

Keep The Change?:

A behavioural approach to class action antipathy where losses are trivial

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Abstract: Certain wrongs impose such small losses that rational victims will not pursue redress. In modern mass-markets, one defendant can wrongfully reap large profits by diffusing such losses across a large class of victims. Opt-out class-action procedures can aggregate losses to make litigation viable and confront the defendant with the total cost of its wrong. Class actions, however, particularly where individual losses are trivial, have attracted criticism from the public and judiciary alike. This paper draws on insights from cognitive psychology and behavioural economics to understand how attitudes toward class actions are shaped by the ways in which their goals and outcomes are presented. Where losses are trivial, individual compensation will never be substantial, thus it is important to understand how emphases on individual losses, defendants' gains, and the compensation of class counsel, influence individuals' evaluative beliefs about such proceedings. Attitude formation in the absence of decisionmaking is an under-researched area in the behavioural analysis of law; however, attention to attitudes may assist in designing procedures that achieve their goals and are regarded as valuable, or in abandoning procedures that undermine confidence in legal institutions.

JEL classification: D18; D91; K41; K42.

Keywords: Attitudes; Class actions; Consumer protection; Deterrence; Litigation process; Role and effects of psychological, emotional, and cognitive factors on attitudes.

I hereby declare and confirm that this thesis is entirely the result of my own work except where otherwise indicated. I acknowledge the supervision and guidance I have received from Professor Avishalom Tor. This thesis is not used as part of any other examination and has not yet been published.

Jonathan Schachter,
15 August 2018.

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“It is better, so the image runs, to take one dime from each of ten million people at the point of a corporation than \$100,000 from each of ten banks at the point of a gun. It is also safer.”

C. Wright Mills (1956:95)

I. INTRODUCTION

Modern firms have immense power to affect many individuals at once. In this context, diffuse wrongs spread across a large class of consumers present a challenge for deterrence because the losses suffered by each consumer are too small for rational individuals to litigate.

In North America, class actions offered hope that defendants would no longer profit from such mass defaults. A procedure to aggregate claims would overcome the rational apathy of individual victims and facilitate compensation; and by including all victims in the proceeding automatically, it could confront the defendant with the full cost of its wrong.

People may agree that diffuse wrongs are undesirable, but class actions attract hostility from class members, judges, and policymakers alike. Meaningful compensation is impossible where individual losses are trivial. If the true value of these proceedings lies in deterring marketplace misconduct, pervasive negative attitudes may thwart their potential.

This paper draws on behavioural research to explore how attitudes toward small-claims class actions are shaped by conceptions of, and relative emphases on, the procedure’s goals and outcomes. Focus on the compensatory power of these actions for individual class members, or on class counsel’s remuneration, distracts from their power to disgorge wrongful gains and deter future wrongdoings. It may be that there is no appetite for disgorgement or deterrence, in which case the inquiry can stop; however, if deterrence is regarded as a laudable objective in cases where marketplace wrongs contribute to market failures, then it is incumbent upon policymakers to design a procedure in which consumers, judges, and policymakers have confidence.

Section II of this paper outlines the problem, canvassing sources of consumer vulnerability and the potential mechanisms for redress. It draws on behavioural insights to understand these phenomena, and describes why renewed, interdisciplinary attention to attitudes is desirable in the legal context. Section III provides an analysis of attitudes toward the goals of small-claims class actions in general, and the various ways in which framing of these actions—in terms of their goals, and the interacting effect of litigation costs—may affect how they are evaluated. Section IV

discusses the limitations of this study, and potential future directions and practical implications of this research. Section V concludes.

Cognitive research has enriched our understanding of economics and law in many ways. If individual attitudes toward consumer class actions are a function, at least in part, of how they are portrayed, then care should be taken to portray them in a manner that furthers their aims. If the way we portray such proceedings hobbles their efficacy, limits their enforcement or deterrent potential, or reduces faith in lawyers or the civil litigation system, then it behooves legal scholars to develop a better understanding of how attitudes are formed, and to what effect.

II. OVERVIEW OF THE PROBLEM

This research focuses on North American, opt-out class actions as a mechanism to redress diffuse wrongs. The consumer context is particularly apt because the dynamics that make consumers vulnerable prior to entering into marketplace transactions persist after they are wronged, and throughout their efforts (if any) to achieve redress. This section outlines the nature of and reasons for consumer vulnerability, before describing the role of class actions, the pervasive antipathy toward them where losses are small, and the potential for behavioural analysis of law to help us understand these attitudes.

(a) Consumer vulnerability and market failure

Neoclassical economic theory predicts that sellers will respond to consumer demand, while consumers, through the act of purchasing and consuming, will provide sellers with information that sellers can use to maximize profit. The implication is that “all power lies with the consumer” (Galbraith 2007:263). This power should enhance market efficiency, but it relies on several heroic assumptions, chiefly that individuals are informed, rational, and act in their self-interest to maximize utility (Lane 1983; Galbraith 2007). Where these assumptions are not met, inefficiencies and market failures can result.

This model depends on the rationality of consumers, *i.e.*, their willingness and ability to acquire and process the information required to identify utility-maximizing transactions. In reality, consumers are boundedly rational. Searching, processing information, deliberating, and bargaining are costly. Even if consumers could devote their full attention to identifying utility-maximizing transactions, there are cognitive limitations on their ability to process complex information (Simon 1955; Conlisk 1996). Cognitive limitations make it difficult for consumers to compare information across multiple dimensions; to assess probabilities without mis-estimating risks or miscalculating the value of future losses and gains; to ignore irrelevant information; to avoid the influence of emotion; and to overcome systematic reasoning errors resulting from the heuristics and biases at

play in the decisionmaking process, among other things (Tversky & Kahneman 1974; Conlisk 1996; Korobkin & Ulen 2000; Howells 2005; Willis 2015).

Firms, on the other hand, are designed to maximize profits and can devote considerable resources toward discovering and processing profit-maximizing information (Howells 2005; Henry 2010). Thus, even when information is available to consumers, it may be too copious or complicated; or sellers may present the information in a way that confuses consumers, or otherwise exploits the bounds of their rationality (Hadfield *et al.* 1998; Howells 2005; Gabaix & Laibson 2006; Ben-Shahar & Schneider 2011; Willis 2015).

Importantly, one firm may deal with thousands or millions of consumers. This asymmetry of numbers permits unscrupulous firms to profit from diffuse wrongs, which researchers have termed “democratized theft” (Issacharoff & Samuel 2009) or “mass defaults” (Trakman 1994):

“mass defaulter[s] deliberately, recklessly, or ignorantly...repeatedly subject consumers to mass breach of contract,...violations of product warranties, and excessive finance charges. Recognizing their victim’s failure or reluctance to sue, mass defaulters sometimes breach with impunity. They compensate only aggressive customers and ignore or intimidate the remainder into submission. Often ignorant about the persistent nature of mass default, most consumers fail to protest their ill-treatment. Thus, defaulters not only benefit from the breach, but the inability of consumer to launch a legal challenge fails to deter future breaches” (1994:617 & 620).

Without a mechanism to assist consumers in litigating such wrongs, existing laws may not deter mass defaults.

Aside from raising distributive-justice and equity concerns, consumer vulnerability justifies intervention to address market failures. Competition requires informed consumers to apply pressure to poorly performing sellers and reward superior ones (Howells 2005). Persistent abuses constitute a social loss, *i.e.*, market deterioration; and, to the extent that a mass defaulter secures an unfair advantage in the market, erects barriers to entry, or distorts market signals, for example, this hampers competition and inhibits efficiency (Lane 1983; Ramsay 1985; Trakman 1994).

Moreover, if private litigation generates rules that influence the future conduct of actors beyond the parties to the litigation (Scott 1975; Posner 2014), this is a public good that class actions may generate as an externality, and one that may go undersupplied with respect to mass defaults without a mechanism to address small losses (Rubenstein 2005).

(b) Enforcement and redress

The twentieth century witnessed dramatically increased awareness of consumer issues, and the development of new regulations and regulatory bodies to protect consumers from “hazardous products, monopolistic practices, endlessly clever frauds, overpricing, and swindles” (Nader

1973:viii), among other abuses. But these regulations require enforcement, whether public or private, to be effective. More recently, it appears that public concern for consumer protection has declined, as has public commitment to the enforcement of consumer rights, often leaving consumers to vindicate their rights themselves (Van den Bergh & Visscher 2008; Ziegel 2009).

The traditional law-and-economics model of deterrence focuses on the wrongdoer's utility calculus: deterrence requires the expected costs of crime—a function of the magnitude of penalty, and the probability of detection and enforcement—to exceed its benefits. The idea is to reduce the attractiveness of wrongdoing by increasing the penalties, the likelihood that they will be applied, or both. Larger penalties can offset underenforcement by increasing the expected cost of wrongdoing (Becker 1968; Becker & Stigler 1974). The basic model, however, is agnostic as to the mechanisms of enforcement.

