development of rational behavior" or "exacerbat[ing] irrational behavior by introducing moral hazard."[109]

B. Further Implications for Corporate Law

1. The Significance of Role

In addition to a number of other nonrational tendencies identified by legal decision theorists, there is a tendency to respond to role assignment by engaging in conduct that is expected rather than responsive to individual taste.[110] In this regard, studies have assessed and demonstrated participants' willingness to administer increasingly

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107 *See* Mitchell, *supra* note 102, at 1945–46 (criticizing empirical studies of behavioral decision theory for "neglect[ing]" or "downplay[ing]" subjects' rational responses and for promoting a "mythology of decision making as rampantly and fundamentally flawed [which] has developed through the repeated use of standard research paradigms that are designed to show biased behavior and . . . use . . . statistical methodology that stacks the decks in favor of finding biased behavior without concern for the practical importance of the behavior outside of the laboratory").

108 *See* Joshua D. Wright, *Behavioral Law and Economics, Paternalism, and Consumer Contracts: An Empirical Perspective*, 2 N.Y.U. J.L. & LIBERTY 470, 474–75, 509–10 (2007) (concluding, after a study of consumer contracts, that "behavioral economic analysis . . . has not provided greater predictive power than its neoclassical counterpart" but acknowledging the study's limits).

109 *Id.* at 472–73.

110 *See* David Luban, *Integrity: Its Causes and Cures*, 72 FORDHAM L. REV. 279, 292 (2003) (observing that an "important feature of the worker-supervisor experiment is that the subjects conformed their own pro- and con-attitudes to the [either worker or supervisor] role they themselves anticipated playing"); Andrew M. Perlman, *Unethical Obedience by Subordinate Attor-*

painful electric shocks to subjects as part of a "teaching" experiment.[111] Over time, the willingness to follow the directions of the experimenter, notwithstanding cries of pain from the putative subjects, appears constant in the range of sixty-five to seventy percent.[112] Somewhat similarly, in the famous "Stanford prison experiment," randomly assigned "prison guards" rapidly became abusive, while the randomly assigned "prisoners" just as quickly became dysfunctionally depressed.[113] It may be a bit of a stretch, but not entirely far-fetched, to find an analogy here for corporate law. If the majority of individuals are willing to cause physical pain in accordance with the perceived demands of a role they have voluntarily assumed, might they not be just as willing, when acting as directors or other managers, to inflict financial pain on consumers in accordance with the perceived demands of their corporate role?

2. *The Role of Accountability*

As noted above, accountability to others tends to improve the quality of decisionmaking.[114] One would generally anticipate this result, insofar as the decisionmaker might be expected to take more care and avoid self-interest more thoroughly than otherwise would be the case. Accountability researchers have suggested, however, that "[s]elf-critical and effortful thinking is most likely" where a decisionmaker feels he or she will be accountable to a reasonably well-informed audience with an interest in process rather than in specific outcomes and a "legitimate reason for inquiring into the reasons behind participants' judgments."[115] Where the views of the audience on outcomes are either known or thought to be known, decisionmaking

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neys: Lessons from Social Psychology, 36 HOFSTRA L. REV. 451, 452 (2007) (observing this phenomenon in the junior attorney-senior attorney relationship).

111 *See* Perlman, *supra* note 110, at 456–59 (describing Stanley Milgram's teacher-learner electric shock experiment).

112 *See* Jerry M. Burger, *Replicating Milgram: Would People Still Obey Today?*, 64 AM. PSYCHOLOGIST 1, 8 (2009) (recreating Milgram's experiment and finding that seventy percent of participants continued to apply a higher "voltage" and "had to be stopped by the experimenter"); Perlman, *supra* note 110, at 458 (noting that sixty-five percent of Milgram's subjects, when directed to do so, continued to administer an "electric shock" for the duration of the experiment).

113 *See* Craig Haney, Curtis Banks & Philip Zimbardo, *Interpersonal Dynamics in a Simulated Prison*, 1 INT'L J. CRIMINOLOGY & PENOLOGY 69, 69–73, 80–81 (1973).

114 *See* Mitchell *supra* note 84, at 110–14 (noting that "predecisional accountability to a legitimate audience with unknown views may well cause decisionmakers to engage in self-critical thinking that often, though not always, leads to more rational behavior").

115 Jennifer S. Lerner & Philip E. Tetlock, *Accounting for the Effects of Accountability*, 125 PSYCHOL. BULL. 255, 259 (1999).

processes often will be truncated and existing biases will be amplified.[116]

This is not particularly good news in the case of corporate directors. It seems fairly obvious that, by reason of the business judgment rule,[117] as well as statutes and provisions in articles of incorporation holding directors financially harmless, there is no serious legal accountability for the outcome of their actions, or, within reason, for the shoddiness of the procedures through which those actions are taken.[118] As a practical matter, however, directors are accountable to markets, with their accountability outcome "scores" flashing on the scoreboards of financial statements and stock price. It should be no surprise when they rather consistently conduct themselves so as to see those scores increase. Similarly, it should be no surprise when the judgments they make do little, if anything, to voluntarily protect consumers.[119]

IV. The Best Practices Proposal

Social scientists aptly caution legal scholars against employing tools they have not been trained to use. At the same time, they appear to believe that it is high time for their insights to be taken seriously and have acknowledged that at least some suggestions for legal reform based on social science findings risk no harm.[120]

This Article does take seriously the possibility that financial consumers are subject to limits on rationality and that many of them, be-

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116 *See id.* at 256 (observing that when a decisionmaker knows his or her audience's views before making a decision, "[p]eople can simply adopt positions likely to gain the favor of those to whom they are accountable, thereby allowing them to avoid the unnecessary cognitive work of analyzing the pros and cons of alternative courses of action, interpreting complex patterns of information, and making difficult trade-offs").

