Reputation Failure: The Limits of Market Discipline in Consumer Markets

Yonathan A. Arbel
University of Alabama - School of Law, yarbel@law.ua.edu

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REPUTATION FAILURE: THE LIMITS OF MARKET DISCIPLINE IN CONSUMER MARKETS

Yonathan A. Arbel*

Many believe that consumer-sourced reputational information about products should increasingly replace top-down regulation. Instead of protecting consumers through coercive laws, reputational information gleaned from the wisdom of the crowd would guide consumer decision-making. There is now a growing pressure to deregulate in diverse fields such as contracts, products liability, consumer protection, and occupational licensing.

This Article presents a common failure mode of systems of reputation: “Reputation Failure.” By spotlighting the public-good nature of reviews, rankings, and even gossip, this Article shows the mismatch between the private incentives consumers have to create reputational information and its social value. As a result of this divergence, reputational information is beset by participation, selection, and social desirability biases that systematically distort it. This Article argues that these distortions are inherent to most systems of reputation and that they make reputation far less reliable than traditionally understood.

The limits of reputation highlight the centrality of the law to the future of the marketplace. Proper legal institutions can deal not only with the symptoms of reputation failure—consumer mistakes—but improve the flow and quality of reputational information, thus correcting reputation failures before they arise. This Article offers a general framework and

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explores a number of strategies. A more robust system of reputation can preserve consumer autonomy without sacrificing consumer welfare.

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I. INTRODUCTION

How much trust should we place in consumer-sourced reputational information? This Article develops the argument that systems of reputational information are subject to a number of distortions that limit the reliability of reputational information. As a result, trusting these systems to replace the law should be done with
great caution. The source of these distortions and the role of the law in addressing them are the key themes developed here.

Some of the most important debates in contract law involve a basic dilemma: to what extent can markets be trusted to regulate themselves? One reason why regulation may be needed is asymmetric information—if sellers know more, they can exploit buyers and promise high but deliver low. A mitigating factor, which counsels against less regulation, is reputation. Reputation information, once the province of small-knit communities, allows parties to develop trust based on self-interest. If the seller cheats, her reputation will suffer, costing her opportunities to deal with other buyers. In the last two decades, reputational information has permeated almost all aspects of consumer markets, online and offline. Through the use of rankings, reviews, and stars, reputation facilitates transactions between complete strangers.

The explosion of reputational information has instilled a sense of optimism among many that the end of asymmetric information is nigh. Why regulate markets, the argument goes, if consumers can easily know in advance which seller is honest, which product is best, and which service provider is most reliable? The increased trust in

1. The debate on law versus markets assisted by reputation is longstanding. For example, Milton Friedman argued that “consumers do not have to be hemmed in by rules and regulation . . . because they are protected by the market itself.” Milton Friedman’s Free to Choose: Who Protects the Consumers? (PBS television broadcast Jan. 11, 1980), https://www.freetochoosenetwork.org/programs/free_to_choose/index_80.php?id=the_power_of_the_market; see also Adam Smith, Lectures On Jurisprudence 327 (R.L. Meek et al. eds., 1978) (“When a person makes perhaps 20 contracts in a day, he cannot gain so much by endeavoring to impose on his neighbors, as the very appearance of a cheat would make him lose.”); Lior Jacob Strahilevitz, Less Regulation, More Reputation, in The Reputation Society 71 (Hassan Massum & Mark Tovey eds., 2012) (arguing that a world with strong reputational information has “diminished need for regulatory oversight and legal remedies”); Rory Van Loo, Helping Buyers Beware: The Need for Supervision of Big Retail, 163 U. PA. L. REV. 1311, 1347 (2015) (“One common argument in consumer protection is that reputational concerns will stamp out many bad practices, thus making some regulations unnecessary.”). On these notions, see infra Subpart II.A.


reputation has galvanized support for deregulatory policies from conservatives and liberals alike. Various scholars have made calls to abolish consumer protections in contracts, torts, and occupational licensing. The Trump Administration has effectively defanged the Consumer Financial Protection Bureau and otherwise stalled many regulatory interventions in markets.

This trust in reputation-based market ordering overlooks a key feature of reputation: it is a public good. Through gossip, word-of-


7. Technically, reputation is a public good because it is neither excludable nor is consumption rivalrous. See Tyler Cowen, Public Goods, in CONCISE
mouth, online reviews, and product ranking, consumers create a body of reputational information covering innumerable products and services—from restaurants and keychains to doctors and car mechanics. This information is then used by future consumers to guide their own decision-making, but the original creators of this information are rarely, if ever, compensated for their efforts. That is, while the costs of creating reputational information are private, the benefits are public. Observing the divergence of private and public costs presents a deep puzzle for all systems of reputation: Who chooses to participate in the creation and dissemination of reputational information, why, and to what effect?

In spotlighting this puzzle and exploring its consequences, this Article identifies a common failure mode of reputational information, called “reputation failure.” Prospective consumers use reputational information to learn about the experiences of a representative sample of similarly situated consumers. This kind of “poll” could inform the consumer about the expected quality of service, the frequency of errors, and the honesty of the seller. However, this poll is subject to three confounding factors: sluggishness, regression to the extreme, and an integrity bias. Reputational information is sluggish, i.e., slow to develop, because sharing consumers are not sufficiently incented to share their experiences. The motivations to share are not only weak, but they are also asymmetric; psychologically, individuals are more inclined to share information when they had a very positive or negative experience. Thus, reputational information tends to “regress to the extremes,” or develop over time in a way that overly emphasizes extreme experiences at the expense of middling ones. And even those experiences that are shared are not always authentic: social and financial motivations to share lead some individuals to misstate their experiences in ways that put themselves in a better light or otherwise favor them. This leads to an integrity bias.

In the presence of reputation failure, dishonest sellers can thrive, not just in the short term but also over longer spans of time. Reputation failure thus suggests the limits of market discipline through reputational information.
These concerns with reputation failure are consistent with some important trends in the empirical data.\textsuperscript{11} Amazon is a case in point; despite the cornucopia of products listed there, reviews follow an unusual distribution.\textsuperscript{12} One might expect that among so many products, some reviews would be exciting and others disappointing, but that the majority would be middling. Evidence from millions of products contradicts this expectation; reviews concentrate in the extremes and are scarce in the middle.\textsuperscript{13} Additional evidence suggests that the properties of the products themselves do not drive this unusual distribution. For example, there is little agreement—quite often, disagreement—between the rating of the same products by professionals and consumers.\textsuperscript{14} There is also little agreement among consumers on different platforms regarding the same products.\textsuperscript{15} And when consumers are asked to rate products in lab settings, their reviews show a remarkably different distribution.\textsuperscript{16} Despite reputation failures, consumers reportedly rely on reputational information. In a recent survey, 82 percent of American adults said they sometimes or always read reviews before making new purchases, and more than two-thirds of those who routinely use reviews described them as “generally accurate.”\textsuperscript{17} Similarly, a survey of online users found that, on average, users rated the credibility of the last review they read as a 4.2 out of five, or roughly 84 percent, on average.\textsuperscript{18}

Not all reputation failures are severe but ignoring the risk of failure is a serious omission. In some cases, sophisticated consumers might be able to mitigate part of the distortionary effect of reputation failure by interpreting reputational information using a combination of freedom of contract have generally rejected intervention by relying on reputational constraints.”\textsuperscript{18}).

11. See infra Subpart III.B for a more general discussion of the evidence.
12. See infra note 171.
13. At least, one would expect a unimodal distribution, but this is contradicted in the data. See infra Subpart III.B.
14. Bart de Langhe et al., \textit{Navigating by the Stars: Investigating the Actual and Perceived Validity of Online User Ratings}, 42 J. CONSUMER RES. 817, 821 (2016) (studying correlations between online reviews and scores provided by the magazine \textit{Consumer Reports} and finding that “[t]he average correlation is 0.18, and 34% of correlations are negative”).
15. See Georgios Zervas et al., \textit{A First Look at Online Reputation on Airbnb, Where Every Stay is Above Average} 10 (Jan. 28, 2015) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2554500 (finding that the ranking on Airbnb only explains 17 percent of the correlation ($R^2$) between cross-listed properties on TripAdvisor).
16. See infra Subpart II.B.2.
17. Aaron Smith, \textit{Online Reviews}, P\textsuperscript{E}W \textit{R}ESEARCH CTR. (Dec. 19, 2016), http://www.pewinternet.org/2016/12/19/online-reviews/ (explaining that even among the general population, 51 percent of US adults described reviews as generally giving an accurate picture).
18. Cindy Man-Yee Cheung et al., \textit{Is This Review Believable?}, 13 J. Ass’N. INF\textsuperscript{O}. SY\textsuperscript{S}. 618, 624 (2012).
of heuristics, statistical analysis, multisource analysis, and experience.\textsuperscript{19} However, it is important to recognize that the power of these methods is limited; there is only so much signal that can be extracted from a biased and noisy sample.\textsuperscript{20} To illustrate this claim, I employ a method known as a Monte-Carlo simulation, which illustrates the limits of such heuristics.\textsuperscript{21}

Like other forms of market failure, the existence of reputation failure has various legal implications. Most directly, reputation failures call for greater scrutiny of consumer transactions and stricter regulation of product safety and quality. Such regulation can come in the form of mandatory warranties, broader disclosure obligations, good-faith requirements, product liability duties, etc.\textsuperscript{22}

Legal interventions, however, need not be limited to the consequences of reputation failure. The law can also improve the quality of reputation itself, thus avoiding the failure of reputation in the first place. To this end, I propose here a new framework of synthesizing legal institutions and markets, called Reputation-by-Regulation. Policymakers can significantly improve consumer welfare while preserving consumer autonomy by focusing on designing rules that improve and increase the flow of reliable reputational information to the market. Building channels through which reputational information can effectively flow to the market can solve reputation failure and allow consumers to choose freely and effectively for themselves. To guide future policymaking, this Article illustrates Reputation-by-Regulation through five concrete types of effective legal interventions.

The analysis in this Article should also inform economic analysis more generally. It is very common, even in leading economic models, to assume that reputation is an inherent feature of the market.\textsuperscript{23} Sellers sell, buyers buy, and reliable reputational information miraculously emerges.\textsuperscript{24} These studies could benefit from explicit

\textsuperscript{19} See, e.g., id. at 627–28.


\textsuperscript{22} See Ranchordás, supra note 4, at 459–61 (discussing regulations imposed and suggested within the sharing economy); see also Stemler, supra note 4, at 703–11 (offering additional regulatory solutions).


recognition of the “microfoundations” of reputation—the incentives that lead individuals to share their experiences with others, and their consequences for the reliability of reputational information.\textsuperscript{25}  

This Article unfolds in five parts. Part II explores the role of reputation in our thinking about the proper scope of intervention in consumer markets. It highlights how central is the idea that reputation is reliable. Part III develops the “microfoundations” of reputation. It surveys the motivations to produce reputational information and explains how these lead to \textit{systemic} bias. Finally, Part IV explores the legal-market interface and the use of the law to improve reputational information flows.

II. LAW VS. MARKETS AND ASYMMETRIC INFORMATION

This Part surveys debates on regulation, deregulation, and the role of reputation. It shows how critical reputation is to these debates and yet how very little attention is given to the reliability of reputational information. As this Article will show, imperfections and failures in reputational information undermine the validity and persuasiveness of many market self-ordering arguments.

A. Law vs. Markets

Most commercial transactions involve asymmetric information between sellers and buyers. Buying a refrigerator or a car, hiring a contractor, and seeking a financial advisor are all quotidian transactions that involve what economists call “experience” goods—i.e., goods where the consumer can only observe quality after consumption or usage.\textsuperscript{26} The concern with such transactions is that

\textsuperscript{25} See, e.g., Roy Shapira, \textit{Reputation Through Litigation: How the Legal System Shapes Behavior by Producing Information}, 91 WASH. L. REV. 1193, 1203 (2016) (describing the perception of reputation in the scholarship as the product of a simple process). This reductive view uncritically assumes, with only a few exceptions, that reputation information is reliable. For prominent examples in economics, see, e.g., Heski Bar-Isaac & Steven Tadelis, \textit{Seller Reputation, 4 FOUND. & TRENDS IN MICROECONOMICS} 273, 282 (2008) (reviewing the literature); Board & Meyer-Ter-Vehn, \textit{supra} note 23, at 2386–87. A leading paper in evolutionary psychology argues that reputation is an evolutionary solution to the tragedy of the commons with respect to public goods, not acknowledging that the creation of reputation itself suffers from the same problem. See Manfred Milinski et al., \textit{Reputation Helps Solve the ‘Tragedy of the Commons’}, 415 NATURE 424, 424 (2002); see also Martin A. Nowack & Karl Sigmund, \textit{Evolution of Indirect Reciprocity}, 437 NATURE 1291, 1291 (2005) (noting the evolutionary roots of reputation).

\textsuperscript{26} See Gary T. Ford et al., \textit{An Empirical Test of the Search, Experience and Credence Attributes Framework}, in 15 ADVANCES IN CONSUMER RESEARCH 239,
they invite opportunistic behavior, as sellers might take advantage of the information asymmetry by promising high but delivering low.\textsuperscript{27} This possibility, left unchecked, would lead to misallocation of resources, abuse of buyers, and increased buyer trepidation, stalling economic activity overall.\textsuperscript{28}

The conventional response to such problems is direct regulation. To give but a few examples, the law sets ex ante minimum quality regulations;\textsuperscript{29} mandates price controls;\textsuperscript{30} imposes good-faith duties;\textsuperscript{31} compels mandatory disclosure;\textsuperscript{32} creates implied warranties of merchantability and fitness;\textsuperscript{33} requires licensing, training, and testing;\textsuperscript{34} enforces truth-in-advertising requirements;\textsuperscript{35} and imposes tort and criminal liability for violations of any of these standards.\textsuperscript{36}

All of these measures are meant to curb abuse of asymmetric information and to facilitate trust in the market. With regulation,

\begin{footnotesize}
241 (Michael J. Houston ed., 1988). A subtle issue is that while individual preferences are idiosyncratic, they are still predictive. A consumer contemplating the purchase of a microwave may be different in any number of ways from past consumers, yet, learning that other consumers disliked the microwave would still inform the consumer’s private decision.


