Bankruptcy Policy in Light of Manipulation in Credit Advertising

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This Article argues that when credit suppliers market and advertise their credit products, they utilize and enhance consumers' cognitive biases, particularly their optimism bias and illusion of control. We apply the concept of manipulation to this practice. The biased and manipulated debtors attribute unrealistically low probability to negative life events, such as job loss, illness, accident or divorce, and high probability to positive life events. As a result of the manipulation, the biased debtors are triggered to borrow more than they would have borrowed otherwise. This additional borrowing may contribute to the default of these debtors and to their eventual bankruptcy. Empirical studies of the causes of bankruptcy show that before their default, bankrupts have often experienced negative life events that decrease income, increase expenses, or both.

The bias and its manipulation justify legal intervention. The Article discusses various justifications for legal intervention and offers tentative and partial prescriptions for intervention. It analyzes the comparative advantages and shortcomings of ex ante *intervention, in the form of regulation of credit marketing practices and credit contracts, of tax and insurance, and* ex post *intervention, at the bankruptcy stage. Its main contribution is in bringing together bodies of literature on cognitive biases, consumer decision making, lifecycle, social influence, advertising and marketing, behavioral law and economics, economic analysis of bankruptcy and socio-legal studies*

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of bankruptcy. By combining these bodies of literature, the Article provides a new perspective on bankruptcy and credit and offers a promising framework for future work.

INTRODUCTION

The title of a recent advertising campaign for unsecured bank loans is "Future Credit." The campaign's TV commercials show a man (or a woman) in his (or her) forties, leaning over the shoulder of a twenty-something look-alike. "Who are you?" asks the young person. "I am you in twenty years." The older self talks the younger self into borrowing money. In different clips the consumer is persuaded to use the money for different purposes: vacationing in Mexico, buying a fancy car, refurbishing a house, or going to graduate school. "How can I afford this?" asks the younger self. "Believe me, in the future you'll have enough money, now be spontaneous and just do it." The campaign's slogan on the Web and in newspaper ads says: "We believe that you will succeed, and therefore you are invited to take what you need now. You will return it in the future, when you have it." The general message is: live the good life and fulfill your (romantic) dreams in your 20s, while you still can. Don't wait until you can afford it. The future is bright. In what seems to encourage a spontaneous decision, the ads promise that loans are approved within ten minutes, twenty-four hours a day. Application is by phone or online, no forms, no fees. In some loan tracks, an "interest only" period of three years before beginning to repay the principal is also offered.[1]

Campaigns such as this provide the basic impetus for this article. Creditors sometimes lure their debtors into borrowing more than they initially intended to. Sometimes this additional borrowing contributes to the default of these debtors and to their eventual bankruptcy. This Article argues that when credit suppliers market and advertise their credit products, they utilize and enhance consumers' cognitive biases, particularly their optimism bias and their illusion of control. This justifies a rethinking of bankruptcy policy

1 A campaign launched by Bank Leumi, on Israeli TV, press, and Internet in March 2005. Bank Leumi is the second largest bank in Israel. Its credit to the public is NIS 169 billion ($39.3 billion). The campaign was designed by the McCann-Erikson Israel advertising agency.

For a press release, see Bank Leumi, Press Releases, http://www.leumi.co.il/Leumi/Article/0,2777,117762,00.html (last visited Dec. 24, 2005).

and doctrine. It also calls for the examination of other related fields of law, such as credit market regulation, and the application of contract and tort law to debtors and their creditors. The Article offers a framework for such rethinking and offers several preliminary proposals.

The application of behavioral and cognitive insights to the discussion of bankruptcy law is relatively new. Yet there are already a number of articles that examine bankruptcy law through this perspective, and even a handful that refer to optimism bias. While this Article offers some advances in drawing policy recommendations from empirical studies on optimism bias, its main contribution is in moving a step forward by adding the perspective of creditors to the perspective of debtors. This Article applies the concept of market manipulation and the literature on advertising to the context of bankruptcy.

Part I introduces the literature on cognitive processes that affect borrowing, debt, failure and bankruptcy. Part II focuses on the active role of creditors in borrowing transactions. Part III discusses possible justifications for legal intervention. Part IV analyzes the prospective effectiveness of different types of intervention. The Conclusion evaluates the prospects and limitations of our framework.

I. The Psychology of the Debtor

Consumer behavior and decision making can be explained by various psychological approaches, among them an approach focusing on cognitive processes. In this Article we are particularly interested in cognitive processes that lead consumers to behave in ways that result in borrowing, debt, failure, and bankruptcy.

To date, legal scholars have been concerned with the effects of cognitive biases and heuristics and their potential effects on legal policy. This section will discuss, in addition to these, two other areas that we believe are relevant for understanding the processes that can lead consumers into bankruptcy. The first is the social influence literature, which focuses on the ways in which one individual can affect the state of mind and behavior of another individual. This literature will also serve as a basis for our discussion of advertising and marketing in the second section. The second area deals with lifecycle models. This body of literature analyses the ways in which individuals manage, and should manage, consumption, debt and savings over their lifecycles.

A. Biases and Illusions

Although psychologists have observed a wide range of biases and heuristics, we will discuss those which mainly influence consumers to believe that negative life events that could lead to insolvency will not happen to them. These are optimism bias and the illusion of control.[2]

1. Optimism Bias

Neil Weinstein was the first to label the phenomenon of optimism bias based on empirical studies.[3] He asked a diverse group of students, "Compared to other students of the same sex at your college, what do you think are the chances that the following events will happen to you?" He then listed forty-two life events. Each event could be clearly classified as either positive (eighteen events including "will like my job," "will own a house," "will have a high starting salary," "will not be hospitalized in five years") or negative (twenty-four events including "will have drinking problems," "will get divorced," "will have a heart attack before age forty," "will be fired," "will drop out of college"). There were no preconditions for any of the events that could make them inapplicable to any of the students.[4] The students were asked to choose whether the probability that each event would occur to them was above average, average, or below average.[5] The results showed that the mean comparative judgment of one's own chances versus others' chances was above

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2 Other relevant biases that we will not discuss include belief perseverance (the tendency of a person to stick to her original hypothesis or explanation after one is constructed) and confirmatory bias (the use people make of additional information presented to them to support and strengthen their beliefs). Both of these biases lead to a more general phenomenon known as motivated reasoning (the tendency of people to utilize a variety of cognitive mechanisms to arrive at the conclusion they desired all along). Some heuristics that are often mentioned: the availability heuristic (giving weight to information that is easily brought to mind, such as past experience of yourself or your acquaintances, or information that is presented dramatically, instead of statistical data); the representativeness heuristic (the tendency to make judgments based on the resemblance to a scheme or stereotype), and anchoring — people's tendency to make judgments according to an initial value.

3 Neil D. Weinstein, *Unrealistic Optimism about Future Life Events*, 39 J. Personality & Soc. Psychol. 806 (1980).

4 Events such as "will be injured while skiing" were excluded.

5 Above average (choices ranged from 10% to 400% above the general probability), average (no deviation from the general probability), or below average (10% to 100% below the general probability). To clarify: the students could be told that 2% of the students in the group would be involved in a car accident. When asked what the probability was that they personally would be involved in an accident they were

average (I am more likely to enjoy these events than others) for fifteen of the eighteen positive events, and below average (I am less likely to suffer these events than others) for twenty-two of the twenty-four negative events. The participants clearly could not all be correct.

Weinstein viewed this bias as a social phenomenon that resulted from systemic cognitive errors, rather than from personality or cognitive dissonance. He thus integrated this bias into the growing literature on biases and heuristics that had been developed in the 1970s by Tversky and Kahneman.[6]

Two-and-a-half decades and dozens of studies later, optimism bias is considered one of the most robustly-confirmed biases in cognitive studies and social psychology. Studies have overwhelmingly confirmed the existence of optimism bias with respect to an array of events, social groups, and localities. The studies have disagreed about the causes of the bias, its moderators, and its magnitude. They studied the effects of several factors: perceived controllability, the frequency of the event, prior experience, cultural factors, mood and anxiety, and the framing of the questions, among others.[7]

The initial application of optimism bias was in the area of health risks and addictions. These issues bordered on consumer decision making. A central aim of the research was to explain why consumers consumed cigarettes and alcohol to the extent they did. The research was intended to direct policymakers who aimed to protect health by changing habits, and to educate toward adopting risk-reducing precautions. The policy agenda soon expanded to legal issues. Here the question was how should over-optimism and its utilization by manufacturers, affect the law that governs product

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given a few choices: 2% (no deviation), 0% (100% below average), 4% (100% above average) and 10% (400% above average).

6 Judgment Under Uncertainty: Heuristics and Biases (Daniel Kahneman et al. eds., 1982); Choices, Values and Frames (Daniel Kahneman & Amos Tversky eds., 2000).

7 For some recent studies, see Mary Helweg-Larsen & James A. Shepperd, *Do Moderators of the Optimistic Bias Affect Personal or Target Risk Estimates? A Review of Literature*, 5 Personality & Soc. Psychol. Rev. 74 (2001); Paul C. Price et al., *Perceived Event Frequency and the Optimistic Bias: Evidence for a Two-Process Model of Personal Risk Judgments*, 38 J. Experimental Soc. Psychol. 242 (2002); Cynthia T. F. Klein & Mary Helweg-Larsen, *Perceived Control and the Optimistic Bias: A Meta-Analytic Review*, 17 Psychol. & Health 437 (2002); Edward C. Chang et al., *Cultural Variations in Optimistic and Pessimistic Bias: Do Easterners Really Expect the Worst and Westerners Really Expect the Best When Predicting Future Life Events?*, 81(3) J. Personality & Soc. Psychol. 476 (2001); Geeta Menon et al., *We're at as Much Risk as We Are Led to Believe: Effects of Message Cues on Judgments of Health Risk*, 28 J. Consumer Res. 533 (2002).

liability and regulation? The extent of the legal liability of the tobacco industry for damage to smokers' health was a major issue.