Legal rights may be enforced publicly, as is typical for criminal and tax offences, or privately, as in tort, contract, and property disputes. Public agencies have informational advantages that make them better suited to prosecute violations “when effort is required to identify and apprehend violators” (Polinsky & Shavell 2000:46), and they may develop information systems that are unlikely to emerge in the market, in the absence of private incentives to develop such systems or collective action problems that inhibit their creation (Polinsky & Shavell 2000). Public agencies can also prosecute violations that private parties have no incentive to prosecute. Public agencies, however, may lack the resources, information, or jurisdiction to provide the optimal level deterrence (Issacharoff 1999). Indeed, “consumer protection agencies must select for action only the most blatant forms of fraud and only those operating on a large enough scale to justify the expenditure of agency time” (Tydings 1970:481).

Private enforcement “was traditionally regarded as the counterpart to the market system of economic exchange” (Ramsay 1985:356). It relies on individuals' interests to incentivize them to detect and litigate wrongs, at the individuals' expense.

The boundary between public and private enforcement is often blurred: public agents may delegate enforcement duties to the private sphere, as with statutory schemes that endow individuals with private rights of action; and many areas of law, such as competition, rely on a mixture of approaches (Becker & Stigler 1974; Landes & Posner 1975; Polinsky & Shavell 2000; Budnitz 2008).

From discovering infringements, to the time, hassle, and uncertainty of litigation, private enforcement is costly for individuals. Thus, it “may fail either to deter socially wasteful activity or to compensate for violations of rights” (Ramsay 1985:356). This risk is particularly acute with mass defaults, where individuals' litigation costs exceed the expected benefits of litigation.

Further, mass defaulters benefit from the asymmetry of diffuse wrongs in that they do not face the coordination problem faced by individual consumers, and, given the enormous stakes that the litigation may involve, they have the incentive to muster comparatively large resources in response to potential claims (Issacharoff 1999). One expects that in cases of mass default, individual rational apathy will, on the aggregate, lead to underenforcement and underdeterrence in the absence of other enforcement mechanisms or stiffer penalties.

Aggregation procedures like class actions can “extend victim enforcement to include many situations where the damage is so widely diffused that no one victim alone has much incentive to enforcement” (Becker & Stigler 1974:13). They attenuate the rational-apaty and coordination problems, and enable plaintiffs to “exploit the same economies of scale as the defendant when investing in the case” (Hay & Rosenberg 2000:1380). Further, they limit the ability of individuals to free-ride on the efforts of others, a temptation that arises from the “marked disparity between concentrated risks and diffuse benefits” (Issacharoff & Miller 2009:203).

The 1966 extension of the US class-action procedure (and the adoption of similar procedures in Canada, in the 1990s), which facilitated larger, *opt-out* litigation, gave rise to North American class actions as we know them (Ford 1969; Hensler *et al.* 2000; Dodson 2016). Opt-out procedures include all victims of a wrong as a default. This ensures greater participation because, for reasons of inertia and status quo bias developed in the behavioural literature (Camerer *et al.* 2003; Gal 2006; Thaler & Sunstein 2009), we expect most individuals not to change from the default, even when opting out is easy. Opt-out proceedings are therefore more likely than opt-in proceedings to confront the wrongdoer with the full costs of the wrong (Issacharoff & Samuel 2009; Mulheron 2009; Van den Bergh 2013).

These considerations have led some to conclude that North American-style class proceedings are an important complement in the optimal enforcement mix for mass wrongs, especially where individual losses are small (Issacharoff 1999; Van den Bergh 2013; Pridgen 2018). As Gilles notes,

“small-claims consumer cases are a—if not *the*—primary reason why class actions exist, and that without class actions many—if not most—of the wrongs perpetrated upon small-claims consumers would not be capable of redress” (2010:307, emphasis in original).

This paper takes no normative position on the optimal mix of enforcement mechanisms, but assumes that, for North American consumers, this mixture includes opt-out class actions. This assumption, which is of course open to challenge, assists in assessing how class actions function and are perceived, where individual losses are small.

(c) **Class-action antipathy**

Opt-out class actions have attracted criticism on many fronts, both in North America and abroad. Observers point to fundamental ethical concerns—including the ability of class actions to bind consumers to a litigation outcome without their knowledge or instruction; and the conflicts of interest or agency costs that may arise between class members and their lawyers—as well as practical concerns—such as disadvantageous settlements; minimal compensation for individual class members; and the incentives they create for entrepreneurial lawyers to launch frivolous suits, among other criticisms (see, *e.g.*: Dam 1975; Rhode 1982; Macey & Miller 1991; Hill 1995; Hensler *et al.* 2000; Finn 2007; Beisner *et al.* 2008; Perell 2009).

A vast body of literature has emerged to assess the merits of these criticisms and identify potential statutory or judicial solutions. But a fundamental criticism remains: while class actions are regarded in the US and in Canada as promoting three goals—compensation or access to justice; deterrence or behaviour modification; and administrative efficiency or judicial economy (Dam 1975; Good 2009)—these objectives may conflict. Crucially, small-claims class actions are ill-equipped to provide meaningful compensation: “The plaintiffs’ potential recoveries in a small claimant case are, by definition, minimal. Even if the case succeeds, the plaintiff and class members will receive a minute sum” (Hill 1995:148).

Indeed, the US and Canadian supreme courts have both affirmed that a primary goal of class proceedings is to enable the litigation of individually non-viable claims by lowering the average cost of litigation for each class member (*Amchem Products, Inc v Windsor*, 521 US 591 at 617 (1997); *Hollick v Toronto*, 2001 SCC 68 at ¶15). Compensation is the primary goal; the potential for deterrence or punishment is a happy corollary (Dam 1975; Gilles 2010). According to the traditional economic view of deterrence, however, to the extent that class actions can enhance deterrence, they do so by forcing wrongdoers to internalize the costs of their wrongs. As Scott notes, “[t]he fact that the cost imposed on the defendant takes the form of a payment to the plaintiff is significant only in that it affords the needed incentive for the plaintiff to bring the action” (1975:939).

The tension in objectives is apparent in reform efforts, judicial scepticism, and criticism from outside observers (Susman 2003; Finn 2007; Gilles 2010; Klonoff 2013; DRI 2014). In 1996, for example, an advisory committee recommended an amendment to the US federal class-action procedure that would require due consideration of “whether the probable relief to individual class members justifies the costs and burdens of class litigation”. The explicit goal of this amendment was to prevent the use of class actions as a means of “aggregate[ing] trivial individual claims” (Mulheron 2004:141). (The proposal was never legislatively enacted.)

There are two dominant criticisms of small-claims class actions as a vehicle for compensation. Firstly, given the costs of such proceedings, they cannot provide full compensation. Indeed, where losses are sufficiently small, administrative costs may preclude any individual compensation. Secondly, where losses are real but trivial, it may be difficult to ascertain which consumers have suffered actual harm and how much. Aggregation may lead to undercompensation of actual victims while proving a windfall to uninjured consumers inadvertently included in the class. Neither concern matters if the objective is deterrence, but both concerns underlie efforts to abandon the procedure, in the case of small claims (Gilles 2010).

Beyond antipathy toward the procedure, plaintiff-side class counsel attract considerable hostility (Hay & Rosenberg 2000; Gilles 2010), particularly in small-claims class actions where counsel's fees inevitably dwarf any payment to individuals (Hill 1995). From an economics perspective, contingency fees shift the risks of litigation from plaintiffs to counsel, and—where private enforcement is deemed to be an important part of the enforcement mix—sufficiently large contingency fees incentivize entrepreneurial lawyers to undertake the costs of discovering wrongs and litigating complex claims that individual plaintiffs or public agencies will not (Lynk 1990; Rickman 1994; Hay & Rosenberg 2000; Van den Bergh 2013). Class actions (and contingency fees) might be unnecessary for consumer redress if public agencies had the resources and will to provide optimal enforcement. But if meaningful class compensation is impossible, and deterrence remains an objective, it does not strictly matter how the defendant's disgorged gains are distributed.

The foregoing criticisms of class actions have been explored at considerable length in American scholarship, and underlie vehement opposition to opt-out class actions outside North America:

“one need spend only a few minutes in conversations with European reformers before the proverbial ‘but’ enters the discourse: ‘But, of course, we shall not have American-style class actions.’ At this point, all participants nod sagely, confident that collective actions, representative actions, group actions, and a host of other aggregative arrangements can bring all the benefits of fair and efficient resolution to disputes without the dreaded world of American entrepreneurial lawyering” (Issacharoff & Miller 2009:180).