117 For an explanation of the modern business judgment rule, see Elizabeth S. Miller & Thomas E. Rutledge, *The Duty of Finest Loyalty and Reasonable Decisions: The Business Judgment Rule In Unincorporated Business Organizations?*, 30 Del. J. Corp. L. 343, 345–50 (2005).

118 *See* Lawrence A. Hamermesh, *Why I Do Not Teach* Van Gorkum, 34 Ga. L. Rev. 477, 479, 489–91 (2000) (discussing the advent of the modern "Raincoat" provision, shielding the corporate director of financial liability for a breach of the duty of care); *see, e.g.*, Del. Code Ann. tit. 8, § 102(b)(7) (2011) (allowing such provisions in the articles of incorporation of Delaware corporations). *See generally* James J. Hanks, Jr., *Evaluating Recent State Legislation on Director and Officer Liability Limitation and Indemnification*, 43 Bus. Law. 1207 (1988) (exhaustively detailing the director and officer liability limiting statutes of a number of states).

119 *See* Yosifon, *supra* note 5, at 270–81 (giving examples of corporate manipulation of markets in order to increase productivity at the expense of consumers in the tobacco, food, and dietary supplement industries).

120 Mitchell, *supra* note 84, at 132–35 (noting that "the legal decision theorists' emphasis on cognitive failings and their call for reforms to counter or protect against irrational behavior may still immediately serve a constructive role in the law").

cause of predictable heuristics or situational pressures, may not make the choices that strict economic analysis might predict. It also takes the position that it risks little, if any, harm to acknowledge that corporations are capable of exploiting this probable reality, that corporate decisionmakers are encouraged to believe they are duty bound to engage in such exploitation, and that they act accordingly. It is the task of the remainder of the Article to persuade that it would do no harm to counter this tendency, and to do so in a manner that can be justified simply as providing consumers with additional information.

In the past, authors expressing concern for the plight of consumers—financial or otherwise—have made a number of suggestions. These include regulation of advertising, criminalizing exploitation, giving shareholders a voice on exploitation, and making directors directly accountable to consumers.[121] Suggestions falling in the last category—director accountability to consumers—have taken a variety of forms, including imposing a new fiduciary duty and permitting consumers to vote in directorial elections.[122] These suggestions have been both extensively criticized and made to no real avail.[123]

The proposal of this Article is more modest. Professor Gregory Mitchell has written of "debiasing reforms" to be employed in behavior research.[124] His suggestions include "asking or directing experimental subjects to consider alternative or opposing arguments," and "asking experimental subjects to explain their choices."[125] This Article proposes that these reforms be employed in the case of corporate

121 *See* Theresa A. Gabaldon, *Joe Camel Explains It to the Board: Corporate Law, Women in the Workforce, and the Exploitation of Children*, 13 DUKE J. GENDER L. & POL'Y 203, 230–31 (2006) (advocating for shareholder votes on matters of arguable exploitation); Samuel H. Johnson, *Who We Really Are: On the Need for the United States to Adopt the European Paradigm for Identity Fraud Protection*, 15 CURRENTS: INT'L TRADE L.J. 123, 137 (2006) (arguing for protection of U.S. consumers by imposing criminal sanctions); Janis Sarra, *The Gender Implications of Corporate Governance Change*, 1 SEATTLE J. FOR SOC. JUST. 457, 466, 470 (2002) (explaining differing rationales for holding directors liable to the community they operate in and the consumers they affect for socially irresponsible decisionmaking); Note, *The Elephant in the Room: Evolution, Behavioralism, and Counteradvertising in the Coming War Against Obesity*, 116 HARV. L. REV. 1161, 1179–81 (2003) (advocating for advertising regulation to combat obesity).

122 *See, e.g.*, Yosifon, *supra* note 5, at 295–311 (suggesting and defending both of these proposals).

123 *See* EASTERBROOK & FISCHEL, *supra* note 83, at 38 (critiquing multifiduciary proposals in part on the basis that "a manager told to serve two masters (a little for equity holders, a little for the community) has been freed of both and is answerable to neither"); Oliver Williamson, *Corporate Governance*, 93 YALE L.J. 1197, 1213 (1984) (noting that consumers' "main protection . . . is generally the option to take their trade elsewhere").

124 Mitchell, *supra* note 84, at 132.

125 *Id.* at 133–34.

directors making decisions relevant to the exploitation of financial consumers. It hardly seems draconian or even particularly burdensome to encourage directors to be specifically mindful of the subject of exploitation and to explain their thinking in this regard. The expected benefits would include increased and highly relevant information for consumers, as well as some possible impact on the actual products offered.

The basic idea is that the CFPB fairly easily could adopt a process for certifying providers of financial products and services as subscribing to corporate decisionmaking practices designed to be less injurious to consumer interests than the usual shareholder primacy model has historically dictated. Most importantly, corporate directors of companies electing certification would be called upon to familiarize themselves with their companies' offerings, to certify their own understanding of those offerings, and to declare their individual opinions about the advisability of those products for consumers in certain identified circumstances. Misrepresentation of opinion would, presumably, be sanctionable as a deceptive practice.[126]

Admittedly, calling on board members to familiarize themselves with all of their companies' offerings and to certify their understanding of those offerings might result in a reduction in the overall number of products offered. To anyone who suspects that obfuscation may be one of the reasons for product proliferation this is not a bad thing. Moreover, those who were paying attention during the recent financial crisis will recall that rampant failure, by both providers and purchasers, to understand the attributes of certain financial products was a recipe for disaster.[127] Very possibly, if a product is too complicated

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126 *See supra* notes 59–66.

