OPEN DOORS, TRAP DOORS, AND THE LAW

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I

INTRODUCTION

Common wisdom teaches us to strive to leave as many options open for as long as possible. We are advised by mentors and peers to constantly re-examine decisions and offers, seek out new ones, and keep sight and control of the old. The general preference to keep all doors open is ubiquitous and exercised in various walks of life. Keeping doors open is a cultural phenomenon that has become part of the unique American experience.

Leaving doors open is not merely a business or social dynamic. It is also reflected and rooted in the law in various ways, and can be articulated in legalistic terminology. The phenomenon of the open door is relevant to a variety of legal facets. This article focuses on open doors in the context of consumer contract law. Accordingly, the term "open door" will be used to refer to situations in which an individual can exercise, ex post, a right to rescind or withdraw from (and thus reverse) an ex ante commitment or decision.[1] More specifically, within the realm of contract theory, this article focuses on

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1. In recent years, interest has grown in the way people make decisions, and its influence, among other things, on well-being and happiness. *See, e.g.*, HEURISTICS AND BIASES: THE PSYCHOLOGY OF INTUITIVE JUDGMENT (Thomas Gilovich, Dale Griffin & Daniel Kahneman eds., 2002); THE LAW AND ECONOMICS OF IRRATIONAL BEHAVIOR (Francesco Parisi & Vernon L. Smith eds., 2005). A few popular books, based on extensive academic research, address issues raised in this article, though not in detail, nor from a legal perspective. *See* DANIEL GILBERT, STUMBLING ON HAPPINESS (2006); BARRY SCHWARTZ, THE PARADOX OF CHOICE: WHY MORE IS LESS (2004).

implications for contract formation interpretation and the design of contractual default rules.

A key example of the abstract notion of the open door in actual business practices is that of return policies. In general, liberal return policies are typical in many consumer markets.[2] Put simply, when a consumer is granted (at the time of the transaction) a right to return a product to the seller and get her money back "no questions asked," she is entitled to an open door.[3] In such a case, the original decision—to enter a transaction and purchase an item—can be reversed. This example is discussed throughout the paper.

On the face of it, leaving doors open makes perfect sense. Firms offering such opportunities should be encouraged and commended. Why shouldn't we put off decision-making as long as possible while leaving all options open? After all, this reflects the general human tendency to procrastinate,[4] and seems to have inherent value as well. In the meantime, another, better option could materialize or come to our attention, or new information may surface. Given the variety of options, the complexity of markets, and the sophisticated tastes of individuals, any extra time to contemplate a decision or transaction at stake must surely be a blessing.[5]

Contrary to this line of reasoning, open doors are often not a blessing, but a curse in disguise. In many instances, keeping doors open might not be the optimal strategy to assure wealth maximization and happiness. Moreover, at times, an open door may be part of a carefully tailored strategy to manipulate individuals—to enter transactions they should avoid.

The benefits associated with open doors and the conventional wisdom that promotes the notion of leaving doors open are detailed in part II. There are three basic ways in which the law can react to (or endorse) this phenomenon. First, it can impose open doors. For example, the law can provide mandatory cooling-off periods in which a party to a transaction can withdraw from it. Second, the law can encourage open doors by, for instance, formulating default

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2. Lenient return policies and similar practices are part of a broader movement of generating trust and confidence in mass retail. These latter forms of commerce were an important shift in the United States, away from small, local shops (that at times discriminated among consumers). *See* JOSEPH TUROW, NICHE ENVY: MARKETING DISCRIMINATION IN THE DIGITAL AGE 31 (2006).

3. Similarly, a borrower's ability, after commencing a financial loan (such as a home equity loan), to refinance, pay, or substantially change its terms without penalty might also be referred to as an "open door." Such rights are popular in U.S. loan markets, and are even mandated in several states. *See* Peter J. Wallison, *Cause and Effect: Government Policies and the Financial Crisis*, FIN. SERVS. OUTLOOK (Am. Enter. Inst. for Pub. Policy Research), Nov. 2008, at 6–7. The issue of whether refinancing resembles an open door or the formulation of a new agreement is beyond the scope of this article.

4. *See, e.g.*, Jeff Sovern, *Toward a New Model of Consumer Protection: The Problem of Inflated Transaction Costs*, 47 WM. & MARY L. REV. 1635, 1675 n.141 (2006) (providing various sources that support this assertion).

5. A recent working paper explains that in many instances, recognizing open door rights leads to efficient outcomes. *See generally* Omri Ben-Shahar & Eric Posner, *The Right to Withdraw in Contract Law* (Univ. of Chicago Law & Econ., Olin Working Paper No. 514, 2010), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1569753.

rules that call for open doors. Third, the law can allow the open door.[6] Here, the law will simply respect parties' decisions to opt for open doors and uphold their preferences. These three basic legal responses are detailed in part III.

Contrary to conventional wisdom, keeping doors open has its own pitfalls. Unfortunately, policymakers—not unlike the general population—tend to neglect the negative aspects of leaving doors open. This will be demonstrated in part IV, where the complex and rather counterintuitive consequences of the law's tendency to allow, uphold, or encourage open doors are considered.

The desire to leave doors open has far-reaching, diverse, and, at times, contradictory psychological, economic, and legal implications. In many cases, people assume that doors remain open for use at a later time when this is not, in fact, the case. Therefore, people's reliance on the open door may lead to inefficient outcomes. This leads people to insist on getting an open door (and compensating the opposing party for it) although they seldom use it. Moreover, this leads people to engage in transactions they should rationally avoid, or to purchase products they need not buy.

The problems associated with open doors call for a broad array of responses which must be inspected carefully. Initial recommendations for research are delineated in part V. However, the notions presented are merely a first step in understanding the impact of psychological phenomena on contract law and consumer protection policy.

II

THE INTUITIVE AND ANALYTICAL ATTRACTIVENESS OF OPEN DOORS

In order to better understand the phenomenon of open doors and to consider the appropriate legal response to this practice, it is necessary to consider its benefits. Thus, the various benefits commonly associated with the notion of leaving doors open are addressed in this part. We set out four basic arguments. The first pertains to information gathering; the second to managing (or limiting) risk; the third to psychological well-being; and the fourth to positive externalities.[7]

A. Open Doors and Information Gathering

One of the most basic assumptions of efficient markets is that sufficient information exists for all parties involved in a transaction.[8] In theory, rational

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6. A fourth response—the law barring voluntary open door provisions and practices—is also possible. However, in view of the many advantages of such provisions as well as other policy considerations (such as avoiding paternalism), such a response seems extremely unlikely.

7. Insofar as our analysis draws clear distinctions among these different aspects, it is mainly for reasons of methodology and clarity. We are well aware that these benefits at times overlap and interact.

8. Human participants are expected to behave in ways that "(1) maximize their utility (2) from a stable set of preferences and (3) accumulate an optimal amount of information and other inputs in a variety of markets." GARY S. BECKER, THE ECONOMIC APPROACH TO HUMAN BEHAVIOR 14 (1976) (numerals inserted).

market participants have the knowledge and understanding of all the attributes of the transaction they engage in. They are well versed in all elements pertaining to competing products or services. They also possess the required attention span to decide among them. This range of knowledge allows market participants to properly select and price a transaction. In doing so they might employ a "weighted adding strategy," which requires a thorough analysis of the options at stake, including all their pertinent attributes.[9]

Clearly, such a setting virtually never materializes. Typically, parties lack sufficient information, or time and attention to gather, analyze, and digest it. This, in itself, is a solvable problem. In theory, parties might apply various decision-making mechanisms to work through the complex datasets they encounter,[10] while using the time and attention they can spare to "satisfice."[11] Moreover, parties might often blunder, but their errors will offset one another so the overall outcome might still be efficient and fair.[12]

However, outcomes are not often efficient and fair. In many transactions, unsophisticated, one-shot players (such as consumers)[13] systematically lack sufficient information and resources. At the same time, sophisticated, repeat players (such as retailers) benefit from superior information—conspicuously in instances when they dictate the contractual framework and terms. In such cases, if the consumers' errors are in the same direction, legal intervention might be justified.

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9. This strategy is discussed in many different decision-making contexts. *See, e.g.*, James R. Bettman, Mary Frances Luce & John W. Payne, *Constructive Consumer Choice Processes*, 25 J. CONSUMER RES. 187 (1998) (applying this strategy in the context of consumers). According to this strategy, a consumer assigns a weight to every attribute she wishes to compare. Important features receive relatively high weight while less significant attributes are given less weight. The consumer presumably scores each product characteristic. Finally, the consumer multiplies the weight and the given score, then adds all factors for one total score. This score will represent the product's overall quality from the consumer's viewpoint. A consumer who seeks to maximize utility chooses the product that received the highest total score.

10. Gerd Gigerenzer, *Why Heuristics Work*, 3 PERSP. ON PSYCHOL. SCI. 20, 20 (2008) (naming logic, probability, and heuristics as three modes in which humans make decisions).

11. Herbert A. Simon, *Rational Choice and the Structure of the Environment*, 63 PSYCHOL. REV. 129, 129 (1956) (noting that when making decisions, "organisms adapt well enough to 'satisfice'; they do not, in general, 'optimize'"). Simon also coined the term "bounded rationality" to refer to human's computational limitations and definite ability. HERBERT A. SIMON, MODELS OF MAN: SOCIAL AND RATIONAL 198 (1957). For an illuminating discussion in the context of consumer decision-making and information overload, see David M. Grether, Alan Schwartz & Louis L. Wilde, *The Irrelevance of Information Overload: An Analysis of Search and Disclosure*, 59 S. CAL. L. REV. 277 (1986); Melvin Aron Eisenberg, Comment, *Text Anxiety*, 59 S. CAL. L. REV. 305 (1986).