29. See, e.g., 7 C.F.R. § 996.13 (2018) (requiring that peanuts considered “Segregation 1” shall not have more than 2.49 percent damaged kernels).

30. See, e.g., ALA. CODE § 8-8-1 (1975) (setting a cap of 8 percent on the price of credit).


33. See, e.g., Choi & Spier, supra note 5, at 735 (explaining that courts are “generally hostile toward[s]” attempts to opt-out of product liability).

34. See, e.g., MISS. CODE ANN. § 73-9-29 (1972) (requiring practicing dentists to attend a board-certified educational program and pass an exam before receiving a license to practice in the state).

35. See, e.g., U.S. FOOD & DRUG ADMIN., \textit{INGREDIENTS DECLARED AS EVAPORATED CANE JUICE: GUIDANCE FOR INDUSTRY} (2016) (providing that a sweetener cannot be described as “evaporated cane juice” because it may mislead consumers to believe that it is juice rather than sugar).

36. See, e.g., 815 ILL. COMP. STAT. ANN. 505/2, 7 (West 2016) (imposing criminal and civil liability for consumer fraud).
\end{footnotesize}
consumers can trust—to an extent—that a car seat, for example, will be sufficiently safe even if the producer is unknown or that an unfamiliar merchant will not engage in unfair business practices.

Free-market advocates contest the need for such laws, which necessarily limit freedom of contract, and instead argue that law is “only one of many social institutions and practices amid which markets function.”37 One such institution, arguably the most central one, is reputation.38 Part of Adam Smith’s genius was the insight that reputation facilitates trust in markets, even if actors are self-interested; as Smith explained, the baker will soon realize that selling low-quality bread will diminish his reputation and thus future profits, making dishonesty an unprofitable business strategy.39 Drawing on this insight, influential scholars such as Milton Friedman, Richard Posner, and Richard Epstein have called to deregulate markets and rely instead on internal market discipline.40

These debates are longstanding and tend to track traditional political stances on the government, top-down regulation, and the free market.41 Recently, however, a sea change has swept many progressives and left-leaning thinkers towards the deregulatory camp.42 The rise of the sharing economy and information technology has inspired widespread belief in the impending death of asymmetric information.43 In the past, private ordering through reputation was understood to be the domain of small-knit communities, such as Orthodox Jewish diamond traders or cattle ranchers in small counties, as these small communities could effectively exchange

39. See SMITH, supra note 1; see also ALBERT HIRSCHMAN, RIVAL VIEWS OF MARKET SOCIETY 106–07 (1992).
41. Venerable traditions in political theory—Godwinian utopia and Smithian natural liberty—believe reputation can effectively constrain self-interested behavior. Klein, supra note 8, at 2–3. As economist Benjamin Klein observed, “[i]f one puts small confidence in the efficacy and integrity of external authority—in particular, governmental institutions—then the hope for self-policing gains in relevance.” Id. at 2.
43. See Tabarrok & Cowen, supra note 3.
gossip and other word-of-mouth reputational information. The rise of information technology now promises gossip at scale. Drug users, involuntary regulatory entrepreneurs as they are, utilize message boards to spread reputational information on which cocaine dealer uses cheap fillers. Less daring consumers use popular reputation platforms such as Amazon and Uber to guide their decisions on everyday purchases. The meteoric rise of these platforms enthused many about a future where regulatory interventions are moot, as consumers do the work organically for their peers without coercive

44. See Robert C. Ellickson, Order Without Law: How Neighbors Settle Disputes v1 (1991); Bernstein, Opting Out, supra note 2, at 115, 130, 139–40 (analyzing the behavior of Jewish Orthodox diamond traders in New York); see also Stewart Macaulay, Non-Contractual Relations in Business: A Preliminary Study, 28 AM. SOC. REV. 55, 55, 63 (1963) (studying the behavior of managers in Wisconsin).


46. See Cheung et al., supra note 18, at 619; Smith, supra note 17.

and often misguided government intervention. Given this new zeitgeist, there is little in the way of effective opposition to the recent policy trends that have dramatically scaled down consumer protection.

To give a sense of where the contemporary battle lines are drawn, consider the influential debate between Professors Richard Epstein and Oren Bar-Gill (who also serves as a reporter for the new Restatement of Consumer Contracts). Both scholars debate the old question of asking how severely contract law should limit the freedom of contract in the name of other interests. Epstein concedes the existence and importance of cognitive constraints on consumer decision-making, which he agrees can lead to “serious mistakes.” Still, in his view, “second-order rationality” in the form of reputation, among other sources, can overcome these shortcomings. Remarkably, Epstein sees reputation as a valid response to the new problems posed to the traditional model by behavioral economics. In contrast, Bar-Gill argues that because goods are sometimes unique, or consumers use them in unique ways, there is too little information that is transferable among consumers. Under such conditions, Bar-Gill contends, there is still a need for regulatory interventions in private contracts, such as safety standards or immutable warranties.

The most surprising feature of this debate is not the disagreement but the broad agreement that underlies it. For standardized goods (or standard uses), reputation, in addition to

48. See Rory Van Loo, The Corporation as Courthouse, 33 YALE J. REG. 547, 569 (2016) (noting the trend where “[t]he consumer legal system is evolving toward a similar reliance on reputation-based governance mechanisms”). On the problem of authority, see MICHAEL HUEMER, THE PROBLEM OF POLITICAL AUTHORITY 100 (2013) (arguing that courts have a limited role and “may not go on to coercively impose paternalistic or moralistic laws”); see also Charny, supra note 47, at 1845–47 (highlighting the centralization inherent to informal systems of ordering); Duncan Kennedy, The Role of Law in Economic Thought: Essays on the Fetishism of Commodities, 34 AM. U. L. REV. 939, 944–49 (1985) (critiquing the tendency to see the market as natural and state interventions as artifice).

49. See sources cited supra note 5.


51. See Bar-Gill, supra note 5, at 749–54; Epstein, supra note 50, at 808–10.

52. Epstein, supra note 5, at 111.

53. Id.

54. Epstein, supra note 50, at 811.

55. Bar-Gill, supra note 5, at 756 (“[Epstein] forcefully argues that mistakes with respect to the value of a standardized product are unlikely to persist in the marketplace. But not all products are standardized . . . . With a non-standardized good, the information obtained by one consumer might not be relevant to another consumer who purchased a different version of the nonstandard good.”).

56. Id. at 793–94.
other background pressures, can be sufficiently potent to curb opportunistic behavior. Hence, contract and consumer law need not worry about intervening in areas where product reputation is abundant.\textsuperscript{57} Similar attitudes were expressed by other leading figures in the field and in the context of torts, occupational licensing, and even drug regulation.\textsuperscript{58} As shall become clear, the existence of reputation failures undermines this view.

B. The Supposed Reliability of Reputation in Legal Thought

These debates highlight the centrality of the belief that reputation is an effective, dependable, credible, and reliable regulator.\textsuperscript{59} Advocates argue that the loss of reputation is immediate, independent of lengthy and uncertain trials, and stems from the interactions of the parties themselves.\textsuperscript{60} Additionally, reputation allows parties to tap into assets that the legal system cannot reach.\textsuperscript{61} For these reasons, advocates believe that what the law does slowly and inaccurately, reputation can do quickly and precisely.\textsuperscript{62}

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\textsuperscript{58} See supra sources cited supra note 5.


\textsuperscript{60} See Richman, supra note 38, at 2335.

\textsuperscript{61} Id. at 2332 (explaining that efficient enforcement is more important than efficient administration in explaining why merchant communities prefer private ordering to contractual enforcement).

As central as reputation is to these debates, it is perplexing to see how little attention is given to reputation’s nature. Instead, the literature mostly relies on a simplistic “emergentist” view of reputation that ignores all questions of how reputation comes to be. The reputation of goods and services is described as simply emerging from complex market interactions. A seller sells a widget and once enough consumers purchase and use it, the widget “automatically” gains a reputation for quality. Somehow, reputation emerges. From where? How? By whom? These issues are hardly ever addressed. Instead, reputation is taken to be, as Shapira pointedly notes, “[a] frictionless, uncomplicated process in which individuals somehow get access to information.”

It is hard to overstate just how common it is for people to perceive that reputation is reliable and how much this perception influences policy. Take, for example, economic models of market transactions; there, it is common to assume that “[t]he moment that a person cheats, it becomes common knowledge that the person lacks integrity, and hence there is no cooperation for the rest of the game.” In the foundational Klein-Leffler model of reputation, consumers are explicitly assumed to “costlessly communicate [quality information] among one another.” Such spontaneous reputational information is then thought to propagate “throughout the community without


64. A view is emergentist if it identifies a phenomenon only at the complex level. For example, the quality of “saltiness” does not describe the taste of chlorine or sodium, yet their combination creates a salty ionic compound; a grain of sand has no “pileness” to it, but once enough grains are collected, a pile emerges; or, more contentiously, no neuron has self-awareness, yet their collection seems to cause conscience. This omission is hardly unique to law; for a recent example in other fields, see Wenqi Shen et al., Competing for Attention: An Empirical Study of Online Reviewers’ Strategic Behavior, 39 MGMT. INFO. SYS. Q. 683, 684 (2015) (“[M]ost of the existing literature has overlooked the question of how online reviewers are incentivized to write reviews.”).

65. See Richman, supra note 59, at 750.

66. See Richman, supra note 59, at 750.

67. Shapira, supra note 25, at 1203.


69. Klein & Leffler, supra note 47, at 617. They do admit the possibility of imperfect recall of reputational information. Id.
In legal scholarship, this conception arises most clearly in defamation law jurisprudence where reputation is thought of as a right—natural, static, or inherent, like property or dignity—that comes into being by immaculate conception and must be “protected” against those who seek to besmirch it.71

Some scholars have started to recognize cracks in the traditional paradigm.72 As they note, reputational information may be costly to obtain, noisy,73 distorted by the incentives of intermediaries,74 or ineffectual (if, for example, a sellers’ presence in the market is short-lived).75 Economists Paul Milgrom and John Roberts focus on the difficulty of creating reputation when opportunistic behavior is hard to detect.76 Similarly, Professor Alan Schwartz notes the potential costs of reputation, explaining that “the innocent party [to a failed transaction] will incur costs in informing others that it was not at fault, and third parties will incur costs learning about which of the contract parties is unreliable.”77 Finally, Professor Bar-Gill emphasizes the possibility that in some markets there will be an insufficient volume of reputational information.78 Still, even admitting reputation’s potential noise does not amount to a claim that recognizes the inherent systematic distortion of reputational information.79 Rather, the noise is thought to disappear, as new information accumulates and “increases the diagnosticity and persuasiveness of reputation.”80 Moreover, these are exceptions. The dominant view in the policy and scholarship is still very much emergentist, expressing great trust in the reliability of reputation.

The emergentist view is problematic for several reasons, not the least of which is its lack of any theoretical underpinnings that explain when—and when not—reputation will come to be. Why is
information about some products abundant whereas information for other products is sparse? Another problem is that many jurists have come to think of reputation as a right that belongs to individuals, rather than the byproducts of dynamic social processes. As a result, much of the discussion about reputation neglects its social value. But most disconcerting is the implication that reputation is generally reliable—that it fairly describes the quality of the underlying good without systematic bias. After all, if reputation simply emerges, there is no process by which it will be “tainted.” Thus, the proposition that reputation can be unreliable cuts at heart, nerve, and sinew of these influential works.

III. REPUTATION FAILURE: MICROFOUNDATIONS, DISTORTIONS, AND SOCIAL WELFARE

When my neighbor complained that his newly purchased lawn mower was shoddy, he created reputational information. When user “daniel” wrote on Amazon that a play tent has “the stability of a house of cards,” he or she created reputational information. When musician Dave Caroll uploaded his song “United Breaks Guitars” to YouTube, he created reputational information, and powerful information at that: United’s stock price fell ten cents, representing a market cap loss of $180 million.

Reputation is information. It is a kind of statistical information which helps consumers predict their own experiences based on the


82. See Posner, supra note 47, at 252–53 (1981) (“It makes no sense to treat reputation as a ‘right.’ Reputation is what others think of us.”).

83. See Heymann, supra note 63, at 1342.

84. See Nick Emler, Gossip, Reputation, and Social Adaptation, in GOOD Gossip 135 (R. F. Goodman & A. Ben-Ze’ev eds., 1994) (“Reputations do not exist except in the conversations that people have about one another.”).


distribution and valence of experiences of past consumers. As such, reputational information is like a poll. But as the examples highlight, this kind of information does not simply emerge; rather, it is the fruit of deliberate action by disparate individuals who decide to take time and effort to share reviews, opinions, gossip, and other word-of-mouth information.

The most basic observation to make is that such peer-to-peer reputational information is a public good. While everyone benefits from having this public resource, producers of reputational information are not directly compensated for their contributions. Private costs and public benefits are a recipe for the well-known free-rider problem—like national defense, clean air, and a vaccinated society—where there is a constant concern with overconsumption and undersupply.

Once reputation is seen as public good, a deep puzzle is exposed: What motivates individuals to share reputational information? Who does so? And, critically, to what effect?

This Part explores these “microfoundations” of reputation and their consequences. It shows how people share experiences for reasons that are mostly private and self-serving. As a result, future consumers are often exposed to a highly unrepresentative and biased sample of limited credibility. Inferences drawn from such samples can be highly misleading, even for those consumers who are aware of them and try to account for them. As data scientists would say: Bias in, bias out.