European proposals for collective-redress mechanisms demonstrate a preoccupation with avoiding “US-style”, “abusive litigation” (European Commission 2013a). A backgrounder from the Commission explains that “the European approach to collective redress clearly rejects the US style system of ‘class actions’” (European Commission 2013b). European scepticism of class actions is rooted in a perception that the procedure benefits class counsel more than it benefits consumers. In a fact sheet about the Commission's “New Deal for Consumers”, which seeks to strengthen enforcement of consumer laws, one heading asks: “Will there be a risk of US style class

actions?” The document assures that, “Thanks to numerous safeguards, the EU representative actions will be different from the US style class action. We want a system that cannot be misused and that bring[s] more fairness to consumers, not more business for law firms” (European Commission 2018).

If compensation is regarded as the sole objective of class actions, and small-claims class actions inevitably fail to achieve it, then such class actions should be abandoned. But if deterrence is regarded as a goal, then some mechanism is required to confront mass defaulters with the costs of their wrongs. Where trivial individual losses amount to sizeable wrongful gains, it is difficult to imagine a mechanism that provides meaningful compensation, adequate deterrence, minimal public enforcement costs, and no additional business for lawyers.

(d) Attitudes and interdisciplinary legal analysis

Economic analysis has substantially enhanced our understanding of legal phenomena. This interdisciplinary bridge has, more recently, facilitated the importation of insights from behavioural economics, which in turn has imported ideas and methods from social and cognitive psychology into the analysis of law. No doubt due to neoclassical economics’ interest in the individuals (and individual firms), these insights often focus on incentives and decisionmaking.

For instance, Kahneman and Tversky’s “prospect theory”, and its compelling description of how individuals make decisions in the face of risk, has profoundly influenced legal scholarship (Jolls *et al.* 1998; Rachlinski 2000). Prospect theory emphasizes that individuals tend to make decisions in terms of gains and losses relative to a reference point, rather than with reference to absolute expected values or ultimate states of wealth; and that “losses loom larger than gains” (Kahneman & Tversky 1979:288, and 1984:346).

Behavioural analysts of law have paid special attention to loss aversion, and two of its corollaries, status quo bias and the endowment effect. The former describes the tendency of people to prefer a state of affairs that they regard as the status quo to the same state of affairs if they regard it as a departure from their status quo. The endowment effect is a narrower application of this principle, describing the tendency of people to place greater value on things that they own than identical things that they do not own (Kahneman *et al.* 1991; Korobkin & Ulen 2000). The broad insight that unites these phenomena is that individuals tend to make judgments based on a reference point. The reference point may or may not be the status quo (Kahneman & Tversky 1979; Kőszegi & Rabin 2006).

Behavioural analysis of law uses empirical evidence to analyse the function and effect of legal rules and institutions (Tor 2008). Crucially, it recognizes that “humans possess limited

cognitive resources and are affected by motivation and emotion” (Tor 2008:242), and explores how these cognitive limits, motivation, and emotion influence judgment and decisionmaking.

Beyond this positive approach, proponents of the behavioural analysis of law envisage a role for the subdiscipline in contributing to policy debate, with the goal of identifying empirically-based, effective prescriptions for legal reform (Korobkin & Ulen 2000; Rachlinski 2000; Camerer & Loewenstein 2004). Yet, practically, policymakers must understand that legal reforms influence not only individuals’ beliefs and decisions, but also influence attitudes toward legal rules and the legal system more generally.

Behavioural scholars have, at times, inquired into individuals’ attitudes (*e.g.*: Kahneman *et al.* 1986a; b), but primarily as a means of understanding consequent decisionmaking. In the context of this paper—where class members are, by default, included in class proceedings, and bound by their outcomes without actively participating—class members’ decisionmaking is of limited relevance. Accordingly, this paper considers how cognitive psychology and behavioural analysis can inform our understanding of attitudes as such.

A robust body of psychological and neuroscientific research investigates how individuals form and update their attitudes (see, *e.g.*: Wilson *et al.* 2000; Cunningham & Zelazo 2007), but this literature remains largely foreign to the analysis of law.

Some basic principles bear outlining. *Attitudes* relate to, and often derive from, beliefs, but they are distinct. Attitudes are relatively stable appraisals of whether the ‘attitude objects’ are good or bad (Bem 1970; Petty & Cacioppo 1981); and attitudes in turn influence how people form more current *evaluations* (Cunningham & Zelazo 2007). Attitudes differ from values and value systems. *Value systems* are stable cognitive structures, with affective links, that help people produce meaning and construct narratives to understand their experiences. *Values* are abstract guides that transcend specific situations, and are formed by “ascertaining the merit of an entity with reference to an abstract value system structure” (Rohan 2000:258).

Early psychological models suggest that attitudes may be formed automatically by a rapid, unconscious, implicit system, or through a slower, conscious, controlled evaluative process—parallel to Kahneman’s (2013) dichotomy of cognitive thought processes, systems 1 and 2. Despite their stability, attitudes may be reappraised, updated and refined. Further, attitudes may be complex: an individual’s appraisal of an attitude object need not be purely positive or negative. People are most likely to form evaluations of an attitude object primarily on the most accessible aspects of their attitude. The activation of positive aspects of a formed attitude may influence subsequent evaluations of the attitude object (Cunningham & Zelazo 2007).

Attitudes are inherently related to core concepts in the behavioural analysis of law in that they “exert powerful influence on people’s evaluations – their current appraisals – and these, in turn, influence people’s choices” (Cunningham & Zelazo 2007:97).

Legal and political scholarship recognizes that the public’s attitudes (as conceived in those areas) influence the performance of the legal system in many regards (see, *e.g.*: Sarat 1975; Gibson *et al.* 1998; Sunshine & Tyler 2003; Benesh 2006; Tyler & Jackson 2014). Yet there is a shortage of research into the ways in which cognitive processes influence individual or collective attitudes in legal contexts, and to what effect. This is an area with untapped potential. It is also important: to the extent that we believe that legal institutions should be regarded as legitimate or fair, this area of research may generate important normative prescriptions.

This paper does not offer new empirical evidence on the research question. Instead, it approaches the question theoretically, drawing on insights from behavioural research, to assess how the design and characterization of legal procedures influence attitudes towards them. This approach is intended to identify testable hypotheses which, if they subsequently find empirical support, will assist policymakers in designing consumer redress procedures to achieve—and to be seen as achieving—their stated purpose.

III. ANALYSIS

This section proceeds in three parts. Section III(a) applies behavioural insights to assess attitudes toward repayment and disgorgement in general. Section III(b) considers the attitudinal effects of framing class actions as proceedings designed to disgorge defendants, achieve collective redress, or compensate individual losses. Section III(c) explores the potential framing effects of introducing litigation costs *versus* lawyers’ fees.

The analysis adopts the following hypothetical facts:

A class action has been commenced against a commercial bank that wrongfully appropriated \$1.50 from each of its 1.5 million customers, for a profit of \$2,250,000.

Class counsel will be paid a 30% contingency fee (\$675,000).

The hypothetical assumes that the appropriation is wrongful, and that each class members has suffered an identical loss. The numbers are arbitrary, but designed to be round figures, with large wrongful profits to the bank, a correspondingly large contingency fee for counsel, and relatively trivial individual losses.

(a) Attitudes toward repayment and disgorgement in general

The traditional conception of private litigation regards lawsuits as two-party affairs. Where the wrong involves a direct transfer of wealth, the defendant's gains and plaintiff's losses are equal, and a lawsuit reversing the transfer will simultaneously compensate and disgorge. If all victims successfully sue, compensation serves a deterrent function by eliminating expected benefits of wrongdoing.¹

By definition, a mass default rewards the defendant with substantial gains, with victims suffering small individual losses. On the facts of the hypothetical, a rational victim is unlikely to bring suit to recover \$1.50. That is not to say that individuals regard their \$1.50 loss as acceptable (though they may), nor that they regard the defendant's \$2,250,000 windfall as acceptable.

One expects that a victim of a loss, however small, will appreciate repayment. This comports with the neoclassical conception of individuals as rational utility-maximizers, if repayment requires little cost or effort. One might expect a rational victim in the hypothetical to be indifferent with respect to the defendant's remaining windfall: that is, it will not directly affect the individual's utility if the defendant enjoys residual gains at the expense of others.

Behavioural and neuroscientific research indicates that people react affectively to perceived unfairness, and that, contrary to neoclassical assumptions, fairness concerns sometimes trump pure self-interest.

Kahneman, Knetsch and Thaler (1986b) demonstrate remarkable consistency among survey respondents in their standards of fairness in marketplace conduct. For example, 82% of respondents considered it unfair for a hardware store to raise the price of snow shovels from \$15 to \$20 after a large snowstorm. Further, 76% considered it unfair for a grocery chain to charge prices 5% higher at an outlet that had no nearby competitors. In the latter scenario, similar results for 10% and 15% price increases suggest that such pricing practices were regarded as unfair irrespective of "the extent of the unwarranted increase" (1986b:735). Even small changes matter. The authors conclude that firms can change their prices (or other terms) if their profit levels are threatened, thereby shifting the loss to customers, without offending community standards; however, consumers overwhelmingly find it unfair for firms to increase prices *arbitrarily*.