In the next stage, the effects of optimism bias on the consumption of credit were analyzed. As students were usually the participants in studies of over-optimism it will not come as a surprise that the effect of the bias on student borrowing was a favorite topic.[8] Students believed that they were likely to earn above the average college graduate's salary, not to suffer accidents or illnesses, and to be able to repay their loans in full before they were due. The bias was found to affect their decision making: "Their financial optimism was significantly linked to borrowing behavior. These results suggest that over-optimism may be a factor in the accumulation of student debt."[9] The most recent step in this direction was the application of over-optimism to the study of the credit card industry and bankruptcy policy.[10]

2. The Illusion of Control

Another bias is what Ellen J. Langer called the illusion of control.[11] Langer showed that people behave as though chance events were subject to control and that they do not distinguish chance from skill-determined events when engaged in behavior that involves some element of control, such as choice. In one of Langer's experiments, participants purchased a lottery ticket for $1; some participants could choose their ticket and others could not; they were then asked at what price they would sell the ticket. The results showed that the choice manipulation had a considerable effect on the value of the tickets. The average price of tickets that were chosen in advance was $8.67, while the average for the no-choice tickets was $1.96. The large difference between prices offered by participants was due only to the choice element in the experiment.

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8 Hamish G. Seaward & Simon Kemp, *Optimism Bias and Student Debt*, 29 N.Z. J. Psychol. 17 (2000); Stephen E.G. Lea et al., *Student Debt: A Psychological Analysis of the UK Experience*, *in* Frontiers in Economic Psychology 1, 430 (Ellen Nyhus & Sigurd V. Troye eds., 1995); Saul Schwartz, *Personal Bankruptcy Law: A Behavioural Perspective*, *in* Consumer Bankruptcy in Global Perspective 61 (Johanna Niemi-Kiesiläinen et al. eds., 2003).

9 Seaward & Kemp, *supra* note 8, at 19.

10 Norman I. Silber, *Observing Reasonable Consumers: Cognitive Psychology, Consumer Behavior and Consumer Law*, 2 Loy. Consumer L. Rev. 69 (1990); Schwartz, *supra* note 8; Oren Bar-Gill, *Seduction by Plastic*, 98 Nw. U. L. Rev. 1373 (2004); Richard M. Hynes, *Overoptimism and Overborrowing*, 2004 BYU L. Rev. 127; Jason J. Kilborn, Behavioral Economics, Overindebtedness and Comparative Consumer Bankruptcy: Searching for Causes and Evaluating Solutions (June 2005) (Cegla Center conference paper), *available at* http://ssrn.com/abstract=690826.

11 Ellen J. Langer, *The Illusion of Control*, 32 J. Personality & Soc. Psychol. 311 (1975).

The illusion of control has been scrutinized in many experiments. It has been discussed by psychologists not only in relation to lottery games and gambling situations, which are clearly chance circumstances, but also with respect to activities such as share trading performance,[12] driving (the majority of individuals consider themselves more immune to accidents when they drive than when they sit next to the driver),[13] and food safety risk in home cooking (most people believe they control food safety in domestic food preparation).[14] The illusion may lead borrowers to believe negative life events that are in fact caused by exogenous factors to be within their control.

B. Life Events and Bankruptcy

What makes optimism bias and the illusion of control the most relevant biases for bankruptcy policy considerations is their demonstrated manifestation in the prediction of life events. The under-prediction of negative events and the over-prediction of positive events, or the over-appreciation of control over negative events, fits the causes of bankruptcy remarkably well. The most comprehensive empirical studies of bankrupts and bankruptcies available are those conducted by Elizabeth Warren, Jay Westbrook, and Teresa Sullivan.[15] These studies conclude that the main causes of bankruptcy are life events such as job loss, illness, accident, divorce, and the like. These crises affect income or expenses and disrupt the balance between the two. A medical crisis resulting from an accident or illness increases medical expenses, at least some of which are not covered by insurance. The same medical problem also lowers the consumer's ability to maintain a job and income. The same life events that over-optimistic or illusionary individuals do not believe could happen to them do in fact happen to some, driving them into bankruptcy. The fit between

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12 Mark Fenton-O'Creevy et al., *Trading on Illusions: Unrealistic Perceptions of Control and Trading Performance*, 76 J. Occupation & Organizational Psychol. 53 (2003).

13 Frank P. McKenna, *It Won't Happen to Me: Unrealistic Optimism or Illusion of Control?*, 84 Brit. J. Psychol. 39 (1993).

14 Elizabeth C. Redmond & Christopher J. Griffith, *Consumer Perceptions of Food Safety Risk, Control and Responsibility*, 43 Appetite 309 (2004).

15 *See* Elizabeth Warren, Jay Westbrook & Teresa Sullivan, As We Forgive Our Debtors: Bankruptcy and Consumer Credit in America (1989); Elizabeth Warren, Jay Westbrook & Teresa Sullivan, The Fragile Middle Class: Americans in Debt (2000); Elizabeth Warren, Jay Westbrook & Teresa Sullivan, *Consumer Debtors Ten Years Later: A Financial Comparison of Consumer Bankrupts 1981-1991*, 68 Am. Bankr. L.J. 121 (1994).

the empirically-established biases and the empirically-established causes of failure is striking.[16]

C. Social Influence

Social influence, an area of social psychology, relates to the ability of individuals to influence and to be influenced by others. According to Forgas and Williams, "[a]ll forms of human interaction involve mutual influence processes, and these function at a variety of levels — cognitive, interpersonal and cultural,"[17] but there are others who refer to social influence in a more restrictive way, including only direct interpersonal influence such as social facilitation effects, conformity, obedience, and persuasion. The effect that social influence may have on advertising and market manipulation is exemplified by Robert Cialdini's research on automatic behavior.[18] Cialdini describes six fundamental types of influence that direct human behavior — consistency, reciprocation, social proof, authority, liking, and scarcity. Such types of influence can produce automatic, mindless compliance.[19]

One type of influence is demonstrated in an experiment performed by Ellen Langer, Arthur Blank and Benzion Chanowitz.[20] Langer, Blank and Chanowitz used different wordings to ask a favor of people standing in line to use a library copying machine. When they asked, "Excuse me, I have five pages. May I use the Xerox machine because I'm in a rush?" ninety-four percent of the people asked agreed. When they asked the question differently: "Excuse me, I have five pages. May I use the Xerox machine?" only sixty percent agreed. This result reflects the effectiveness of a request-plus-reason; people agreed to do a favor when a reason was presented. Interestingly, when Langer, Blank and Chanowitz did not present a real reason for their request,

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16 To be clear, Warren, Westbrook, and Sullivan did not argue that bankrupts failed because of their biases. Their research purposes and methodology did not touch upon biases. We are the ones to make this connection by linking two distinct bodies of literature.

17 Joseph P. Forgas & Kipling D. Williams, *Social Influence — Introduction and Overview*, *in* Social Influence — Direct and Indirect Processes 4, 4 (2001).

18 Robert B. Cialdini, Influence — the Psychology of Persuasion (1993).

19 Automatic compliance is the most extreme form of compliance with influence. There are other more moderate forms of positive response that are still relevant to our argument.

20 Ellen Langer et al., *The Mindlessness of Ostensibly Thoughtful Action: The Role of "Placebic" Information in Interpersonal Interaction*, 36 J. Personality & Soc. Psychol. 635 (1978). This Study was mentioned by Cialdini, basing one of his claims. Cialdini, *supra* note 18, at 4-5.

but only used the word "because" ("Excuse me, I have five pages. May I use the Xerox machine because I have to make some copies?"), ninety-three percent agreed. The use of the word "because" led people automatically to agree to the request, without thinking. This emphasizes the power of wording, which will be discussed further in the next Part.

One of Cialdini's principles is the rule of reciprocation: people tend to repay when they receive something from another person, even when the favor is unsolicited. For example, if a person sends us a birthday present or a greeting card, we tend to do something in return. In terms of marketing, this technique may be used to engage the consumer's compliance. Another manifestation of the rule of reciprocation is a situation where a person makes a concession; for example, offers a discount. In this case people feel obliged to act in a favorable way toward the person or firm that reduced the price, and this gesture may lead to an automatic reaction, without thinking about its consequences.

Another of Cialdini's principles is social proof: the tendency to view an action as appropriate when other people are doing it.[21] This provides individuals with a shortcut for determining how to behave without thinking about the consequences of the specific behavior in their specific life circumstances. People acting under such social influence believe that if most people take mortgages in order to buy a house, then this must be a reasonable action and they may not check carefully whether this long-term obligation suits them. One example of the use of social proof by advertisers is saying that a product is the "fastest growing" or "best selling." The fact that consumers think this way allows advertisers to bypass the need to convince them that the product is actually good for them.[22]

The weapons of social influence may divert credit consumers from thinking about various life events that could occur and influence their ability to pay their loans, thus leading to overindebtedness and eventually to bankruptcy. Nevertheless, the behavioral economics and the law and economics literature on bankruptcy has not taken influence literature into account. This is because influence has many forms; its effect can differ from one person to another, and it may change in different situations and circumstances. Its consequences are not as robust, systematic and predictable as the consequences of biases and heuristics.[23] We would like to

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21 Robert B. Cialdini, Influence — Science and Practice 100 (2001).