127 *See* James Fanto, *Stress Testing and Scenario Analysis in Risk Management: Preparing for the Worst*, *in* THE PANIC OF 2008: CAUSES, CONSEQUENCES AND IMPLICATIONS FOR REFORM 77, 81–84 (Lawrence E. Mitchell & Arthur E. Wilmarth, Jr. eds., 2010) [hereinafter PANIC OF 2008] (criticizing "[s]enior executives and boards of directors of many financial firms [who] clearly did not pay enough attention to the risk profiles of their firms, or even to risk management in general"); Theresa A. Gabaldon, *The Sewers of Jefferson County: Disclosure, Trust and Truth in Modern Finance*, *in* PANIC OF 2008, *supra*, at 255, 271–73 (giving an example of the disparity in sophistication between some municipal borrowers and the national banks with which the borrowers did business); Patricia A. McCoy, *Federal Preemption, Regulatory Failure and the Race to the Bottom in US Mortgage Lending Standards*, *in* PANIC OF 2008, *supra* at 132, 139–41 (documenting the "arcane" and "baffling" features of subprime mortgages, which, when "bur[ied]," made it difficult for safe lenders to compete with risky lenders for borrowers' business); Frank Partnoy, *Overdependence on Credit Ratings Was a Primary Cause of the Crisis*, *in* PANIC OF 2008, *supra* at 116, 117–18 ("The rating agencies faced little or no risk of loss from inaccurate ratings, while the potential gains from inaccurate ratings increased. Ratings substantially lagged the revelation of public information about rated issuers and instruments . . . .").

to be understood by the average board member, it simply should not be sold. If the entire slate of product offerings is too expansive for any one director to grasp, perhaps no one is really adequately minding the store.[128]

As a practical matter, identifying financial consumers' circumstances—or generating meaningful classifications for them—would present challenges. On the other hand, at least a few easy cases would exist. For instance, should anyone ever take a payday loan if he or she cannot expect to pay it back on payday? Should anyone ever take out a loan at a triple digit interest rate? Should any student who needs to borrow for his or her education ever take out a private loan before exhausting lower-cost federal options? Should anyone ever take out a mortgage in an amount highly correlated with defaults by borrowers with similar earnings levels? One can imagine, then, a regime in which directors would be prompted to answer questions such as the following:

> Q: With respect to short-term loans intended to be repaid out of the borrower's next paycheck: In which circumstances should this loan be considered?
>
> [*Presumably nondeceptive answer: Only if the borrower is extremely confident that his or her next paycheck will be adequate to repay the loan and its carrying costs, as well as provide for continuing living expenses so that no additional borrowing or extension of the term will be necessary.*][129]
>
> Q: With respect to loans bearing interest rates in excess of those likely to be available from alternative lenders: In which circumstances should this loan be considered?
>
> [*Presumably nondeceptive answer: Never.*]
>
> Q: With respect to private student loans: In which circumstances should this loan be considered?
>
> [*Presumably nondeceptive answer: Only after all lower-cost federal options are exhausted.*][130]
>
> Q: With respect to mortgage loans in the amount of $X: In which circumstances should this loan be considered?

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128 The proposal could be tweaked, however, to assign certain product lines to certain groups of directors.

129 *See* Creola Johnson, *Payday Loans: Shrewd Business or Predatory Lending?*, 87 MINN. L. REV. 1, 139–40 (2002) (advocating rules for payday lenders that base the availability and amount of a payday loan on the borrower's financial condition).

130 *See* REED ET AL., *supra* note 2 (noting that a majority of undergraduate students fail to exhaust federal loans before turning to private lenders).

> [*Presumably nondeceptive answer: A mortgage loan in the amount of $X should not be considered by prospective borrowers with annual income below $Y.*][131]

V. Possible Perspectives on the Best Practices Proposal

A. *Contractarians*

The contractarians described earlier in this Article characterize the "best," or "most efficient," corporate law as providing the set of default contract rules most likely to minimize transaction costs.[132] These rules generally reflect the assumption that corporate managers—primarily the board of directors—act as fiduciaries for the shareholders.[133] Limiting the duties of the board of directors to serving shareholder interests is thought to be the single best method of limiting managerial opportunism and shirking, owing to the relative efficiency of monitoring by a single class of beneficiaries.[134] The board therefore is regarded as responsible for maximizing the residual value of the firm remaining after nonshareholder claimants are satisfied.[135] This easily translates to the conjoined assertions that the goal of the corporation is to make money for its shareholders and that management and the board must prefer the interests of shareholders over those of all others with interests in the firm.[136] The resulting template for corporate law is, of course, known as the "shareholder primacy" model. Under this view, even a modest proposal to encourage the board of directors to be purposely mindful of interests other than those of shareholders is controversial;[137] psychological acculturation toward shareholder primacy manifested through profit maximization is distinctly to be favored. This means, as a policy matter, that directors really should be encouraged to exploit consumers if that will contribute to the corporate bottom line. Only if public recognition of the practice were likely and apt to lead to enough public outcry to result

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131 The CFPB already has suggested that consumers take such considerations into account when taking out a mortgage. *See How Can I Figure Out If I Can Afford to Buy a Home and Take Out a Mortgage*?, Consumer Fin. Prot. Bureau: Ask CFPB (last updated Mar. 22, 2012), http://www.consumerfinance.gov/askcfpb/118/how-can-i-figure-out-if-i-can-afford-to-buy-a-home-and-take-out-a-mortgage.html ("To know how much you can afford to repay, you'll need to take a hard look at your family's income, expenses and savings priorities to see what fits comfortably within your budget.").