Experiments involving the ultimatum game confirm that fairness concerns predictably motivate individuals to forego economic gains to punish unfair conduct. These experiments provide one subject, the proposer, with a sum of money to be divided between her and the other

¹ If not all victims sue or not all plaintiffs succeed, deterrence theory recommends that unsuccessful defendants pay more than the costs of the wrong (see Polinsky & Shavell 1998 for a discussion of underdetection, underenforcement, and supracompensatory damages).

subject, the responder, as she sees fit. The responder may accept the proposed distribution, or reject it, leaving both subjects with nothing. The results challenge rational-choice assumptions, both in the frequency of relatively fair proposals, and the consistency of responders in rejecting unfair proposals, thereby sacrificing a small gain (Thaler 1988; Camerer 2003).

Nowak *et al.*'s (2000) meta-analysis reveals that approximately half of (human) responders rejected unfair divisions below 30%. The authors interpret this “irrational human emphasis on a fair division” to suggest “that players have preferences which do not depend solely on their own payoff... [R]esponders are ready to punish proposers offering only a small share by rejecting the deal (which costs less to themselves than to the proposers)” (2000:1773).

Neuroscientific investigations reveal that unfair proposals engage parts of the brain associated with pain, anger, and disgust (Sanfey *et al.* 2003; van 't Wout *et al.* 2006). This research highlights the emotional dimension of judgment: “A basic sense of fairness...is essential to many aspects of societal and personal decision-making and underlies notions as diverse as ethics, social policy, legal practice, and personal morality” (Sanfey *et al.* 2003:1757). The willingness of individuals to sacrifice gains to punish unfair conduct has prompted behavioural economic efforts to incorporate social goals and conceptions of fairness, or disadvantageous inequality, into our understanding of utility (*e.g.*, Rabin 1993; Fehr & Schmidt 1999).

Interestingly, Kahneman, Knetsch and Thaler (1986a) offer experimental evidence that individuals react to unfair conduct directed at others. Part 1 of their experiment paired students and gave one the option to split \$20 evenly with the other, or unevenly (keeping \$18 and giving the other \$2), with no opportunity for the other to retaliate. Part 2 matched each subject with two proposers from part 1. The subjects were told how the two other students acted in part 1 (*i.e.*, whether they proposed an even or uneven split). Where the two had previously proposed different distributions, the subject could choose between sharing \$12 equally with the student had proposed an uneven split, or sharing \$10 equally (\$1 less, each) with the student who had proposed an even split. A majority (74%) of subjects sacrificed \$1 to reward the fair proposer. The authors repeated part 2 of the experiment at another university and obtained even stronger (81%) results. The outcome indicates that many individuals will incur a cost to punish unfair conduct, even when they are not victim to it.

It is likely that a majority of survey respondents would regard the hypothetical mass default as unfair. After all, as Kahneman, Knetsch and Thaler suggest, “The cardinal rule of fair behavior is surely that one person should not achieve a gain by simply imposing an equivalent loss on another” (1986b:731). It is also likely that most respondents would not want the defendant to keep its wrongful gains.

This proposition can be tested by surveying attitudes, on the following Likert item:

QUESTION 1A: Your bank, which has illegally taken \$1.50 from each of its 1.5 million customers, including you, should be allowed to keep its \$2,250,000 in profit from this conduct.

A modified item can test whether the bank's conduct alone (rather than the respondents' sense of victimhood) would prompt similar responses:

1B: A bank, which has illegally taken \$1.50 from each of its 1.5 million customers, should be allowed to keep its \$2,250,000 in profit from this conduct.

If, as predicted, a majority disagree with Question 1B, it would call into question individuals' indifference to the losses of others.

It is, of course, easy for survey respondents to respond that they would hypothetically like to be repaid, or see the defendant disgorged. Where, however, a proceeding is required, with its attendant costs, to litigate individually small claims, compensation may not be perfect, or feasible. Whether individuals regard such litigation as desirable likely depends on the context. Thus, individuals who regard repayment and disgorgement positively in general may not positively appraise litigation concerning trivial losses.

(b) Attitudes towards legal proceedings for repayment or disgorgement

If most individuals have positive attitudes to disgorgement and compensation in the abstract, it is puzzling that class actions for mass defaults are frequently derided. It is expected, based on the analysis that follows, that individuals' attitudes toward small-claims class actions will depend on whether the proceeding is described as an instrument to disgorge wrongful gains, achieve collective redress, or repay individual losses.

(i) Framing: different evaluations based on different descriptions

Tversky and Kahneman (1981) observe that people's preferences violate the assumption of consistency and coherence when risky choices are framed in different manners, *i.e.*, in terms of gains or losses. Different descriptions of the same acts, contingencies, or outcomes, can result in preference reversals. Their classic illustration (1981; 1984) concerns a disease that threatens to kill 600 people. Subjects presented with the same cover story were asked to select between two programs to respond to the disease, one involving a certain outcome and one involving a risk with the same expected outcome. For one group of respondents, the programs were framed in terms of the expected number of lives saved (gains), and for the other group, in terms of the expected number of deaths (losses). In the gains frame, a majority (72%) preferred to save 200 lives with certainty. In the losses frame, a majority (78%) preferred the risky program—a 1/3 probability

that nobody would die, and a 2/3 probability that 600 people would die—over the certain death of 400 people. The programs are equivalent, but the reversal in preference is dramatic.

Framing effects have garnered considerable attention across disciplines (in the context of law, and the psychology of litigation, see *e.g.*: Rachlinski 1996; Guthrie 2000). They are not limited to risky choices. The effects extend to riskless choice (Tversky & Kahneman 1991), and beyond. Framing research predominantly concerns the differential effects of casting risky choices, specific attributes, or particular goals positively or negatively (Levin *et al.* 1998).²

There is a comparative dearth of research into the effects of neutral frames or different positive frames. In a survey of framing literature, Grüne-Yanoff (2016) refers in passing to ethically loaded frames, with the sole example of Bacharach’s (2006) research on the effects of individual (“What should I do?”) and collective (“What should we do?”) frames on strategy in game theory. Bacharach’s work is situated within broader game theory research into the ways in which individuals label strategies and outcomes (see *e.g.*: Schelling 1960; Sugden 1995), rather than the effects of frames on preferences. Beyond the observation that labelling processes help individuals make sense of their environment, this literature is of limited applicability to the instant research question, because the opt-out class action minimizes coordination problems and removes the link between individual strategies and payoffs.

(ii) Three frames describing one proceeding

This paper hypothesizes that the manner in which a class action’s outcomes are framed will influence individuals’ evaluations of the procedure. Consider the following:

Your bank has profited by \$2,250,000 by wrongfully taking money from each of its 1.5 million customers, including you.

QUESTION 2A: Would you support litigation to ensure that the bank does not keep this \$2,250,000 profit?

2B: Would you support litigation to compensate the bank’s 1.5 million customers for their \$2,250,000 loss?

2C: Would you support litigation for the bank to repay you, and its other customers, \$1.50 each?

This is a framing exercise because it describes the same procedure—assuming perfect disgorgement and repayment, without costs—in three different ways. It is distinct from the

² In attitude framing, a single attribute of the object is framed either positively or negatively, *e.g.*, respondents prefer the taste of “75% lean” ground beef to “25% fat” (Levin & Gaeth 1988). Goal framing concerns the positive consequences of an action *versus* the negative consequences of inaction, *e.g.*, more women perform breast self-examinations when told of the negative consequences of not doing so than when told of the positive consequences doing so (Levin *et al.* 1998; Levin & Gaeth 1988). Subsequent research distinguishes procedural framing, which concerns how measurement procedures influence responses, and temporal frames, which relate to different temporal perspectives (Grüne-Yanoff 2016).

framing examples above in that it identifies different positive goals: disgorgement, collective redress, and individual compensation.

Given that the questions describe the same procedure, one would expect three random samples of respondents, each considering a different frame, to show the same average level of support for the proceeding. The individual compensation frame, however, which emphasizes a small individual payoff, seems likely to attract less support.

The following two subsections outline potential behavioural explanations—reference dependence, and sources of motivation—of why this framing effect is expected. If empirical investigation supports this intuition, and if the frames elicit statistically significant differences, it would help explain negative attitudes toward mass-default class actions.

(iii) Reference dependence and the individual compensation frame

The hypothetical mass default imposes trivial losses on individuals. While people prefer more to less, a consumer in such a situation may not notice the loss or, if she does, may accept it and move on.