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87. See Goldman, supra note 9, at 294; Shapira, supra note 25, at 1201.
88. See Cowen, supra note 7. Once reputational information exists, it is hard to prevent people from using it (i.e., it is non-excludability); nor does use of this resource diminish it (i.e., it is non-rivalry). See Larry Downes, The Economics of Information: From Dismal Science to Strange Tales, in The Next Digital Decade 273, 277–78 (Berin Szoka & Adam Marcus eds., 2010). Professional publications solve these problems by commoditizing the information they produce, which is subject to copyright and other protections. See, e.g., N.Y. GEN. BUS. LAW § 397 (McKinney 1961) (prohibiting the unconsented use of nonprofits’ test results by nonprofits).
89. Today, reputational platforms reap most of the benefit of reputation aggregation, but reputation’s direct producers receive very little reward. These issues are sometimes conceptualized as a tragedy of the commons. See Garrett Hardin, The Tragedy of the Commons, 162 SCI. MAG. 1243, 1243–48 (1968).
90. By and large, legal scholars have glossed over this question. One notable exception is Robert D. Cooter, Decentralized Law for A Complex Economy: The Structural Approach to Adjudicating the New Law Merchant, 144 U. PA. L. REV. 1643, 1669 (1996) (arguing that individuals disseminate reputational information due to an internalized social norm).
91. For an exploration of consumer activism in the marketplace, see Yonathan A. Arbel & Roy Shapira, Consumer Activism: From the Informed Minority to the Crusading Minority, DePaul L. Rev. (forthcoming 2019) and Arbel & Shapira, supra note 2.
A. The Microfoundations of Reputation

1. The Costs of Gossip

Creating and sharing reputational information involves effort, time, and, in some cases, the risk of legal liability. "Bianca S." must have spent the better part of her lunch break writing a 143-word review of a cleaning service attached alongside six photos of her home.93 One anonymous Amazon user probably spent at least a few minutes writing a 291-word review of his experiences with Kevlar gloves,94 and "The Amazing Lucas" in all likelihood spent a few hours creating and editing a seven-minute review of the movie It.95 Not only is creating reviews time consuming, it is also sometimes emotionally difficult to say negative things about others.96 Beyond these costs, as will be elaborated below, there is a growing tendency among some service providers to sue consumers for negative reviews, using factual inaccuracies and misstatements to ground their lawsuits.97 Such lawsuits can involve months of litigation, a serious disruption, and—in some rare cases—large judgments.98

These broadly-defined costs suggest that there must be countervailing motivations to produce reputational information, or else people—as distinct from sellers, advertisers, and affiliates—will not generate reputational information. Citing the utility of reputation to the operation and efficiency of the market, as well as the welfare of future consumers, is insufficient as these are public benefits.99 What needs to be determined, then, are the specific private benefits—what the sharing individual gets from incurring these costs.

2. Internal Drives: On Spite and Gratitude

Starting in the 1960s, psychologists began investigating the psychological drives impelling individuals to participate in

95. The Amazing Lucas, it movie 2017 review WHY THIS MOVIE IS BAD, YOUTUBE (Sept. 12, 2017), https://www.youtube.com/watch?v=PEKLBj6-nY.
97. See infra Subpart IV.B.5.
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word-of-mouth activity.100 In an influential paper, psychologist Ernest Dichter highlighted four internal motivations: self-centered perceptions, quality of experience, altruistic motivations, and message involvement.101 In the presence of these factors, individuals would be motivated to create and share reputational information.102 Over time, however, this theory encountered difficulties. Most problematic were the empirical findings that consumers are more likely to share reputational information when they had a favorable experience.103 Yet other evidence showed the exact opposite: dissatisfaction yields greater propensity to share.104 In 1998, business professor Eugene Anderson reconciled these findings by explaining that the underlying issue is the extremity of experience rather than its valence.105 Further, current work in psychology explains the creation of favorable and negative reviews as a distinct activity motivated by different internal impetus. For example, D.S. Sundaram et al. argued that positive word-of-mouth results from altruism,106 product involvement, self-enhancement, and a desire to help the company, whereas negative word-of-mouth is due to anxiety reduction, vengeance, altruism, and advice-seeking purposes.107

Critically, these internal drivers are related to the quality of the experience. The standard Expectation Disconfirmation Theory holds that the gap between expectation and reality creates a sense of

100. The propensity to help others, as well as the idea that one must “retaliate” against wrongs and “reward” generosity, has strong roots in evolutionary psychology and social norms. See ELINOR OSTROM, TRUST AND RECIPROCITY: INTERDISCIPLINARY LESSONS FOR EXPERIMENTAL RESEARCH 41–44 (2003); Yonathan A. Arbel & Yotam Kaplan, Tort Reform Through the Back Door: A Critique of Law and Apologies, 90 S. CAL. L. REV. 1199, 1212 n.60 (2017); see also Jeffrey L. Harrison, Spite: Legal and Social Implications, 22 LEWIS & CLARK L. REV. 991, 993 (2018) (“[P]erhaps actions that appear spiteful are actually not self-regarding but have deontological significance in that the detractor acts out of sense of duty.”).


102. See Yoo & Gretzel, supra note 101, at 286–88.


106. One oddity with altruistic motivations is that consumers tend to review products that were already extensively reviewed despite the low information value of such reviews. See Jonathan Laffky, Why Do People Rate? Theory and Evidence on Online Ratings, 87 GAMES & ECON. BEHAV. 554, 567 (2014); Fang Wu & Bernardo A. Huberman, Opinion Formation Under Costly Expression, 1 ACM TRANSACTIONS ON INTELLIGENT SYS. & TECH. 1, 3 (2010).

disequilibrium in the consumer that manifests as feelings of spite or gratitude that motivate action. A recently developed, empirically successful variant of this theory is the tractable “brag and moan” model. This model stipulates that independent of expectations, extreme experiences would motivate individuals to share their opinions with others. The problem is, however, that many if not most products and services are not extreme in the experiences they generate. The theory holds that these tepid experiences will tend to be suppressed because they are “boring” and do not evoke any sense of spite or gratitude. Empirical research strongly supports this prediction.

3. Social Pressures and Herd Behavior

Aristotle was not wrong: man is a social animal. As such, we are in some sense “programmed” to cooperate, reciprocate, and engage in social behavior. It is no coincidence that reputation-creating activities stand at the center of so many social activities. In social gatherings, individuals gossip, share experiences, and impart opinions with other members of the social community. Such activities have a clear social function. When transgressors violate community norms, gossip and related activities allow members of the community to learn of the violation and take concerted social action against the transgressor, such as avoidance, disrespect, and in extreme cases, shunning and excommunication. Fearing this,
community members feel a strong pressure to conform, thus maintaining social norms.\footnote{117}{Id. at 57.}

The standard view of social pressures fails to consider the many ways that social forces can also undermine cooperation.\footnote{118}{This conversion—of how social tendencies undermine cooperation—is similar to Adam Smith’s conversion—the idea that selfish behavior can promote cooperation. SMITH, supra note 1, at 326–27.} If a seller misbehaves in a market, it is important that buyers share this information. But proper socialization often consists of masking one’s true feelings, forgiving slights, and avoiding offending others even at the cost of distorting reality (i.e., “white lies”). Forgiveness and charity can play a negative role by leading consumers to avoid pursuing action.\footnote{119}{See Arbel & Shapira, supra note 2 (discussing findings showing that most consumers avoid reacting to seller failure).} Even reciprocity can be problematic, as discovered inadvertently by eBay’s engineers.\footnote{120}{See Chrysanthos Dellarocas et al., Self-Interest, Reciprocity, and Participation in Online Reputation Systems 3 (MIT Sloan, Working Paper No. 4500-04, 2004).} In one iteration, buyers and sellers could rate each other after every transaction.\footnote{121}{Id.} This led reviewers to post (artificially) favorable reviews in the hope that their counterparts will positively review them.\footnote{122}{Id. at 1.} Consumers explained their behavior as being motivated by fear of retaliation: “[I]f I left a bad review, I might be afraid of being retaliated against.”\footnote{123}{See FTC, supra note 47, at 42; Edelman & Geradin, supra note 4, at 316 (“Some users seem to fear retaliation through a review platform.”); see also Bryant Cannon & Hanna Chung, A Framework for Designing Co-Regulation Models Well-Adapted to Technology-Facilitated Sharing Economies, 31 SANTA CLARA HIGH TECH. L.J. 23, 38 (2015).} A similar issue arises with Uber and Lyft, where both drivers and passengers rate each other.\footnote{124}{See, e.g., SAUL KASSIN ET AL., SOCIAL PSYCHOLOGY 285 (10th ed. 2017) (discussing the role of reciprocity with respect to reviews); Stemler, supra note 4, at 692 (discussing the effects of reciprocity in the sharing economy).} In addition, individuals often mask their opinions due to the Social Desirability Bias,\footnote{125}{See Maryon F. King & Gordon C. Bruner, Social Desirability Bias: A Neglected Aspect of Validity Testing, 17 PSYCHOL. & MARKETING 79, 82 (2000) (“Today, [Social Desirability Bias] is considered to be one of the most common and pervasive sources of bias affecting the validity of experimental and survey research findings in psychology.”).} the pressure to strategically project socially acceptable opinions.\footnote{126}{See Lisa Bleydes & Rachel M. Gillum, Religiosity-of-Interviewer Effects: Assessing the Impact of Veiled Enumerators on Survey Response in Egypt, 6 POL. & RELIGION 459, 462 (2013).} A hijab-wearing interviewer would hear more women reporting themselves as religious than an unveiled one.\footnote{127}{Id. at 476.} Similarly, this bias often leads people to misreport tax compliance, porn consumption, homosexual...
activities, recycling, and charity. It is hard to overstate the tendency of individuals to misstate opinions given this bias.

Social pressures often result in individuals herding around popular opinions. Herding is the convergence of opinions, a phenomenon very familiar in public debates, whereby participants “often shift their public statements in accordance with reputational incentives.” Herding is also well documented in the context of reviews. Experiments by University of Washington Professor Ann Schlosser found that exposing subjects to past negative reviews increases the likelihood that the subject will also voice a negative review. Similarly, reviews for popular movies tend to lump around leading opinions. Interestingly, some individuals exhibit an antitherding behavior whereby they strategically express nonconforming opinions, possibly in an attempt to lead the herd. While it is hard to assess the overall effect of social motivations in the abstract, the effect seems large. As marketing professors Wendy Moe and David Schwiedel concluded: “[A] vocal subset of the customer base may dominate the ratings environment, consequently steering the subsequently posted evaluations and deterring some customers from contributing to the environments.”

129. See King & Bruner, supra note 125, at 82.
130. See Timur Kuran & Cass R. Sunstein, Availability Cascades and Risk Regulation, 51 STAN. L. REV. 683, 727–30 (1999); Maria del Mar Rueda et al., Use of Randomized Response Techniques When Data Are Obtained from Two Frames, 9 APPLIED MATHEMATICS & INFO. SCI. 389, 389 (2015). Social motivations are complex and their effects can go in many different directions, including antitherding, as in Radu Jurca et al., Reporting Incentives and Biases in Online Review Forums, 4 ACM TRANSACTIONS ON WEB 1, 1–3, 14, 20, 21, 22, 25 (2010).
132. See Stemler, supra note 4, at 693–94 (discussing evidence of herding in online reviews).
133. See Ann E. Schlosser, Posting Versus Lurking: Communicating in a Multiple Audience Context, 32 J. CONSUMER RES. 260, 264 (2005) (“[R]eadying a negative review triggers posters’ concerns with the social outcomes of their public evaluations, thereby causing them to lower their public ratings strategically.”).
134. See Young-Jin Lee et al., Do I Follow My Friends or the Crowd? Information Cascades in Online Movie Ratings, 61 MGMT. SCI. 2241, 2256 (2015).
135. Wendy W. Moe & David A. Schweidel, Online Product Opinions: Incidence, Evaluation, and Evolution, 31 MARKETING SCI. 372, 383 (2012); Shen et al., supra note 64, at 689–90 (finding that raters choose to review less reviewed books in order to stand out and gain more attention where there are reviewer rankings systems).
136. Moe & Schweidel, supra note 135, at 385. Similarly, others find that attention seeking is another important social motivator (where there are reviewer ranking systems). See Shen et al., supra note 64, at 685. Additionally, maintaining an online social identity (rather than anonymity) was found to lead to more quality content. Zhongmin Wang, Anonymity, Social Image, and the
4. Material Incentives: Shilling and Cherry-Picking

Material rewards are the most direct form of incentivizing individuals to share reputational information. The familiar version of that is “shilling,” also known as “fake reviews” or “astroturfing,” which involves the provision of payments in exchange for (unfounded) positive reviews. Shilling is reported to be quite common, with some estimating that as much as 30 percent of online reviews are fake. In 2013, for example, Samsung was fined $340,000 because it paid for fake reviews—both positive reviews for their own products and negative reviews for their competitors. Various websites offer full reimbursement of the purchase of certain products in exchange for positive reviews, which are then reported by the unwitting platforms as being made by “verified users.” Firms also use negative rewards, i.e., sanctions, to deter consumers from sharing negative reviews. Until the recent passing of the Consumer Review Fairness Act, and perhaps continuing despite the law, firms would include nondisparagement clauses in contracts with consumers. In addition, firms sometimes threaten consumers with legal action for defamation or use copyright law to argue that a review infringes on...

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137. See generally FTC, supra note 47, at 41–42 (reviewing evidence on shilling and reporting some attempts by reputation platforms to curb shilling); Kaitlin A. Dohse, Fabricating Feedback: Blurring the Line Between Brand Management and Bogus Reviews, 2013 U. Ill. JL. Tech. & Pol’y 363, 370–71 (reviewing some of the services that offer bogus reviews).