22 *Id.* at 101.

23 Feldman and MacCoun, in a recent article, argue for the relevance of the social influence literature to law and economics and to legal policy in general. *See* Yuval Feldman & Robert J. MacCoun, *Some Well-Aged Wines for the "New Norms"*

stress that we do not view influence literature and bias literature as mutually exclusive but rather as complementary. Consumers of credit may respond automatically, emotionally, or mindlessly. But even in situations in which they are operating cognitive thinking in full, when they act within the bounded rationality paradigm and consider the probability and effect of negative life events, cognitive biases, such as optimism bias and the illusion of control, may lead them to irrationally accept credit offered.

D. Lifecycle Models

Naïve theories of the consumption of credit assume that individuals and families borrow in order to smooth their consumption over the lifecycle.[24] They borrow when they are young, pay back their loans and save when they are in their prime in terms of earnings, and live on their savings after retirement. In order to achieve this smoothing, they need to calculate and decide how much to borrow, how much to save, and how much to consume at different points over the lifecycle. They are assumed to be unboundedly rational decision makers. They are assumed to have sufficient cognitive abilities to correctly perform the calculations involved.

However, lifecycle literature has exposed a large set of problems and difficulties.[25] The lifecycle planner has to account for the fact that he may have young children and other dependants at unknown points in time, and these will greatly affect his consumption and, as a result, his need for credit and his ability to save. He has to account for the fact that his tastes and preferences

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Bottles: Implications of Social Psychology for Law and Economics, *in* The Law and Economics of Irrational Behavior 358 (Francesco Parisi & Vernon L. Smith eds., 2005).

24 Such theories are presented in various textbooks. For one such example, see Robert J. Barro, Macroeconomics 91-132 (1997).

25 For some introductions to this literature, see David Laibson et al., *A Debt Puzzle*, *in* Documentos de Trabaju 80 (2000); David Laibson et al., Estimating Discount Functions from Lifecycle Consumption Choices, *available at* http://post.economics.harvard.edu/faculty/laibson/papers/EstimatingDiscountFunctions 16aug2005.pdf (Aug. 2004); Zhikang Chua & Colin F. Camerer, Experiments on Intertemporal Consumption with Habit Formation and Social Learning, *available at* http://www.hss.caltech.edu/~camerer/savingsjpe7.doc (Apr. 2006); Shane Frederick et al., *Time Discounting and Time Preference: A Critical Review*, 40(2) J. Econ. Literature 351 (2002); Christopher J. Harris & David Laibson, *Hyperbolic Discounting and Consumption*, *in* 1 Advances in Economics and Econometrics: Theory and Applications, Eighth World Congress 258 (Mathias Dewatripont et al. eds., 2002).

for the consumption of goods and services are likely to change. Part of this change may result from exogenous introduction of new technologies. Some may result from the formation of new social norms, from learning, or from personal habits formed by becoming accustomed to previous consumption. Future fluctuation in the prices of consumer goods, including house prices, is likely to affect consumption. Consumption may be affected by negative life events, such as illness, that can have dramatic implications on the consumption of healthcare. Advanced planning of lifecycle credit and savings relies heavily on the estimation of future earnings. These are also affected by positive life events such as promotion, and negative ones such as illnesses, accidents and job loss. Life expectancy is also important data for planning lifecycle credit. In recent years behavioral economists have recognized the immense problems involved in the choices that individuals have to make with respect to their lifecycles. Two of the main problems identified are computation and biases.[26]

The computational task of a fully-rational and fully-informed individual wishing to plan his lifecycle consumption, borrowing, and saving, is immense. That individual has to take into account a variety of uncertainties, and deal with a variety of risks and a large set of data. The lifecycle literature now also accepts the fact that hyperbolic discounting, rather than exponential discounting, empirically reflects the genuine preferences of many, if not all, individuals. A hyperbolic discounter does not discount future payments based on a constant interest rate, but rather based on a changing one.[27] This type of discounting adds another complication to the calculative tasks of the individual attempting to prepare his lifecycle plan. Making lifecycle calculations using hyperbolic discounting is extremely complicated mathematically. Brilliant economists using powerful computers have to invest a great deal of time to integrate hyperbolic discounting formulas into their models. When complications such as risk and uncertainty about future adverse events, payoffs, interest rates, costs of living, and the like, are added, the problem of managing one's lifecycle becomes an impossible task. The task is impossible because of the bounded rationality of the individual in its most basic computational sense.

26 Another is often called the multiple selves. when we are twenty-five we decide to start saving for retirement at thirty, when we are thirty we decide to start saving only at thirty-five. We may commit ourselves irrevocably at twenty-five to start saving at thirty. But by the time we reach thirty this commitment will contradict our genuine preferences. We will not enter here the discussion in economics and philosophy of the inconsistency of preferences over time.

27 A hyperbolic discounter may prefer to receive $100 in a year over $140 in two years, but $120 in seven years over $100 in six years.

While the computational errors that result from the bounded rationality of individuals with respect to their lifecycles do not necessarily lead to overborrowing, and may even lead to underborrowing, the optimism and illusion of control biases of these same individuals are unidirectional and can lead only to overborrowing. These well-established biases of consumers are clearly reflected in the context of lifecycle decisions. Even when credible information about probabilities of negative and positive life events is available to an individual wishing to plan his lifecycle, that individual will process the information in a systematically biased way that may lead him to overconsume credit and undersave. The probability of financial default and bankruptcy increase in such situations. The findings of Warren, Westbrook, and Sullivan fit the prediction of behavioral lifecycle theorists and the results of empirical studies conducted by lifecycle scholars.[28]

We can conclude from the above psychological and empirical analysis that the fact that consumers end up insolvent does not necessarily indicate their intention to do so. One cannot attribute fault, or even negligence, to a consumer who could not meet the complicated, even impossible, task of optimizing utilities over the lifecycle. When taking into account biases and social influence, one would expect systematic mistakes, leading, among other things, to higher indebtedness of most individuals. These insights can serve as a basis for discussion of the need for intervention and for a rethinking of bankruptcy policy, that will follow in Part III.

II. ADVERTISING AND MARKET MANIPULATION

The cognitive processes illustrated above are known not only to psychologists but also to lenders of credit. Through marketing techniques and especially advertising, lenders of credit take advantage of consumers using persuasion and manipulation.[29]

In our context, we refer to Daniel O'Keefe's six common features of persuasion: (1) a successful attempt to influence; (2) the presence of a criterion or a goal set by the persuader; (3) intent to reach that goal; (4) some measure of freedom on the persuadee's part, otherwise the case would be one of a "done deal" in which persuasion is not involved; (5) the effects of persuasion are achieved through communication; and (6) a change in

28 *See* sources cited in *supra* note 15.

29 Persuasive communication research is one of the main aspects of social influence research. *See* Forgas & Williams, *supra* note 17.

the mental state of the persuadee.[30] All six features of persuasion, as listed by O'keefe, are evident in the advertisement process. Advertisers attempt to influence the consumer by changing her mental state, achieving the goal set before the persuader — acceptance of the offer, or even a more indirect modest goal, such as raising the credibility of the persuader. The effect is achieved through mass media communication — newspapers, television, and recently, the Internet. There are other means of communication used by advertisers, such as direct marketing, event planning, and personal selling, including door to door selling and telemarketing, that will not be discussed in this article.

Based on O'Keefe's features we define manipulation, in our context, as an act that looks as if it constitutes an intention by the lender to lead a consumer to borrow, while trying to persuade her to reach a decision that is not based on her genuine (non-biased) preferences, through exploitation of one or more of the following: biases and illusions, heuristics, inability to perform complex calculations, lack of relevant information, or a state of mind in which not enough cognitive resources are allocated to the decision. Persuasion does not amount to manipulation when it does not exploit these weaknesses of the borrower. However, manipulation is constituted irrespective of whether the lender fully intends to manipulate or is fully aware of the cognitive processes that allow manipulation.[31]

Jon Hanson and Douglas Kyser argue that "consumers . . . are susceptible to manipulation by manufacturers due to their cognitive anomalies. This susceptibility to manipulation produces an opportunity for exploitation that no profit-maximizing manufacturer can ignore."[32] In a series of articles, Hanson and Kyser explore behavioral research and consumer behavior studies,[33] and exemplify the ways in which manufacturers manipulate consumers' perceptions. A large part of their argument refers to advertising. In this section we will discuss some of the advertising techniques used by advertisers and show how the psychological processes

30 Daniel J. O'Keefe, Persuasion — Theory and Research 15-16 (1990).

31 Our definition does not deal with persuasion and manipulation that do not relate directly to borrowing. We are aware of the fact that manipulation with respect to consumption of goods and services may lead to additional borrowing even when there is no manipulation by the lender. Parts of our discussion may be relevant to such manipulations. However, they are beyond the scope of the present Article.

32 Jon D. Hanson & Douglas A. Kyser, *Taking Behavioralism Seriously: The Problem of Market Manipulation*, 74 N.Y.U. L. Rev. 630, 722 (1999).

33 These are two areas of study which developed separately but address very similar situations.

of social influence and biases are utilized by advertisers. We believe that this manipulation amplifies the need to rethink bankruptcy policy.