12. *See, e.g.*, Milton Friedman, *The Methodology of Positive Economics*, *in* ESSAYS IN POSITIVE ECONOMICS 3 (1953).

13. Indeed, consumers themselves are repeat players in the sense that they engage in repeated transactions, at times even with the same vendor. However, as a class they lack sophistication, resources, and experience for the following reasons: First, even though consumers engage in many transactions, vendors engage in far more. Second, vendors have the ability, motivation, and knowledge to use information that transactions generate to learn a great deal about the transaction and the transacting party—something most consumers are unable to do. Third, vendors are able to structure the transaction based on the knowledge and insights they gather—architecturally, legally, and financially.

Considering this background, open doors provide consumers with more time to reflect on the pros and cons of a transaction.[14] This time allows for examination of additional, competing options. And as time passes, new options may emerge or be discovered. This benefits consumers who are not familiar with the options that markets offer, or might offer in the near future. In addition, during this time, more information (negative or positive) might become available from third parties.

Moreover, open doors provide parties with additional opportunities to learn about the product they have purchased, as they allow consumers to *experience* the product.[15] A classic example would be a distance-selling transaction (by phone or the Internet) involving tangible products, accompanied by a lenient return policy.[16] Typically, in distance selling, the consumer has not had a chance to interact directly with the product prior to purchase. By using the product, the consumer can ascertain its attributes and whether it truly suits her preferences and needs.

To a lesser degree, similar logic applies to all sales of tangibles. Prior to a transaction, consumers can learn of a product's attributes by reading about the product and examining it at the store. But the experience of using a product in the comfort of their home (where the pressures of sales representatives are absent) allows consumers to quickly and easily learn a great deal about the product.

Of course, learning through experience is not limited to tangibles. A similar dynamic might transpire with intangible assets as well. Consider a newspaper subscription, a cell phone service, or any other service that comes at a set price. Ex ante, consumers typically believe they will be able to afford the service without financial hardship. However, after some time, consumers might learn that they have committed themselves to a demanding payment schedule that is beyond their means. If consumers have an open door, they can rescind their contract and enter a new one that accommodates their economic circumstances. Living through the contractual terms assists individuals in understanding the "true" meaning, implications, and complications of a transaction.

Rather than outward, extra time allows a party to look inward. Time allows a purchaser to better understand her preferences, financial situation, and personal taste—whether through further investigating, or experiencing a product or service.

14. Open doors can assist consumers in learning how products fit in their home or with other products. *See* Ben-Shahar & Posner, *supra* note 5, at 20.

15. This is often the case because the purchaser has the actual possession. *See, e.g.*, Ben-Shahar & Posner, *supra* note 5, at 15 (referring, for example, to musical equipment).

16. Interestingly, some legislatures outside the United States provide consumers with a mandatory right to cancel a long-distance selling transaction. *See* Georg Borges & Bernd Irlenbusch, *Fairness Crowded out by Law: An Experimental Study on Withdrawal Rights*, 163 J. INST. & THEORETICAL ECON. 84, 85–86 (2007) (comparing general EU rules on consumer withdrawal rights with policies of members states).

B. Open Doors and the Allocation of Risk

Information gathering is merely one aspect of open doors. Additionally, open doors assist in allocating risks among parties. If a consumer wishes to maximize her utility through open market transactions, she must accurately assess the risks involved. In consumer markets, there are various forms of risk (for instance, that a product's value will fall, or that circumstances will change, influencing a consumer's subjective value of the product). The contractual bargain constitutes a risk allocation.

But drawing up contract terms to address all relevant risks is easier said than done. Markets commonly lead to inefficient outcomes as some participants—typically one-shot, unsophisticated ones—tend to miscalculate the underlying risks.[17] Repeat and sophisticated players have the opportunity, resources, and profit incentive to hedge, minimize, properly evaluate, and avoid unwarranted risks. Open doors can help weaker parties minimize some risks and evaluate others better.[18]

In addition, open doors can minimize the risk that relevant preferences will change in the near future. As a simple example, assume that a consumer purchases an item and shortly after, receives a similar item as a gift. Her need for the purchased item usually diminishes. A similar dynamic occurs after a consumer purchases a warm coat for the upcoming winter, and then learns that the winter is forecast to be rather mild. The longer period an open door provides, the more likely it is to help individuals who face changing circumstances.

Moreover, open door mechanisms help unsophisticated players minimize an additional risk: that the opposing party will breach the agreement and shirk its short-term obligations. An open door reassures the consumer, at least to some extent, that the purchased product or service is not defective and that it will meet its asserted specifications and descriptions. With an open door mechanism in place, potential aggrieved consumers can automatically obtain the remedy they would seek should the product or service be defective. In such a case, consumers can rescind the transaction at minimal cost, without the need to litigate their claims.[19] Thus, an open door limits the risk that the consumer will suffer from a breach[20] or a defective product.[21]

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17. For a debate on consumers' ability to learn from experience and minimize risk, see Oren Bar-Gill, *The Behavioral Economics of Consumer Contracts*, 92 MINN. L. REV. 749 (2008); Richard A. Epstein, *The Neoclassical Economics of Consumer Contracts*, 92 MINN. L. REV. 803 (2008).

18. For a discussion of how return policies can minimize uncertainty in these transactions, see Ben-Shahar & Posner, *supra* note 5, at 7–8.

19. While the risk of shirking parties might seem minimal in view of the clear course of legal action that harmed parties may take, things are far from being so simple. For one-shot, unsophisticated players, access to the legal system is costly and limited. Thus, in many cases (especially given the limited benefits of such claims), consumers will refrain from initiating legal action.

20. Note, however, that open door mechanisms merely protect consumers' restitution interest. A breach might generate greater damages and thus call for the protection of a consumers' reliance and expectation interest. To meet this objective, consumers would still have to consider litigation.

C. Open Doors, Positive Emotions, and Psychological Effects

The reasons noted thus far support open doors from what can be viewed as an economic perspective. Thus far, this article has dealt with individuals' preferences. Yet open doors have additional, psychological dimensions as well.

By and large, even when individuals do not anticipate immediate changes in their preferences or circumstances, they feel much more confident making decisions once they know the decisions can be easily reversed, with minimal costs. In western liberal countries, people tend to view such a right as part of our freedom, which we so greatly cherish. The mere option to cancel decisions, or at least postpone them, is psychologically reassuring. If we must choose between making a final decision and making one that can be revoked, we will most likely opt for the latter—and doing so will give us comfort. Thus, open door strategies and provisions are not only efficient in the strictly monetary sense. They also promote emotional well-being on the most basic level: by enhancing satisfaction.[22]

D. Open Doors, Competition, and Positive Externalities

Lastly, the phenomenon of open doors can lead to positive externalities by proving beneficial to competitors. When contracts are "final" and no open door is available, individuals are "locked" into their initial decision. Once a binding contract exists, it is quite expensive or difficult for consumers to breach and opt to contract with a competitor. Usually these "lock-in" effects are enforced by harsh penalties if contracts are breached midway. Given the high switching costs consumers might encounter, potential competitors have very limited ability to compete for consumers who have entered into a binding contract.

By providing consumers with an easy exit option, open door provisions can enhance efficiency. Open doors enable competitors to pursue potential consumers even when they are in a contractual relationship with another firm.[23] This dynamic lowers entry costs to markets and facilitates competition. As a result, open doors may encourage variety and quality in consumer markets.

Before proceeding, an important caveat should be inserted. So far, the assumption has been that the open door mechanism devised in the underlying contract and the open door put into practice are the same. This is not always the case. In many instances, the policies formulated in a contractual framework are

21. The specific benefits mentioned here can be also achieved through other legal means, such as consumer protection laws, class actions, et cetera. *See generally* Shmuel I. Becher & Tal Z. Zarsky, *Consumers' Right of Withdrawal: A Well-Reasoned Right or a Pyrrhic Victory?*, 32 TEL AVIV U. L. REV. 127 (2010) (in Hebrew).

22. This intuition has been examined and challenged in several psychological experiments. *See, e.g.*, GILBERT, *supra* note 1.

23. This ability has the most relevance in the context of long-term contracts, especially for services.

far harsher than those applied in practice.[24] For various reasons, firms have little to lose and much to gain from practicing a more lenient approach than is articulated in the contract.[25] However, for clarity, and since these are unstable and unpredictable outcomes, this article assumes that most firms often exercise their formal policy as stipulated in the contract.[26]

III

THE COMMON WISDOM OF OPEN DOORS AND THE LAW

Open doors have various positive attributes. Hence, it might seem natural that the law adopt the idea of open doors and, perhaps, encourage its usage. As detailed next, the notions of open door are embedded in the existing legal framework in three main ways.

In the most drastic and obvious form, open doors are rendered mandatory. In other instances, the law approves open door policies in more subtle ways, such as setting them as defaults. Finally, the law can simply uphold open door provisions in a contractual framework. By allowing the implementation of open doors, the law further enables market participants to employ open doors.