139. See Andreas Munzel, Malicious Practice of Fake Reviews: Experimental Insight into the Potential of Contextual Indicators in Assisting Consumers to Detect Deceptive Opinion Spam, 30 RECHERCHE & APPLICATIONS MARKETING 24, 41 (2015).


their copyright and should be taken down. Shilling strategies are highly diverse, sophisticated, and reportedly quite potent. A related but less understood problem is that of “cherry-picking.” Companies often selectively choose consumers who are most likely to disseminate either favorable or unfavorable information and reward them. As is very familiar, businesses offer thinly veiled bribes to unhappy consumers in the form of reimbursements, free meals, or “heartfelt” apologies. Celebrities and other influencers are also more likely to receive special treatment in the hope that they will share their (unrepresentative) experiences with their many followers.

Both shilling and cherry-picking result from strategic behavior on behalf of firms. Both result in and emphasize more extreme opinions, at the extreme of middling ones. This is because it would not pay to invest in promoting middling reviews.

B. Reputational Distortions

Placing reputation within a framework of individual rationality allows us to draw meaningful conclusions about the integrity, evolution, and credibility of reputational information. Based on the

143. See infra Subpart IV.B.
146. See generally Arbel & Kaplan, supra note 100, at 1216 (exploring the corrosive effects of apologies on deterrence).
147. See Becher & Zarsky, supra note 145, at 90–91 (finding that firms often consider consumers’ “online influence over peers” when deciding how to handle complaints).
149. Astroturfing is a form of advertising, although a highly misleading one. For some economic dynamics of reputation and advertising, see Kyle Bagwell, The Economic Analysis of Advertising, in 3 HANDBOOK OF INDUSTRIAL ORGANIZATION 1701, 1703 (Mark Armstrong ed., 2007); Phillip Nelson, Advertising as Information, 82 J. POL. ECON. 729, 730 (1974); see also Lingfang (Ivy) Li et al., Buying Reputation as a Signal of Quality: Evidence from an Online Marketplace 2 (Nat’l Bureau of Econ. Research, Working Paper No. 22584, 2016) (finding that quality sellers tended to participate more often in a program where they offer rebates for (all) reviews of their products).
150. Professor Abbey Stemler recently provided an insightful account of such biases in the context of the sharing economy where intimate interactions between peers occur often (such as sharing a stranger’s house or car). Stemler, supra note 4, at 674. Unlike her account, I focus on developing the microfoundations of reputation of consumer goods generally and explore how sophisticated, rational consumers would process flawed reputational information.
framework developed in the last Subpart, three systemic distortions will be expounded here, relating to participation, selection, and content biases. The implications for consumer action are explored in the following Part, but the overall arc of the argument is that in the presence of these distortions, a reputation failure emerges, which undermines the reliability of reputational information.

1. Reputational Sluggishness

Reputational sluggishness is the consequence of feeble, yet existing, motivations to contribute to the public good of reputation. On the one hand, reputation creators do not benefit financially from creating reputational information. It is hard to commoditize opinions and the transaction costs of doing so are prohibitive. On the other hand, there are drivers that incentivize individuals to create reputational information even in the absence of monetary compensation. Altruism, desire for social recognition, gratitude, and anger all provide reasons for people to create reputational information that benefits others. Sluggishness emphasizes the concern that for many individuals, or in many circumstances, these benefits are insufficient. As a result, participation rates in reputation creation are going to be low, leading reputational information to be more slowly developed than is generally recognized.

Empirical data, while wanting, suggests the broad scope of this issue. One study found a sharing rate of fifteen out of a thousand consumers. More optimistic estimates suggest a rate of one in ten. In my analysis of product review data from Amazon, I found that among electronics products with at least one review, the median product only had two reviews. Moreover, few elect to write long

151. Today, reputational platforms reap most of the benefit of reputation aggregation, but reputation’s direct producers receive very little reward. See also Goldman, supra note 9, at 301.

152. Blockchain and cryptocurrencies may be promising solutions to such transactions as they offer—in theory—trivial transaction costs. In the future, it may be possible to commoditize opinions and employ a pay-per-use model.

153. See Lafky, supra note 106, at 555.


157. The mean was considerably higher at sixteen; the result of a few products amassing many reviews. The analysis was based on data collected by Ruining He & Julian McAuley, Ups and Downs: Modeling the Visual Evolution of Fashion
verbal reviews. Another indication comes from eBay. There, for every negative review there are three times as many complaints to customer service, which strongly indicates that many negative reviews are either not generated or are deleted. In fact, this three to one ratio seems like a lower bound on the scope of suppression of opinions by users because it is reasonable that there would be many more negative reviews than there would be active complaints. A more speculative source of data, but interesting nonetheless, comes from the sanitation reputation of restaurants in Los Angeles. In a series of studies, researchers attempted to establish the effect of a law that required restaurants to disclose their sanitation ratings. In a naïve model of reputation the impact of such a law on food-borne illnesses should be relatively small. If a person contracts such an illness, then conditions are ripe for the word to travel fast: a food-borne illness is highly salient, it is moderately easy to establish its cause, and it is of great interest to prospective diners. Then, mandatory disclosure of sanitation levels would then not be expected to have a significant effect on food-borne illness because the information would already exist throughout the market. Despite that, the study found that the law had a powerful effect, with a sharp decline in hospitalizations due to foodborne illnesses. The law’s effectiveness is amenable to a few explanations, but one is that the reputation system was too congested to work properly before the law—despite the ideal background conditions.


158. Most reviews on Amazon for electronics are in the range of one hundred-150 characters, or about half a paragraph. See Max Woolf, A Statistical Analysis of 1.2 Million Amazon Reviews, MAX WOOLF’S BLOG (June 17, 2014), http://minimaxir.com/2014/06/reviewing-reviews/.

159. See Nosko & Tadelis, supra note 4, at 9 (concluding “there are a substantial number of transactions that went badly for which negative feedback was not left”).


161. See Simon et al., supra note 160, at 32 (explaining that some studies have not found a connection between low department of health inspection scores and foodborne-disease outbreaks at restaurants).

162. See Jin & Leslie, Reputational Incentives, supra note 160, at 238 (“Local customers can learn about a restaurant’s hygiene quality by repeatedly patronizing the restaurant, by talking to friends who have patronized the restaurant, or through exposure to local news reports about the restaurant.”).

2. Regression to the Extreme

So far, we saw that only some consumers would choose to produce reputational information, but this leaves the question of who those consumers are. If the sample of consumers who produce reputation is randomly selected, then we would expect the outliers to experience what statisticians call “regression to the mean,” i.e., the eventual balancing of outliers towards the mean of the group.\textsuperscript{164} Indeed, the regression to the mean will be impeded by sluggishness, but there is the possibility of self-correction over time with a randomly selected sample. Unfortunately, the selection of consumers is all but random.

Regression to the extreme is the propensity of reputational data to emphasize, rather than eliminate, outlier experiences over time. Internal motivations select against middling reviews because those reviews are based on experiences that are too “boring” to generate the requisite sense of spite or gratitude that will overcome the costs of producing reputational information.\textsuperscript{165} Additionally, reciprocity norms would lead consumers to overly represent positive experience, in hopes of receiving reciprocal reviews from sellers,\textsuperscript{166} and herding would tend to silence nonpopular reviews that might betray the consumer’s lack of sophistication.\textsuperscript{167} If a bottle of French wine receives paeans, an individual consumer may be embarrassed to reveal that she did not like it, noted no accents of “forest floor,” and was not seduced by its “interplay of plump grapes and jazzy oak.”\textsuperscript{168} Lastly, financial incentives select against middling reviews because shilling and cherry-picking foster creation of extreme opinions. All these tendencies lead to “regression to the extreme”: the propensity of reputational data to emphasize, rather than eliminate, outlier experiences over time.\textsuperscript{169}

Product reviews consistently provide strong evidence of regression to the extreme. One might expect that most products sold on the market would follow some generalized, bell-shaped (Gaussian) distribution—after all, very few products are really outstanding or truly atrocious. Instead, most reviews on a large variety of online platforms form a so-called “J-shaped distribution,” with most reviews

\begin{itemize}
\item \textsuperscript{165} Nan Hu et al., \textit{Overcoming the J-shaped Distribution of Product Reviews}, 52 \textit{Comm. ACM} 144, 145 (2009).
\item \textsuperscript{166} See Stemler, \textit{supra} note 4, at 692.
\item \textsuperscript{167} \textit{Id.} at 693.
\end{itemize}
amassed in the extremes.¹⁷⁰ On Amazon, more than 72 percent of the products have an average rating of at least four stars.¹⁷¹ In Airbnb listings, the average rating is 4.7 stars.¹⁷² Studies repeatedly find that middling reviews are rare and that even products with an average rating of two or three stars have only a few middling reviews.¹⁷³ Further evidence suggests this pattern is not unique to online settings but carries over to offline settings.¹⁷⁴ Figure 1 shows the distribution of 1.2 million electronic products listed on Amazon,¹⁷⁵ while Figure 2 shows a comparison of three specific products.¹⁷⁶

¹⁷⁰ See, e.g., Chrysanthos Dellarocas & Ritu Narayan, A Statistical Measure of a Population’s Propensity to Engage in Post-Purchase Online Word-of-Mouth, 21 STAT. SCI. 277, 279–80 (2006); Yi-Chun Ho et al., Disconfirmation Effect on Online Rating Behavior: A Structural Analysis, 28 INFO. SYS. RES. 626, 630 (2017); Hu et al., supra note 165, at 144–45 (detailing evidence from Amazon and arguing that the J shaped distribution “contradicts the law of ‘large numbers’ that would imply a normal distribution”); Hu et al., supra note 109, at 328 (finding that 54 percent of all products on Amazon have a review distribution that is neither normal or bimodal, and 35 percent have a unimodal, nonnormal distribution); Woolf, supra note 158.

¹⁷¹ See Wu & Huberman, supra note 106, at 3; Woolf, supra note 158.

¹⁷² See Zervas et al., supra note 15, at 3.

¹⁷³ See Lafky, supra note 106, at 556.


¹⁷⁵ See Woolf, supra note 158.

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FIGURE 1. DISTRIBUTION OF RATINGS OF 1.2 MILLION ELECTRONIC PRODUCTS LISTED ON AMAZON

FIGURE 2. REVIEWS OF THREE SAMPLE PRODUCTS
Although the J-shaped distribution strongly supports the idea of regression to the extreme, alternative explanations should also be considered. One alternative is that market dynamics push low-quality products out of the market. Because such pressures leave only high-quality products on the market, reviews would be (accurately) amassed in the right tail. While worthy of further investigation, this explanation appears unlikely for a number of reasons. Even if the products on the market are of high quality, there should still be some middling reviews, and, in particular, there should be more middling reviews than negative reviews. This explanation suggests that high ranking is indicative of quality, but in fact, rankings of identical products listed on different platforms are often negatively correlated, such that a high ranking of the same product in one place does not predict a high ranking elsewhere.

A more general issue, and one that clouds other alternative explanations, is that voluntary consumer reviews systematically diverge from other types of evaluations. Across a variety of products, professional testing of the same products listed on consumer websites shows low correlation with consumer reviews. Not only does the average quality differ, but a systematic difference in the distribution of opinions also exists. While consumers’ reviews follow the noted J-distribution, professional reviews of the same products follow a bell-shaped distribution. One can almost hear the exasperation in the voice of the researchers who concluded that “critics are more normal than normal users.” If professional reviewers are competent, one would expect a strong correlation between their judgments and consumer reviews; the lack of such correlations suggests that at least one of these sources of information is amiss. To test whether the professional reviewers are actually inaccurate, consider the following experiment. 218 participants, none of them a professional critic, were

177. A related theory is that consumers select products that they will probably like and so it is expected that there will be a concentration of satisfied consumers. See Nilesh Dalvi et al., Para ‘normal’ Activity: On the Distribution of Average Ratings, 7 Proc. 7th Int’l AAAI Conf. Weblogs & Soc. Media 110, 111, 115 (2013). This theory, however, needs to explain why, in the absence of regression to the extreme, there are so few middling reviews, which are to be expected in light of possible consumer mistakes among similarly highly rated products.

178. See Hu et al., supra note 165, at 145–46.

179. See Stigler, supra note 164, at 104–05.

180. See de Langhe et al., supra note 14, at 826.

181. See generally Roberto Centeno et al., On the Inaccuracy of Numerical Ratings: Dealing with Biased Opinions in Social Networks, 17 Info. Sys. Frontiers 809, 809 (2015) (discussing how reputation rankings within current social networks are likely skewed due to subjectivity issues); Dalvi et al., supra note 177 (discussing a theory that consumers select products that they will probably like, thus leading to concentrations of satisfied customers); de Langhe et al., supra note 14, at 818 (comparing online reviews to reviews of the same products in Consumer Reports).

182. See Centeno et al., supra note 181, at 811.

183. See Dalvi et al., supra note 177, at 114.
asked to review a product that—unbeknownst to them—was also listed on Amazon. The experimental reviews followed the bell curve, unlike their Amazon counterparts, as illustrated in reproduced Figure 3 below:

**FIGURE 3. AMAZON REVIEWS VS. REVIEWS BY TEST PARTICIPANTS**

3. Reputation Integrity

The last issue is the concern that even when consumers have an incentive to report experiences, they may face adverse incentives about the content of their reviews. For multiple reasons, individuals may misstate the quality of their own experience. Consider, for example, social pressures to conform, financial incentives, a desire to avoid confrontation, an endowment effect, personal style, and other similar considerations. All of these may lead individuals to report their experiences more or less favorably than they actually were.