The aim of advertisers is to persuade and manipulate the consumer to enter a deal or to purchase merchandise.[34] As Pratkanis and Aronson have stated, "[e]very day we are bombarded with one persuasive communication after another. These appeals persuade not through the give-and-take of argument and debate but through the manipulation of symbols and of our most basic human emotions. For better or worse, ours is an age of propaganda."[35] The art of advertisement persuasion has been studied and taught in thousands of articles, books and lectures since the beginning of the 20th century.[36] It is based on numerous experiments and studies that tested the effects of persuasive communication. Researchers agree that advertising affects the consumer's decision making process. As Larson noted, "[t]he most dominant, and perhaps the most effective, forms of persuasion in contemporary culture are print and electronic advertising."[37] It is unlikely that billions of dollars would be spent on advertising manipulation if it did not work.[38]

How do advertisers manipulate consumers to purchase merchandise or to enter into a financial transaction? Various articles and books have addressed this question.[39] We will discuss a number of studies (most relating to credit) in an attempt to illustrate the wide use of cognitive processes by advertisers. Three techniques will be discussed: wording, framing, and self image models. All attempt to utilize social influence and take advantage of the biases presented above.

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34 *See* Anthony Pratkanis & Elliot Aronson, Age of Propaganda: The Everyday Use and Abuse of Persuasion (1991); Michael Pfau & Roxanne Parrott, Persuasive Communication Campaigns (1993).

35 Pratkanis & Aronson, *supra* note 34, at 5-6.

36 *See, e.g.*, Henry F. Adams, Advertising and its Mental Law (1916); Walter D. Scott, The Psychology of Advertising (1917); O'Keefe, *supra* note 30, at 14.

37 Charles U. Larson, Persuasion — Receptions and Responsibility 338 (2001). *See also* Advertising, Exposure, Memory and Choice (Andrew A. Mitchell ed., 1993); Max Sutherland & Alice K. Sylvester, Advertising and the Mind of the Consumer (2000); Cialdini, *supra* note 18; Cialdini, *supra* note 21; William Wells et al., Advertising: Principles and Practice (1995); S. Watson Dunn, Advertising: Its Role in Modern Marketing (1969).

38 Jon D. Hanson & Douglas A. Kyser, *Taking Behavioralism Seriously: A Response to Market Manipulation*, 6 Roger Williams U. L. Rev. 259, 284-85 (2000).

39 *See supra* note 36; In addition, hundreds of articles on mechanisms of advertisement were published in various journals including: Journal of Consumer Psychology; Journal of Marketing Communications; Journal of Consumer Research; Psychology and Marketing; Journal of Advertising; Journal of Economic Psychology; Journal of Marketing; Applied Cognitive Psychology.

A. Wording

A study conducted in 1988 exemplifies the importance of message wording in the consumer's attitude toward the consumption of ground beef. Consumers preferred beef that was labeled "75% lean" to beef labeled "25% fat."[40] Other studies demonstrate that some words, such as "fresh," "strong" and "freedom," lead to positive thoughts and that these thoughts may have an important effect on how the product is conceptualized and encoded.[41] Thus, the words "you will succeed," used in the Israeli bank campaign presented in the Introduction to this Article, have a positive connotation. Another example of wording technique can be seen in an Internet ad that offers a UK credit card. The ad opens with a question to consumers: "Need a UK credit card?" This is followed, in the center, by the words: "We'll say *YES* if you do. We promise."[42] The words "we promise" send a positive message to the consumer who is searching for credit, and may well influence his or her decision to sign a contract with the credit card company, on the spot, directly through the Internet. Another example of wording is the advertisement by an American loan center — Nellie Mae — which offers, among other things, student loans. In one of its ads, the loan center makes the following statement: "The most common student loan, a Federal Stafford Loan, offers the money you need, a super low rate, and no payments until you're out of school. *And with Nellie Mae, you can earn 3.3% cash or credit back!*"[43] Can you really earn by taking out a loan? Of course not, but the word "earn" leads to such a positive response in the credit market that consumers will not miss a chance at least to check out the loan offer presented by Nellie Mae, even if they had not intended to do so in advance.

The wording technique is a good example of social influence. It is used by advertisers to manipulate consumers and cause them to ignore problematic outcomes that may arise in the future, such as lack of ability to repay a loan. The bank ad also utilizes the optimism bias — the belief people have that

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40 Irwin P. Levin & Gary J. Gaeth, *How Consumers are Affected by the Frame of Attribute Information Before and After Consuming the Product*, 15 J. Consumer Res. 374 (1988).

41 Alice M. Isen, *The Influence of Positive Affect on Cognitive Organization: Some Implications for Consumer Decision Making in Response to Advertising*, *in* Advertising, Exposure, Memory and Choice, *supra* note 37, at 249.

42 Debtbuster Loans, http://www.useyourbrain.co.uk/credit-cards/debtbuster-loans.htm (last visited May 23, 2005).

43 Nellie Mae, Loan Center, http://www.nelliemae.com/loancenter/ (last visited May 23, 2005). This example is brought in order to demonstrate the wording technique.

negative life events that could influence their ability to repay the loan will not happen to them.

B. Framing

In one of Kahneman and Tversky's most famous experiments,[44] they asked participants to choose between two options in one of two sets. The first set was a choice between a program that would save two hundred people out of six hundred and a program in which there is a one-third probability that six hundred people will be saved and a two-thirds probability that no one will be saved. The second set was framed the other way around: four hundred people will die or there is a one third probability that no one will die and a two-thirds probability that all six hundred will die. The choices offered in the two sets differed; yet in both cases, the preference was for the more "positively" framed option. In the first set there was a prominent preference for choice A, and in the second set, for choice B.

The framing effect identified in Tversky and Kahneman's experiment has also been studied in the area of advertising. Research shows that the framing of an ad has a major effect on consumer decisions, and this framing is entirely in the hands of the advertiser. For example, consumers tend to purchase goods tagged with a flat fee, even in situations where the flat fee is not favorable to them. In that sense, framing the ad in a specific way may lead more people to enter the deal. Thus, telephone companies offer their customers fixed monthly payments or free airtime at specific hours or to specific phone numbers. The consumers believe that they will use the phone enough and justify the price. This is not always the case. Nevertheless, consumers continue to join flat fee programs because it is very difficult for them to estimate future usage in advance.[45] Companies take advantage of this tendency and offer fixed price deals in numerous ads. They even frame their payment offer in this way in situations where the price is far from flat. For example, most cellular phone companies in Israel advertise their merchandise by offering the consumer a small fixed payment for a phone: "Get a phone for X shekels a month." At the bottom of the ad, in small print, they mention that this is the minimal payment and that additional calls will lead to additional charges. A consumer who sees the flat fee offer presented in the ad tends to ignore or pay little attention to the small print,

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44 Daniel Kahnman & Amos Tversky, *Choices, Values and Frames*, 39 Am. Psychologist 341, 343 (1984).

45 Tali Freedman, The Psychology of Advertising 120-24 (2002) (Hebrew).

and may be persuaded by such ads. This strategy is not an Israeli invention; it is used in advertisements worldwide. One example is the advertising of "Infonex — the world's internet phone company." This company's website posts the following offer: "Unlimited calling to the USA and Canada $19.95 per month."[46] If consumers read the ad closely, they learn that this price is relevant only in some situations and does not include, for example, calls to cellular phones. The flat fee offered is far from flat. The cellular phone consumer, persuaded by the flat fee offer, signs a contract with the phone company that is similar to credit transactions, especially in regard to the long term obligation for payments. This is another example of social influencing of consumers; it can also be viewed as exploitation of the illusion of control, since the consumer believes she can control her extra spending above the flat fee price, not a very easy task.

C. Self-Image Models

How do you see yourself? What are your characteristics? These two questions lead advertisers in their search for the person whose picture will be placed in an ad. If the ad targets the macho smoker, then the Marlboro Cowboy will do; if it targets a housewife, a student, or a young person starting out — the model chosen should meet their needs. Advertisers are aware of the fact that they are trying to sell consumers a self-image. According to Pratkanis and Aronson, "[w]e hold our beliefs and attitudes in order to define and make sense of our *selves*. By shaving with the right razor or eating the right cereal, we are saying 'I am just like that ballplayer; I am part of the attractive in-group.'"[47]

* * *

The tactics mentioned above, and many others, are used to achieve one goal — to persuade consumers and often to manipulate them into entering credit transactions. They do this by triggering and exploiting cognitive processes. We believe that this manipulation should be taken into consideration by the legal system when it addresses bankruptcy policy.

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46 Inphonex, Basic Membership, http://www.inphonex.com/products/basic.php (last visited May 23, 2005).

47 Pratkanis & Aronson, *supra* note 34, at 93.

III. JUSTIFICATION FOR LEGAL INTERVENTION

In the previous sections we saw that advertisers manipulate consumers into taking on credit, basing their strategy on heuristics and biases, mainly the optimism bias and the illusion of control, on social influence and on computationally bounded rationality.[48] When this is the case — can legal intervention be justified? The discussion here is based on a handful of earlier works that ask whether optimism bias in itself justifies intervention. It carries the discussion a step further by reexamining justifications based on biases and adding justifications based on manipulation. This issue is addressed on three levels: that of the individual debtor, that of the bilateral relationship between the debtor and a single creditor, and that of society at large.

A. Debtors' Autonomy and Fault

Respect for the autonomy and genuine preferences of borrowers calls for intervention in the face of biases and manipulation. The only challenge in this respect is distinguishing between a genuine preference to borrow more, even at the risk of default, and borrowing that results from biases and manipulation. This challenge is only apparent when the intervention is aimed at consumer decision making and not when it is aimed at the manipulating act, the credit market, or the creditors.