A. Mandatory Open Doors

The rulebooks provide a variety of instances in which a contractual open door mechanism is mandated.[27] Perhaps the most famous example is that of

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24. Jason Scott Johnston, *The Return of Bargain: An Economic Theory of How Standard-Form Contracts Enable Cooperative Negotiation Between Businesses and Consumers*, 104 MICH. L. REV. 857, 858 (2006).

25. *See generally* Shmuel I. Becher & Tal Z. Zarsky, *E-Contract Doctrine 2.0: Standard Form Contracting in the Age of Online User Participation*, 14 MICH. TELECOMM. & TECH. L. REV. 303 (2008). Some commentators argue that such strategies are even efficient and preferable in certain circumstances. *See* Lucian A. Bebchuk & Richard A. Posner, *One-Sided Contracts in Competitive Consumer Markets*, 104 MICH. L. REV. 827, 827–28 (2006) ("A seller concerned about its reputation can be expected to treat consumers better than is required by the letter of the contract.").

26. A mirroring problem is possible as well: firms might contractually provide open doors that go beyond those that the sales representative conveys to consumers. For a discussion of instances when this form of conduct is purposeful and strategic (as a measure to generate price discrimination among consumers), see David Gilo & Ariel Porat, *Viewing Unconscionability Through a Market Lens*, 52 WM. & MARY L. REV. 133, 155 (2010). Gilo and Porat refer to such practices as relying upon "Selective Beneficial Terms." Their example is of a subscription to an Internet Service Provider (ISP), which provides, in fine print only, for the right to cancel within a certain period of time. This right is not evident to consumers who do not read the fine print. We refrain from developing this point for the reasons set forth in the text. Also, we believe that novel ways for distributing consumer information will prove helpful in closing this information gap. For an analysis of this dynamic, see Becher & Zarsky, *supra* note 25.

27. For some reviews of this legal framework, see JOHN A. SPANOGLE, RALPH J. ROHNER, DEE PRIDGEN & JEFF SOVERN, CONSUMER LAW: CASES AND MATERIALS 252–53 (3d ed. 2007); Colin Camerer, Samuel Issacharoff, George Loewenstein, Ted O'Donoghue & Matthew Rabin, *Regulation for Conservatives: Behavioral Economics and the Case of "Asymmetric Paternalism*,*"* 151 U. PA. L. REV. 1211, 1238 (2003); Ben-Shahar & Posner, *supra* note 5. *See also* IAIN RAMSAY, CONSUMER LAW AND POLICY 141, 330–46, 555 (2d ed. 2007) (United Kingdom); Becher & Zarsky, *supra* note 21 (Israel).

mandatory "cooling off" periods.[28] These are set by federal[29] and state[30] legislators and regulators for door-to-door sales, and, in some cases, time-sharing sales. In these circumstances, open door mechanisms protect consumers from falling prey to aggressive sales tactics and undue pressure.[31]

Mandatory open doors, however, go beyond door-to-door and time-sharing sales.[32] Regulators have set them in place for somewhat risky transactions (and therefore as an appropriate measure to reassess risk) such as used car sales (so-called lemons laws).[33] In addition, they have been set in place for important and substantial transactions (such as home equity loans),[34] where both reassessment of risk and the additional information gathering by the weaker party might be essential. In the European Union (EU)[35] and other countries,[36] extensive regulatory frameworks provide a "right to rescind" distance sales. These laws pertain to catalogs and phone orders, and have been broadened to e-commerce transactions.[37] So far, such regulation has not been enacted in the United States.[38]

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28. For a general background and discussion, see SPANOGLE ET AL., *supra* note 27, at 251–59.

29. *See* 16 C.F.R. § 429.1 (1995) (mandating a cooling-off period in door-to-door transactions).

30. According to one study, every state—and the District of Columbia—has enacted a cooling-off statute. *See* DEE PRIDGEN & RICHARD M. ALDERMAN, CONSUMER CREDIT AND THE LAW app. 14A (2009).

31. *See, e.g.*, Arizona v. Direct Sellers Ass'n of Ariz., 494 P. 2d 361 (1972) (upholding a statute regulating door-to-door salesmen, citing a Congressional report that noted "a disproportionate number of door-to-door sales involve misleading or high pressure sales").

32. Some loan and financing regulations allow borrowers to refinance or terminate their loan with minimum costs, at any time. There is heated debate as to how these policies impacted the recent economic crisis. *See* Wallison, *supra* note 3. The law also assures that firms provide consumers with portability, that is, the ability to switch easily to a different provider. The Health Insurance Portability and Accountability Act of 1996, Pub L. No. 104-191, 110 Stat. 1936 (HIPAA) ensures that medical insurance providers allow the insured to switch jobs by requiring firms to insure against preexisting conditions. The Federal Communication Commission (FCC) mandates local phone number portability, which promotes competition in telecommunications markets and limits incumbents' ability to lock up their existing customer base.

33. *See, e.g.*, N.Y. GEN. BUS. LAW § 198-b (McKinney 2004). One might argue that these rules counter "aggressive" tactics of used car salesmen as well.

34. *See* 15 U.S.C. § 1635 (1995) (Truth in Lending Act (15 U.S.C. §§ 1601–1667(f)) (provision mandating a three-day right to rescind home equity loans)); Home Equity Loan Consumer Protection Act of 1988, Pub. L. No. 100-709, 102 Stat. 4725 (amending provisions of the Truth in Lending Act).

35. *See* Pamaria Rekaiti & Roger Van den Bergh, *Cooling-off Periods in the Consumer Laws of the EC Member States: A Comparative Law and Economics Approach*, 23 J. CONSUMER POL'Y 371 (2000); Borges & Irlenbusch, *supra* note 16.

36. Australia and New Zealand are two examples. For a report addressing this issue in the Asia–Pacific Economic Cooperation (APEC) region, see Elec. Commerce Steering Grp., Int'l, *Approaches to Consumer Protection Within the APEC Region*, NORTH AM. CONSUMER PROJECT ON ELEC. COMMERCE (Oct. 2002), http://www.nacpec.org/docs/Approaches_to_consumer_protection.pdf.

37. *See, e.g.*, Rekaiti & Van den Bergh, *supra* note 35. One of the rationales for extending such protection to the Internet in the EU was to promote e-commerce. Some argue that applying this rationale to the U.S. legal and business setting on its own seems unfitting. Ben-Shahar & Posner, *supra* note 5, at 4. For a challenge to the basic premise of this rationale, see Becher & Zarsky, *supra* note 21, at 190–92.

38. For a recent call to extend the current legal setting and add additional default "open door" rules, see Ben-Shahar & Posner, *supra* note 5.

B. Legal Frameworks that Promote Open Door Policies

Imposing a mandatory open door regime is a harsh legal intervention in the market. Setting default rules is a milder measure.[39] Defaults are usually set to meet the common preferences of transacting parties, thus limiting overall transaction costs. In some instances, defaults take on a different role—one which strives to encourage the transfer of information among transacting parties ("penalty default rules") or affect the transacting parties' behavior in a manner the state deems fit.[40]

In various contractual frameworks, open doors are set as defaults in accordance with these latter rationales.[41] In the realm of retail, several states have enacted regulation concerning consumers' right to return goods or the way vendors should present their return policies.[42] Arguably, regulators strive to use defaults as instruments for promoting the transfer of information on return policies. Or else, the default is used to encourage the adoption of open doors in the market.

At other points, the law gives a milder, subtler nod. This occurs in the context of rolling contracts or online software agreements. Here, courts and commentators have been debating whether the terms included in a software package constitute a binding contract. A major impediment to recognizing the existence of a contractual framework is the lack of actual consent to the terms by the purchasing party prior to entering and "accepting" the transaction.

A famous court decision, *ProCD, Inc. v. Zeidenberg*,[43] may illustrate. In this decision, still considered by many as good law,[44] Judge Easterbrook of the Seventh Circuit held that a binding contract was formulated when the software was purchased, in accordance with the terms detailed in the software box. The court did so, even though the contractual terms could not be viewed prior to formation. The court found that the ex ante flaw regarding actual assent could be cured by the purchasers' ex post ability to view the terms and *return the*

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39. *See, e.g.*, Cass R. Sunstein & Richard H. Thaler, *Libertarian Paternalism Is Not an Oxymoron*, 70 U. CHI. L. REV. 1159, 1162 (2003) (introducing the concept of libertarian paternalism, associating consumer cooling-off periods with it, and explaining that libertarian paternalism "is a relatively weak and nonintrusive type of paternalism, because choices are not blocked or fenced off").

40. *See, e.g.*, Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87 (1989). *See also* Russell Korobkin, *The Status Quo Bias and Contract Default Rules*, 83 CORNELL L. REV. 608 (1998).

41. In the financial context, policy, at times, actively facilitates open doors. For instance, the federal government has put in place an elaborate system that enables banks to offer fixed-rate or long-term loans which allow refinancing at any time. In other words, these loans allow the borrower to exit one loan and opt for another. The government does so at considerable expense. The rise and fall of Fannie Mae and Freddie Mac are possibly related to these issues. *See* Wallison, *supra* note 3, at 4–6.

42. N.Y. GEN. BUS. LAW § 218-a (McKinney 2009); Consumer Sales Practices Act, OHIO REV. CODE ANN. § 1345.03 (LexisNexis 2009); CAL. CIV. CODE § 1723 (Deering 2009).

43. ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir. 1996). For a recent analysis revisiting this case, see Randal C. Picker, *Easterbrook on Copyright*, 77 U. CHI. L. REV. 1165 (2010).