Threats to the integrity of reputational information are hard to measure through data itself, but there is evidence that exposure to the opinions of others will make others report more or less favorably about their own experiences. Sociologist Ronald Burt noted, in the

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185. The graph reproduces the data presented in *Id.* at 146.
context of gossip and stories told about others, that “[a]ccuracy is a nicety more than a requirement for the stories.”\textsuperscript{187} Thus, he finds significant echo chamber effects, where people shape the valance of reputational information on the basis of context and audience rather than merit.\textsuperscript{188} One such experimental finding is made by Tory Higgins, who gave research subjects a description of a person called Donald.\textsuperscript{189} The key was that the descriptions were very ambiguous about whether Donald had positive or negative characteristics.\textsuperscript{190} Then, a confederate entered the room and said that he “kinda likes” or “kinda dislikes” Donald, and asked the subjects for their opinion.\textsuperscript{191} The subjects then offered a distorted view of Donald that accorded with the confederate’s disposition.\textsuperscript{192}

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In sum, the theory of the microfoundations of reputation suggests that (1) there will be a trend in reputational data towards more extreme reviews, (2) that the integrity of information will be compromised, and (3) that the volume of reputational data will be constrained by reputational sluggishness. The predictions of this theory are consistent with available data, which show that significant divergence exists between voluntary consumer reviews and other measures of quality.\textsuperscript{193} While there is much to be desired in the way of additional evidence, the existing data come from millions of different products and across various platforms. All in all, the case for distortions seems robust, given current knowledge.

C. Flawed Information, Flawed Decisions

When consumers make purchase decisions, one key type of information they seek is data on the experiences of past consumers. From the perspective of a prospective consumer, it is useful to know how frequently the product or service resulted in a favorable experience along some dimension (e.g., quality of food, promptness of service, durability).\textsuperscript{194} Consumers seek to extrapolate from these data to predict their own individual experience despite the obvious

\begin{flushleft}
\textsuperscript{187} Id. at 1. \\
\textsuperscript{188} Id. at 9–10. \\
\textsuperscript{190} Id. at 366–67. \\
\textsuperscript{191} Id. at 367. \\
\textsuperscript{192} Id. at 368–70, 374–77. For more examples of social pressures, see discussion and notes supra Subpart III.A.3. \\
\textsuperscript{193} See supra notes 172–87 and accompanying text. \\
\textsuperscript{194} Xinxin Li & Lorin M. Hitt, Self-Selection and Information Role of Online Product Reviews, 19 INFO. SYS. RES. 456, 459–60 (2008).
\end{flushleft}
differences in taste among individuals. Moreover, consumers care about more than the average expected experience—whether it is good or bad on average—but also about its variance, e.g., a phone that generally functions perfectly but will on rare occasions explode could have the same average rating as a phone that is consistently mediocre. To the risk-averse consumer, the high-variance phone would be inferior. To optimize decisions, then, consumers would like to have access to the distribution of past consumer experiences, rather than just their average.

Understood this way, the deleterious effect of sluggishness, integrity, and regression to the extreme become apparent as they make estimation less accurate. This loss of accuracy is because both the quantity and quality of reputational information themselves are jeopardized. The goal of this Part is to study these effects, using both theory and a Monte Carlo simulation. One key insight from the simulation, which is worth emphasizing here and throughout, is that not all reputation failures are born equal. Some may lead to small distortions that are largely inconsequential. Understanding the circumstances under which reputation failures are most severe is key to policymaking but, unfortunately, is largely outside the ambit of this paper.

1. Informational Distortions

Sluggishness makes quality estimation difficult because it limits the quantity of available data. Because consumers lack incentives to share reputational information data exist for only a fraction of all consumers. This limited quantity of information has two related adverse effects. First, sluggishness leads outlier, unrepresentative experiences to appear more common than they actually are—there is not enough “regular use” data to contradict them. If, by chance alone, one of these consumers had an extreme but unrepresentative experience, an outlier, this will taint the perception of the product. Sluggishness prolongs the time it takes for more reviews to accumulate and correct the noise.

Second, less information also

195. Id. at 459.
197. See Eyal Zamir, Loss Aversion and the Law, 65 VAND. L. REV. 829, 872 (2012) (articulating that individuals who perceive losses as more painful than potential gains are less inclined to pursue the potential gains).
198. Consider an example of a product that has, on average, a three-star quality. If the first consumer, by chance, ranks it at one star, then it would take two higher-than-average consumers rankings of four stars to correct this impression.
199. For an analysis of the dynamic evolution of reputation, including the possibility that early adopters may be systematically different in their
means less information regarding the distribution of experiences. Even if the average is accurate, consumers also care about the distribution, but sluggishness limits the volume of available information.\footnote{See Li & Hitt, supra note 194, at 457–58, 463 and accompanying text.}

The problem of sluggishness is the same familiar problem of surveys with small sample sizes. Figure 4 illustrates, using randomly generated values, how much sluggishness can distort one’s impression of products. Both graphs track the distribution of reviews that were given by a sample of all consumers who chose to share their reviews of the same product. In the top graph, only ten consumers chose to do so, whereas in the bottom graph, one hundred consumers shared their reviews. The dashed line indicates the full distribution of all consumer experiences while the full line denotes the estimated distribution based on the limited number of consumer reviews. As can be seen, a smaller sample distorts one’s view of both the mean and the distribution.
The next distortion concerns the quality of information and is caused by regression to the extreme. Because incentives to report experiences are weakest when the experiences are rote or bland, very few reviews fall in the middle range, leaving only extreme reviews reported.201 Trying to infer quality based on such a sample involves a thorny statistical problem known as “middle censoring.” From a statistical perspective, most methods of estimation assume that the

201. See Hu et al., supra note 165, at 145.
sample is taken from a random sample. If, instead, subjects self-select—as is the case here—then this bias could undermine the validity of statistical inferences. Figure 5 demonstrates the potential implications of regression to the extreme. Similarly, the figure collects, using randomly generated data, different consumer reviews—with a sample of one hundred participating consumers—but it omits the reviews of people with middling reviews who presumably lacked an incentive to share. A prospective consumer, seeking to decide whether to buy the product, only observes the filled bars (the empty bars are not visible and illustrate the distribution of unreported experiences). The full lines again mark the consumer’s best guess about the mean and distribution based on this limited information. The difference between the estimated mean and the mean of all experiences (dashed) is highlighted by the arrow. As can be seen, naïve estimation methods would yield widely inaccurate outcomes.

**Figure 5. Estimated Average vs. Real Average as the Number of Opinions Increase**

*Dashed = Estimated Average; Full = Average of all consumers. The shorter the gap between the curves and the means, the more accurate the estimate*

Notedly, Figure 5 illustrates that the extremes do not “even out.” It may seem that in a large sample, extreme results on one

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203. See infra Subpart III.C.2.
204. See Bavli, *supra* note 169, at 17.
end will be balanced by extreme results on the other end. This logic, however, only applies to symmetric distributions—not the positively-biased J distribution here.  

Finally, there are problems with the integrity of information. Herding (or antiherding) is a highly path-dependent phenomenon. Some products will appear to draw more and more favorable reviews, but this can be the result of chance that led the group of first consumers to have a favorable experience. Or, a product may appear overly negative simply because a random group of first consumers experienced some rare issues.

In sum, for a prospective consumer to accurately estimate the quality of the underlying good, both the quantity and quality of reputational information are essential. Sluggishness and regression to the extreme make reputational information scarce and biased. Consequently, the estimated mean and distribution of reported reviews systematically diverge from the actual mean and distribution, thus making them unreliable as sole guides for consumer decision-making. The question still remains, however, whether consumers can adjust for these distortions.

2. Overcoming Bias

Distorted information is likely to have a strong effect on consumers. Survey after survey, consumers express strong confidence in reputational information, describing it as a reliable source of information. While it is unclear whether consumers take reputation at face value, the level of their confidence is at least suggestive of the former. Moreover, evidence shows a strong monotonic relationship between ratings and sales—a half-star increase in a restaurant rating resulting in a 19 percent higher likelihood that the restaurant would sell out and another half-star increase resulted in a 5 percent–9 percent increase in revenues.

Consumers can also be affected by distorted information through a
variety of behavioral, cognitive limitations, most notably anchoring. Anchoring is the well-replicated psychological phenomenon that describes how the introduction of arbitrary and irrelevant numbers affects the outcomes of negotiations, evaluations, and work performance ratings. If the consumer is exposed to inflated reviews, then this can anchor an inflated sense of value. In addition, even if consumers learn that the data is biased, it is unclear that they can effectively discount it. In a set of studies, researchers investigated how individuals reacted when they learn that they receive biased advice. Participants were asked to estimate the cost of a house in Pittsburgh. To aid them, they were given an estimate by a local realtor who knew the local market. However, the realtor also had an incentive to exaggerate her estimate, because her commission was based on the final sale price. Surprisingly, the control group that was unaware of the realtor’s bias had more accurate estimates than the treatment group which was informed that the realtor had a conflict of interest. Finally, even if consumers were capable of mentally detaching from these effects, it is unclear that most have the statistical literacy to effectively discount online data.

209. See Bar-Gill, supra note 5, at 749.
211. See id.
212. See Daylian M. Cain et al., When Sunlight Fails to Disinfect: Understanding the Perverse Effects of Disclosing Conflicts of Interest, 37 J. CONSUMER RES. 836, 845, 847 (2011) (finding an absence of the ability to effectively discount the biased information when disclosed).
214. See id.
215. See id.
216. See Cain et al., supra note 212, at 840–41 (finding that groups that were aware of the bias had a higher variation in results).
217. See id. at 845, 847.
218. See, e.g., Laurent E. Calvet et al., Measuring the Financial Sophistication of Households, 99 AM. ECON. REV. 393, 393 (2009) (“Many households invest in ways that are hard to reconcile with standard financial theory and that have been labelled as investment mistakes.”); Mark Grinblatt, et al., IQ, Trading Behavior, and Performance, 104 J. FIN. ECON. 339, 360 (2012) (finding that measured levels of IQ affect stock market sophistication).
219. See Pranjal Gupta & Judy Harris, How E-WOM Recommendations Influence Product Consideration and Quality of Choice, 63 J. BUS. RES. 1041, 1042 (2010) (explaining how research finds that consumers sometimes lack motivation to process information, sometimes trusting even a single data point).
be a bank teller than be both a bank teller and a feminist.\textsuperscript{220} But this, of course, cannot be. Obviously there are more bank tellers than there are bank tellers who are also feminists, but still, people find it difficult to intuit statistical judgments.\textsuperscript{221}

Consequently, the law is generally skeptical of consumers’ abilities to correct biased data, even in situations where consumers may be aware of the existence of distortions and where third-party services may be used to correct them.\textsuperscript{222} Such are, for example, the limits on contractual misrepresentation, investor fraud through pump-and-dump strategies, false advertising, defamation, and false lights. The pump-and-dump scheme is especially telling because it involves the dissemination of wrong reputational information about firms.\textsuperscript{223} Even though investors may be thought to be, on average, somewhat more sophisticated than consumers and even though it may be clear to those investors that pump-and-dump schemes take place, the law still chooses to proscribe such activities, fearing that consumers will not be able to compensate for such misleading strategies adequately.\textsuperscript{224}

While it is clear that reputation failure could have a strong effect on most consumers, in the rest of this Part, I focus on a harder question. Can consumers—at least those that are rational, sophisticated, and informed—overcome these distortions? After all, it is fair to assume that many consumers at least suspect that reputational information should not be taken at face value. This Part investigates these issues, using both examples and computer simulations to evaluate three central consumer strategies: cardinal evaluations—i.e., choosing a product based on its score or mean; ordinal ranking—i.e., choosing the relatively better-rated product; and evaluating qualitative information—i.e., choosing on the basis of the content of reviews.

**Cardinal Evaluations.** Suppose that a consumer is trying to estimate the quality of a hypothetical product based on the valence of reviews. She knows that reviews in the middle, rated two or three


\textsuperscript{222} See *Truth In Advertising*, FTC, https://www.ftc.gov/news-events/media-resources/truth-advertising (last visited Dec. 3, 2019) (showing the Federal Trade Commission aims to protect consumers by enforcing federal law which says information given to consumers must be truthful and not misleading).


\textsuperscript{224} In the unregulated space of Bitcoin, a recent research paper found that the market price of bitcoin rose up in 2013 tenfold due to manipulative trading tactics by a single trader. Neil Gandal et al., *Price Manipulation in the Bitcoin Ecosystem*, 95 J. Monetary Econ. 86, 87 (2018).
stars, are suppressed, so she only sees extreme reviews. Figure 6 lists the information that is available to her. Armed with the knowledge that middling reviews are censored, what can she say about the quality of the underlying product? What would she believe the mean to be? How confident should she be?225

**Figure 6. Frequency of Reviews Under Regression to the Extreme**

*Bars show the number of reviews in each ranking category*

Next, based on this analysis, which of Figures 7 and 8 best represents the quality of the underlying product?

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225. As I shall argue, consumers care about more than the mean, but average star rating is often the first filter consumers use in their searches.
Figures 7 & 8. Frequency of Potential Reviews Under Regression to the Extreme
Bars, full and empty, show the number of reviews in each ranking category

Of course, these questions are not answerable. In fact, these figures are only two of many possible distributions. There is just not enough information to make accurate so-called cardinal evaluations, i.e., determinations of the quality of the product on the basis of review valence. In particular, estimating the mean on the basis of a

226. If one has enough data about the relationship between full reviews (as in reviews solicited from all consumers) and voluntary reviews, it may be possible to make some educated guesses to fill in the missing data. Whether this will be
truncated sample is a risky proposition, doubly so when the sample is small due to sluggishness, and triply so when the data is misstated due to integrity bias. Still, consumers often try to estimate quality on the basis of review valence, especially by limiting their searches to products above a certain mean.

**Ordinal Comparisons.** Suppose that the consumer reluctantly accepts that means are problematic, and instead seeks to compare among products, reasoning that if all are subject to biases, at least the comparison of the means would reveal which one is superior.227 The following Table describes two products that the consumer is trying to compare; the shaded area is middling information that is not available to her. On the basis of available information, she takes the mean of product A to be 2.8 and that of product B to be also 2.8. She also notes that they both have the same distribution of reviews. She concludes that the two products are of equal value. Based on your knowledge of the shaded information, is this a correct conclusion?