Rachlinski (1996) deploys prospect theory to describe why plaintiffs' risk preferences vary systematically from defendants': plaintiffs, who tend to be in the gains domain, should prefer the certainty of settlement to the risk of trial with the same expected value; while defendants, facing a loss, should prefer the risk of trial. Whether a party is in the domain of gains and losses depends on her reference point. Importantly, reference points can change. While an individual filing suit has suffered a loss, over time "the loss becomes part of the plaintiff's 'endowment'; it becomes the status quo" (Rachlinski 1996:147). Additionally, intermediaries such as lawyers may recast the litigation to change the litigant's reference state. In both instances, the new reference state puts the plaintiff in the domain of gains. This recasting of the status quo is relevant to this paper.

The traditional prospect theory explanation of loss aversion is that people evaluate outcomes in terms of changes to their reference state, value their endowments, and resist changes from the status quo. Gal (2006) suggests that these phenomena are better understood through inertia. In his view, people's preference for the status quo is a function of two variables: their need for a psychological motive to justify a departure from the status quo; and the ill-defined nature of their preferences. A potential gain, for example, may provide the motive to depart from the status quo; but if the magnitude of the gain is insufficient, or if the individual's preference for the alternative option is so ill-defined to cause "fuzzy indifference" between the options, the individual will prefer the status quo.

Taking up Kahneman's (2003, 2013) observation that loss aversion does not apply where people exchange ostensibly identical items (*e.g.*, a \$5 bill for five \$1 bills), Gal reports experimental evidence that 85% of participants endowed with a quarter minted in one of two US states declined the opportunity to trade for a quarter minted in the other state. Gal concludes that the predominant choice not to exchange is evidence of inertia in the absence of potential loss.

It is possible that victims of a mass default who do not notice a loss, or who accept it, regard their post-default status quo as their reference point. If you ask them if they would like their money back, they may say yes. If, however, you ask them if they support litigation to recover their \$1.50 loss, the prospect of gaining \$1.50 may not provide enough psychological motive to depart from the status quo. Although the Question 2 frames are silent on costs, it may be that the word "litigation" implies costs—effort, emotion, uncertainty—and that some amount above \$1.50 is required to overcome inertia and motivate support.

(iv) Prosocial goals and the sources of motivation

An alternative theory of motivation suggests that individuals may value mass-default class actions for prosocial reasons and not for the individual payoff.

While traditional economics focuses on extrinsic motivation, *i.e.*, economic incentives, psychology scholars have long pointed to the importance of intrinsic, non-economic motivation. Intrinsic motivation induces actors to perform an activity without any evident reward other than the activity itself (Deci 1971; Frey & Jegen 2001). Economists' focus on price, and extrinsic motivation, is pragmatic: it reflects difficulties in manipulating intrinsic motivations and isolating their effect (Frey & Jegen 2001).

Motivation crowding theory seeks to bridge economic and psychological conceptions of motivation, to explain how different sources of motivation interact. Frey and Jegen (2001) conceive of motivation as falling on a continuum from purely extrinsic to purely intrinsic. They note that "[b]asic intuition tells us that we are more willing to undertake a task if we can expect a reward" (2001:596); however, when intrinsic motivation is sufficient for an individual to perform, the introduction of external incentives may crowd out this motivation. They offer an example based on intuition: children may do yard work because they like doing it, but once they are paid by their parents, they may expect (or require) such extrinsic incentives in future.

Since crowding theory pertains to motivations, rather than attitudes, research frequently concerns labour and productivity. At its extreme, people may refuse to do work for pay that they would otherwise have done for free because the introduction of economic incentives crowds out intrinsic motivation. Ariely (2008) illustrates this with anecdotal evidence from the AARP, an

American advocacy organization. The AARP found that when it offered lawyers \$30 per hour to provide legal services to retired persons, the lawyers refused to do so. Undoubtedly, this amount was beneath their reference income. When it asked lawyers to provide services *pro bono*, however, many lawyers agreed. Whatever intrinsic motivation leads lawyers to donate their services vanished when extrinsic motivation was introduced.

Experimental results suggest crowding out effects both in the performance of mundane tasks in a lab setting (Heyman & Ariely 2004) and with students asked to collect charitable donations (Gneezy & Rustichini 2000). In both experiments, participants who received compensation performed better with more compensation than with less; however, participants who received no compensation performed better still.

Further, the literature devotes much attention to Titmuss's (1970) theory that monetary incentives crowd out intrinsic motivations to engage in prosocial conduct. Frey and Götte (1999), for instance, report crowding-out effects in volunteer efforts. Studies on blood donation, Titmuss's influential example, are inconclusive. One meta-analysis suggests that extrinsic incentives are inefficient but do not crowd out prosocial motivation (Niza *et al.* 2013). Notably, this meta-analysis's relatively small sample includes studies involving non-monetary extrinsic incentives, such as free cholesterol tests. Another study suggests that the introduction of monetary incentives can demotivate previous voluntary donors; and that non-monetary external incentives increase donation among certain populations (Chell *et al.* 2018). Different reward types have different effects, and the effects are heterogeneous between groups (Goette & Stutzer 2008; Mellström & Johannesson 2008). Few insights can be transplanted to legal analysis without empirical testing in this context.

Though these studies concentrate on productivity and participation, it is plausible that the same extrinsic incentives may alter individuals' perceptions of the value of an endeavour, generally. This is in line with the findings of Frey and Oberholzer-Gee's (1997) study of NIMBYism and levels of community support for the siting of nuclear waste repositories. Their evidence suggests that compensation crowds out public spirit among individuals who would otherwise have supported the siting. This application of the theory suggests that the phenomenon operates even where support levels, rather than individual productivity, are in issue.

The application of motivation crowding theory to attitudes requires conceptual tweaks. Diverse explanations for the effect suggests that external rewards shift control from intrinsically-motivated individuals, removing the individuals' sense of personal causation (deCharms 1968; Deci 1971); that rewards impair individuals' self-esteem by signalling that their involvement or competence is underappreciated (Frey & Jegen 2001); or that observable prosocial conduct

provides individuals with reputational rewards that compensation undermines (Bénabou & Tirole 2006). These explanations fit poorly with the instant research question, because (most) individual class members in an opt-out action do not have control over the activity and are not required to act, and accordingly there are no expected signalling effects associated with their involvement. These explanations also minimize the finding that it is the introduction of *insufficient* rewards that reduces output. Gneezy and Rustichini (2000) capture this principle in the title of their article, “Pay Enough or Don’t Pay at All”.

Heyman and Ariely (2004) provide a two-market explanation: in monetary markets, there is a strong relationship between payment and performance; whereas in social markets, effort stems from altruistic motives. The introduction of money shifts individuals’ perception of the nature of the market and the norms governing it. The reward casts the purpose in individual material terms, shifting focus away from prosocial purposes. Indeed, rewards can become the purpose: “Do this and you’ll get that’...focuses attention on the ‘that’ instead of the ‘this’” (Kohn 1993:62).

Question 2C may therefore transmute the class action in individuals’ perceptions from a proceeding with the power to achieve prosocial goals into a procedure to provide the individual with \$1.50. If Question 2C elicits significantly lower support than the other frames, it would bolster the hypothesis that a focus on individual compensation for such a small amount crowds out other, prosocial motivations for the class action.

Additionally, it is plausible that a focus on disgorgement, punishment, and deterrence, or class-wide vindication, engages individuals’ social value priorities; whereas individual compensation instead engages individuals’ personal and material value priorities. Personal and social value priorities, to the extent that they exist (and conflict), will influence perceptions and behaviours in potentially different ways (Rohan 2000). That is, comparatively positive attitudes toward a lawsuit that disgorges the defendant and a lawsuit that compensates the class as a whole (2A and 2B) would support the idea that a collective frame engages social value priorities.

Much of this research on group values emphasizes self-identification of individuals with a group (Turner *et al.* 1994; Garcia *et al.* 2005; Hogg & Abrams 2006; Blader & Tyler 2009). If the frames in Questions 2A and 2B are found to encourage collective identification among individuals, then they may reinforce prosocial motivations. Just as Bacharach (2006) conceives of the “we frame” (rather than the “I frame”) as facilitating cooperative outcomes in the prisoners’ dilemma, it is possible that Questions 2A and 2B reinforce a collective, social identity in individuals, whereas Question 2C, which introduces individual compensation, reinforces personal identity.

It is conceptually easier to imagine why deterrence-orientation may create a community relationship among victims than the collective redress frame, which (like the procedure) simply aggregates individual losses. The discussion above on reference points, inertia, and motivation crowding, provide a potential explanation of why attitudes toward individual compensation and collective redress may differ, assuming individuals do not reason through the equivalence.

The implications of self-identification are important but complex, and the validity of applying these insights here, where individuals may not be aware of their loss or their inclusion in the class action, is questionable. The potential effects of group identification are therefore left to future research, as described in section IV(b), below.