132 *See supra* note 83 and accompanying text.

133 *See* Easterbrook & Fischel, *supra* note 83, at 90–91.

134 *See id.* at 35–38.

135 *See id.* at 36.

136 *See id.* at 90–93.

137 *See supra* notes 13–18 and accompanying text.

in boycotts, legal prohibition, or something of the sort, should exploitation voluntarily be avoided.[138]

B. Other Approaches

Although quite dominant for decades, the contractarian approach faces competitors, including the behavioral economic approach earlier described.[139] Brief descriptions of the primary competitors are provided below, along with speculation as to the possible responses of each school to the proposal that corporate directors be prompted toward mindfulness of the exploitation of financial consumers.

1. Behavioral Economics

As noted above, the contractarian approach is the product of strict law and economics analysis.[140] One of its more vigorous recent challengers is a close relative known as behavioral economics. Behavioral economics accepts the insights of social science and utilizes empirical studies of human behavior in order to reassess some of the assumptions of the traditional law and economics movement.[141] Its proponents have established to their own satisfaction that not all economic actors act in their own self-interest—in some instances because of altruism, in some because of predictable cognitive heuristics, and in some because of plain old stupidity.[142]

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138 This is not intended to mean that economists do not recognize misleading consumers or the like as a form of market failure. Market failures, in their view, generally are to be managed as a matter of law external to the corporation. For discussion of the distinction between corporate governance and external law, see *supra* notes 13–18 and accompanying text.

139 *See supra* Part III.A.2–3.

140 *See supra* Part III.A.4.

141 *See, e.g.*, Kent Greenfield, *Using Behavioral Economics to Show the Power and Efficiency of Corporate Law as Regulatory Tool*, 35 U.C. DAVIS L. REV. 581, 583 (2002) ("While adopting some of the conventional premises of law and economics, such as the belief that legal rules affect behavior, [behavioral law and economics] distances itself from many of the traditional assumptions of law and economics, such as a dependence on individual economic 'rationality' as the determinant of behavior."); Christine Jolls, Cass R. Sunstein & Richard Thaler, *A Behavioral Approach to Law and Economics*, 50 STAN. L. REV. 1471, 1473–76 (1998) (arguing for an analytical approach that "allows us to model and predict behavior relevant to law with the tools of traditional economic analysis, but with more accurate assumptions about human behavior"); *see also* Donald C. Langevoort, *Monitoring: The Behavioral Economics of Corporate Compliance with Law*, 2002 COLUM. BUS. L. REV. 71, 73–77 (applying behavioral economic analysis to the design of corporate compliance systems).

142 *See* Jolls, Sunstein & Thaler, *supra* note 141, at 1476–79 (laying out the three "bounds"—"bounded rationality," "bounded willpower," and "bounded self-interest"—that underlie behavioral law and economics analysis).

In accepting that economic actors—including, presumably, shareholders—sometimes act altruistically,[143] behavioral economics could be used to formulate a modified iteration of shareholder primacy. In this version, shareholder welfare might be examined in terms of what shareholders might affirmatively desire, other than, or in addition to, profit maximization. In other words, psychic income[144] could be counted toward the desired "bottom line." Thus, other-regarding shareholders might prefer less consumer exploitation, even if it leads to less profitability. This possibility is problematic, though, for at least three reasons. The first is that a number of shareholders are not individuals but institutions.[145] The second is the perceived problem of the commons. If the shareholders of one corporation learn that it will limit consumer exploitation but believe that other entities will continue the practice, they are apt to regard their own sacrifice as pointless. The third is that although some shareholders may be other-regarding, it is by no means clear that all would be. Presumably, it is this expected diversity of viewpoints that explains why mainstream corporate America does not, by and large, attempt to accommodate the possible nonmonetary preferences of shareholders as to a number of matters.

As noted above, another of the heuristic phenomena explored by behavioral economics has to do with the importance of how a decision is framed.[146] This recognition has prompted some of the school's adherents to propose an approach known as "libertarian paternalism," pursuant to which policymakers may determine which resolution of an issue generally would be preferable, and frame decisionmaking contexts accordingly.[147] Although individuals thus are psychologically encouraged to make decisions in a particular manner, deviation—or "opting out"—is possible. A simple example involves placing fruit

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143 *See* Neel P. Parekh, Note, *When Nice Guys Finish First: The Evolution of Cooperation, the Study of Law, and the Ordering of Legal Regimes*, 37 U. MICH. J.L. REFORM 909, 918, 935, 940 (2004).

144 "Psychic income" is the concept that individuals perform certain actions because they "provide[ ] a sense of pleasure that tilts the balance of cost versus benefit on the side on benefit." *Id.* at 934.

145 This problem may or may not be assumed away by positing that after all institutional stacking, or "nesting," is considered, individual shareholders will be revealed.

146 *See supra* note 93 and accompanying text.