We cannot attribute to borrowers the intention to over-borrow, to the extent that the over-borrowing resulted from a socially widespread optimism bias or from the illusion of control. Their decision was not fully rational. If they could not easily debias themselves, we should not attribute fault to them simply because they were overly optimistic. The intention to avoid repaying debts, to become insolvent, to resort to bankruptcy, and to discharge debts, cannot be attributed to them, insofar as these resulted from the overborrowing that resulted from the biases. The contribution of manipulation to overborrowing only adds to the above conclusion. If lenders manipulatively persuaded borrowers to borrow more than they had originally intended, then the fault on the part of borrower-debtors would be further reduced and that of lenders would increase.

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48 In this section and the next when we mention biases we are referring to all of these deviations from full rationality as one package, unless we expressly justify intervention based on only one of them or prescribe modes of intervention that address only one of them.

Intervention can be justified based on considerations of restoring rational decision making, maintaining autonomy, lack of fault on the part of debtors, or possible fault on the part of creditors. Such considerations may be given priority over efficiency considerations if the two are in conflict, though as we will show below, we doubt the existence of such a conflict.

B. Distribution Between Creditors and Debtors

1. Creditors' Gains

Is there a distributive consequence to borrowers' biases? Do lenders benefit from the biases of borrowers? At first — naïve — sight, lenders lose by extending credit to borrowers who cannot repay them. This section will show that lenders can benefit from the bias and gain from its manipulation.

We have already seen that optimism bias affects borrowers. It does not, however, affect repeat institutional lenders. Lenders are aware of the life events statistics of the population at large, of various subgroups, and of their borrowers in particular. In many systems, they also have access to the credit history of their potential borrowers. They can refuse or limit lending to over-optimistic borrowers or offer them higher interest rates on loans. In fact, they not only lend money but also actively persuade and manipulate over-optimistic borrowers to consume more credit.

We will use two examples of sectors shown in Part II to have actively persuaded consumers to borrow more. The purpose of these examples is to show that firms in these sectors target low-income consumers, persuading them to increase their debt-to-income ratios. The expected result, increase in default, is then manifested. Yet, the persuasion strategy continues, and these firms and the sector as a whole profit. We will begin with the credit card industry in the US and move to the cellular telephone sector in Israel.

Industry studies of the credit card industry in the US indicate that the industry is willing to market and extend more and more credit to low-income borrowers. The total consumer debt of low-income families (earning less than $50,000 a year) in the US rose from $256 billion in 1983 to $437 billion in 1992. The percentage of the total consumer credit extended to families whose income (in 1992 dollars) was less than $50,000 rose from 42% to 56%.[49] Some scholars consider the new marketing strategy to be a leading explanation for the dramatic rise in the number of bankruptcies in the US over

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49 David A. Moss & Gibbs A. Johnson, *The Rise of Consumer Bankruptcy: Evolution, Revolution, or Both?*, 73 Am. Bankr. L.J. 311 (1999); Lawrence Ausubel, *Credit Card Default, Credit Card Profits, and Bankruptcy*, 71 Am. Bankr. L.J. 249 (1997).

the last two decades.[50] However, this strategy does not seem to have led a large and increasing number of credit card companies to bankruptcy. We do not aim here to provide a full-scale explanation for the performance and profits of the credit card industry.[51] We will suggest ways by which credit card companies can increase profitability by marketing credit to low-income borrowers whose income-to-debt ratio is low and probability of failure is high.

Marketing of credit to low-income families caused the total consumer debt to rise, and thus the revenues of credit card companies from interest payments grew, even irrespective of a rise in interest rates. The risk premium embedded in real interest rates rose due to deregulation and declining inflation. By raising interest rates, lenders distributed the growing risk of bankruptcy among their low-income borrowers. They also expanded the generation of revenues from hidden fees such as late and over-limit fees. These were sometimes hidden in lengthy standard form contracts without being fully disclosed in advertisements. But even if such fees are disclosed today, due to stricter regulation, over-optimistic borrowers, those with imperfect self-control, or forgetful borrowers, may believe that the fees will not apply to them.[52] These factors taken together may lead to situations in which credit card companies profit from low-income card holders, even if a relatively large percentage of these card holders end up bankrupt. This may lead companies to prefer over-optimistic borrowers. It may further lead them to manipulate and enhance optimism biases of potential debtors, as demonstrated in Part II.

Similarly, after achieving high penetration rates among high- and middle-income consumers, cellular telephone companies in Israel turned to low-income consumers. In recent years they have been marketing aggressively among teenagers, students, and various low-income segments of society. They offer "free phones" to customers willing to commit to a three-year

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50 Ausubel, *supra* note 49. The rise in proportion of unsecured debts compared with secured debt among low-income families was also offered by Moss & Johnson, *supra* note 49, as part of the explanation.

51 In this section and the next we will focus on the credit card industry. Credit card debt comprises a significant part of consumer debt in the US. As an industry that is based on unsecured debt and that extends credit to new entrants, this industry serves as a good case for examining the unsubstantiated hypothesis that optimism bias may benefit debtors at the expense of creditors. This industry is highly visual in public debate, in studies of causes of bankruptcies and, as such, has been well-studied. The analysis offered here is applicable to other types of unsecured debt that are marketed by financial institutions and banks to consumers, such as personal unsecured loans and lines of credit. In Israel, for example, lines of credit together with debit cards perform a function quite similar to that of credit cards in the US.

52 Bar-Gill, *supra* note 10, at 1393-94, 1399-1401.

contract. Not surprisingly, the percentage of low-income customers who fail to perform on these long-term contracts is high. Altogether some 100,000 debt collection files by the cell phone companies against their customers are now open.[53] The companies nevertheless showed high profits in recent years. They achieved this first and foremost from low-income customers who do pay their fees, at times with very high interest; and additionally through other activities, such as cross subsidy from higher-income customers and risk-spreading among low-income customers by way of higher rates. They may also benefit from network effects: attraction of new customers, due to the mere size of the network, calls made by high-income customers to low-income customers, and more. Again, as in the credit card case, the cellular phone companies rationally manipulate optimistically-biased consumers in a manner that can only be explained as advancing the ends of these companies. Companies that act rationally (and it is assumed that these companies are rational players, at least much more so than the debtors) would have not acted this way if it wasn't to their benefit.

2. Debtors' Gains?

Do debtors lose due to the fact that they are over-optimistic and are being manipulated? At first blush it appears that they gain. Debtors' wealth is increased when they borrow more and this allows them to consume more. The effect of over-optimism about life events in the context of consumer credit is quite different from its effect in the context of smoking or other dangerous activities. It does not couple immediate pleasure with a longer-term increase in probability to bodily harm. Yet, it increases the probability of bankruptcy. Insofar as one views bankruptcy as detrimental to debtors, the increase in probability is disadvantageous to them. Bankruptcy is detrimental in that it leads to the loss of assets and future earnings, it generates a social stigma and it creates a negative credit history that limits access to future credit. Bankruptcy is also detrimental to debtors due to the unpleasant legal procedure involved. In some bankruptcy systems, debtors have to pay their future earnings to their creditors, their motivation to work vanishes, and they may, as a result, give up or lose their jobs, their houses, and even their freedom.

Some scholars view bankruptcy discharge, particularly swift and automatic discharge as offered in the US by Chapter 7 and in Britain by the

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53 Israel's population is nearly 6.9 million, of which nearly two million are below the age of fourteen. Roughly one in every fifty Israelis over the age of fourteen is subject to debt collection procedures by a cellular telephone company.

Enterprise Act, as an insurance policy against the loss of future earnings. If debtors are indeed fully insured, a moral hazard is created. Debtors' *ex ante* awareness that they will be able to discharge their debts causes them, so it is argued, to borrow more and consume more. They have no incentive to avoid failure.[54] Yet this interpretation involves several nontrivial assumptions. First, it assumes that debtors are fully aware of the legal options offered to them by bankruptcy laws. Second, it assumes that the monetary and non-monetary damage caused to debtors in the bankruptcy process are non-existent or lower than the gains. Third, it ignores post-bankruptcy effects, such as the resulting credit history that limits access to credit, and the legal prohibition on frequent repeat discharge. It doesn't fully account for the fact that lenders, when deciding whether or not to extend credit, are aware of the discharge option.

The bottom line of this analysis is that wealth is transferred systematically from one type of party to the credit transactions, the debtors, to the other, the creditors. This results from the fact that creditors have the ability to manipulate due to the fact that they are large institutional players, they have superior information due to the fact that they are repeat players, and they are not as biased as debtors are. All of these factors justify balancing intervention.

C. Externalities

In this section we will demonstrate not only the existence of externalities in bankruptcy but also the manner by which optimism bias and the illusion of control and their manipulation enlarge these externalities. A convincing case for the effect of the biases and their manipulation on externalities is the basis for the justification of intervention aimed at internalizing these externalities.