Potential class-action framing effects present an opportunity for future research into comparative value systems, attitude formation, and interattitudinal consistency. In a system that relies on private enforcement, a worldview that prefers for wrongdoers not to profit from mass defaults is inconsistent with anti-class action sentiments. But, in the case of mass defaults, if a person more highly values litigation that provides meaningful compensation, class-action antipathy makes sense. The objectives inevitably conflict, particularly because the costs of discovering and prosecuting mass defaults and the administrative costs of repaying class members will make compensation (if any) even more trivial than the individual loss.

(c) The effect of legal fees

The analysis thus far has ignored the role of class counsel. This is a significant omission considering that class counsel are among “the most frequently derided players” in the North American legal system, based on the common perception “that class actions are little more than a device for the lawyers to enrich themselves at the expense of the class” (Fitzpatrick 2010:2043–44). Class-action sceptics regularly emphasize fees:

“Among critics, the contention that class members have received too little in a class settlement *almost always is accompanied by the corresponding charge* that the class' counsel has received too much; in other words, the settlement has resulted in handsome fees for the lawyers but inadequate relief for the class members” (Hay 1997:1433, emphasis added).

There is no shortage of class actions that attract criticism because of the juxtaposition of trivial gains for the class and enormous fees for its lawyers. For example, a US class action against the owner of Subway alleged that the restaurant chain's footlong sandwiches were shorter than 12 inches. A settlement that received preliminary approval, would have paid each of 10 named class members \$500, with \$520,000 to class counsel, and offered no further benefits to the class beyond a series of commitments by the company to ensure quality control in the future. Theodore Frank, a “professional objector” and director of the Competitive Enterprise Institute's Center for Class

Action Fairness (CCAF), successfully challenged the settlement. The court concluded that the case had no merit, ultimately holding that the class should never have been certified “[b]ecause the settlement yields fees for class counsel and ‘zero benefits for the class’” (869 F.3d 551, 557 (7th Cir. 2017)).

In another CCAF settlement challenge, concerning Walgreen’s stockholder litigation, Judge Posner penned this scathing critique:

“[A] class action that yields fees for class counsel and nothing for the class...is no better than a racket. It must end... No class action settlement that yields zero benefits for the class should be approved, and a class action that seeks only worthless benefits for the class should be dismissed out of hand... Certainly class counsel, if one may judge from their performance in this litigation, can’t be trusted to represent the interests of the class” (832 F.3d 718, 724&726 (7th Cir. 2016)).

In *Smith*, a notable Canadian class action concerning predatory lending practices, the defendants agreed to a settlement that would include, *inter alia*, \$56 million in debt forgiveness and \$30.5 million worth of \$5 coupons to be applied by class members to future loans. In approving the settlement, the motion judge reduced class counsel’s fees from the agreed \$27.5 million to \$14.5 million (a \$3.5 million premium over fees and disbursements billed). The Court of Appeal for Ontario upheld this part of the order, but noted the motion judge’s concern that the settlement would not achieve behaviour modification, explaining that, for some class members, the settlement “destined them to continue to borrow payday loans from the defendants” (2011 ONCA 233 at ¶¶96-97, *aff’g* 2010 ONSC 1334). It is difficult to review this outcome—including a fee award representing a \$3.5 million premium above the lawyers’ billed fees and disbursements, or 11.25% of the settlement (as valued by the lawyers)—albeit “adequate or satisfactory” according to the motion judge, without viewing the fee award in light of the \$5 coupons.

Because of the nature of mass defaults, any individual compensation will look trivial in light of the compensation demanded by counsel prepared to undertake such litigation. The questions then arise as to whether such proceedings can ever garner widespread support from individuals, whether the cost of the litigation *per se* or the enrichment of lawyers influences attitudes, and whether and how framing effects interact with this attribute of class actions.

This section maintains the hypothetical facts above and assumes that class counsel will receive 30% of the amount recovered. This percentage contingency is adopted because it is simple, significant, and not an uncommon ask by class counsel. In reality, average fee awards may be considerably smaller as a percentage of the damages (Fitzpatrick 2010), and courts may calculate fees based on a multiplier of counsel’s bills having regard to the risk of the litigation and the reasonableness of their hours and rates, among other factors (Lynk 1990; Alexander 1998).

For simplicity, this analysis ignores discounted settlements and non-monetary compensation to class members.

Consider the following two sets of questions, the first set framed in terms of unspecified litigation costs (in parentheses), and the second framed in terms of lawyers' fees [in brackets]:

Your bank has profited by \$2,250,000 by wrongfully taking money from each of its 1.5 million customers, including you. (A successful lawsuit against your bank will cost \$675,000.)[On successful completion of the litigation, lawyers who have agreed to sue the bank on its customers' behalf, will be paid \$675,000.]

QUESTION (3)[4]A: Would you support litigation to ensure that the bank does not keep this \$2,250,000 profit? The (litigation costs)[lawyers' fees] will be paid out of the amount recovered from the bank.

(3)[4]B: Would you support litigation to compensate the bank's 1.5 million customers for their losses? Taking into account the \$675,000 (cost of the litigation)[in lawyers' fees], \$1,575,000 will be available to compensate the class.

(3)[4]C: Would you support litigation for the bank to repay you, and its other customer, for their losses? Taking into account the \$675,000 (cost of the litigation)[in lawyers' fees], each customer will receive \$1.05.

This author's intuition is that the introduction of costs into Question 3 may cause lower support in each frame than in the equivalent frames in Question 2, but that any differences in attitudes between the Question 2 frames would persist. That is, Question 3C is expected to attract considerably less support than Questions 3A and 3B.

If Questions 3A and 3B attract considerably lower levels of support than the equivalent frames in Question 2, it would suggest that individuals have a reserve price for collective redress, whether conceived in terms of disgorgement or compensation. (A reduction in support for either 3A or 3B but not both might suggest different evaluative beliefs about the relative desirability of disgorgement and compensation, but the inferences would be trickier to draw without further analysis.) A test for this reserve price might instruct respondents that they have been appointed to represent the class of consumers and that individual compensation is not feasible, and then elicit the maximum amount they are willing to pay to ensure the defendant does not keep its wrongful gains or to ensure that the customers' rights are vindicated.

Explicit reference to "lawyers' fees" in Question 4 is expected to reduce support still, in line with Justice Posner's description of such class actions as "a racket". If contingency fees are the cost of discovering mass wrongs and disgorging wrongful gains, it is puzzling why people tend to view class counsels' fees with such disdain. The immense disparity between small individual claims and large contingency fees almost certainly influences attitudes affectively.

There are a number of reasons to believe that explicit reference to lawyers and their fees will affect attitudes, both in general and relative to the “litigation costs” frames.

Firstly, lawyers are unpopular in North America. A 1952 *ABA Journal* article, describing itself as “not pleasant reading” for the profession, noted that lawyers ranked lowest out of five professions in terms of their “importance in the community”, and were the only occupation that no respondent selected as “most interested in church” or “most interested in you as a person” (Blaustein 1952:39–40). Little changed in the 41 years that followed: the journal reported in 1993 that a minority of respondents had a favourable impression of lawyers; only 36% believed lawyers were “a constructive part of the community”; and, when asked if the phrase “honest and ethical” describes various professions, 40% of respondents indicated that the term did not apply to lawyers. Notably, 63% of respondents said lawyers earn too much, 59% said they were greedy, and 55% said they charge excessive fees (Hengstler 1993). More recent polling data suggests that 34% of Americans believe lawyers contribute “not very much” or “nothing at all” to society, compared with only 18% (the lowest among all professions in the poll) who believed lawyers contribute “a lot” (Pew Research Center 2013). In Canada’s common law jurisdictions, fewer than 15% of people have a “very positive” view of lawyers (Insights West 2017).

Beyond the unpopularity of lawyers, several behavioural insights suggest that Question 4 frames will attract less support than Question 3. This section draws from the literature on loss aversion, social utility, availability, and mental accounting, and suggests that these insights may interact in this context.

Kahneman, Knetsch and Thaler conclude from their public-opinion surveys on fairness that “disutility associated with an outcome that is coded as a loss may be greater than the disutility of the same objective outcome when coded as the elimination of a gain” (1986b:732). In a simple example involving a car dealer responding to a shortage of a popular model of car, 58% of respondents found it acceptable for the dealer to eliminate a previously-offered \$200 discount, whereas 71% found it unfair for the dealer to increase the price by \$200. The former, according to the authors, was coded as a foregone gain, while the latter was coded as a loss.

The authors highlight similar results with respect to a company’s payroll decisions during a time of recession and high unemployment. The survey presented two frames, one involving no inflation and one involving 12% inflation. In the former frame, the company decreased employee wages by 7%, which 62% of survey respondents found unfair. In the inflationary frame, the company limited wage increases by 5%—equivalent to a 7% decrease in real wages—which only 22% of respondents found unfair. The authors conclude that respondents coded the former, but

not the latter, as a loss. Similarly, “litigation costs” may sound less like a loss to the class and more like a foregone gain.