147 *See generally* Cass R. Sunstein & Richard H. Thaler, *Libertarian Paternalism Is Not an Oxymoron*, 70 U. CHI. L. REV. 1159 (2003) (making the case for "libertarian paternalism," by which decisions are framed in such a way as to "steer" individuals towards the welfare-enhancing choice while maintaining their ultimate freedom to choose).

before sugary desserts in school cafeteria lines.[148] Hopefully, children then find themselves with scurvy-fighting oranges on their trays and less room for other desserts, but those who are "rational" enough to see through the ploy (say the second time through the line) are free to skip the fruit and go straight for the cupcakes. Given this example, the model does seem a bit odd, since it contemplates that actors may self-prove rationality by opting away from the choice urged by presumably well informed social planners. In any event, libertarian paternalism would seem to easily accommodate a CFPB-sponsored regime in which consumer choices are framed, in part, by directorial recommendation.

Behavioral economic analysis has spurred the growth of another approach reacting to the recognition that humans do not always act in the ways that conventional law and economics would predict. The "asymmetric paternalism" school calls for paternalistic intervention where the benefits to irrational individuals significantly outweigh the cost to rational individuals of losing the right of choice.[149] This easily would go so far as to permit the government to dictate outright the terms pursuant to which products would be marketed, thus protecting the irrational consumer while still leaving the rational consumer, who is capable of avoiding the framing effect, freedom to choose. Providing a sponsored platform for directorial recommendations certainly also should be acceptable.

2. *The Progressive Approach*

During the 1990s, a group of vaguely-to-expressly self-identifying communitarian corporate law scholars also self-identified as "progressive"[150] and proceeded to express their rejection of shareholder primacy.[151] Corporate progressives generally endorse an expansion of the goals of the corporation and the duties of management to include responsibility to other constituents,[152] frequently arguing for the rec-

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148 *See id.* at 1164–66.

149 *See* Colin Camerer et al., *Regulation for Conservatives: Behavioral Economics and the Case for "Asymmetric Paternalism,"* 151 U. PA. L. REV. 1211, 1212 (2003).

150 David Millon, *Communitarianism in Corporate Law: Foundations and Law Reform Strategies*, *in* PROGRESSIVE CORPORATE LAW, *supra* note 17, at 16–22; *see also* Stephen M. Bainbridge, *Community and Statism: A Conservative Contractarian Critique of Progressive Corporate Law Scholarship*, 82 CORNELL L. REV. 856, 857 n.1 (1997) (reviewing PROGRESSIVE CORPORATE LAW, *supra* note 17, and criticizing the use of the term).

151 *See* Millon*, supra* note 150, at 16–22.

152 *See, e.g.*, Wai Shun Wilson Leung, *The Inadequacy of Shareholder Primacy: A Proposed Corporate Regime That Recognizes Non-Shareholder Interests*, 30 COLUM. J.L. & SOC. PROBS. 587, 589 (1997) (arguing that the model of shareholder primacy should be replaced with a regime

ognition of enforceable fiduciary duties running from directors to groups such as creditors and employees.[153] As an alternative or supplemental approach, progressives also have proposed methods of increasing the board's discretion to recognize nonshareholder interests.[154] These methods include extending the terms for which members of the board are elected and adopting methods of effectively enforcing nonshareholder rights in constituency statutes.[155] It has also been suggested that board members be given additional fiduciary duties owed to, and enforceable by, other stakeholders.[156] Although corporate progressives have not devoted a great deal of attention to the issue of consumer exploitation, their general concern with corporate social responsibility and the interests of nonshareholders suggests that they would strongly support consumer protection initiatives.

3. *The Team Production Model*

The "team production" approach speaks the language of neoclassical economics, but makes somewhat different starting assumptions.[157] The consequence is a set of conclusions that often resonate with corporate progressives.[158] Team production scholars describe the board of directors as an independent "hierarch" mediating among all

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under which "[b]oards must consider equally the interests of non-shareholding stakeholders and shareholders when making decisions that can affect both groups"); Millon, *supra* note 150, at 1 ("Those scholars who have challenged the shareholder primacy principle may be referred to as communitarians, because . . . their work focuses on the sociological and moral phenomenon of the corporation as community, in contrast to the individualistic, self-reliant, contractarian stance . . . .").

153 *See* Lawrence E. Mitchell, *The Fairness Rights of Corporate Bondholders*, 65 N.Y.U. L. REV. 1165, 1178 (1990) (arguing that fiduciary rights should be extended to corporate bondholders); O'Connor, *supra* note 14, at 1194–96 (arguing that fiduciary duties should extend to displaced workers).

154 *See* Lawrence E. Mitchell, *A Theoretical and Practical Framework for Enforcing Corporate Constituency Statutes*, 70 TEX. L. REV. 579, 582–86 (1992).

155 *See* LAWRENCE E. MITCHELL, CORPORATE IRRESPONSIBILITY: AMERICA'S NEWEST EXPORT 112–18 (2001) (advocating for self-perpetuating boards); Mitchell, *supra* note 154, at 635–40 (explaining a method of enforcing constituency statutes that accounts for and protects multiple interests).

156 *See, e.g.*, O'Connor, *supra* note 14, at 1196 (arguing "that the corporation's nexus of contracts should be restructured to recognize that directors have fiduciary duties to mitigate the effects of layoffs and plant closings upon displaced workers").

157 *See* Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 249 (1999) (questioning whether principal-agent problems are unique to corporations as compared to other business firms and suggesting the team production approach to the corporation).

