Consumer Protection Economics at the FTC
Prepared Remarks for Chief Economist Roundtable

By

Michael A. Salinger
Director, Bureau of Economics
Federal Trade Commission

International Industrial Organization Conference
Boston, Massachusetts
April 8, 2006

Thanks to Daniel Kaufman, Pauline Ippolito, Paul Pautler, and Lee Peeler for helpful suggestions and comments.

Good afternoon. I want to thank Larry[1] for putting together this session. I have always admired him for his ability to move between the policy and academic world. Of course, that admiration, like everything I say today, is just my opinion. The opinions I express today, including but not limited to those about Larry, do not necessarily represent the positions of the Federal Trade Commission or any of the individual Commissioners.

A few years ago, I was at an NBER conference where one of the papers concerned why auto insurance is not priced by the mile. I forget who the author was, but I found the paper interesting at the time. Currently at the Federal Trade Commission, we are interested in how automobile insurance is priced, but we are focusing on a different question from the one covered at the academic conference. Rather than analyzing why the price does not depend on something that an academic imagines *in theory* could matter, we are studying why the price of auto insurance *in fact* depends on something that might surprise you – credit scores. Congress has charged us with understanding why insurance companies use credit scores to set insurance rates. The companies tell us that, even controlling for experience ratings, credit scores predict claims. The concern, though, is that they are a proxy for race. To satisfy the Congressional mandate, we have a data set from several major auto insurers that gives policy characteristics and claim losses for a large sample of drivers. We will also be able to match this information with demographic information. From this, we expect to be able to ascertain whether credit scores are useful in predicting claims and/or whether they proxy for race.

From my perspective as Bureau Director, it is clear that sound economic research can be highly influential; but the research that ends up being influential and the research valued in academia are not necessarily the same. As I have recently written in an article with Alden Abbott from the Bureau of Competition, I believe this point applies to antitrust research.[2] For those of you who are interested, I brought copies of that article along. Today, though, I thought I would focus my prepared remarks on the other main mission of the Federal Trade Commission, consumer protection.

Larry has asked us to keep our preliminary comments brief, so let me discuss just one other current consumer protection issue we confront. Shortly after I arrived at the Commission, the FTC held a joint workshop with HHS on the growing problem of childhood obesity. There are several possible reasons for this problem.[3] One factor that is consistently raised with the FTC is

---

[1] Lawrence J. White, currently Arthur E. Imperatore Professor of Entrepreneurial Studies and Professor of Economics at New York University Stern School of Business and former member of the Federal Home Loan Bank Board and chief economist in the Antitrust Division of the U.S. Department of Justice.

[2] Alden F. Abbott and Michael A. Salinger, "Learning from the Past: The Lessons of Vietnam, IBM, and Tying," *Competition Policy International*, Vol. 2, No. 1, Spring 2006.

[3] Many of these factors have been examined by Cutler, Philipson, and others. David M. Cutler, Edward L. Glaeser, and Jesse M. Shapiro, "Why Have Americans Become More Obese?" 17(3) *J. of Econ. Perspectives*, 2003, 93-118; Tomas J. Philipson and Richard A. Posner, "The Long Run Growth in Obesity as a Function of Technological Change," NBER Working Paper

the possibility that childhood obesity is caused by food advertising, particularly on TV. Based on research that BE's Pauline Ippolito and Debra Holt are currently doing, it appears that blaming TV-based food advertising for obesity is misplaced. First of all, compared to the late 1970's when kids were thinner, kids are not watching more television. Nielsen reported that in 1976 children watched approximately 4 hours of television per day. Estimates of current viewing vary, but consistently find lower viewing times. For instance, the Kaiser Family Foundation estimated that in 1999 children watched less than 3 hours of television per day. When you think about it, this should not be a surprise. When I was a kid, we did not have video games, instant messaging, computer games, DVDs, video movies, and the like. Kids may be sitting in front of screens more than they used to, but it is not in front of advertising-supported television shows; and they are not watching more food ads.

Without discussing in detail the other issues we are working on, I will make three observations about our consumer protection work.