**TABLE 1. ORDINAL COMPARISON WITH TRUNCATED DATA**

<table>
<thead>
<tr>
<th>Star Ranking</th>
<th>No. Reviews</th>
<th>Product A</th>
<th>Product B</th>
</tr>
</thead>
<tbody>
<tr>
<td>†</td>
<td>10</td>
<td></td>
<td></td>
</tr>
<tr>
<td>★★</td>
<td>15</td>
<td>5</td>
<td></td>
</tr>
<tr>
<td>★★★</td>
<td>5</td>
<td>15</td>
<td></td>
</tr>
<tr>
<td>★★★</td>
<td>4</td>
<td>4</td>
<td></td>
</tr>
<tr>
<td>★★★★</td>
<td>6</td>
<td>6</td>
<td></td>
</tr>
<tr>
<td>Estimated mean</td>
<td>2.8</td>
<td>2.8</td>
<td></td>
</tr>
<tr>
<td>Real mean</td>
<td>2.5</td>
<td>2.8</td>
<td></td>
</tr>
</tbody>
</table>

To give a sense of the scope of mistakes based on interproduct comparisons, I conducted various Monte Carlo simulations, reported in Figures 9, 10, and 11.228 Monte-Carlo simulations are a computer-assisted technique used in finance, physics, and computer science to track complex interactions in domains where the parameter space is possible, the accuracy of such process and its transferability across domains remains to be seen.

227. It is worth recalling that statistical tests of significance of mean difference (Student’s T-Test) are unhelpful when the sample is not randomly chosen. See Moore & McCabe, supra note 202, at 463. Nonparametric tests also depend on various assumptions that may not hold in these contexts. Id.

228. The computer simulation is on file and can be replicated by the reader. Given the use of randomness, actual results may vary slightly among runs, but given the large volume of trials, this deviation will not affect any of the conclusions here.
large and uncertain. By running thousands of simulated experiments, each with random deviations, the experimenter can learn of trends in the data. Methodologically, the Monte Carlo simulation is akin to a quasi experiment; it is useful in demonstrating the existence of certain phenomena and indicating their potential magnitude, although it is not at the epistemic level of natural experiments as it only studies possibilities rather than actual quantities.

The first simulation generated two products of arbitrarily chosen mean quality (although they shared all other statistical features). Each product was “tried” by one hundred different “consumers,” which means that each consumer has a random experience based on the quality of the product. The higher mean product was more likely to generate a favorable experience. After trying the product, each consumer could report the experience by rating it from one to five stars in half-star increments. Because of regression to the extreme, the consumers are coded not to share experiences in the range of two to three stars. Once all the information accumulates, a new consumer comes and tries to decide which product to purchase on the basis of interproduct comparisons. She chooses the one with the higher reported mean, based on the reasoning noted above. The code then counts every instance where the consumer was misled into choosing the inferior product. This process, for the same products, was repeated ten thousand times. This gives an account of the frequency of mistakes, given products of different means. To see how a higher difference would affect the frequency of mistakes, the simulation then ran the same process but increased the mean of product B by a slight amount. The following figures report this simulation, and two others, explained below.


230. See Bihani, supra note 229, at 218–19.

FIGURE 9. DIFFERENCE IN MEAN

![Frequency of Mistakes as a Function of Product B's Average Quality](image1)

FIGURE 10. DIFFERENCE IN SALES VOLUME

![Frequency of Mistakes as a Function of Product B's Sale Volume](image2)
Figure 9 shows how the mean quality of the underlying goods affects consumer mistakes. For products that are not clearly distinguishable, i.e., they have a somewhat similar mean, consumer mistakes are widespread. For example, if the difference in mean is 0.1 stars, then under the parameters of the simulation consumers would choose the wrong products in 25 percent of the cases. For products that are even harder to distinguish, with only a 0.05 star difference, the ratio of mistakes rises to 35 percent. On the flip side, the more different the products are, the fewer mistakes consumers commit, despite regression to the extreme. When the difference is 0.25 stars, the ratio of mistakes falls below 10 percent, and when it is 0.5 stars, it mostly disappears.

Figure 10 reports the same simulation, but this time it holds the mean difference constant at 0.3 stars and only varies the sale volume. One product is reviewed throughout by one hundred consumers, whereas the other is reviewed by a variable number of consumers. When the second product is reviewed by only fifteen consumers, the ratio of mistakes raises to about 20 percent. This is important, in part because the difference in means is relatively significant (0.3 stars), and in part because most products have very few reviews, making this scenario likely.

232 Part of the distortion of reputational information is also due to the use of integers or half integers (i.e., a consumer reports a 2.5-star review, whereas the actual experience is 2.34). Despite its flaws, the integer ranking system is almost universal.

233 As noted, the median product only has two reviews. See supra note 157 and accompanying text.
Finally, Figure 11 reports the same simulation but this time holding the mean and sale volume equal, and only changing the variability of experiences. From a consumer perspective, in choosing between two products with equal means, the one with the lower variability would be preferred due to risk aversion. Here we find the most considerable degree of mistakes. When one product yields consistent experiences and the other variable ones, the ratio of mistake is very high—when the variance of one product is 0.1 stars, but the variance of the other is 0.5 stars, consumers mistakenly prefer the inferior product in over 80 percent of the cases. Only when both products are highly variable does the ratio of mistakes start to fall.

Taken together, and under some important caveats, these simulations demonstrate the potential scope of consumer errors given reputation failure. At the same time, the simulations also demonstrated a broad range of cases where reputation failure is unlikely—specifically, environments where there is a great difference in product quality, when the sale volume is large, and when quality variability is large or constant across products. This conclusion is important in evaluating the social harm and the contexts in which it is likely to arise from reputational distortions. An important caveat, however, is that these simulations are based on stylized examples and use arbitrarily chosen parametric values. This limits the interpretation of the results reported here. On the other hand, real-life considerations tend to increase the problematic nature of reviews relative to the simulations. For example, satisfied consumers may be more or less likely to report their experiences than disgruntled consumers. After all, the tendency to complain is different from the tendency to praise, and spite is not simply gratitude multiplied by negative one. Other practical complications involve consumers ascribing different meaning to star reviews (for some, a four-star review means high-valence, while for others, it will indicate a negative experience); the possibility that some products will have bimodal or other nonstandard distributions; the dynamic effect caused by buyers experimenting less with low-reviewed products; and firms investing different amounts of efforts in shilling and cherry-picking. These considerations would tend to make not only the simulations less reliable but also any quantitative approach to the data.

**Qualitative Analysis.** Suppose now that the consumer seeks to only read reviews and focus only on qualitative content. In particular, she is trying to decide between two brands of toilet paper sold on one

platform. It turns out that there are almost 8000 different reviews for the two brands. How long would it take her to read them all? How confident should she be in her ability to spot fake reviews? Suppose that she finds some regularity in reviews that she deems suspect, so she dismisses them; how long would it take for financially motivated sellers to produce reviews that avoid the pattern?

Stated more generally, qualitative analysis does not scale, and trying to peruse all the reviews of more than a few products can often be unmanageable. Yet, limiting attention to a few potential products is also unworkable—what would be the selection criteria? If it is reputation (e.g., only products with 4.5 stars), this runs into exactly the same issues discussed above. Moreover, the ability to spot fake reviews—consumer overconfidence notwithstanding—is in fact quite limited. Finally, even if a consumer can find a useful guiding heuristic, it will be exploitable. If consumers only trust the reviews of serial reviewers, for example, a seller may derive a sizeable financial benefit from bribing this serial reviewer. If consumers mostly care about negative reviews, for another example, then a seller will pay to invest heavily in shilling against competitors’ products. If consumers mostly care about the volume of sales, the seller may artificially inflate sales by giving away products.

Stated more generally, heuristics beget loopholes which beget exploitation by opportunistic sellers.

* * *

To summarize, this Part demonstrated how the microfoundations of reputation result in informational distortions. Because the reasons to share information are often private and self-serving, three types of information distortions emerge—sluggishness, regression to the mean, and strategic manipulation.


236. See, e.g., Ponte, supra note 142, at 64–65 (“[I]t is becoming challenging to decipher more sophisticated forms of fake online reviews.”); Bing Liu, **Opinion Spam Detection: Detecting Fake Reviews and Reviewers**, U. ILL. CHI. https://www.cs.uic.edu/~liub/FBS/fake-reviews.html#reviews (last visited Dec. 3, 2019) (providing an example to test one’s ability in detecting fraud reviews).


239. See Ponte, supra note 142, at 134.
extreme, and integrity bias. As a result, peer-to-peer reputational information tends to provide a false sense of the true quality of the underlying product. While consumers can try to account for these distortions, many will lack the requisite sophistication, and even consumers who do account for the distortions might not be able to do so given the potentially corrupting effect of the distortions. This is not to say that distortions are always strong or that consumer heuristics are not helpful. Still, reputation failures have important normative implications which I now move to discuss.

IV. LEGAL IMPLICATIONS OF REPUTATION FAILURE

What does the law have to say or do about reputation failures? I start with the most direct legal interventions that are needed when the symptoms of reputation failure are present and acute (which is not always the case). I then move to outline a more ambitious program: Reputation-by-Regulation. The key idea is to shift attention from symptoms—such as consumer mistakes— to causes. Legal institutions can be improved to facilitate the creation of quality reputational information, thus mitigating some of the root causes of reputation failure.

A. REPUTATION FAILURE AND CONTEMPORARY DEBATES IN CONTRACTS AND TORTS

There are many who call for deregulation on the basis of the rise of reputational information. There has also recently been growing support among sharing-market enthusiasts, liberals and conservatives alike, who believe that online platforms open avenues for effective self-regulation “outside the law.”

Recognizing reputation failures highlights the dangers of relying on existing market mechanisms. Naïve reliance on reputation-based market mechanisms often leads to perverse outcomes in the presence of acute reputation failures. When consumers select products on the basis of biased or distorted reputational information, they are likely to make persistent mistakes—a social deadweight loss. These mistakes have negative dynamic effects because they make the production of quality products less rewarding and the production of unsafe products more rewarding. Such a dynamic can devolve into

240. See supra notes 4–6 and accompanying text.
241. See supra note 47 and accompanying text (providing deregulatory examples among lawmakers and scholars).
242. See supra Subpart III.C.1.
what economists call a “lemon market,” where sellers decide to stop selling quality goods even though consumers would want to buy them because consumers cannot distinguish between high and low-quality goods.245

In the presence of persistent and systematic consumer errors, recent scholarship has shown that some type of regulation can be welfare-enhancing even when accounting for the limitations of a top-down regulator.246 If sellers cannot be trusted to meet consumer expectations, then setting boundaries for permissible dealings may improve matters.247 Thus, laws and regulations such as lemon laws, implied warranties, safety audits and recalls, restaurant safety grading, and many other measures may be needed more than critics would admit. It also helps draw the boundaries of the sharing economy and the continued need for traditional reputational sources, such as professional critics or professional review media (Consumer Reports, for example).

In sum, reputation failure fits in the family of market failures. It is a market friction that can justify intervention in consumer markets in order to improve consumer and social welfare. Of course, reputation failures do not give a carte blanche for regulation. These failures vary in scope and severity and in some cases, the costs of product regulation by an outside regulator may outweigh the benefits.248 Still, modern debates on deregulation—especially those involving the sharing economy—fail to recognize that reputation is subject to systematic failures.249 Bringing this insight into modern debates should temper some deregulatory trends.

B. Reputation-by-Regulation

Today, the regulatory schema is one of competition between legal ordering and market ordering “outside the law.”250 Policymakers are told to choose between heavy-handed regulation and unbridled trust

245. See Akerlof, supra note 28, at 489.
248. Harold Demsetz, Information and Efficiency: Another Viewpoint, 12 J.L. ECON. 1, 19 (1969) (describing the “I,” the fallacious assumption that against market failures there is a perfect regulator).
249. See Stemler, supra note 4, at 687–88.
in the market. The analysis presented here suggests a novel third way, a complementarity model between these two options. The key insight is that the law has an active role to play ex ante in designing the rules of the game, such that the information that flows to the market is more reliable and abundant. I name this family of strategies Reputation-by-Regulation to indicate how closely related reputation is to regulation. Rather than an organic and “natural” outgrowth of market relations, reputation is deeply influenced by background legal institutions. Drawing awareness to Reputation-by-Regulation helps expose the role legal institutions play in the development of reputational information and highlights alternative institutional strategies. The rest of this Part suggests a menu of five options that illustrate how the law can take various degrees of involvement in removing reputational bottlenecks.

To provide some initial motivation to Reputation-by-Regulation, it is worth noting that when reputation works it has an important advantage over standard disclosures rules in that it communicates with consumers in their own terms, thus avoiding some of the critiques brought against mandatory disclosure over the last few years. As a peer-to-peer mechanism, consumers directly transmit the information that they find pertinent using their language and emphasizing their use patterns. For example, consumer comments on fuel economy can track normal use patterns more accurately than the abstract categories of pure city or highway miles required by law. Similarly, annual percentage interest rates that credit issuers must disclose may be less intelligible to consumers than actual examples of costs per use. As these examples highlight, there is great potential in Reputation-By-Regulation.

1. Leveraging Market Players: The Role of Reputational Platforms

It goes without saying that market players will often have an incentive and ability to deal with market problems themselves. In the last two decades, for example, reputational platforms specializing in the aggregation of peer-to-peer reputational information have blossomed. Such platforms have realized the value of “reputation for reputation,” i.e., the value of garnering consumer trust which can

251. Id. at 1398.
then be monetized using various business models. Although it may seem natural now, in the early days of the internet it was far from evident that a shopping website would want to display information that could portray some of its traded products in a negative light. The sentiment at the time was that “[l]etting consumers rant about products in public was a recipe for retail suicide.” It was also incredible that consumers could trust the advertised opinions of complete strangers. Still, a small online bookseller by the name of Amazon took a bold step and adopted a system of consumer feedback. The rest, is, well, history.