158 Note, however, that the adherents of this model specifically disavow identification as progressives. *See id.* at 253–54.

those with inputs to the corporation that are team-specific.[159] In this view, the proper function of the board is to employ the inputs of financiers, workers, communities, and others in order to maximize the value of the firm. Not incidentally, this requires the board to allocate corporate profits among all inputting groups in a manner all participants will tolerate.[160] Although the proponents of the model do not characterize consumers as having team-specific inputs, they have acknowledged the board of directors' ability to engage in corporate philanthropy[161] and presumably would find aversion to consumer exploitation an acceptable motivation for directorial decisionmaking. In fact, the writings of Professor Einer Elhauge endow the team production model with sufficient latitude to permit the board to engage in at least limited moral decisionmaking[162]—extensive enough, at any rate, to roughly emulate the non-self-interested conduct of entrepreneurs.

4. *Feminism*

The multiple concerns of feminists share a common overlay of focus on the position of women in a patriarchal society and tend to share a common method of examining the actual experiences of women.[163] As an integral part of their analytical process, feminist schol-

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159 *See id.* at 250–51.

160 *See id.* ("Within the corporation, control over those assets [belonging to team members] is exercised by an internal hierarchy whose job is to coordinate the activities of the team members, allocate the resulting production, and mediate disputes among team members over that allocation.").

161 *See generally* Margaret M. Blair, *A Contractarian Defense of Corporate Philanthropy*, 28 STETSON L. REV. 27 (1998) (invoking the team production model in defense of corporate charity).

162 *See generally* Einer Elhauge, *Sacrificing Corporate Profits in the Public Interest*, 80 N.Y.U. L. REV. 733 (2005) (arguing that the law allows corporate managers to at least somewhat forego profits to the public interest).

163 *See* SANDRA HARDING, THE SCIENCE QUESTION IN FEMINISM 244 (1986) ("It would be historically premature and delusionary for feminism to arrive at a 'master theory,' at a 'normal science' paradigm with conceptual and methodological assumptions that we all think we accept . . . . We need to learn how to see our goal for the present moment as a kind of illuminating 'riffing' between and over the beats of the various patriarchal theories and our own transformations of them . . . ."); NEW FRENCH FEMINISMS: AN ANTHOLOGY, at x–xiii (Elaine Marks & Isabelle de Courtivron eds., 1980) ("[American feminists'] style of reasoning, with few exceptions, follows the Anglo-American empirical, inductive, anti-speculative tradition. They are often suspicious of theories and theorizing."); Christine A. Littleton, *Feminist Jurisprudence: The Difference Method Makes*, 41 STAN. L. REV. 751, 753 n.11 (1989) (book review) ("If . . . the need for diversity within feminism . . . is answered simply with uncritical pluralism, nothing has been gained. . . . To the extent that any articulation of feminism is white, it is not only incomplete but also inadequately centered in women's experience, and therefore inadequately feminist.").

ars make use of the concept of "gender," which is defined as the socially constructed (as opposed to biological) differences between being male and female.[164] The term "gendered" sometimes is used to describe structures, analyses, etc. that are the outcome of gender. It may, for example, be said that corporate law is gendered because it predominantly is the product of men, constructed in reliance on their own taught values. Corporate law's traditional celebration of assumed rationality thus is suspect; feminist invocation of experience as financial consumers and victims may, in fact, lead to conviction that the assumption is somewhat ridiculous.[165] Although "paternalistic" would not be the preferred adjective for intervention, the protection of consumers, financial or otherwise, is not inconsistent with feminist concerns and analysis.[166]

5. *Critical Race Theory*

"A central claim of [critical race theory] is that antiracist politics and legal theory should be informed by the voices of people 'on the bottom' of discrimination."[167] In part this is because on issues of race,[168] voices on the bottom simply are seen as more credible than the voices of those on the top.[169] Eliciting those voices logically promotes improvement in substantive results[170] and inviting speech from the for-

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164 For discussion of "gendering," see generally Mary Anne C. Case, *Disaggregating Gender from Sex and Sexual Orientation: The Effeminate Man in the Law and Feminist Jurisprudence*, 105 YALE L.J. 1 (1995) (treating "gender" and "sex" separately and the applicability of that distinction to employment discrimination and other areas of law). As an example, for a time between the Industrial Revolution and the advent of the women's liberation movement, the popularly ascribed gender role of women was to remain at home, raising children (although, most certainly, some women, either as a matter of aspiration or necessity, did deviate).

165 *See* Theresa A. Gabaldon, *Corporate Conscience and the White Man's Burden*, 70 GEO. WASH. L. REV. 944, 945–46 (2002) (discussing outsider suspicion of the white male in shaping corporations, corporate law, and corporate law commentary).

166 *See generally* Gabaldon, *supra* note 121 (discussing feminist concern with corporate exploitation of children as consumers).

167 Devon W. Carbado, *Race to the Bottom*, 49 UCLA L. REV. 1283, 1284 (2002).

168 It should be noted that, as race has come to be regarded as a matter of social construct rather than genetic immutability, the inclusion of other social categories of inequity in critical race theorization has become quite natural. *See* Darren Lenard Hutchinson, *Progressive Race Blindness?: Individual Identity, Group Politics, and Reform*, 49 UCLA L. REV. 1455, 1459 (2002) ("Advocates of progressive race blindness embrace the persuasive contemporary social theories that dispel traditional accounts of race (and other identity categories) as products of biology.").