As over-optimism and the illusion of control lead to a higher level of indebtedness by consumers, by way of an increase in the income-to-debt ratio, they increase the likelihood of default. As default leads to bankruptcy and to resulting externalities, externalities are increased by optimism bias. Externalities can be borne by society at large through the welfare state. If bankruptcy rules allow creditors to deprive their debtors of essential assets such as their household equipment, cars, and even homes, as well as their future income, these debtors will turn to the welfare state for support. Even if some of the bankrupts' assets are exempt, part of their salary is

54 Hynes, *supra* note 10.

protected against garnishment, and they can, at some point in time, get a discharge, the externalities are reduced but not necessarily eliminated. The extent of externalities is also determined by the nature of the welfare state. Externalities are higher in countries in which welfare benefits, in the form of social security, negative taxation, and services in kind, are higher. Bankruptcy in a state that accommodates homeless persons at its cost will result in higher externalities than bankruptcy in a state that does not provide the homeless with even basic shelter. Bankruptcy in a legal system that does not define residences as exempted assets will lead to higher externalities than bankruptcy in a system that does. Terms of discharge, the extent of asset exemption, and the level of welfare benefits are all factors in the level of externalities.[55]

Another form of externality is the cost to the state of running the bankruptcy process. When costs are not fully carried by the parties, either because fees are not priced at real cost or because the costs are placed on the bankrupt's estate and this turns out to be worthless, externalities occur. These costs to the state of running the bankruptcy process are financed by taxes.[56]

Externalities can be borne by family members of the debtors. Typically, bankruptcy of a debtor will affect his or her dependants. The bankrupt's children may lose their home, deteriorate educationally, and end up without full medical insurance. They will lose their familiar childhood environment. The debtor's spouse, often a woman, is likely to go through a similarly degrading process. Further, the debtor's relatives may come to his rescue by paying back some of his debts. Debt in liberal legal systems is the individual responsibility of the bankrupt debtor. Collective liability is not the rule. Thus, such assistance to optimistically-biased debtors who were manipulated by their lenders should also be viewed as an undesirable externality.

Lastly, externalities can be borne by other creditors. A lender who manipulated his borrowers into overindebtedness may as a result lead them

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55 See Richard M. Hynes, *Non-Procrustean Bankruptcy*, [2004] 2 U. Ill. L. Rev. 301, 340-42, for an argument that in the US externalities should not justify generous debt relief. But each country requires individual analysis of the extent of externalities. It is likely that externalities are higher in European welfare states than in the US.

56 The state is expected to maintain public order and protect property rights as well as to enforce contracts. The provision of these to the public is not considered in economic theory to constitute externalities. However, in our view, the enforcement, not only at the contractual level but also at the bankruptcy level, of loans that borrower-debtors accumulated due to their cognitive biases that were manipulated and exploited by their lender-creditors, should be classified as externalities.

into bankruptcy. The accumulation of debts owed to this creditor may cause failure to pay all other creditors. Furthermore, it increases the manipulative creditor's share of the total debt owed. Thus, it decreases the share of other creditors in the distribution of the bankrupt's assets or flow of future income.

IV. Modes of Intervention

Now that we, the wise scholars, are aware of the biases, illusions, and cognitive limits of credit consumers, why can't we just share the news with the consumers of credit? This would be the most direct and least intrusive form of intervention. Indeed, several studies, discussing the effects of behavioral theory and consumer decision making, reach the conclusion that the best way to intervene is by educating consumers or debtors. In their book, *Age of Propaganda*,[57] Pratkanis and Aronson aim do just this. They state that they "wrote this book because we passionately believe that . . . it is important . . . that Americans become informed about these devices, the psychological dynamics of what makes them effective, and how to counteract their effectiveness without withdrawing into abject cynicism."[58] Sutherland and Sylvester set themselves the same goal in their book, *Advertising and the Mind of the Consumer*.[59]

However, empirical studies of the potential effectiveness of debiasing, as well as actual, unsuccessful debiasing campaigns aimed at consumers of tobacco products, alcohol, and gambling show that the task is far from trivial. In the following discussion we will consider some modes of intervention that are aimed at biased consumers and others that are aimed at manipulating lenders. Some are general in character, and apply to all debtors, all creditors, or all practices and transactions. Others are individualized to the level of the specific creditor, the specific debtor or the specific credit transaction. We will begin with possible modes of intervention at the pre-credit transaction stage and move on to intervention at the post-failure bankruptcy stage.

A. *Ex Ante* Intervention

1. Regulation of Credit Marketing and Credit Contracts

Regulation that determines interest rates — usury laws — is out of favor

57 Pratkanis & Aronson, *supra* note 34.
58 *Id.* at xii.
59 Sutherland & Sylvester, *supra* note 37.

these days and is not tailored to meet the behavioral concerns of this article. Regulation that intervenes in the content of credit contracts, on the other hand, may limit biased borrowing and manipulation by creditors. For example, regulation that limits late payment fees or over-the-limit fees, while it may lead to a rise of the unregulated interest rate, reduces the potential exploitation of optimism bias or the illusion of control by lenders, and allows borrowers to reach more rational decisions. Such an intervention in the freedom of contract is relatively intrusive and paternalistic. It was recently discussed elsewhere.[60] The focus of this section is on regulation that mandates the disclosure of information.[61]

At first blush, borrowers are better positioned informationally to judge their creditworthiness than their lenders. It has often been argued that the asymmetry in information between lenders and borrowers is one in which the borrower holds vital information unavailable to lenders. The borrower, it is argued, has better information, not only about her assets, but also about her human capital and motivation to work, and thus about future earnings. This assumed asymmetry is reflected in many legal systems in bankruptcy and contract doctrines that place the burden on borrowers to prove that they have no assets or no significant potential income as a precondition to establishing good faith, to meeting a means test, to being entitled to discharge, and more.[62]

Once aware of optimism bias and the illusion of control among consumers of credit, we should rethink the adequacy of the current regulation. These borrowers appear not to have all of the accurate and valid information needed for decision making. Their lack of information begins with the boilerplate terms of the loan or credit card contract. But even mandatory disclosure of

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60 Bar-Gill, *supra* note 10.

61 *See* Ronald J. Mann, *Optimizing Consumer Credit Markets and Bankruptcy Policy*, 7 Theoretical Inquiries L. 395 (2006).

62 An exception to the assumption of the informational advantage of borrowers is found in the context of lending contracts. Regulations such as the American Truth in Lending Act, 15 U.S.C. § 1601 (1982), the British Consumer Credit (Advertisements) Regulations, (2004) SI 2004/1484, and the Irish Consumer Credit Act, 1995, aim to force disclosure of the content of borrowing contracts. They require strict disclosure of information such as the effective interest rate and how it is computed, hidden fees, and penalties. The underlying assumption here is that lenders draft loan and credit contracts as standard form contracts, that borrowers do not read such contracts, and that even if borrowers were to read such contracts they could not understand or interpret them correctly. They would be overwhelmed by the length and complexity of these contracts. This regulation is not necessarily premised on the behavioral biases of borrowers.

the essence of the content of the loan contract is not sufficient. Borrowers overestimate the likelihood of positive life events and underestimate the likelihood of negative life events. As a result, they misjudge their future income and expenses and their creditworthiness, and thus the application of various contractual terms to their case.[63] Many borrowers believe that they will not use their credit line in full, will never go over the limit, will not make late payments or fail to pay altogether, and will not default and go bankrupt. The information that has to be transmitted to credit consumers in order to achieve debiasing is first and foremost about the likelihood of life events and default, and only secondly about the content of contracts.

As mentioned above, institutional repeat lenders are not ensconced in the same biases. The unbiased lender-creditor is better positioned than the biased borrower-debtor to estimate the likelihood of that borrower's failure due to life events. Institutional lenders have access to general population statistics and to the statistics of their own customers. They know what percentage of their debtors, and of subsets among them, end up unable to pay debts due to adverse life events. They are also better positioned than individual debtors to analyze long-term demographic, social, macroeconomic and medical trends, and the effects of governmental policies on these. Regulation can mandate that such lenders share some of this information with borrowers. The regulation may force lenders to disclose to potential borrowers the likelihood that they will encounter negative life events (illness, accidents, job loss, divorce). The regulation may require disclosure of data regarding the probability that debtors will end up spending more or earning less than they do when they take out loans. The aim of such disclosure is to debias the borrowers and thus to restore their autonomy by improving their judgment and allowing them more rational decision making.

Can such regulation be detrimental? The main advantage of regulation that aims at debiasing over-optimistic borrowers is that it does not harm unbiased debtors or society at large. It can be seen as "asymmetric paternalism."[64]

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63 Further, types of information that were in the past in the sole possession of individual debtors are now available to creditors through credit reporting agencies. The availability of low-cost information about the credit history of potential debtors is a major means of creating symmetry regarding some types of information. We do not wish to argue that creditors have equal or superior information about every relevant component of the credit transaction. Some pieces of information are still more readily available to specific debtors.

64 This term was coined by Colin Camerer et al., *Regulations for Conservatives: Behavioral Economics and the Case for "Asymmetric Paternalism,"* 151 U. Pa. L. Rev. 1211 (2003).

Regulation is asymmetrically paternalistic if it "creates large benefits for those who make errors, while imposing little or no harm on those who are fully rational."[65] We cannot screen or test individuals *ex ante* at reasonable cost in order to determine whether or not their individualized biases and illusions justify paternalistic intervention in their decision making. A disclosure requirement is intended to debias the biased and not to affect others. It must be a low-cost requirement in order to be justified, and it seems to be one.

Can such information disclosure regulation be effective? Regulation requiring disclosure by lenders regarding real life event probabilities and the likelihood of their leading to bankruptcy can be justified, but is limited in its effect. This is not a reason not to prescribe it; the benefits are likely to exceed the costs. But the limited effect of information disclosure should lead us to the conclusion that solutions of other types and on different levels should also be sought.

To be effective, regulation should force creditors, who possess information that is not available to borrowers or to the state, to share this information with debtors. But this should go beyond informational considerations, and deal with cognitive considerations as well. The debate about debiasing is still raging.[66] The challenges of debiasing over-optimistic borrowers may turn out to be more demanding than those of debiasing smokers or practitioners of other unhealthy or life threatening behavior. The risks borrowing involves are of a variety of types. They involve both positive and negative life events. They include a variety of contexts: health risks, accident risks, job-related adverse developments, and family relationships. The causal relationship between borrowing, life events, default, and bankruptcy is more indirect and complex than that between smoking and cancer.