44. Mark Lemley, *Terms of Use*, 91 MINN. L. REV. 459, 469 (2006).

product thereafter.[45] The existence of the open doors in this context served as a substitute for one of the most fundamental elements of contract formation: ex ante consent to the contract and its terms. That is, not only are open door options useful, they could actually replace one of the most important components of a binding contract. Interestingly, a somewhat refined but generally similar notion was accepted most recently in the Principles of Software Contracts.[46]

C. Upholding and Reinforcing Open Doors

In many realms of business—retail and wholesale are cornerstone examples—market participants use open doors voluntarily. Recent studies indicate the enormous popularity of such practices, which in some instances are extremely lenient.[47] Firms offer these mechanisms for a variety of reasons: to meet consumer preferences, to signal quality, to promote goodwill, or to engage in sophisticated marketing.

These instances might seem to be located outside the realm of regulation and legal intervention. But they are not. This is so because courts uphold contracted open door rights, with regard to both the existence of the right and its limits. Additionally, regulators may intervene in these relations, by mandating additional disclosures or changing the rights and obligations of the contracting parties.

This perspective may seem trivial and its analysis futile. Why not uphold contractual obligations that seem to benefit weaker parties in closing information gaps and assessing risks, as well as having positive psychological and externality effects? On its face, there is no reason to object to agreements that allow consumers more time to contemplate their transactions, thus maximizing their utility and satisfaction. Yet as we now explain, this sunny outlook of open doors is not always accurate.

IV

THE PROBLEMS OF OPEN DOORS

Open doors lead to very different outcomes from those portrayed in the previous parts. The intuitions that support open doors are, in many instances, wrong.[48] This misunderstanding leads to a flurry of problems, which at times override the apparent benefits that open doors present.

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45. For a recent analysis, see Ben-Shahar & Posner, *supra* note 5.

46. AM. LAW INST., PRINCIPLES OF THE LAW OF SOFTWARE CONTRACTS § 2.02 (2010). For a recent discussion, see Hannibal B. Travis, *The Principles of the Law of Software Contracts: At Odds With Copyright, Consumers, and European Law?*, 84 TUL. L. REV. 1557 (2010).

47. Examples include, inter alia, Costco, Macy's, Walmart, and Target. For a sample of these lenient policies, see Ben-Shahar & Posner, *supra* note 5, at 6–7.

48. Having additional (or "more") legal rights as opposed to less is, at times, detrimental to society at large. *See generally* Daphna Lewinsohn-Zamir, *More Is Not Always Better Than Less: An Exploration in Property Law*, 92 MINN. L. REV. 634 (2008). Lewinsohn-Zamir shows how many existing

In this context, regulators seem to do too little. Currently, open door mechanisms are mandated, encouraged, or upheld, with the parties left to their own devices. Understanding the pitfalls that come with open doors might help regulators and policy-makers formulate the way the legal approach to open doors ought to be crafted.

In many instances, open doors lead to negative outcomes for the unsophisticated contracting party that occur without that party's understanding or knowledge.[49] First and foremost, firms commonly (and at times subtly) inflate the transaction costs involved in rescinding a contract in various ways.[50] For instance, firms make sure that contacting the representative in charge of canceling a service is next to impossible. In other instances, they set strict demands for physically returning a product. These problems are quite common and cannot be corrected by competition or consumer complaints given several persistent market failures.[51]

Misrepresentations of open doors and imposing undue burdens on consumers who wish to return a product or cancel a contract, are indeed problematic. But there are further problems in the open door process that are currently unrevealed.

A. Are Open Doors Indeed Open? Valuing and Perceiving Open Doors

In many cases, and for many consumers, open doors are not truly open. The ability to rescind an agreement and exercise an open door might not be as straightforward as it seemed at the time of formation. To verify this claim, one should examine the marketing, business, and psychological dynamics involved in open door mechanisms.

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property-related norms strangely limit the autonomy and rights of various players—supposedly undermining efficiency and fairness. However, her analysis shows that, in light of behavioral insights and cognitive failings, these rules are, in many cases, optimal. Our premise differs from Lewinsohn-Zamir's on a central point: rather than explaining the rationale behind existing law and justifying it based on a behavioral analysis, we use behavioral analysis to demonstrate that current law ought to be reexamined.

49. For example, regulators intervened in transactions which included open doors that were apparently misleading or fraudulent. In some cases, signs indicating "Free Trial Period!" and "Money Back—GUARANTEED!" were, indeed, too good to be true. Some involved "bait and switch" schemes, where the product provided was not the one advertised. Others misled consumers as to the difficulty of rescinding the initial transaction. The Federal Trade Commission has taken steps to regulate "negative option plans" and "free trial offers" involving "book of the month clubs" and other such settings. *See* SPANOGLE ET AL., *supra* note 27, at 236–37. Regulators moved to assure proper disclosure prior to the transaction regarding the nature of the open door option, as well as the steps required to rescind it.

50. Sovern, *supra* note 4, at 1644. *But see* Ben-Shahar & Posner, *supra* note 5, at 16 (indicating that firms at times "exploit natural barriers" as a measure to limit the consumers' ability to rescind contracts for strategic reasons). The use of such implicit barriers, even for achieving this fair outcome, is troubling.

51. Sovern, *supra* note 4, at 1667.

1. Are Open Doors Salient?

A preliminary question is whether parties presented with an open door factor it into their decision of whether to transact. The analysis here assumes that often this is indeed the case. It further assumes that parties implicitly "price" the open door option, and willingly pay for it. To this end, the distinction between salient and non-salient open door mechanisms should be explained.

As many standard form contracts include dozens of pages and hundreds of elements, it is highly unlikely that a contracting party will allocate sufficient attention to them all.[52] A major reason for the existence of an open door is to assist the consenting party in overcoming the almost impossible task of reading and understanding all contract terms. It is widely agreed, for example, that consumers tend not to read form contracts most of the time, and for various good reasons.[53]

In light of this reality, contract law scholars distinguish between "salient" and "non-salient" terms and provisions.[54] The salient ones are those that parties read (or learn of their existence in another way),[55] comprehend, and consider. Non-salient provisions are given less weight or are simply ignored.[56]

The distinction is significant. According to this line of reasoning, salient provisions—the most usual examples are price and quantity terms—can generally be enforced by courts, requiring limited judicial scrutiny. In competitive markets, parties effectively signal to each other their preferences and consent insofar that salient attributes are at stake. These instances conform to the overall notion of the freedom to contract and the autonomy of contracting parties.

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52. A classic economic assertion in this context is that, where strong competition exists, it is enough that some consumers (a substantial minority) shop for contract terms in order to discipline sellers and generate a fair and efficient market. *See, e.g.*, Alan Schwartz & Louis L. Wilde, *Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis*, 127 U. PA. L. REV. 630 (1979). This thesis has been questioned and criticized from various perspectives. *See, e.g.*, R. Ted Cruz & Jeffery J. Hinck, *Not My Brother's Keeper: The Inability of an Informed Minority to Correct for Imperfect Information*, 47 HASTINGS L.J. 635 (1996).

53. *See, e.g.*, Yannis Bakos, Florencia Marotta-Wurgler & David R. Trossen, *Does Anyone Read the Fine Print? Testing a Law and Economics Approach to Standard Form Contracts* (N.Y.U. Law & Econ. Research Paper No. 09-40, 2009), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1443256; Shmuel I. Becher & Esther Unger-Aviram, *The Law of Standard Form Contracts: Misguided Intuitions and Suggestions for Reconstruction*, 8 DEPAUL BUS. & COM. L.J. 199 (2010); Debra Pogrund Stark & Jessica M. Choplin, *A License to Deceive: Enforcing Contractual Myths Despite Consumer Psychological Realities*, 5 N.Y.U. J.L. & BUS. 617 (2009).

54. *See, e.g.*, Shmuel I. Becher, *Behavioral Science and Consumer Standard Form Contracts*, 68 LA. L. REV. 118, 170–177 (2007); Russell Korobkin, *Bounded Rationality, Standard Form Contracts, and Unconscionability*, 70 U. CHI. L. REV. 1203, 1206 (2003).

55. This flow of information is generated by (usually experienced) consumers in various ways. For a detailed analysis, see Becher & Zarsky, *supra* note 25.

56. The distinction between these categories is not clear-cut, and a term that is non-salient at the time of the transaction might become salient at a later time.

Non-salient elements should be treated differently. If individuals do not pay attention to some contract provisions, no consent emerges and no signaling occurs. Thus, the preferences of market participants cannot be incorporated and reflected in the contractual terms. Rather, in such a case, the contract is a result of the will of the drafting party and the ignorance of the other. For that reason, commentators have noted that courts (ex post) and regulators (ex ante) should intervene to protect ignorant, unsophisticated players from imbalanced, non-salient provisions.[57]

One of the fundamental questions in this respect is whether open door mechanisms are salient. On the one hand, open doors resemble many other elements that are considered non-salient. Open door provisions pertain to an uncertain and relatively unpleasant event which might take place in the future (the dissatisfaction with the product or service purchased). The chances of it occurring may seem rather slim.[58] This places open door provisions among typically neglected elements such as remedies, forum selection clauses, and arbitration terms. The potential non-saliency of open doors presents a strong argument for setting open doors as defaults or through mandatory rules.