169 Carbado, *supra* note 167, at 1304 ("The argument is based on that notion that Whites are the beneficiaries and perpetrators of racism (therefore, their perspectives cannot be trusted), and Asian Americans are the victims of racism (therefore, their voices should be listened to).").

170 *See* Richard Delgado, *The Imperial Scholar: Reflections on a Review of Civil Rights Literature*, 132 U. PA. L. REV. 561, 569 (1984) (arguing that increasing minority representation in work and school has three main justifications: reparations, social utility, and distributive justice);

merly silent may have benefits of its own independent of outcome.[171] These contentions, however, beg two obvious questions. First, how broadly is the concept of "antiracist politics and legal theory" to be defined? Second, how is one to identify those "on the bottom" with respect to any particular issue?

For purposes of a corporate law analysis, the second question is far simpler than the first, for it is easy to identify both a "bottom" and a "top." Economically privileged white males have predominantly shaped corporations, corporate law, and corporate law commentary;[172] eliciting the voices of those "outsiders" not sharing all three of those characteristics would, from a critical race perspective, have intrinsic value in addressing relevant issues. This suggests a fairly clear answer to the first question as well. In any situation in which "top" and "bottom" are so easily discerned in terms of race, gender, and economic class, issues within the realm of critical race analysis clearly are implicated.

Outsiders have, of course, increased their participation in financial markets.[173] Still, racial minorities are less likely than whites to participate in the equity ownership that corporate directors are psychologically pledged to protect.[174] Moreover, the experience of racial minorities as consumers—financial or otherwise—can be radically different than those of white males. For instance, it has been known for decades that lending practices often discriminate on the basis of race,[175] and that minorities (and women) pay higher car prices than do

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Mari J. Matsuda, *Looking to the Bottom: Critical Legal Studies and Reparations*, 22 HARV. C.R.-C.L. L. REV. 323, 362 (1987) ("suggest[ing] a new, reconstructed legalism that attempts" to develop "new norms and new law that will achieve and maintain the utopian vision" of critical legal studies).

171 *See* Carbado, *supra* note 167, at 1299 ("The reason to look to the bottom is not to generate a particular substantive outcome, but to get an authentic voice.").

172 *See* Gabaldon, *supra* note 165, at 945–46 (noting that "the cultural bias and world view of corporate authors manifests itself in the proposal of solutions that work for people 'like us'").

173 *See* Theresa A. Gabaldon, *John Law, with a Tulip, in the South Seas: Gambling and the Regulation of Euphoric Market Transactions*, 26 J. CORP. L. 225, 229, 233–34 (2001) (noting that "hunch investors" tend to participate in the market quite frequently "[d]uring times of volatility or times when the markets are at significant highs").

174 *See* Dorothy A. Brown, *Pensions, Risk, and Race,* 61 WASH. & LEE L. REV. 1501, 1536–38 (2004) (noting that "Blacks and Hispanics are less likely to invest their money in the stock market than are Whites").

175 *See, e.g.*, FRANKLIN J. JAMES, BETTY L. MCCUMMINGS & EILEEN A. TYNAN, MINORITIES IN THE SUNBELT 121 (1984) (finding that although the data concerning rental discrimination were inconclusive, in the Denver market to purchase real estate, "less assistance was offered to Hispanics and blacks in financing home purchases").

white males.[176] A recent study even has shown that minorities pay higher closing costs for mortgage loans.[177] Positing the exact content of the views of those "on the bottom" of corporate America may be somewhat risky, but it is unlikely that a hymn in praise of shareholder primacy and correlative exploitation of financial consumers would be sung.

C. Contractarian Rejoinders

Contractarians generally do not bother to rebut feminist or critical race theorists, but have produced responses to other schools.[178] Some portion of these responses have comprised a reiteration of some of law and economics' basic assumptions in the context of an examination of the precise claims of the newer schools, generating statements along the lines of the following (specifically in response to the team production model): "By vesting shareholders with an exclusive right to a corporation's residual, then, the principal-agent model facilitates adoption of the sort of mechanisms that can reduce the risk of opportunism and thus minimize the transaction costs associated with inducing team-specific investment."[179] This is no more or less than a simple reassertion of the basic norm of shareholder primacy, indicating that debate on the subject is at least as much cultural as it is logical. As discussed in the following Section, sufficiently divergent world views are unlikely to prevail upon one another by means of public reason.

D. Cultural Cognition

Libertarian and asymmetric paternalisms might be praised by some for their theoretic ability to slip the paternalistic (or interventionist) camel's nose under the libertarian (or free market) tent on matters including, but not limited to, the framing of various issues. Neither approach is likely to be satisfying, however, to those who would rename the camel "communitarian," "feminist," or "critical" and escort it into the living room through the front door. This same

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176 *See* Ian Ayres, *Fair Driving: Gender and Race Discrimination in Retail Car Negotiations*, 104 HARV. L. REV. 817, 827–33 (1991) (finding that "[b]lack female testers were asked to pay over three times the markup of white male testers, and black male testers were asked to pay over twice the white male markup").

177 *See* WOODWARD, *supra* note 90, at 45–48 (finding that of "all non-subsidized loans, Latino borrowers are charged $1,043 more and African American borrowers $756 more, on average, than nonminority borrowers").

178 *See, e.g.*, Bainbridge, *supra* note 150; Alan J. Meese, Essay, *The Team Production Theory of Corporate Law: A Critical Assessment*, 43 WM. & MARY L. REV. 1629, 1634 (2002) (offering a contractarian response to the team production approach).