The form of the disclosure should take into account the cognitive biases of borrowers. It should not trigger biased perceptions by overly optimistic consumers. It should not settle for introducing statistical data, but rather,

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65 *Id.* at 1212.

66 In legal discourse, the main focus of this debate is still smoking. Scholars disagree as to the effectiveness of warnings and disclosures about the health risks of smoking. See, for example, the debate between Viscusi and Slovic: *compare* Kip W. Viscusi, *Using Warnings to Extend the Boundaries of Consumer Sovereignty*, 23 Harv. J.L. & Pub. Pol'y 211 (1999), *and* Kip W. Viscusi, *The New Cigarette Paternalism*, 25(4) Regulation 58 (2003), *with* Paul Slovic, *What Does it Mean to Know a Cumulative Risk? Adolescents' Perceptions of Short-term and Long-term Consequences of Smoking*, 13 J. Behav. Decision Making 259 (2000), *and* Paul Slovic, *Rejoinder: The Perils of Viscusi's Analyses of Smoking Risk Perceptions*, 13 J. Behav. Decision Making 273 (2000).

should be salient and personal in its persuasion of the individual consumer. The information disclosed should be framed in a manner that will utilize anchoring.[67] It should emphasize the loss that will be caused by ignoring the disclosure rather than the gains attained by taking it into account, making use of the tendency towards loss aversion.[68] In short, it should counter-manipulate consumers. In fact, by prescribing counter-manipulation we may have crossed the line from disclosure to warning. While conceptually disclosure requires presentation of facts, preferably an objective and balanced presentation, if such is at all possible, warning forces a non-neutral message. A requirement to publish bankruptcy statistics with credit card companies' application forms or contracts is a disclosure requirement. A requirement to include in monthly statements a message such as "X% of the debtors who maintain a balance at your level will go bankrupt in the next 3 years" is a counter-manipulating disclosure requirement. A requirement to post on every credit card the slogan "credit card charging causes bankruptcy" is a warning requirement.

Based on our analysis of the relevant cognitive biases, the bounded computational capabilities of credit consumers, and the influence, persuasion, and manipulation exercised by marketers and advertisers, we recommend *ex ante* regulation in five areas. They are: (1) limits on the inclusion in loan contracts of clauses and pricing schemes whose main intention is to trigger or exploit the bounded rationality of borrowers; (2) within the disclosure requirement regarding the essence of the contract, giving particular emphasis to clauses that are likely to be activated only on the occurrence of negative life events; (3) regulation that restricts manipulative practices in advertisement to some degree; (4) a requirement of well-framed disclosure of information on the likelihood of negative life events; and (cautiously) (5) a requirement that warnings be attached to the marketing of some credit products. These recommendations are preliminary and tentative. Each requires close examination of costs, benefits, and details. They should be informed by empirical studies. Yet, because of the limitations on the effectiveness of these recommendations, policymakers should consider intervention on other fronts as well.

2. Tax and Insurance

In recent years, Belgium has experimented with the use of taxation in order to increase lenders' responsibility and defray the costs of bankruptcy

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67 *See supra* note 2.

68 See Christine Jolls et al., *A Behavioral Approach to Law and Economics*, 50 Stan. L. Rev. 1471, 1533-37 (1998), for strategies that may render disclosure more effective.

proceedings. Initially all institutional consumer lenders were taxed per transaction. The money collected was placed in a fund that was used to cover the operation of the bankruptcy system. In 2002 the tax base was altered, and now the total consumer lending portfolio in default, as of the end of each year, is taxed.[69] Ronald Mann properly views such a tax as one whose main purpose is to internalize externalities.[70] The collected money can be used for covering the damages caused to third parties by bankruptcies of consumer debtors. Moreover, the threat of taxation should create a better *ex ante* incentive for consumer lenders to reduce loans that may end up defaulting, even if such loans are profitable to the lender. Mann realizes that the costs of the tax may be shifted from lenders to borrowers and increase the price of credit. Further, competition among lenders would lead to a situation in which low means-high risk borrowers carry more of the tax burden than high means-low risk borrowers. This creates a dilemma, as the attempt to minimize externalities using this type of tax is likely to lead to adverse distributive outcomes.

From the perspective of this article, the attractiveness of the use of such a tax is that it bypasses the need to define and identify manipulation. Lenders are taxed based on outcome and not on intentions or practices. This tax also fits into the view of this article that identifies externalities as a basic problem, that holds institutional lenders as having an informational advantage, and that prefers *ex ante* over *ex post* solutions. Yet we are not yet convinced that the tax can be tailored to fully internalize the externalities, without being either overinclusive or underinclusive.

A variation on the tax idea is a return to the initial Belgian scheme of a per transaction surcharge. This surcharge would fund a borrowers' education program whose main aim would be to debias potential borrowers. In addition, a mandatory requirement would be added, requiring every borrower who wished to enter into a loan contract for a sum above a certain threshold to participate in such a program. Here lifecycle flow of earnings, expenses, savings, and loans could be examined based on non-biased assumptions about negative and positive life events. We believe that the focus of such programs on debtors' debiasing rather than on creditors' use of biases should not be viewed as attributing fault to debtors. Such programs would focus on providing borrowers with negative life event statistics and other relevant

69 Jason Kilborn, *Continuity, Change, and Innovation in Emerging Consumer Bankruptcy Systems: Belgium and Luxembourg*, 14 Am. Bankr. Inst. L. Rev. (forthcoming 2006).

70 Mann, *supra* note 61.

information, as well as some debiasing, thus restoring their autonomy. In the first paragraphs of this Section, in contrast, we focused on reducing externalities and better aligning the incentives of creditors.

Another somewhat similar solution would be to impose mandatory insurance, at least on institutional lenders. The parties to a loan contract would be obliged to insure themselves — against damages to third parties, not to the lender or borrower. The parties to the credit transaction would share the premium, which would be determined by the failure record of both parties. Reckless lenders would have to pay higher premiums and would not be able to shift the premium in full to their borrowers because of competition with more prudent and less manipulative lenders. These reckless lenders would have to improve their records.

This insurance scheme is unconventional. Third parties suffer damage only when the borrower is in default. At that point in time it would be necessary to determine which of the lenders caused the damage suffered by other lenders, otherwise only externalities to non-institutional creditors would be covered by the insurance. All institutional lenders would prompt their insurance policies and share the damages of the default irrespective of reckless manipulation. A determination as to which of the institutional lenders was at fault would allow the internalization of the externalities imposed by one institutional lender on other institutional lenders. Such a determination is a complicated matter in terms of substantive law, facts, and procedure. However, the insurance system could create desirable incentives even if fault is not determined, or is determined incompletely. Premiums would presumably be affected by the incidence of default cases in which a lender is involved; reckless lenders are bound to be involved in more such cases.

B. *Ex Post* Intervention

We now move from intervention at the pre-credit transaction and pre-loan contract stage, to intervention at the default and bankruptcy stage.[71] An important advantage of intervention at the bankruptcy stage is that such intervention affects only failed debtors. It is at the point of bankruptcy that consumers are in a position in which their borrowing can clearly be viewed as overborrowing. It does not benefit them any more and it inflicts externalities

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71 We believe that the two ends of the timeline are the more interesting points in time for analysis. Yet we do not reject the possibility of intervention at other points in time between these two ends.

on society. Policy considerations should aim at focusing legal intervention on those stages in which the effect of biases and manipulation are most evident, stages which can be regulated without affecting debtors, transactions, or creditors not involved in undesirable over-borrowing and default. The downside of intervention at this stage is that some of the damage to debtors and to society has already been done.

Two approaches can be taken on the bankruptcy law level. The first prescribes solutions on the level of general bankruptcy doctrines, mainly as a response to optimism bias, the illusion of control and bounded computational rationality. On this level we will consider discharge, asset exemption, and the doctrine of the fraudulent debtor. The second approach suggests using bankruptcy law as a trailer of contract and tort law that identifies and deals with specific manipulative creditors and manipulated transactions. Here specific debt claims made by creditors will be examined within the bankruptcy process. Claims by manipulating creditors can be stopped, rejected, accepted only in part, or downgraded to a lower priority level than claims of non-manipulating creditors.

1. Implications for General Bankruptcy Doctrines

While behavioral law and economics has flourished in recent years, the application of behavioral insights to bankruptcy law is still limited. Only a handful of scholars have addressed the implications of cognitive biases of debtors to bankruptcy policy. In 1985, Thomas Jackson wrote an innovative article in which he argued for the non-waivability of discharge.[72] This was an exceptional article for its time. Jackson, one of the first and most influential to apply the methodology of law and economics to bankruptcy, typically focused on business bankruptcies and not on consumer bankruptcies, and prescribed recommendations that were considered pro-creditor. Here, on the other hand, he dealt with consumers and justified discharge for debtors. What makes his article even more relevant to our discussion is the fact that Jackson used behavioral insights to support his recommendation.[73] He was ahead of his time by more than a decade. But on the other hand, his discussion was limited by the fact that the behavioral literature on biases, particularly on optimism bias, was still young, and its application to economics and to law was still in its infancy. We take Jackson's justification further. Now that the empirical basis

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72 Thomas H. Jackson, *The Fresh-Start Policy in Bankruptcy*, 98 Harv. L. Rev. 1393 (1985) [hereinafter Jackson, *Fresh-Start Policy*]; *see also* Thomas H. Jackson, The Logic and Limits of Bankruptcy Law (1986).