Reputational platforms are metaregulators and, within their limits, should be enlisted to address some of the problems of reputation failure. Given that consumer trust is a source of the “new oil”—internet traffic—platforms have an incentive to develop metareputation for being honest curators of reputational information. Indeed, some platforms have already taken voluntarily action to stamp out fake reviews. Amazon uses a variety of algorithms to detect suspect reviews, prohibits the provision of incentives-for-reviews, and sues violators. Moreover, Amazon also lists some reviews as those done by “Verified Purchasers” to further limit manipulation, although this has led to a cottage industry of payments for purchases coupled with fake reviews.

256. Id.
257. Id. at 47.
258. Id.
259. See Tadelis, supra note 98.
260. Ante, supra note 255, at 47. For a review of eBay’s history and success, see Tadelis, supra note 98, at 321.
261. For historical examples of reputation systems, see supra note 5.
263. See Communications Decency Act of 1996, 47 U.S.C. § 230 (2012) (immunizing websites from liability for restricting material that the website considers to be obscene or otherwise objectionable, “whether or not such material is constitutionally protected”).
265. Various websites offer refunds, sometimes with commission, for reviews. See list of websites cited supra note 140. A further list of sites is on record with the author.
To the extent that such systems work, they are desirable and helpful. But reputational platforms are also limited in their policing powers. For the most part, platforms only rely on contractual agreements between themselves, sellers, and buyers.\footnote{266} Thus, their ability to investigate and sanction fake reviews is very limited. Platforms also risk harmful public relations implications if they take actions that consumers deem too aggressive.\footnote{267} Moreover, platforms’ ability to correct consumer misstatements, investigate cherry-picking, or validate information is also limited. There is not much TripAdvisor can do to enforce its ban of reviews by family members of an owner’s hotel.\footnote{268}

A deeper problem is that platforms do not always have the incentive to act in the public interest. Platforms face a conflict of interest because profits and sales can be in tension with consumer trust. The existence and type of a conflict depends on the specific business model, but any platform that profits from the transactions it facilitates may be tempted to promote higher margin items.\footnote{269} As a result, the platform may list these products first, suppress negative reviews of its own products, or otherwise manipulate the market for its own advantage.\footnote{270} Even if gross violations of consumer trust can be detected, small violations of consumer trust—“fudging’ on the margin”—will be all but impossible to detect by consumers.\footnote{271} When Amazon, for example, lists its own products prominently on the first page and before higher-rated products, it trades off some of the trust consumers place in it, the trust that it will feature best products first, against its own profits.\footnote{272}


\footnote{269} See David Adam Friedman, Do We Need Help Using Yelp? Regulating Advertising on Mediated Reputation Systems, 51 U. MIC\footnote{H} J.L. REFORM 97, 111, 161 (2017) (exploring the conflict of interest).


\footnote{271} See Friedman, supra note 269, at 111.

\footnote{272} See id. at 130; Angwin & Mattu, supra note 270.
systematically censors reviews from passengers who give four-star or less reviews more than a few times.\(^{273}\) A large class action was brought and settled against Angie’s List in which the primary allegation was that Angie’s List reviewer ratings were influenced by payments from providers.\(^{274}\) Yelp has been the subject of extensive litigation for allegedly manipulating reviews against businesses that were not willing to pay advertising fees.\(^{275}\) According to an investigation by the Wall Street Journal, the Federal Trade Commission (“FTC”) received hundreds of complaints against Yelp alleging that businesses received unfair reviews after refusing to advertise on the website.\(^{276}\) Another platform, Consumer Affairs, has similarly been subject to litigation for allegedly presenting reviews of certain paying members in a more favorable light.\(^{277}\) A ProPublica report also suggests that Amazon may be unfairly manipulating listings in order to promote its own goods.\(^{278}\)

Exacerbating the conflict of interest is the right courts granted to platforms to almost arbitrarily curate reviews. The Ninth Circuit recently considered whether a platform could arbitrarily choose the reviews it presents to consumers.\(^{279}\) The court held that the reviewee has no right to have any review posted at all and as such, cannot compel the platform to publish reviews it does not want to publish.\(^{280}\) This decision licenses platforms to present reviews according to their own discretion—with a minimal check on their behavior.\(^{281}\) Additionally, the fight against fake reviews exacerbates the problem


\(^{278}\) See Angwin & Mattu, supra note 270 (“About three-quarters of the time, Amazon placed its own products and those of companies that pay for its services in [a prominently placed] position.”).  

\(^{279}\) Levitt v. Yelp! Inc., 765 F.3d 1123, 1126 (9th Cir. 2014).  

\(^{280}\) Id. at 1133.  

\(^{281}\) Id. at 1133–34.
because screening of reviews, often done algorithmically, relies on necessarily opaque standards since disclosing the algorithm would invite abuse by sellers. 282 At the same time, these opaque algorithms give the platform more power to abuse consumer trust. 283

To the extent regulators are worried about these issues, a few options to leverage market players present themselves: regulation, investigation, and accreditation.

a. Regulating Platforms

On the regulatory side, consumer agencies and legislators can create a unified set of rules that governs what constitutes fair and reasonable treatment of consumer peer-to-peer reputational information. 284 A platform should not promote its own products, or higher-margin products, when it presents consumer-sourced reputational information. A clear first step in this direction is to revise the holding that platforms are free to arbitrarily curate reviews. 285 Additionally, platforms should be considered as forum providers for speech, limiting their ability to arbitrarily censor reviews. Platforms should also be required to publish their review curation, aggregation, and display standards. Another possibility is to require platforms to release certain key statistical information such as the volume of sales. Additionally, platforms might be required to display the ratio of consumers who did not rate the product to those who did in order to aid consumers (or assistive technology) in drawing better statistical inferences. Alternatively, they might simply be required to create and follow their own choice of standards of regulation—thus creating metaregulation of sorts, relying on the platforms to find the right balance of substantive rules.

A useful source of inspiration (although with some caution) is the evolving international standards of platform regulation developed by the International Consumer Protection Enforcement Network (“ICPEN”), a network of consumer protection authorities from nearly sixty countries. 286 The ICPEN standards include disclosure

282. See David Adam Friedman, Addressing the Commercialization of Business Reputation, 80 LAW & CONTEMP. PROBS. 73, 83 (2017).
283. See id. at 79 (relating the conflict of interest to the business model of the platform).
284. See Strahilevitz, supra note 1, at 64, 69, 71 (arguing that the government should subsidize and encourage transparency among reputational platforms); Van Loo, supra note 48, at 585–99 (developing an account of the regulation of platforms by agencies, highlighting the need for regulation in certain key areas).
285. See Levitt, 765 F.3d at 1126, 1134.
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standards governing platforms’ methods for curating and aggregating reviews, requirements for platform functionality of review sorting according to consumer criteria, and obligations to present negative reviews of a platforms’ own products.287 It should be noted, however, that some of these regulations can run into potential First Amendment constraints.288 At the same time, their usefulness and importance merits serious consideration.

b. Policing Platforms

To ensure the integrity of reputational information, it may be necessary for an external agency to regularly inspect and police the inner workings of reputational platforms.289 This is already done, to some extent, by the FTC.290 However, there are still some important informational gaps.291 The agency should first have access to all reviews posted to the platform, including their timestamps, IP addresses, and external information relating to the product price and type. Then, it should access the (anonymized) reviewer data itself—past transactions and past review history—in order to identify shell accounts. Then, the agency should trace typical consumer searches and the corresponding results: what products are featured, in which order, and by which criteria. Finally, the agency should review the platform’s algorithms for identifying faux reviews and test their operation. Such investigations are crucial given that many of the processes for collecting and curating reputational information are opaque and that opaqueness may be necessary to avoid manipulation by other market players. In addition to audits, the agency should also investigate claims of unfair treatment by market players.

c. Platform Accreditation

Accreditation is perhaps the least intensive form of regulatory intervention. Accreditation will involve using a badge to indicate that the platform is monitored by the agency and that it complies with its own standards. Receiving accreditation may be entirely voluntary,

287. Id. at 7–11.
289. See Van Loo, supra note 48, at 585–98 (suggesting the need for external policing).
290. See Brogaard, supra note 221.
thus sidestepping any potential First Amendment concerns. Of course, if the agency finds at any time that the platform is not in compliance, it may strip its badge.

Receiving a badge would garner consumer trust. Such a system can thus be valuable even if it is entirely voluntary because it will be in the platform’s interest to receive accreditation. Remember that consumers may be suspicious even when platforms act honestly because the platform has superior information regarding its own internal practices. The badge would allow platforms to credibly communicate their honesty to the public.

2. Professional Publications

An alternative or supplement to a system of accreditation involves using professional rating agencies and publications. Some successful examples include Consumer Reports, US News, PC Magazine, Michelin Restaurant Review, and the New York Times Book Review section. Like reputation platforms, these services are also premised on the idea of a reputation for reputation, i.e., monetizing consumer trust in their reputation production services. Moreover, they have some advantages over amateur consumer reviews in that they have both the facilities and knowledge to extensively test products. Such publications are demonstrably valuable, as consumers continue to use them despite their cost and the rise of free online consumer-generated information. Indeed,
their continued existence is a possible testament to the existence of reputation failure in peer-to-peer reputational information.297

Still, reliance on such publications is not without its limitations. Professional critics do not always care about the same things as less-sophisticated consumers.298 Professional publications can only cover a sliver of the product-space, and it is unlikely that they can ever approach the comprehensiveness of consumer-sourced reviews.299 But, most acutely, as consumers place more confidence in such publications, it becomes more profitable for sellers to bribe those reviewers to publish favorable reviews.300

The government may increase the use of such services by either subsidizing them or otherwise requiring testing in some areas. Notably, the state already supports these publications by protecting their copyright and intellectual property. Such protections can be extended through broader, more aggressive copyright protections, subject—of course—to a full cost-benefit analysis.

3. Fighting Fake Reviews

As noted earlier, fake reviews are the scourge of the reputation system. The more consumers use and trust reviews, the more it pays to invest in creating fake reviews.301 And while reputation platforms have some incentive to fight fake reviews, their efforts tend to fall short.302

A useful market-based solution here is the leveraging of a competitor's interest. Importantly, I propose that fake reviews will


297. While professional reviews continue to exist, consumers rely more often on peer-to-peer reputational information. See Mehdi Ghazisaeedi et al., Trustworthiness of Product Review Blogs: A Source Trustworthiness Scale Validation, 6 AFR. J. BUS. MGMT. 7498, 7498 (2012).


299. Compare Woolf, supra note 158 (examining over 1.2 million consumer product reviews on Amazon), with All Products A-Z, CONSUMER REP. https://www.consumerreports.org/ecr/index.htm (last visited Dec. 3, 2019) (noting that the service has only reviewed just over 9,000 products).


301. See supra notes 145–47.

302. See David Adam Friedman, supra note 269, at 142 (questioning the “effectiveness of these internal initiatives to discourage and eliminate false reviews”); Stemler, supra note 4, at 707–10.
be considered a form of false advertising and subject to the Lanham Act of 1940 or state-level antitrust laws, which permit competitors to bring private suits against sellers for posting fake reviews. Some courts have authorized the use of this provision to impose liability for fake reviews. This tool is helpful—competitors may lose market share when a firm fakes its own reviews or use reviews to attack another—but it is also quite limited. Only competitors may employ this tool, and they themselves have limited resources to investigate claims. More fundamentally, the cost of fighting false advertising by a competitor is private, but the benefit accrues to all the firms that compete in the space.

In contrast to private market players, the FTC, the Consumer Financial Protection Bureau, and some state agencies have broad investigative powers. These agencies can investigate fraud and have both the authority and resources to do so effectively. They can also use their powers to fine market players for unlawful behavior, creating the strong deterrence needed to effectively combat the generation of fake reviews. Importantly, fake reviews can be considered a form of false advertising and subject to the Lanham Act or state-level antitrust laws, although the exact mechanisms are beyond the scope of this Article. Reputation failure provides strong reasons for further investment in resources in these measures.

One issue in combating fake reviews is the First Amendment protection of speech. Historically, the First Amendment was not thought to cover fraudulent speech. In In re R.M.J., the Supreme Court held that states are free to regulate advertising that is inherently misleading. And while the recent decision in United States v. Alvarez allowed some protection of fraudulent speech in the context of the Stolen Valor Act, such protection is very limited.

307. See also Arbel, supra note 291, at 171–72.
312. Id. at 207.
314. Id. at 719, 730 (allowing regulation of fraudulent speech); see also Donaldson v. Read Magazine, Inc., 333 U.S. 178, 190 (1948) (holding that the government’s power “to protect people against fraud” has “always been recognized in this country and is firmly established”).

Electronic copy available at: https://ssrn.com/abstract=3239995
Fake reviews are by their nature misleading, thus it seems that well-tailored regulations meant to apply this standard would be justified. In addition, the law should limit businesses’ ability to offer incentives for favorable reviews, i.e., cherry-picking consumers. Such an approach could sidestep many of the thorny constitutional tensions while advancing the goal of combating reputation failure.

To be clear, it is not expected that regulatory action alone will be capable of eliminating fake reviews. Still, decisive regulatory action can significantly curtail the profitability of this practice. It should also be noted that investing in some of the other measures proposed here would also be helpful in fighting fake reviews. It is much easier and cheaper to cultivate a favorable view of one’s restaurant when competing with a handful of reviews; it is much more complex to do so when there are dozens of reviews.

4. Fostering Positive Incentives

As argued earlier, because reputation is a public good, consumers often lack sufficient incentive to create it—a problem most acute with respect to middling experiences and unpopular opinions. The nascent law regulating consumer benefits exhibits considerable confusion about this basic point and takes an overly strong stance against incentivizing reviews. Here, again, the microfoundations framework helps delineate the proper limits of providing incentives and behavioral nudges to consumers.