On the other hand, open door clauses enjoy some degree of public attention. For instance, recent surveys indicate that consumers assign considerable importance to return policies.[59] This might be explained given the cultural significance of this element in U.S. retailing.[60] In view of these findings, some degree of salience of open doors from consumers' perspective may be reasonably assumed.

Until robust empirical data is gathered, the analysis should include several preliminary distinctions. First, open doors have salient and non-salient elements. Arguably, people often notice their mere existence or absence, and maybe even the extent of the period they are open for. However, the specific terms that accompany open doors (for example, requirements such as keeping

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57. *See, e.g.*, Shmuel I. Becher, *A "Fair Contracts" Approval Mechanism: Reconciling Consumer Contracts and Conventional Contract Law*, 42 U. MICH. J.L. REFORM 747, 749 n.2–4 (2009); Korobkin, *supra* note 54.

58. There are different perspectives and findings on this issue. For empirical data regarding the low rate of actual returns (in this study, sixteen percent), see J. Andrew Petersen & V. Kumar, *Can Product Returns Make You Money?*, 51 MIT SLOAN MGMT. REV. No. 3, 85 (2010), *available at* http://sloanreview.mit.edu/the-magazine/articles/2010/spring/51316/can-product-returns-make-you-money/. For somewhat different findings in the electronics and computer realm, see Yeon-Koo Che, *Customer Return Policies for Experience Goods*, 44 J. INDUS. ECON. 17, 17 (1996) ("As many as 20% of personal computers sold to home buyers are known to be returned. . . .").

59. *See, e.g.*, Erika Morphy, *Survey: Customers Want Flexible Return Policies* (Jan. 8, 2007), *available at* http://www.crmbuyer.com/story/55031.html?wlc=1286145522 (seventy-five percent find a clear and simple return policy to be a highly important attribute); Ben-Shahar & Posner, *supra* note 5, at 20 ("Return policy is not the type of fine print term that goes under the radar, hidden from consumers' plain sight.").

60. TUROW, *supra* note 2. *See also* Ben-Shahar & Posner, *supra* note 5, at 20 ("Buyers seek information about the sellers' return policies, because most buyers anticipate returns as a non-trivial contingency.").

receipts or original packaging—which lead to "transaction costs"[61]) might frequently be beyond the attention span of the average consumer.

Second, firms offering open door mechanisms sometimes take steps to render them salient or non-salient. In some cases, firms promote the salience of open door provisions by advertising: explicitly indicating specific transactions as "free trial periods," or emphasizing "money back guarantee" or "cancel anytime" elements.[62] In other cases, firms strive to render these elements non-salient by "burying" references to the actual open door mechanism in their contracts.[63] Clearly, different instances require different analyses.

Third, even if consumers account for the existence of the open door and its "price," we must inquire whether they calculate its value correctly. When addressing options and their pricing in general, the option holder takes into account the chance that the relevant event will materialize. At the time of an initial consumer-related transaction, individuals must take into account the factors addressed in part II: the chance that at a later time, additional information, added risks, or changes in preferences will render the transaction undesirable. Also, the option holder should take into account the possibility that her analysis is wrong—a risk that, in many markets, is quite predictable (and thus subsequently hedged). Moreover, consumers should furthermore consider whether the direct or indirect (or perhaps hidden) costs and requirements involved in exercising the option would render such actions unfeasible. This is especially important in ordinary consumer markets, which deal with relatively cheap and simple goods.

These elements make a proper assessment of open door options rather difficult. People face serious difficulties assessing outcomes of specific events that have the general traits of open door dynamics. Those difficulties are aggravated by the problems and phenomena addressed below. And once the error is predictable and can be induced by the interested party, the problem becomes worse and might call for more aggressive regulatory measures.

2. Open Doors and the Endowment Effect

The endowment effect is one of the key contributors to the misperception of open doors. It refers to the additional disproportionate value individuals attach to assets they possess or own. For instance, in one famous study, students were randomly assigned mugs. Those who owned the mugs demanded far more money as sellers than those who were not given mugs were willing to pay as

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61. *See* Sovern, *supra* note 4.

62. For examples in ISP markets, see SPANOGLE ET AL., *supra* note 27, at 237. For an interesting illustration, see the General Motors (GM) TV ad, *available at* http://www.youtube.com/watch?v=jpqr4_ONew0 (featuring GM CEO Ed Whittaker conspicuously promoting the "60-Day-Money-Back guarantee").

63. This might lead to efficient outcomes by allowing firms to discriminate between diligent and non-diligent consumers. *See* Gilo & Porat, *supra* note 26, at 155 (providing insightful, though esoteric and rare examples).

buyers.[64] In another study, one group of students was assigned mugs, while a second was assigned Swiss chocolate. After a short while, both groups were asked whether they would like to replace the assigned item. In both groups, an overwhelming majority (about ninety percent) preferred staying with the item they were originally assigned.[65]

This effect was replicated in a variety of settings, cultures, and participants.[66] Studies indicate that such a change in subjective value is significant, attaches instantaneously, and grows with time.[67] The endowment effect is activated as early as the moment when goods are purchased remotely (online or through a catalog),[68] or even earlier.[69] This can lead to overestimation of one's rights or assets, which can lead to mistakes.[70]

The endowment effect generates a force that should not be underestimated. Yet, it commonly is.[71] This leads to a problem: because individuals do not correctly predict the extent of the endowment effect, they are unable to assess it accurately.[72] As one scholar puts it,

> If we are not sure whether or not we should get a new sofa, the guarantee of being able to change our mind later may push us over the hump so that we end up getting it. We fail to appreciate how our perspective will shift once we have it at home, and how we will start viewing the sofa—as ours—and consequently start viewing returning it as a loss. We might think we are taking it home only to try it out for a few days, but in fact we are becoming owners of it and are unaware of the emotions the sofa can ignite in us.[73]

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64. The phenomenon was first documented by Richard Thaler some thirty years ago. *See* Richard Thaler, *Toward a Positive Theory of Consumer Choice*, 1 J. ECON. BEHAV. & ORG. 39, 44 (1980).

65. Jack L. Knetsch, *The Endowment Effect and Evidence of Nonreversible Indifference Curves*, 79 AM. ECON. REV. 1277, 1278 (1989).

66. *But see* Charles R. Plott & Kathryn Zeiler, *The Willingness to Pay—Willingness to Accept Gap: the "Endowment Effect," Subject Misconceptions, and Experimental Procedures for Eliciting Valuations*, 95 AM. ECON. REV. 530 (2005) (challenging the robustness of the endowment effect).

67. *See, e.g.*, Ziv Carmon & Dan Ariely, *Focusing on the Forgone: Why Value Can Appear So Different to Buyers and Sellers*, 27 J. CONSUMER RES. 360 (2000).

68. Stacy L. Wood, *Remote Purchase Environments: The Influence of Return Policy Leniency on Two-Stage Decision Processes*, 38 J. MARKETING RES. 157, 160 (2001).

69. A possible earlier point is when a bidder in an online auction has remained the highest bidder for an extended period of time. *See* DAN ARIELY, PREDICTABLY IRRATIONAL 135–36 (2008) (stating that, in these instances, the endowment effect is triggered by "virtual ownership").

70. For example, the endowment effect can distort litigants' willingness to settle a case. *See generally* Ward Farnsworth, *Do Parties To Nuisance Cases Bargain After Judgment? A Glimpse Inside the Cathedral*, 66 U. CHI. L. REV. 373 (1999).

71. S*ee generally* George Loewenstein & Daniel Adler, *A Bias in the Prediction of Tastes*, 105 ECON. J. 929 (1995) (study indicating individuals' inability to predict the endowment effect). *See also* sources cited *infra* note 73. For applying the concept of the endowment effect to contract law, see, for example, Russell Korobkin, *The Endowment Effect and Legal Analysis*, 97 NW. U. L. REV. 1227, 1232 (2003).

72. Whether consumers can learn over time about these effects and correct their decision-making process is a thorny question. As explained below, we are skeptical whether this is indeed possible in this context.

73. ARIELY, *supra* note 69, at 137. *See also* Jon D. Hanson & Douglas A. Kysar, *Taking Behavioralism Seriously: The Problem of Market Manipulation*, 74 N.Y.U. L. REV. 630, 734 (1999) ("Significantly, it has been demonstrated that people are unable to predict the operation of the

While the strength and breadth of the endowment effect is not always fully understood by consumers, it is surely appreciated in the world of business and marketing. Vendors, service providers, and their consultants fully recognize that "moving" merchandise into the hands of consumers is the way to get the deal done.[74] To do so, they employ various strategies. One of them is providing consumers with open doors.

Thus, the endowment effect plays a crucial—yet underestimated—role in the open door dynamic. Individuals who are provided with an open door misperceive the impact the endowment effect will have on their decision to ultimately exercise that option.[75] Ex ante, consumers assume they will exercise the open door option should the product (or service) not meet their preferences *as they see them at that time*. However, they misperceive the fact that their chances of exercising the option are *substantially lower*. The endowment effect strengthens the consumer's connection to a possessed product and increases its value in her eyes. Slightly restated, the consumer assumes her preferences will remain stable. But she is typically unaware that the transaction itself might change her preferences. Such a change will undermine her will to exercise the open doors option. In a way, therefore, open doors give consumers a false sense of market power. But, they end up perpetuating the inequalities between contracting parties that they were supposed to minimize.