First, what makes the work interesting is that it can really matter. In academia, we get excited when our papers show up having many citations in the *Social Science Citation Index*. At the FTC, we get excited when the Supreme Court cites our work in its decisions, as it did recently when it overturned a state law limiting the interstate shipment of wine.[4] We have also had a significant influence on food advertising policy. Obesity is the current pressing issue in food advertising, but the effect of rules about food advertising has long been a subject of study in the Bureau of Economics. Earlier work by Pauline Ippolito on health information in food ads has been used as a guide to the regulation of health claims.[5] Another possible indicator of influence is whether we have made someone angry enough to silence us. My predecessor Luke Froeb used to quip that one of his objectives as Bureau Director was to get the FTC banned from an industry. In 1979, Mike Lynch, a BE staff economist who went on to become Bureau Director, showed that whole life insurance was a bad buy for consumers.[6] The insurance industry was not

---

7423, 1999.

4 *Granholm v Heald*, 125 S. Ct. 1885, 1907 (2005). Alan E. Wiseman and Jerry Ellig, "Market and Nonmarket Barriers to Internet Wine Sales: the Case of Virginia," *Business & Politics*, Vol. 6(2), Art 4, (2004) and *Possible Anticompetitive Barriers to E-Commerce: Wine*, FTC Staff Report (2003) at http://www.ftc.gov/os/2003/07/winereport2.pdf.

5 Pauline M. Ippolito and Alan D. Mathios, *Health Claims in Advertising and Labeling: A Study of the Cereal Market*, Bureau of Economics Staff Report, Federal Trade Commission, Washington, D.C., August 1989, and "Information, Advertising and Health Choices: A Study of the Cereal Market," *RAND Journal of Economics*, 21 Autumn 1990, 459-80. Also see, Pauline M. Ippolito and Janis K. Pappalardo, *Advertising, Nutrition, & Health: Evidence from Food Advertising 1977-1997*, FTC, Washington D.C, September 2002.

6 Michael Lynch, et al. *Life Insurance Cost Disclosure*, Federal Trade Commission, (July 1979); and FTC History: Bureau of Economics Contributions to Law Enforcement, Research,

amused. It successfully lobbied Congress to bar the FTC from studying insurance without a specific Congressional mandate like the one for the study I just mentioned.

Second, more often than not, the work that turns out to be influential is not all that sophisticated technically. When you know what the interesting issues are and you can get good data, a simple comparison of means can do the trick.

Third, even though the work does not require a great deal of technical sophistication, the consumer protection work is still conceptually fascinating. The Federal Trade Commission Act bans "unfair or deceptive acts or practices." These terms are very broad. You simply cannot do sophisticated analysis of firms' marketing practices without moving beyond the world of completely rational behavior, perfect information, and zero contracting costs. The challenge is how to relax the standard economic assumptions while maintaining a core set of underlying principles.[7] You can try to do that sitting in your office, but I for one find the real issues confronting us to be helpful in shaping my thinking. A magazine offers you four free issues "free of obligation," but they require your credit card number and charge you for a paid subscription after the four issues are up unless you tell them you are not interested. Is that either deceptive or unfair? You download a piece of "free" software, but you get pop-up ads as a consequence. Is that deceptive or unfair? How is it different from advertising on "free" television? A company offers a mail-in rebate precisely because it knows that some people will respond to the post-rebate price but fail to get the rebate. Is there a point where the hurdles needed to collect the rebate make the practice deceptive or unfair?[8] These are not easy issues, but we have to make real decisions that depend on judgments about how to resolve them.

We need more smart people to work with us on these issues. These can be students whom you get interested in consumer protection matters. It can be you. We have many former professors in the Bureau. We have professors who visit for a year. I did that twenty years ago, and it was ultimately one of the most important and best-spent years of my career. For an applied microeconomist looking to do work that is both intellectually stimulating and influential, I don't think you can beat us. And remember, you heard that from someone who works at the agency that enforces laws against deceptive claims.

---

and Economic Knowledge and Policy - Roundtable with the Former Directors of the Bureau of Economics, September 2004, Transcript 191-192, 194 (available at http://www.ftc.gov/be/workshops/directorsconference/index.htm)

[7] Homo Economicus, Homo Myopicus, and the Law and Economics of Consumer Choice, *Univ. of Chic. Law Review Symposium*, 73(1), 2006.