While the survey results support the authors’ contention that foregone gains are less painful than losses, the preference reversal may hinge more on perceptions of the employer’s conduct than the coding of the decrease.

As described above, beyond people’s perception that they are being treated unfairly, they are motivated by a concern that others are acting unfairly. People care about actions and outcomes, but in assessing the fairness of outcomes, people consider the motives and intentions of the actor that caused those outcomes (Greenberg & Frisch 1972; Rabin 1993; Blount 1995). This observation is supported by ultimatum game findings that people are more likely to accept unfair allocations proposed by a computer than by another human (Sanfey *et al.* 2003; van ’t Wout *et al.* 2006).

Blount notes that an outcome is less likely to be perceived as unfair if it has a non-human (or environmental) cause than if it has a human or social cause, because “random or natural occurrences are not typically perceived [to be] as intentional or controllable” (1995:133). She concludes that unfairness evaluations of an outcome are a function of perceptions that the outcome was caused intentionally by a human actor who was motivated by selfishness.

More so than the car example, the wage example requires a degree of additional reasoning from respondents, in that they must understand inflation to realize that the real wages are the same in both frames. Without stopping to think about the cost of 12% inflation, a 5% raise does not immediately sound like a 7% wage cut attributable to the employer. In the no-inflation frame, it is easier to assign blame to the company for the 7% wage cut. In the inflationary frame, inflation intuitively seems responsible.

It is likely that people will process “lawyers’ fees” more than “litigation costs” as a loss deliberately-imposed by an identifiable actor. This identification may invite social comparison and cause disutility among inequity-averse individuals (Fehr & Fischbacher 2002). Costs, on the other hand, are not generally treated as losses, and are less aversive (Kahneman & Tversky 1984; Thaler 1985). Lay respondents faced with Question 3 frames may answer with their intuitions, without stopping to consider that “litigation costs” will likely be comprised of lawyers’ fees. (A sample of lawyers or judges may more readily intuit the connection.) Respondents may infer from the mere mention of lawyers that lawyers intend to enrich themselves at the expense of class compensation. If respondents interpret “litigation costs” to be the cost of achieving the litigation’s goals, they may be more likely to accept the cost than if they unpack the concept and realize that, in this context, “litigation costs” means redistributing 30% of their losses from the wrongdoer to lawyers.

Further, the availability heuristic and saliency bias may facilitate the inference of class counsels' selfishness. Ask the nearest person "Who benefits from class actions?" Unless you are sitting in class counsels' office, "class counsel" is the probable answer. Coverage of zero-benefit class actions likely makes such outcomes more easily retrievable in the minds of average respondents. This availability, no doubt enhanced by publicity and the work of "availability entrepreneurs" like the CCAF, may cause respondents to underestimate the frequency of proceedings that benefit class members (Tversky & Kahneman 1974; Kuran & Sunstein 1999). Similarly, the description of zero-benefit actions ("a racket"!) is more "emotionally interesting" to individuals than statistics about class-action outcomes. This salience potentially increases their availability (Nisbett & Ross 1980:45; Guthrie 2000). Accordingly, one expects respondents to infer the selfishness of lawyers' motives in assessing the fairness of the outcomes as framed in Question 4.

Though this paper leaves group identification to be explored in future research, it likely matters how winners and losers are conceived. Observers can focus on the disgorged defendant as the loser (and the class, or class counsel, as winners), or on class counsel as winners (and the class as losers). To people with social preferences, *i.e.*, who are not solely concerned with their own material self-interest, these different focuses invite comparison with different reference agents (Fehr & Fischbacher 2002). A focus on lawyers' fees likely recasts what was a zero-sum game between the class of victims and the wrongdoer as a zero-sum game between plaintiffs and their lawyer.

The asymmetry of gains between counsel and class members is inevitable in mass defaults: even full compensation is trivial where losses are trivial; and, no lawyer will litigate a class action for a trivial sum, for the same reason that rational individuals will not bring suit. To the extent that individuals are inequity averse, employing "complicated social comparison processes" to evaluate outcomes (Fehr & Schmidt 1999:821), the relative payoff to class counsel may carry disutility to class members. Alternately, if individuals self-categorize as class members/victims, it may encourage social comparison with their lawyers as an outgroup, thus inflaming class members' perceptions of disadvantageous inequality (Garcia *et al.* 2005).

Finally, Thaler's (1985, 1999) work on mental accounting suggests that the segregation of lawyers' fees from the individual benefits of class actions (if any) may reduce the perceived value of the class device. He proposes that individuals, like companies, face choices in processing expenses and revenues. Accounting requires them to record (book) these changes and post (categorize) them into accounts (Heath & Soll 1996; Thaler 1999). How individuals post gains and losses may affect their happiness. Drawing on prospect theory, and particularly on reference

dependence and loss aversion, Thaler's principles of hedonic framing suggest that gains should be segregated, losses should be considered together, mixed (net) gains should be integrated to cancel out the losses, and mixed losses should be integrated unless the loss is much larger than the gain.

Question 4C may force individuals to segregate the gain (compensation) and loss (contingent fee), contrary to the principles of hedonic framing. The reference point is crucial in determining gains and losses (Tversky & Kahneman 1981; Kőszegi & Rabin 2006). In the hypothetical default, the loss is small and may have gone unnoticed, or may have been forgotten. Thaler (1999) notes that small costs are often not booked, and that people eventually ignore sunk costs. In Rachlinski's (1996) terminology, the loss has become part of the individual's endowment. If so, the reference point is the status quo, and individual compensation offers a gain of \$1.50 accompanied with an aversive 30% loss (\$0.45) in fees. If integrated, the individual can code this as a net gain of \$1.05. If segregated, given the steeper curve of the value function in the loss domain suggests, the value of the loss will almost cancel out the gain. Note that if the individual's reference point is an *expected gain* from the litigation of \$1.50, the outcome is a pure loss of \$0.45 to lawyers.

Nonetheless, the amounts—both the individual's compensation, and the lawyers' share of that—are so trivial, that this explanation does not seem compelling. If these hedonic principles apply to individuals' assessments of group gains and losses, the explanation may provide a more compelling explanation in the event that the collective redress frame (4B) attracts considerably less support than the equivalent "litigation costs" frame (3B), or the disgorgement frame (4A). As Levy (2003) notes, however, prospect theory derives from observations of individual decisionmaking, and its extension collective decisionmaking cannot be assumed without further research.

On the basis of the foregoing analysis, it is expected that Question 4 frames will attract less support than Question 3 frames. The difference is expected to be less pronounced in the disgorgement frames (3A and 4A)—which invite respondents to perceive counsel fees as the cost of punishing the defendant's wrong—than in the collective compensation frames (3B and 4B)—which presents counsels' gains against the backdrop of class losses, inviting the perception that the lawyer is revictimizing the class. Of course, any conclusions are impossible without empirical evidence. A more direct test of differing attitudes toward the Question 3 and 4 frames could ask two groups of respondents to state the maximum percentage of the defendant's gains they would be willing to pay—as "litigation costs", or as "lawyers' fees"—to disgorge the defendant or to provide collective redress.

IV. DISCUSSION

(a) Limitations of this analysis

Behavioural decision theory complements traditional legal analysis and law-and-economics approaches by permitting scholars to address different questions (Rachlinski 2000). The value of studying behavioural phenomena is that “they reveal important influences on human judgment and choice that other approaches to law do not expose” (Rachlinski 2000:765).

The analysis in this paper is fundamentally limited by the dearth of empirical evidence in this area. Several of the earlier propositions in this paper, such as the prediction that people will agree that firms should not be entitled to keep the profits of their wrongs, or that people will agree that they should be repaid, seem obvious. Further, judicial hostility to class actions in which lawyers profit immensely and class members receive little or nothing, supports the intuition that the size of individual and class counsel’s compensation (or their comparison) influences attitudes. For members of the public, who may support deterrence in the abstract, the unpopularity of lawyers plausibly explains why this comparison of compensation attracts negative attitudes. These intuitions are helpful for formulating hypotheses, but intuitions are no substitute for empirical investigation (Kahneman *et al.* 1986a; Tor 2008, 2014).

Intuitions aside, research from other contexts provides potential explanation of why disgorgement is expected to be valued, how individual compensation may crowd out intrinsic and prosocial motivations, and why counsels’ fees shift focus away from the original wrong. That research, however, generally concerns individual interactions and market transactions. The legal context is very different, and one must take care in applying insights from existing research here.

For instance, findings on the subjective utility of punishing unfair conduct derive from experimental research concerning decisionmaking in pairs or small groups. The findings, compelling as they may be, do not necessarily apply to attitude formation in the absence of decisionmaking, or extend outside lab settings to evaluations of legal institutions. This problem of external validity is critical, and it requires careful analysis designed to address this specific research question, in this particular context (Tor 2008).