This argument is challenging philosophically, because it requires a flexible and layered use of the concept of "consumer preferences." Consumers are not coerced into refraining from exercising an open door option, or misled as to its terms. Furthermore, consumers' decision to refrain from rescinding the contract is based on a genuine value they attach to their possession. That is, their preferences regarding the relevant product might have changed in light of their ownership, but their decision (not to rescind the contract) reflects their preferences once they possess the product. In economic terms, this is Pareto efficient: the transaction moves the product to the hands of the party that values it the most.

To explain why this seemingly legitimate exercise of preference merits legal attention (and perhaps even intervention), the notions of first-order and second-order preferences should be introduced.[76] This terminology highlights the difference between one's short-term, or current, preferences, and one's long-term preferences. That is, the value one assigns to a product (for example,

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endowment effect. . . . [C]onsumers will fail to perceive the risks of taking a product home—they will, in effect, really perceive it as a 'no risk' offer.").

74. Gerald E. Smith & Thomas T. Nagle, *Frames of Reference and Buyers' Perceptions of Price and Value*, 38 CAL. MGMT. REV. 98, 101 (1995). It is generally agreed that sellers are not subject to the endowment effect with regard to their merchandise.

75. Articulating the exact influence on consumers is yet a challenge due to lack of empirical data. *See* Wood, *supra* note 68, at 158 ("Behavioral investigation of the issue is nonexistent.").

76. For a discussion of these terms, coined by Harry Frankfurt, in the legal context, see generally Cass R. Sunstein, *Legal Interferences With Private Preferences*, 53 U. CHI. L. REV. 1129 (1986). *See also* Eyal Zamir, *The Efficiency of Paternalism*, 84 VA. L. REV. 229, 243 (1998).

a new luxury car or an expensive piece of jewelry) at the time he purchases it (or chooses not to return it) is not always aligned with his long-term life goals (for example, education, saving, or health care). Therefore, in the examples presented above, individuals misperceive the change in their first-order preferences, which may not match their second-order ones—a change they might regret later.

This analysis still might confront powerful challenges. Not in every case does a consumer-based transaction potentially involve an internal conflict between long- and short-term goals. Therefore, a different way to explain the problem might be needed. This alternative explanation relies on the need to maintain the consumers' ability to engage in autonomous decisions, free from external influences of interested parties. Open doors might undermine such an ability.

The hidden elements of the endowment effect, which open doors bring to life, conflict with the human preference for autonomous decisions. This is so for two main reasons. First, individuals are unable to account for the cognitive failings occurring in the open door context.[77] Second, external forces generate an endowment effect that is powerful enough to manipulate an individual's choices, and might be doing so intentionally.[78]

3. Inertia and the Costs of Exercising Open Doors

Consumers tend to overestimate their chance of exercising open door options, and their ability to do so. At the time of contract formation, individuals are unlikely to understand the full implications of later rescinding the contract. This misunderstanding occurs even when the entire process of applying the open door option is transparent to consumers.[79] In other words, individuals are not likely to fully comprehend the cost—in time, attention, anxiety, and out-of-pocket expenses—involved in exercising an open door. At the same time, sophisticated parties understand quite well the true obstacles inherent in using the open door option.

Individuals tend to overestimate their ability to exercise open door options because of several cognitive shortcomings. Generally, people are hard pressed to properly assess risks and actions that transpire in the distant, uncertain future. They tend to be over-confident and over-optimistic about future outcomes.[80] Their inclination is to employ optimistic narratives about future

77. The question as to whether the law must engage in active debiasing when cognitive failings lead to errors of judgment is quite complex and calls for legal analysis beyond the scope of this paper. On this issue, see Avishalom Tor, *Whether and When To Debias Through Law*, LAW AND BUSINESS (forthcoming) (in Hebrew, on file with authors), and sources quoted therein.

78. This form of manipulation presents a much easier case for government intervention. *See* Sunstein, *supra* note 76, at 1159. Yet, this intervention does not pertain to all instances of open doors, as it calls for some level of a sellers' intent to manipulate consumers.

79. As opposed to instances in which such misunderstanding results from the firm's withholding relevant information about this issue at the time of the transaction, providing misleading data, or providing full data in an incomprehensible manner. *See generally* Sovern, *supra* note 4.

80. *See generally* Lynn A. Baker & Robert E. Emery, *When Every Relationship Is Above Average: Perceptions and Expectations of Divorce At the Time of Marriage*, 17 LAW & HUM. BEHAV. 439 (1993).

deeds and plans: standing in line to return a product, they assume, will take only a short time; the phone representative will respond to their request relatively promptly. And all this will take place when the individual has ample free time to deal with these matters.

Even if individuals properly understand the meaning of exercising an open door option ex ante, they are likely to err and overestimate their ability and willingness to actually do so. In most cases, rescinding a contract requires action. But people tend to maintain the status quo and remain passive, even if by doing so they fail to maximize utility.[81] Even when choosing action, they often procrastinate and postpone what has to be done.

Procrastination in the open door context acts as a double threat. First, it might lead to accidentally missing the timeframe in which a transaction can be rescinded. Second, procrastination will cause individuals to put off a decision to use an open door as much as possible. By that later point in time, the endowment effect will contribute to inaction. Thus, procrastination leads to a higher chance of ignoring an open door option. These considerations are mostly unapparent to an individual, so they cannot be incorporated into her calculations and decision.[82]

4. Open Doors and the (Mis)perception of Happiness[83]

Open doors serve a basic psychological function. They allow one party to delay, albeit for a limited period of time, a sometimes painful human activity: decision-making. Studies indicate that many individuals do not care for certain experiences of decision-making. It seems that open doors afford individuals a soothing experience of extra time to make decisions.[84]

For a discussion of over-optimism in the context of consumer borrowing, see, for example, Oren Bar-Gill, *Seduction By Plastic*, 98 NW. U. L. REV. 1373 (2004); Richard M. Hynes, *Overoptimism and Overborrowing*, 2004 BYU L. REV. 127 (2004). One might ask why firms (and their executives) are not also overoptimistic in formulating these return policies. The classic response would be that the firms can easily de-bias such a tendency, relying on extensive experience, empirical data, and expert advice.

81. For an interesting discussion of the status quo bias, people's preference toward inaction, and the omission bias, see generally Ilana Ritov & Jonathan Baron, *Status-Quo and Omission Bias*, 5 J. RISK & UNCERTAINTY 49 (1992). Current research suggests mechanisms that may at times overcome this tendency. *See, e.g.*, Richard H. Thaler & Shlomo Benartzi, *Save More Tomorrow™: Using Behavioral Economics to Increase Employee Savings*, 112 J. POL. ECON. S164 (2004).

82. We further assume that it is unlikely that consumers will adopt a "correction mechanism" as a result of their past experience. For a different opinion on consumers' ability to learn from experience, see Epstein, *supra* note 17, at 811–13.

83. As well-being and happiness are vague and elusive notions, one might wonder whether it is the role of regulators to directly advance individuals' well-being and happiness, as opposed to the customary objectives of maximizing utility. We submit that there is no reason to limit legal analysis of utility to the narrow meaning of monetary gain. Moreover, as the economic analysis of open doors is closely aligned with the psychological one, we present the latter as mere corroborative evidence of our central point concerning the hidden problems of open doors.

84. Although we are not aware of empirical findings on consumers' perception regarding this point, this understanding can be inferred from Daniel Gilbert's lecture. Daniel Gilbert, Address on Happiness (Feb. 2004), *available at* http://www.ted.com/talks/dan_gilbert_asks_why_are_we_happy.html.

Yet, psychology studies show that at the end of the day, open doors prove to be something very different. Open door provisions may cause people to depreciate their choices. For example, in one study, participants were happy to select an item and be allowed to opt out and replace it with another. However, the option to opt out caused participants to devalue the item they initially chose.[85] At the same time, participants that were not allowed to change their chosen item increased their preference for that item. Phenomena such as this can lead to hesitation and doubt, which can lead to stress or dissatisfaction.

In the same study, participants who were not provided with the open door showed no regret, confusion, or doubt. Quite the contrary: the fact that this group's decision was irreversible triggered their "psychological immune system,"[86] which encourages satisfaction with one's choice. The group that had to make inescapable decisions liked their items more than the group that was able to regret its decisions.[87]

Individuals thus often tend to overestimate the psychological benefits associated with open doors. They underestimate the anxiety and anguish open doors might entail. At the same time, people are ignorant about the effect of the "psychological immune system" and its ability to enhance their satisfaction with an item they are unable to return. Therefore, individuals tend to err in evaluating the chances that they will want to use an open door.

B. The Consequences of Misperception

At the ex ante stage, individuals will misperceive the likelihood that they will make actual usage of an open doors option. They will most probably assume that the chances of exercising this option are higher than they really are. Such misperception may lead to several outcomes, which are, at times, detrimental to the weaker contracting party as well as to society at large.

The first outcome is that misperception of an open door option will lead to overpaying, which is both unfair and inefficient. The second outcome is that the misperception might lead to flaws in the weaker party's perception of *other, broader attributes* of the product or service—again, leading to an unfair and inefficient outcome. The third outcome is that the misperception generates flaws in the market's ability to regard an open door option as an accurate signaling mechanism, an outcome that systematically disfavors weaker parties. In most cases, only the latter two outcomes warrant concern.