179 Meese, *supra* note 178, at 1671.

lack of satisfaction might also be directed at the theory of cultural cognition, which nonetheless is quite practically compelling.

Cultural cognition theory recognizes the priority of culture in an individual's assessment of such matters as the validity of facts and the perception of risk.[180] Pursuant to the theory, "culture worldviews" may be usefully classified by "group" and "grid."[181] "Group" is a question of whether one is oriented toward individualism or communitarianism.[182] "Grid" refers to whether one is inclined toward hierarchical or egalitarian values.[183] The theory rejects public reasoning as a method of resolving intensely polarizing issues,[184] instead suggesting a process of "identity-affirmation" to minimize social discord.[185] Identity affirmation calls for crafting solutions that permit validation of divergent world views.[186] Its proponents suggest, for instance, a resolution of the gun control debate pursuant to which gun owners registering their guns are paid bounties for doing so, thus validating both the safety concerns of those who would prefer gun control and the autonomy of those who fear loss of the "right" to bear arms of their choosing.[187]

Although corporate exploitation of financial consumers may not be of sufficiently high profile to qualify as an intensely polarizing issue, perhaps it would be if sincere attempts were made to outlaw any large number of financial goods or services simply on the grounds that they are substantively abusive. In any event, the issue obviously is one as to which divergent world views would come into play. Individualists and communitarians would be likely to selectively and differentially perceive the validity of scientific studies on heuristics and the like. Individualists might insistently postulate the rationality of consumers and oppose government intervention on their behalf. This is particularly true if they also are hierarchists who regard consumers who either lack financial stability or perfect rationality as not worthy

180 *See* Dan M. Kahan & Donald Braman, *Cultural Cognition and Public Policy*, 24 YALE L. & POL'Y REV. 149, 150–57 (2006) (defining "cultural cognition" as "the psychological disposition of persons to conform their factual beliefs about the instrumental efficacy (or perversity) of law to their cultural evaluations of the activities subject to regulation").

181 *Id.* at 153.

182 *Id.*

183 *Id.*

184 *Id.* at 151.

185 *Id.* at 168.

186 *Id.* ("Policymakers can harness this identity-affirmation effect by designing policies that are sufficiently rich in their social meanings to affirm the values of persons of diverse cultural worldviews simultaneously.").

187 *Id.* at 170.

of protection if they are not capable of protecting themselves. Communitarians, on the other hand (particularly those of an egalitarian bent), might go so far as to prefer outright governmental limitations on consumer choice if such limitations would reduce personal bankruptcies, economically forced relocations, etc. A solution acceptable to many necessarily will disappoint some.

That said, cultural cognition does seem to teach that without some sort of cultural agreement, some problems simply will not be resolved;[188] in fact, there may not even be a consensus that they exist. It may well be that exploitation of financial consumers falls into this latter category. Accordingly, those who do see a problem realistically must circumscribe their attempts to solve it. As to this, cultural cognition almost certainly has something to teach. For instance, it would be well to characterize remedial proposals as simple attempts to redress market malfunction. Corporate manipulation of the preferences of financial consumers thus should be described as a type of market failure rooted in lack of disclosure. That lack may be redressed by encouraging providers of financial goods and services to compete on the basis of the disclosure that they are willing to provide. Although there presently is no legal impediment to such competition, CFPB sponsorship of an appropriate platform (with concomitant enforcement against disclosures that are misleading) would seem to be a useful first step in bringing it about.

Conclusion

This Article has taken the position that financial consumers cannot be expected to be rational in the strict economic sense. In light of the complexity and proliferation of various financial goods and services, as well as limits on individual time and cognitive ability, consumers inevitably take shortcuts in making decisions. Some of these decisions then turn out to be wrong—in fact, so very wrong that it is almost inevitable that the providers of the goods and services in question foresaw this would be the case. Still, because many of those providers are corporate entities, the argument can be made that the

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188 Kahan and Braman suggest solutions that try to join conflicting cultural values together, because

> [i]t's only when [citizens] perceive that a policy bears a social meaning congenial to their cultural values that citizens become receptive to sound empirical evidence about what consequences that policy will have. It's therefore essential to devise policies that can bear acceptable social meanings to citizens of diverse cultural persuasions simultaneously.

Id. at 171.

individuals managing the entities were obliged to assist consumers in cutting their own financial throats. Although the obligation might not be a legal one, it nonetheless is one that is psychologically encouraged by market accountability.

The proposal discussed above is intended to provide financial consumers with better guidance, at least as to decisions that are most likely to be truly disastrous, and to do so in a method that might counter at least a bit of the psychological pressure on corporate directors to make decisions in the name of shareholder primacy. The precise mechanism suggested is to ask directors to (1) familiarize themselves with the consumer financial offerings of the firms for which they act and (2) express (truthful) opinions as to the advisability of those offerings for consumers in particular straits. The platform on which the mechanism would operate is a best-practices certification sponsored by the CFPB. Such sponsorship clearly is within the mandate of the CFPB—so clearly so that some will regard the proposal as quite disappointing. Attempts to aggressively exercise the full extent of the Bureau's authority might, however, result in the type of intense polarization said by cultural cognitivists to defeat resolution of any type. The proposal therefore is pragmatically oriented toward emphasizing that the existing plight of at least some financial consumers is a failure of disclosure—one that may be addressed by encouraging corporations to experiment with competition on the basis of their consumer-friendly decisionmaking processes and recommendations. If the experiment is quickly abandoned or not undertaken in any significant regard, the time for more aggressive measures may have arrived.