Notably, the foregoing analysis identifies several hypotheses about how cognitive processes shape attitudes, but this paper deals with average attitudes. It simplifies matters to imagine individuals as homogeneous, but they are not. While survey research may identify community standards of fairness, individuals’ social preferences (*e.g.*, tendencies toward self-interest, inequity aversion, or spite) differ (Fehr & Fischbacher 2002). Conceptions of fairness, or their effects, may vary between cultures (Henrich 2000; Oosterbeek *et al.* 2004), or even between

students in different disciplines (Kahneman *et al.* 1986a). Likewise, while cognitive effects may help explain how different frames elicit different attitudes in the aggregate, these cognitive effects vary among individuals, and likely between different groups (*e.g.*, laypeople *versus* judges). Careful attention must be paid to this variability, and to what conclusions can validly be drawn as a result (Tor 2014).

For example, while anecdotal evidence suggests class-action antipathy among the public and judges alike, attitudinal research must distinguish between these actors. Judges have more experience with legal proceedings than members of the public and should be expected to have devoted more cognitive effort to understanding how litigation works. Experimental research in political science suggests that experts have more consistent attitudes than novices with respect to political policies: where experts perceive strong implicational relations between different attitudes, there is more interattitudinal consistency pressure (Lavine *et al.* 1997). In the hypothetical, compensation and disgorgement are different sides of the same coin, so one would expect judges, as experts, to understand the implicational relations between the frames, and hold more consistent attitudes across them. One would expect laypeople, on average, to be less likely to identify such implicational relations.

Aside from the heterogeneous effects of cognitive phenomena, future research must bear in mind that these effects may interact in unexpected ways. Thus even if empirical evidence provides support for the hypotheses identified in this paper, it is imperative to consider the interplay of these hypotheses, and to take care to isolate each behavioural phenomenon in order to test whether and to what effect it applies, to whom and to what extent, and under what conditions (Rachlinski 2000; Tor 2008).

(b) Future research and practical implications

The foregoing analysis has several implications for future research and for policymaking. If differences in attitudes toward class actions, when framed in terms of disgorgement, collective redress, and individual compensation, are significant, several obvious questions arise. Behavioural scholars note that, in certain conditions, “[a] loss to another is a gain to oneself” (Jolls *et al.* 1998:1495). How much do individuals value disgorgement? And, if trivial compensation distracts from the disgorgement value of a proceeding, what is the threshold of triviality?

A difference in attitudes toward “litigation costs” and “lawyers’ fees” would be interesting *per se*, but of minimal practical importance to policymakers. It would be impossible to prevent people from understanding that litigation costs in this context are comprised of lawyers’ fees. It would, however, be of academic importance to future researchers hoping to isolate people’s

attitudes toward the disgorgement and compensation functions of class proceedings, as distinct from their attitudes toward lawyers, which are expected to be somewhat unflattering.

Evidence suggests that group identification among individuals fosters prosocial conduct to help ingroup members (see *e.g.*: Simon *et al.* 2000 on volunteerism; Levine *et al.* 2002 on bystander intervention). Identification can also influence the preferences of individuals who self-categorize in the group, potentially increasing social comparison with outgroup targets (Garcia *et al.* 2005, 2013). Whether class-action frames can foster a sense of group membership among class members, and to what effect, are important questions. If group identification effects are found, how do they vary across frames? Does the collective-redress frame motivate prosocial support for class actions? Does the disgorgement frame, or the introduction of lawyers' fees, create a target outgroup for social comparison?

There are several practical implications of this research. If indeed most individuals value disgorgement as a goal, it would support the use of small-claims class actions for deterrence objectives. Since class actions are a procedural tool and are not intended to alter substantive rights, careful attention should be paid to the statutory rights of action provided to consumers for trivial losses. Statutory rights to disgorge wrongful gains, with preambulatory reference to the deterrence objective, would enable judges to get past their reservations about proceedings that provide “zero benefits” to class members; *ex ante* deterrence of future wrongs would be the benefit.

Judges understand that faith in the justice system matters: “it is...of fundamental importance that justice should not only be done, but should manifestly and undoubtedly be seen to be done.”³ Empirical research into attitudes may demonstrate that framing small-claims class actions in terms of compensation can undermine the perceived legitimacy of legal institutions. This, however, is not a foregone conclusion. Gold (2016) argues that compensation is crucial to the deterrence function of class actions, because it signals the merit of the action and imposes more reputational harm on defendants than non-compensatory outcomes. He argues, accordingly, that *cy-près* distributions of disgorged gains erode public confidence in the procedure, while decreasing “reputational deterrence”. His “instinct is that seeing victims get some compensation is better for legitimacy than no compensation” (2016:2035). He may be correct, but the issue deserves investigation.

³ *R v Sussex Justices; Ex parte McCarthy* [1924] 1 KB 256 at 259, Lord Heward CJ (Eng H Ct).

With greater conceptual clarity on the goals of small-claims class actions, debate on legal reform can proceed to isolate problems and address them specifically, rather than attack aggregation procedures wholesale.

For example, if compensation is the goal—or a requisite for reputational deterrence—coupon settlements should not, *per se*, be rejected, bearing in mind the virtually inescapable perception that class counsel are the real winners in such settlements. From a deterrence perspective, however, coupon settlements are inappropriate where they force class members to continue their relationship with the defendant rather than confront it with the costs of its wrong.

Research in this area may yield important policy insights on the distribution of disgorged gains. If deterrence is the primary objective, and compensation serves only to distract from this and undermine attitudes toward the procedure, then policymakers may wish to abandon individual compensation of claims below a certain monetary threshold. How to do this should depend on what cognitive forces are shaping negative attitudes.

If, for example, negative attitudes are primarily driven by the direct comparison of individual repayment with counsel fees, one solution would award sizeable amounts to a subset of class members by lottery (Lavie 2011). By awarding large payments randomly, individual pay outs (to whomever receives them) will look less trivial alongside counsel's fees; and, building on behavioural evidence that individuals prefer a lottery to the expected value of the lottery ticket (Kahneman & Tversky 1979:281), this approach may provide sufficient extrinsic motivation to overcome the crowding out of non-economic motivations (even if *expected* benefits remain the same). Indeed, in the blood donation context, donation rates increased when lottery tickets were offered as a reward (Goette & Stutzer 2008), whereas modest direct payments do not generally increase donation rates. On the other hand, this approach would exacerbate a problem already decried by critics, namely that some victims go undercompensated while others receive windfalls.

Alternatively, if individual compensation crowds out prosocial support of this public good, a *cy-près* distribution of proceeds to charity may minimize crowding out effects. Returning to blood donation rates, one experiment concluded that cash payments crowded out motivation among women, but donation rates rebounded when donors could direct the payment to charity (Mellström & Johannesson 2008). A large *cy-près* distribution to charity may also balance the negative effects that class counsel fees have on attitudes toward these procedures. Kahneman, Knetsch and Thaler (1986b) observe that 74% percent of respondents thought it unfair for the seller of a highly-coveted doll to auction it to the highest bidder, whereas only 21% found this unfair when the seller pledged the proceeds to charity. While individuals may view trivial compensation as unfair in light of counsel's fees, a *cy-près* distribution may re-engage prosocial

motivations and reduce perceived unfairness associated with the comparison of individuals' and counsels' litigation gains.

Ultimately, if deterrence of mass defaults is desirable, several strands of future research will have to be connected. If we continue to rely on private enforcement, how should we optimally incentivize lawyers to detect wrongs, without raising the ire of judges and the public? Can disgorgement and reputational harm alone provide sufficient deterrence where some wrongs go undetected? And how do we strike the balance, to ensure public faith in the fairness of marketplace conduct and in the legitimacy of enforcement procedures?

V. CONCLUSION

Behavioural analysis offers empirical insights into the sources of consumer vulnerability, with normative implications for the design of consumer-protection regimes. In North America, opt-out class actions are part of the enforcement mix. This procedure was once hailed as a powerful mechanism to empower consumers and deter marketplace misconduct. The reality of such proceedings, however, is that they offer little compensation to individuals in cases of mass default.

This study draws on psychological insights to suggest that the manner in which class actions are conceived influences attitudes toward the procedure. Industry groups and organizations like the CCAF likely understand this and rely on it in lobbying for reform. Compensation will inevitably be trivial in cases of mass default, and glaringly so in comparison with the litigation costs. If deterrence is the goal of class actions, a focus on trivial compensation distracts from their mission.

This is a novel area of legal analysis, with great potential to apply theoretical insights from other disciplines, but empirical research is required to support the validity of these new applications.

Socially, this issue matters because negative attitudes toward the procedure may undermine its legitimacy, with knock-on effects on the perceived legitimacy of the legal system in general. Economically, this matter because, if private enforcement and deterrence are regarded as desirable, pervasive negative attitudes toward such proceedings will constrain their potential to accomplish these goals.

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