The analysis moves to examine these outcomes, while employing several distinctions made above. First, it distinguishes the three forms of open door manifestations in law: mandatory, default, and voluntary. The analysis also distinguishes open doors of various forms and levels of salience. And, it

85. Daniel T. Gilbert & Jane E.J. Ebert, *Decision and Revisions: The Affective Forecasting of Changeable Outcomes*, 82 J. PERSONALITY & SOC. PSYCHOL. 503, 509–10 (2002).

86. *Id.* at 504.

87. *Id.* at 509.

distinguishes between misperceptions that transpire, perhaps innocently, in the market, and those that are induced or exacerbated by sophisticated, repeat players.

1. Misperception and Option Pricing

Open doors, like other options, have a price. They come at a cost to firms, and have inherent value to purchasers.[88] Where possible, firms will strive to roll such costs over to ex ante consumers (as opposed to rolling the costs ex post to those making use of the open doors).[89] The price will thus be the incremental rise in the overall price of the transaction as a result of the open door option.

The first potential negative outcome of consumers' misperception regarding the actual use of open doors is miscalculation of the value of open doors. According to this line of thinking, consumers believe that the option is worth more than it really is. They may overpay for it.

While this analysis is interesting (and calls for further economic modeling), this article will not pursue this line of thought. The inefficiencies and unfairness for unsophisticated players in this context are negligible. The "price" of the option cannot be more than a small fraction of the overall price, and any unfair increment will not be more than a small fraction of the price. It is questionable as to whether pursuing such limited inefficiencies through regulation is worthwhile, especially in markets where strong competition exists.[90]

In addition, several countering cognitive heuristics might be at play—at times possibly offsetting each other's effects.[91] For instance, countering the tendency of unsophisticated players to *overvalue* an open door option is their tendency to underestimate the likelihood of exercising that option. This is because of individuals' well-reported tendency to be over-optimistic and over-confident. Accordingly, over-optimism might lead unsophisticated players to *underprice* these options, thus countering their tendency to overvalue open doors.

The problem of miscalculation of the value of open doors pertains to all forms of open door options (mandatory, default, or voluntary). However, it is

88. For an explanation of the costs in terms of depreciation of the product, see Ben-Shahar & Posner, *supra* note 5, at 5. For a broader description of other costs and expenses, see generally Becher & Zarsky, *supra* note 21.

89. This can be done by employing restacking fees and fines. Firms usually refrain from setting fees so high that they will clearly impede the perception of the open door. Some scholars note that in specific instances, fees are appropriate. *See* Ben-Shahar & Posner, *supra* note 5, at 16.

90. Furthermore, the analysis calls for an extensive set of assumptions, which are not supported by empirical findings. For instance, we must assume that, not only is the open door option salient in the eyes of the ex post party, but the incremental rise in the overall costs of the transaction is salient as well—a questionable notion which would be very difficult to prove empirically.

91. This point is made with caution. At times, cognitive effects that *seem* to be pointing in opposite directions, thus offsetting each other, rely on very different cognitive processes. For a critical discussion of the analysis of countering heuristics, see Avishalom Tor, *The Methodology of the Behavioral Approach to Law*, 4 HAIFA L. REV. 237, 275 (2008).

hard to believe that firms will risk public backlash for such minute gains.[92] Such backlash may transpire if the public learns of these unfair pricing strategies that take advantage of consumer shortcomings. It is furthermore questionable as to whether this concern indicates actual manipulation and deliberate deception by firms.[93] But as we explain next, the implications of the misperceptions at play are far broader.

2. Open Doors and Risk Miscalculation of the Overall Transaction

The misperceptions regarding open door options make a substantial impact on parties' perception of the *entire* transaction. This leads parties to engage in transactions that are contrary to their long-term, second-order preferences.[94]

The existence of an open door affects the decision-making process of the relevant parties. Typically, transacting parties focus their attention and calculation at the time of contract formation. Here, they should consider both long- and short-term objectives. However, the existence of an open door allows a contracting party to split the decision-making process into two stages. The first takes place at the time of the transaction (T'_0). The second occurs later on, close to the point at which the open door is about to close (T'_1). This split in the decision-making process is perhaps the most crucial outcome of the open door—and leads to surprising results.

With T'_1 in view, a consumer will postpone part of her deliberation process, and thus pass through T'_0 with greater ease. How much of the overall decision-making process will the consumer allocate to T'_0? In the context of a two-week return policy, "[i]f the transaction[] costs are less than the value of the utilization of the good for two weeks, then the maximizing consumer pays for the good and takes it home."[95] While one can easily argue that the *average* consumer is not a fully rational "maximizing" decision-maker, the postponing of a substantial part of the overall decision-making process to T'_1 seems very plausible. And considering the general tendency to maintain flexibility and delay irreversible decisions,[96] such actions are indeed feasible.[97]

92. In terms of the limited sums firms can overcharge for such options.

93. As mentioned, it is easier to justify intervention in instances where the consumers' preferences might have been manipulated intentionally, as opposed to regulation countering cognitive failure (such regulation might raise the specter of paternalism). *See supra* note 78. In addition, competition probably cannot resolve this issue because firms are aware of the cognitive failures at play and they all have an incentive to exploit them. Moreover, firms might be reluctant to educate consumers because once consumers are educated, other firms will follow and switch their policies. This will render the initial educational efforts worthless. *See, e.g.*, Gilo & Porat, *supra* note 26.

94. For an explanation of these terms in this context, see *supra* note 76 and accompanying text. The second-order preference in this context might be, inter alia, aesthetics, frugality, free will, and freedom from manipulations.

95. *Id.*

96. Wood, *supra* note 68, at 158 (referring to Barbara Kahn, William L. Moore & Rashi Glazer, *Experiments in Constrained Choice*, 14 J. CONSUMER RES. 96 (1987)).

97. Once again, it is assumed that the existence of the open door option is salient, at least as regards to taking into account its existence (and not necessarily its price and terms).

At first glance, the mere splitting of the decision-making process should not be deemed problematic. However, the (usually subconscious) analysis carried out at T'_0 with regard to splitting the decision-making process is flawed. At T'_0, individuals base their analysis on the assumption of a specific level of costs that the decision at T'_1 will entail. Additionally, the analysis is premised on the presumption that their short-term, first-order preferences will remain stable and that the process as a whole will not prove unpleasant. As noted, all three assumptions are wrong, to the detriment of consumers.

When these factors are taken in account, an open door seems less like a consumer perk and more like an enticing retail trap. It lures individuals into transactions with the promise of exit. This promise is not likely to be fulfilled.[98] Consumers end up accepting contracts that do not meet their second-order preferences after wrongfully believing they will have an easy exit. These dynamics lead to outcomes detrimental not only to consumers (by hindering their autonomy), but also to the market at large. They yield inefficient outcomes that distort the market and undermine firms' incentives—and ability—to provide better products and services.

To briefly summarize, open doors are problematic because they shift decisions to T'_1. Decisions at T'_1 are not necessarily aligned with long-term, second-order preferences because they are affected by cognitive biases, which lead to irrational decisions. The lack of such cognitive failings at T'_0 is the reason why we prefer decisions to be made at that juncture. Of course, at T'_0, there are problems as well (such as insufficient information and unclear risks). But, assuming that providing an open door is a consumer panacea is simply wrong.

The problems associated with the open door dynamic can occur inadvertently. But, they can also result from a carefully structured manipulative scheme. Sophisticated players can strive to enhance the salience of specific elements, such as the existence of an open door option, thus encouraging the opposing party to split their decision-making process.[99] This can be done through advertising that clearly emphasizes the benefits of open doors while leaving out the low rate of their use, as well as by utilizing the hidden effects of endowment and procrastination.

It is, of course, difficult to establish whether firms deliberately engage in such manipulative practices. However, when an opportunity to manipulate arises, and incentives to do so exist, there is a very high chance that manipulation will indeed occur.[100] When consumers' miscalculations result from such manipulation, the case for intervention and regulation is easier to make.[101]

98. ARIELY, *supra* note 73, at 137.

99. *See* sources cited *supra* note 62.

100. Hanson & Kyser, *supra* note 73, at 743 ("Manufacturers will respond to market incentives by manipulating consumer perceptions in whatever manner maximizes profits.").

101. Once again, the vigilant reader might wonder whether the cognitive failures relied on here do not cancel out or mitigate each other. On one hand, individuals do not grasp the need for exercising the open door option (which might lead to underestimating such an occurrence and the value of this

Keeping the specter of manipulation in mind is of great importance when structuring the relationship between open doors and the law.[102]

Finally, it deserves emphasis that consumers differ in their attitude towards risk. Likewise, the behavioral and cognitive failing (or "trap"—depending on the seller's intent) does not pertain equally to all consumers. Some savvy consumers will learn to adapt to new market strategies. Others will learn about the seductive pull of open door mechanisms from peers and contacts. Some will do even better, by benefiting from the additional time to contemplate transactions. Yet other consumers will use open doors to "borrow" products at no fee.

The existence of these different groups, however, does not undermine the argument set out here. Some individuals might be immune to the lure of open doors. Yet for less sophisticated consumers, lenient open door options are powerful tools that convince them to engage in transactions that may not suit their long-term, second-order preferences, and are inefficient overall.

Furthermore, the phenomenon of consumers "escaping" the problems of open doors probably exacerbates those problems. Abuse and misuse of open door options generate additional costs to firms. Firms providing open doors will strive to roll these costs over to less sophisticated consumers, thus generating a problematic cross-subsidy among these groups.[103] These issues increase the need to examine the legal protection of less sophisticated segments of consumers.