To promote transparency in the market and curb false advertising, the FTC announced new guidelines in 2015 that regulate incentivized reviews. The context of these guidelines is facially reasonable: the ascendency of social media has created a new form of endorsement—reviews by “influencers,” or individuals who amass many followers. Companies are estimated to be spending billions of dollars paying influencers to endorse products on their social media accounts. In response, the FTC sought to require influencers to disclose their financial interests. The result, however, is the proverbial throwing out the baby with the bathwater. Consumers need incentives and nudges to produce accurate reputational information, which are outcomes of consumers not internalizing the benefits of reputational information. Direct incentives consist of free products, discounts, payments, and commissions. Nudges, such as prompts to rate the previous

316. Id.
318. 16 C.F.R. § 255.5 (2019).
319. See supra Subpart III.B.
experience before engaging in a new transaction or reminders to rate and review, also increase the creation of consumer reputational information.320

Despite the importance of such incentives and nudges, the FTC guidelines impose onerous disclosure requirements that are triggered almost indiscriminately without attention to context. For example, if a restaurant chooses to offer free meals on its opening night so as to incentivize traffic, every person dining there has to disclose her financial stakes when discussing her experience—even if the restaurant never asked for any review, much less a favorable one.321 The same goes for a “dollar-off” coupon, sweepstakes promotions, or even charity donations.322 The imposition of such broad duties is not only onerous but it also has unwanted secondary effects. Like the harried student highlighting the entire textbook, there is danger in indiscriminate disclosure. Using the same disclosure standards for content-neutral and content-biased reviews can be misleading. Even worse, mandating such disclosures may exacerbate the problem of regression to the extreme. Research finds that disclosing financial incentives may create a “moral license” to exaggeratedly extol the virtues of the product.323

There is a readily available alternative. The developing international standard permits the use of content-neutral incentives.324 Under this standard, businesses may legitimately offer incentives to reputation creators if it ensures that the resulting opinion arises independently of the incentive.325 A content-neutral incentive may include offering free products under an agreement that clearly states that the user has full discretion over the content of the review and that future promotions will not be made contingent on her response.326 Or businesses can provide discounts to consumers who review a product, so long as the review is anonymized by a trusted third-party.327 Research on the effect of such incentives is scant, but it suggests that content-neutral reviews are effective. A recent study compared incentivized reviews to organic ones, both qualitatively and

320. Stemler, supra note 4, at 684–85 (discussing creation of reputational information by encouraging or requiring users to leave feedback after a transaction is complete).
322. Id. at 4.
323. See Loewenstein et al., supra note 213, at 424–25.
325. See id.
326. See id. (stating that financial or material benefits should be given by review administrators to all types of reviews); see, e.g., FTC, supra note 321.
327. See Int’l Consumer Prot. & Enf’t Network, supra note 324, at 8; see, e.g., Maria Petrescu et al., Incentivized Reviews: Promising the Moon for a Few Stars, 41 J. RETAILING AND CONSUMER SERVS. 288, 292 (2018) (stating reviewers are given incentives such as discounted products from third party companies).
quantitatively. Not surprisingly, incentivized reviews put less emphasis on price; but importantly, there was no difference in rating between the content-neutral-incentivized and organic reviews. Thus, incentives can have desirable effects for creating reliable reputational information.

5. **Controlling Costs: First Amendment and Reputation**

The last set of solutions builds on the key insight that the costs of reputation generation are wholly private, but the benefits are partly public. This Subpart advocates the expansion of free speech safeguards provided by the First Amendment to consumer reviews.

Today, with increasing frequency, lawsuits are brought against consumers for providing reviews. Businesses latch onto factual inaccuracies (some small or innocent) and sue using a variety of doctrines including defamation, tortious interference, injurious falsehoods (commercial disparagement), and false light. One report finds that “negative reviews have become the subject of dozens of lawsuits across Texas in recent years,” and there is a growing sense that this happens across the nation. The consequences of such lawsuits can be dire: a woman complaining online about the services of her divorce attorney was charged with $350,000 in damages. Admittedly, such judgments are relatively exceptional. However, the threat is not just liability but also litigation. Indeed, according to Professor Lyrissa Lydsky, a primary reason such lawsuits are brought is not to collect damages but to silence. And this menacing effect is amplified by consistent media coverage of such lawsuits.

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328. Petrescu et al., supra note 327, at 291, 293.
329. See id. at 294 (finding that providing incentives does not affect the “satisfaction ratings assigned to the product in the form of ‘stars’ from one to five” although they do find some evidence of “potential linguistic and sentiment differences found in the qualitative analysis”).
333. Glas, supra note 330.
336. See, e.g., Beth Landman & Julia Marsh, I Wrote a Negative Yelp Review – and It Made My Life a Nightmare, N.Y. Post (May 28, 2018),...
To compound the matter further, in handling these lawsuits, consumers face the common risk of de-anonymization. Nor is state legislation very helpful. Anti-Strategic Lawsuits Against Public Participation (“Anti-SLAPP”) legislation meant to combat abusive lawsuits is not broadly adopted or consistently applied. Finally, even slight increases in cost can dissuade reviewers (reduce the number of reviews). One experiment, for example, tested how small costs affect behavior and found that “[r]emoving a cost of only $0.25 . . . leads to a more than 50 percentage point increase in the frequency of rating.”

Some examples might be helpful in appreciating the chilling effect of litigation risk. One New Jersey consumer, Jane Perez, complained online about her contractor, stating, “My home was damaged: the ‘work’ had to be re-accomplished . . . he invoiced me for work not even performed.” The contractor sued Perez for $750,000 in damages for defamation. The contractor finally lost the suit, but along the way, Ms. Perez deleted her review and had to defend herself through an expensive five-day jury trial. Or, take the case of Las Vegas consumer Pamela Boling. She sought the assistance of a tax professional to help demonstrate her economic hardships to tax authorities. However, the service she received was below her expectations, so she turned to Yelp and wrote a review concluding “this is MALPRACTICE!” Soon after, the business filed a defamation lawsuit against her. To ward off the lawsuit, she spent $40,852 in litigation costs. Although she ultimately won the case


339. Lafky, supra note 106, at 561.


341. Id. at 9–10.


344. Id. at 4.

345. Id. at 15.
and recovered some costs, the process was long, risky, and caused her to redact her original opinion—suppressing a view that the court deemed legitimate.\footnote{See id.} Finally, consider the case of Stephen Glover, who posted a negative review about his lawyer, claiming that he was the “[w]orst ever” because he yelled at him to “GOOGLE IT!” in response to a question and otherwise acted unprofessionally.\footnote{Spencer v. Glover, 397 P.3d 780, 783 (Utah Ct. App. 2017).} This review led to a two-year defamation lawsuit and appeal where Glover, finally, prevailed.

The chilling effect of lawsuits is related to the lack of legal safeguards to protect consumer speech.\footnote{See Dan B. Dobbs et al., The Law of Torts, 159–61 (2d ed. 2011 & Supp. 2016); W. Page Keeton et al., Prosser and Keeton on the Law of Torts 771–72, 839–40 (5th ed. 1984).} Under prevailing standards, businesses can bring a defamation lawsuit against consumers if the review contains some factual inaccuracies.\footnote{Dobbs et al., supra note 348, at 167–71; McNamara, supra note 63, at 2; see Sim v. Stretch [1936] 52 Times L. Rep. 669, 669–71 (UK).} From a First Amendment perspective, some courts have been willing to accept that reviews are a matter of public interest and therefore should be protected under the First Amendment, but the scope of protection is slim. In a recent case, the Oregon Supreme Court explained that reviews are protected only if “a reasonable factfinder could not conclude that [the consumer’s] review implies an assertion of fact.”\footnote{Neumann v. Liles, 369 P.3d 1117, 1126 (Ore. 2016) (interpreting Milkovich v. Lorain Journal Co., 497 U.S. 1 (1990)).} In effect, the decision underscores the costs borne by consumers who pen reviews. Beyond the possibility of an anticonsumer mistake by judges or juries,\footnote{Neumann v. Liles, 369 P.3d 1117, 1126 (Ore. 2016) (interpreting Milkovich v. Lorain Journal Co., 497 U.S. 1 (1990)).} it is simply difficult for most consumers—especially those who are emotional—to write reviews that clearly communicate an opinion or avoid any factual inaccuracies given inevitable gaps in recollection, errors in phrasing, or strong emotions.\footnote{Nuno Garoupa, Dishonesty and Libel Law: The Economics of the “Chilling” Effect, 155 J. InstitutionaL THEOREtical Econom. 284, 285, 289 (1999).}

If we recognize the social importance of consumer reviews, the weak positive incentives to produce them, and the risk of liability or even just litigation, a few solutions present themselves. One moderate solution is greater adoption and broader implementation of anti-SLAPP legislation.\footnote{Lidsky, Silencing John Doe supra note 335, at 865 (noting the current protections are “inadequate”).} This legislation is useful because it imposes costs on strategic lawsuits by businesses. But it is also limited. To win such a suit, the consumer has to prove that the

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346. See id.
352. Lidsky, Silencing John Doe supra note 335, at 865 (noting the current protections are “inadequate”).
}
business does not stand a good chance of prevailing, which—given the current legal standards and the limited resources consumers have—is tough.\textsuperscript{354} Other options also include the use of legal aid subsidies or crowdfunding to defend consumers, arbitration, and other forms of alternative dispute resolution, and agency audits.\textsuperscript{355}

The most powerful solution would be a First Amendment protection in the form of a consumer review privilege.\textsuperscript{356} Today, political speech enjoys broad protections under the New York Times \textit{v. Sullivan}\textsuperscript{357} standard.\textsuperscript{358} Despite the recognition that protecting political speech could foster false allegations, the Supreme Court expressed a strong preference for the promotion of speech on matters involving public figures.\textsuperscript{359} As a result, the Court ruled that unless plaintiffs can show malice on the defendant’s side, a lawsuit cannot be brought.\textsuperscript{360} As a result, such lawsuits are relatively rare. Future cases, most notably \textit{Dun & Bradstreet, Inc. v. Greenmoss Builders},\textsuperscript{361} emphasized that issues of public interest are also deserving of greater protection.\textsuperscript{362} This is explained on the basis of the positive externality of speech, a feature that consumer reviews also share.\textsuperscript{363}

A consumer review privilege would still permit businesses to bring lawsuits against false reviews, but they will have to be able to show malice on the consumer side. Such a privilege will greatly reduce the business ability to strategically drag consumers to court.\textsuperscript{364} The privilege would also protect consumers in the lawsuit itself, although given the high win rate consumers enjoy today, this effect is admittedly small. Additionally, this privilege will considerably limit

\textsuperscript{354} See \textit{id.} at 305, 316–18, 325.


\textsuperscript{357} 376 U.S. 254 (1964).


\textsuperscript{359} See \textit{Sullivan}, 376 U.S. at 269–70.

\textsuperscript{360} See \textit{id.} at 279–80.

\textsuperscript{361} 472 U.S. 749 (1985).


\textsuperscript{363} See Posner, supra note 47, at 297–98.

\textsuperscript{364} For an early expression of this sentiment, see \textit{THOMAS STARKIE, A TREATISE ON THE LAW OF SLANDER, LIBEL, SCANDALUM MAGNATUM, AND FALSE RUMOURS xx–xxi} (New York, J. & J. Harper 1826).
the ability of businesses to de-anonymize consumers. As a result, this privilege would significantly reduce the cost of legal liability making speech more attractive on the margin. Indeed, existing privileges are also justified by the positive externalities of speech, so this privilege would be a natural extension.

Some have objected to protecting consumers’ reviews on the ground that it encourages reckless or deliberate lies by consumers against businesses. However, objections of this sort have not sufficiently accounted for the public value of reputation or its microfoundations. They assume that consumers share a desire to besmirch the reputation of firms but say little about why (or when) consumers care to tell the truth in the first place. Moreover, they have not analyzed the dynamic equilibrium that emerges from a lax defamation regime. In short, people tend to place less trust in assertions that are made in the absence of defamation law and so the negative impact of lies would be much abated. Thus, the opposition to consumer review privileges should be revisited. At the very least, scholars and policymakers should adopt a more skeptical approach to the social utility of defamation laws, and courts should better understand the chilling effect of their rulings, even when the case is finally disposed of in favor the consumer.

V. CONCLUSION

Reputation is fundamental to the operation of many markets. When reputation works, it works extremely well; it disciplines sellers at a low cost, saving the need for courts and lawyers. But reputation can also fail. Today, many are too excited by the rise of the sharing economy to see that the microfoundations on which it rests are faltering.

Earlier scholarship—in law, economics, sociology, and biology—has trusted reputation to work well, at least in certain domains. This Article explained why careful analysis of the microfoundations of reputation—the microincentives that lead individuals to create and share reputational information—suggests the potential of reputation failures. Such failures have a significant bearing on future policymaking and contracts scholarship in particular. Most directly, it invites greater skepticism towards current trends to deregulate consumer transactions on the basis of faith in the internal regulatory power of market forces.

365. See Dohse, supra note 137, at 390–91.
366. See Heymann, supra note 63, at 1417–23 (arguing that the public interest dimension of reputation has been neglected).
The most ambitious goal of this Article is to carve a path for future regulation of consumer markets—Reputation-by-Regulation, i.e., the use of laws and institutions to improve the flow of reputational information to the market. This approach holds considerable promise. Like mandatory disclosures, the law of reputation seeks to improve markets indirectly by providing consumers with reliable information that would allow them to make informed purchasing decisions. By identifying and removing reputational failures, the law can increase consumer welfare without mandating any specific set of terms, thus preserving autonomy and freedom of contract. Addressing reputation failure should be the cornerstone of future consumer policy.