3. Open Doors as an Inaccurate Signaling Mechanism

Another way to understand open door options is as "signaling mechanisms." An open door assures buyers that the firm is willing to rescind the contract and incur associated costs.[104] By doing so, the firm signals that it is confident that buyers will rarely experience dissatisfaction and exercise their open door option.[105] Slightly restated, vendors can express their confidence that their product will basically meet buyers' expectations by offering open doors.

Signaling can play out in several ways. First and foremost, it can occur by the mere offering of open door provisions (as opposed to not offering any). It

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contractual right). On the other hand, they overestimate its value. We do not find these elements aligned so we do not believe that they cancel each other out. True, the benefits of open doors might be discounted at T_0. Yet, the benefits that are recognized lead to the splitting of the decision-making process, and pushing part of it into the future—where cognitive fallacies come alive. Additional research is still required to resolve this point.

102. Hopefully, future work will establish whether applying mandatory or default open doors can impact the problem of deliberate manipulation.

103. *Cf.* Gregory Mitchell, *Libertarian Paternalism Is an Oxymoron*, 99 NW. U. L. REV. 1245 (2005) (opining that the solutions and suggestions associated with libertarian paternalism will often improve the welfare of irrational persons at the expense of the rational ones).

104. As explained above, in many cases, at least some of the costs are rolled over to the other party. Yet it is not necessarily known or salient to the average consumer at the time of contract formation. In addition, in competitive markets, a consumer's intuition that at least some of the costs will be borne by the seller is mostly correct.

105. Wood, *supra* note 68, at 159.

could be manifest in the features of open doors: the extended time period for rescinding the original contract, the limited transaction costs associated with rescinding the contract ("Hassle Free!"), et cetera. This form of signaling is added to the great variety of other signals coming from parties in the marketplace, such as price, brand, and reputation.

Accepting an open door as a signaling mechanism calls for several assumptions discussed above regarding its salience. First, we must assume that consumers understand that exercising an open door mechanism entails costs, so firms adopting such provisions signal quality. For such signaling to occur, the ex ante weaker party (usually the consumer) must take into account the existence of the open door option at the time of transacting. For other—more detailed—elements of this signal (period, cost, et cetera), we must assume that the parties account for, recall, and even compare various facets of the available open door options in the market. This latter assumption is quite weak; therefore, assuming this form of fine signaling is incorrect.

In view of the previous analysis, it becomes clear that the signaling mechanism at play is flawed. The analysis shows that firms' exposure to expenses related to an open door is substantially *less* than the typical consumer might assume.[106] In fact, the signal a firm sends out by employing an open door is not backed by the firm's or the product's actual performance. Thus, the consumer will engage in the transaction or overpay for the product because of an inaccurate signal. What makes this issue exceptional and complicated is that the firm's presentation is factually true. That is, the firm is indeed willing to replace the product or rescind the transaction at the consumer's will. Yet firms might still mislead, given consumers' lack of understanding *of their own behavior*.

As in other areas of the law, a possible response to consumers' misunderstanding as to the true meaning of signals is information disclosure. Accordingly, legislatures might require sellers to disclose information regarding the extent of actual returns. By making such information available, consumers will learn that the open door is hardly a signal for quality.

However, such disclosures can backfire. Providing consumers with information about the limited number of returns might exacerbate the signaling distortion. Consumers might wrongfully interpret the low rate of returns as a signal of satisfaction, whereas the complete picture is much more complicated. Thus, this problem calls for a more nuanced response.

While open doors clearly function as signals when they are voluntary (and especially when rendered salient by advertising), it is a more complicated issue with regard to mandatory and default open doors. Seemingly, the enactment of

106. This is aside from the fact that costs are, in part, borne by the buyers from the very beginning.

mandatory open doors neutralizes all signaling. In a mandatory regime, an open door is not the result of a firm's goodwill but of a governmental mandate.[107]

One might argue that even in this setting, firms can signal their use of open doors by providing terms that go beyond the regulatory mandate. But this would be a costly venture. It would also probably be unnoticed by the average consumer, for whom such contractual elements are non-salient. Thus, a mandatory open door policy is a partial solution to the signaling problems. However, it comes at the high price of market inefficiency and harm to autonomy.[108]

Default open door mechanisms set by law raise additional questions, which call for further examination. For instance, one interesting question is whether consumers would view adhering to a default government standard as a sign of a firm's goodwill.[109] At first glance, it seems that setting defaults (if these are well-known to the public) will indeed weaken the signaling force of lenient open doors adopted by firms. This is an additional element that policy-makers ought to consider.

V

CONCLUSION: THE PATH TO NEW PERSPECTIVES ON OPEN DOORS

Open doors have positive attributes. Their existence is rooted in the American culture. Consumers appreciate open doors, and are willing to pay a premium for them. At the same time, firms are willing to provide open doors. Modern commerce proves that open doors are sometimes a necessary tool to enhance market activity and guarantee a minimal standard of fairness.

Yet, open doors lead to intricate consequences. Some of which are detrimental and manipulative to the weaker party, who is typically not aware of the open door's inner workings. Legislatures cannot assume that open doors are a simple "one-size-fits-all" solution to thorny problems. Consumers are heterogeneous. They differ in their decision-making processes, risk preferences, and degrees of rationality. Therefore, the legal response to open doors presents an intriguing analytical question, which is made more acute by the very different approaches taken on either side of the Atlantic.

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107. One might indeed argue that the analysis assumes that the public is aware of the mandatory element in the open door policy. Whether this is true or not is for empirical testing to decide. However, this issue could be resolved by increasing education on existing and future mandatory open doors to limit this problem. It could also be resolved by forbidding vendors to present open doors as voluntary when they are mandatory.

108. *See generally* Becher and Zarsky, *supra* note 21; Ben-Shahar & Posner, *supra* note 5. This is clearly an issue that requires additional research. Additionally, a mandatory regime will prevent consumers from learning from experience and mistakes.

109. *Cf.* Borges & Irlenbusch, *supra* note 16, at 99 (hypothesizing that "a statutory entitlement might weaken the adoption of fairness considerations in the decision-making process," and that "a shift from a voluntarily granted withdrawal right to a statutory one indeed seems to . . . encourage[] [consumers] to seek their own benefit [and exercise their withdrawal right]").

As U.S. vendors continue to voluntarily offer extremely lenient return polices, EU (and elsewhere) regulators are pushing to expand mandatory return polices in many markets.[110] One way or another, regulators are missing crucial elements that are an inevitable part of the open door dynamic. Some of these behavioral, cognitive, and economic elements have been addressed in this article.

Society is constantly striving to achieve a balance. It aims to maintain fair markets and consumer autonomy on one hand, yet allows marketers to innovate and exercise their autonomy on the other. Whereas many forms of marketing that take advantage of cognitive failings are considered "fair play,"[111] it looks as if the current balance is inappropriate and flawed.

Society should deal with the complexities facing consumers one at a time. In every context, we ought to establish which forms of conduct are acceptable—that is, do not generate extensive market failures or impose impediments on individual autonomy—and which forms go too far. This article made the first step, unraveling the hidden sides of open door provisions.

Further policy recommendations in the context of open doors require additional studies, some of which were outlined throughout this article. One prominent example is the question of whether open doors are salient. It is important to examine which elements of open doors consumers account for, and which they ignore. Another important issue is the endowment effect, which plays a crucial role in our analysis. While economists and psychologists are extremely interested in this effect, our analysis calls for refined experiments that will take into account various products and elements of open door provisions. In addition, studies must address inertia and procrastination trends, and differentiate between various markets and products, as well as groups of consumers. Regulators will face difficult decisions as to which groups should receive preferential treatment at every juncture.

When mapping out this market-specific response to open doors, two additional challenges are worth mentioning. First is the challenge of identifying and dealing with markets where the existence of open doors is especially beneficial, given the risks and the information gaps that consumers face.[112] Second is the need to take into account the costs that open door options generate to both firms and consumers. Such costs include depreciation,[113] but

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110. *See supra* notes 35–36; Becher & Zarsky, *supra* note 21 (noting mandatory cooling-off period in consumer transactions in Israel); SPANOGLE ET AL., *supra* note 27, at 253 (noting that "cooling-off periods have been widely adopted in Europe for a wide variety of consumer transactions").

111. Indeed, consumer markets are filled with aggressive, suggestive, and manipulative marketing techniques. Merely having a handsome model promote a product constitutes a manipulation. "Two for the price of one!" is another marketing scheme that abuses cognitive failings. In these (and other) cases, consumers are left to their own devices, and must learn on their own (at times with the help of peers, elders, or market forces) how to interpret the surfeit of information that markets provide.

112. For a discussion of such specific markets, see generally Becher & Zarsky, *supra* note 21; Ben-Shahar & Posner, *supra* note 5. One example is the market for home electronic appliances.

113. Depreciation is the dominant element considered by Ben-Shahar & Posner, *supra* note 5.

also operational costs, missed transactions because of return-policy abuse, as well as plain theft.[114] These varied costs will sometimes point regulators in opposite directions.

Finally, academics and regulators should explore novel solutions that could allow some consumers to enjoy the benefits of open doors while protecting others from their enticements.[115] This article is merely a modest step. The seemingly simple story of open doors opens many interesting doors to intriguing questions of human behavior, markets, policy, and law.

114. Open doors enable some forms of theft. *See generally* Becher & Zarsky, *supra* note 21.
115. *Cf.* Camerer et al., *supra* note 27.