73 Jackson, *Fresh-Start Policy*, *supra* note 72, at 1408-15.

of the bias is stronger, mandatory discharge is even more justified. Now that we understand the problems involved in *ex ante* regulation and debiasing, we place more hope on discharge.

We take this logic one step further by taking manipulation into account. The debtor has to be protected not only from his biases but also from the creditors' manipulation. We believe, as argued above, that manipulation, by increasing the debt-to-income ratio, increases the likelihood of default for the individual and the total number of bankruptcies (if defaulters are given access to bankruptcy). Manipulation raises the externalities to society, due to the need to provide for the subsistence of debtors without means, and due to dead weight loss caused by the costs of the bankruptcy process. These costs are added to disutility to consumers caused by biases and errors. Thus the justification for discharge is further enhanced by the analysis offered in this Article. The practical application of this conclusion varies between legal systems. Where discharge is not offered at all, it should be offered. Where it is offered subject to conditions, such as long bankruptcy repayment plans before discharge, judicial discretion rather than automatic discharge, means testing, or the like, such conditions should be reviewed and possibly eased, to avoid the larger losses to society associated with manipulation.

Debtors who are allowed to keep future earnings in discharge are less dependent on the welfare state. Swift and simple discharge reduces the costs to the state and to society at large of administering the bankruptcy process.[74] The disadvantage of permissive discharge rules is that they apply uniformly to both non-manipulating and manipulating creditors. Not only will the former be disadvantaged, but no incentive will be created for the reduction of the level of manipulation. Discharge will be granted both to debtors who acted upon their biases and to debtors who were not biased, or those whose biases were not relevant to their decision making in the specific transaction that led to debt and default.

A similar analysis can be applied to exempt assets. While discharge protects future income, exemption protects current assets. Some of these assets, such as pensions and some other forms of savings, are intended as wage substitutes. Other assets are to be used for the generation of income. Insofar as discharge is justified, exemption of such assets is also justified. A third type of asset provides basic subsistence. In a system that does not provide exemption for basic residential dwellings, bankrupts either become homeless or are provided

74 Two years ago, Saul Schwartz analyzed the new Canadian bankruptcy policy supporting debtors' relief, exempt status of various assets, and so on. *See* Schwartz, *supra* note 8.

with public housing by the state. Exemption of assets is justified in order to prevent such externalities, and in order to protect basic human rights. A too far-reaching non-waivable exemption of assets is not justified because it creates an incentive for debtors to go into bankruptcy and eventually makes credit more expensive for these and other debtors.[75]

A third relevant bankruptcy doctrine on which the behavioral insights on biases and manipulation may have bearing is that of the fraudulent debtor. In some legal systems fraudulent debtors are not entitled to a discharge or to other protections and privileges. In other systems, they are subject to civil or criminal imprisonment. Individuals who borrowed at a point in time in which their ability to pay seemed highly doubtful to objective observers may be held as fraudulent debtors in some systems. We believe that due to the fact that lenders sometimes manipulate debtors into borrowing more than they initially intended, debtors should not be held as fraudulent merely because they over-borrowed. Their mental state and the behavior of their lenders should be taken into account as well in the formula that determines fraudulence.

Other collection measures offered by the state at its expense should also be reconsidered in light of the increase in externalities caused by creditors' manipulative behavior. Furthermore, moral considerations, namely the fault of manipulating creditors, may justify the objection to providing such measures, irrespective of externalities. In particular, measures that inflict harm and pressure on debtors and interfere with their human rights should be reconsidered. In Israel, for example, a debtor imprisonment procedure is still in effect.[76] This procedure is very costly to the state. It also violates the rights of debtors. Even if there are reasons for the state to take similar measures upon itself in ordinary circumstances, when manipulation of debtors may be involved there can be no justification for such measures.

2. *Implications for Specific Claims in Bankruptcy*

A different policy approach may allow debtors and bankruptcy trustees to raise the claim that a creditor manipulated them. Any policy recommendation that aims at establishing distinctions at the bankruptcy stage between manipulating creditors and non-manipulating creditors belongs in this category.

It seems like manipulation of a borrower by a lender might be dealt with by

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75 See *id.* at 74-81 for a discussion of some of these considerations from a behavioral perspective.

76 Ron Harris, *The Fall and Rise of Imprisonment for Debt*, 20 Tel-Aviv U. L. Rev. 439 (1996) (Hebrew); Pablo Lerner, *The Chief Enforcement Officer and Insolvency in Israeli Law*, 7 Theoretical Inquiries L. 565 (2006).

contract law doctrines and remedies. Manipulated bankrupt borrowers can, in principle, turn to existing doctrines such as fraud, duress, undue influence, and lack of good faith. At the moment, none of these doctrines have been applied successfully in our circumstances. These doctrines could, however, be interpreted and expanded by courts to apply to our circumstances. Debt claims by manipulating creditors could then be stopped or rejected. Bankrupts may be unaware of, and unable to establish, the connection between any single credit contract they entered into, a negative life event that they exogenously experienced, and an eventual failure and bankruptcy. They have to be debiased in order to realize that the probability they attributed to negative life events was unrealistic and was augmented or at least exploited by a manipulative lender. One of the advantages of contractual intervention at the bankruptcy stage is that at this stage, a bankruptcy trustee who is a repeat player and as such more immune to biases and their manipulation, now holds the cause of action. Examination of credit transactions and advertising practices that advance them, in search of manipulation, can theoretically be performed at any stage between the initial contracting and the eventual bankruptcy. It is only in bankruptcy, however, that the full unfolding of transactions, life events, and accumulated debt can be examined. Thus, it is only in bankruptcy that we examine the question of whether a manipulation was causally connected to a default.

But in order to distinguish between manipulation and non-manipulation, each individual transaction between the debtor and any of his creditors would need to be scrutinized. Such a detailed examination raises a whole set of problems. The bankrupts themselves may lack the incentive, resources and legal status to challenge debt claims submitted in bankruptcy by manipulating creditors. The trustee or receiver could revoke claims by manipulating creditors. However, such an act would usually not serve the bankrupt debtor, who would still be in deep debt, and may not serve the trustee either if not properly incentivized. Non-manipulating creditors would be the major winners. As the most significant incentives lie with other creditors, the victims of externalization, we should look for ways that would allow them to act.[77]

A determination of which creditors manipulated their debtors and which did not could lead to the revoking of claims. But in bankruptcy it could

77 Externalities toward other creditors work as follows: borrowing from a manipulating lender by a debtor increases debt, reduces the percentage of dividend made in bankruptcy, and decreases the share of non-manipulating creditors in the dividend pie.

have another interesting consequence, the ranking of creditors' priorities according to their manipulative actions. Unsecured creditors who acted manipulatively would be positioned below unsecured creditors who were not manipulative. It might even be worth considering placing manipulating secured creditors in lower priority. Such a rule would not only allow non-manipulating creditors to reverse the externalities imposed on them, it would also create an *ex ante* incentive for creditors to avoid manipulative behavior in the future. It would "educate" creditors.

Tort law might also be applicable to the relationship between a borrower and a manipulating lender. Here liability could be imposed upon the lender-creditor for damages caused to the borrower-debtor due to failure and bankruptcy, to the extent that these were caused by manipulation. The wrong could be classified as deceit. However, it is not clear that tort law should be preferred over contract law as the proper doctrinal vehicle for recovering damages in a context that is basically that of voluntary transactions. One advantage of the application of torts is that it may allow the application of a strict liability regime if we believe that this is justified due to the fact that the lender is the cheapest cost avoider, the party that can best reflect the possible damages in the price charged.

Another advantage of tort over contract in this context is that it bestows other creditors with causes of claim. If we believe that bankrupts and their trustees may not act, then other creditors may act when they have high enough incentives. Further, as they are in direct dispute with the manipulating creditors, other creditors may lay down their claims outside bankruptcy proceedings. If we view bankruptcy proceedings as problematic, this is an advantage.

A final advantage of tort law is that it is somewhat less atomistic and divisive than contract law in terms of the manner in which it structures litigation. In contract, rejection of claims by manipulating creditors has to be done on a one-by-one basis on the transaction level: for each bankrupt, each manipulating creditor, and each transaction. There are advantages to putting the manipulative practices of a large institutional lender to examination in a single suit when the stakes are high, sufficient resources are invested in determining the issue in contention, and remedies can cover a variety of damaged parties. Tort doctrines stretching from the joint tortfeasor doctrine to the alternative liability doctrine to market share liability may allow for less atomistic litigation.

Conclusion

Should we apply behavioral literature and insights from consumer studies to bankruptcy policy? We believe that the answer is yes. The studies that find widespread optimism bias and illusion of control are numerous and unequivocal. The evidence for persuasion and manipulation by creditors of their debtors is voluminous. The justifications presented for legal intervention, i.e. restoration of the debtor's autonomy, minimization of externalities, and distributive considerations, are compelling. Yet we conclude on a somewhat pessimistic tone. Neither of the possible stages for intervention or modes of intervention seems to sufficiently advance the intended aims of this intervention.

Our intention was not to offer very specific recommendations and doctrinal prescriptions, but rather to propose a theoretical framework. This Article does not argue that the optimism bias and the illusion of control are the only relevant biases for bankruptcy law. It does not recommend the adoption of any single policy. It does not argue that we know exactly what form the regulation we recommend should have. It does not fully balance between the perspective of the creditor and the perspective of the debtor. It aims at integrating the discussion of biases and manipulation into bankruptcy discourse.

This framework, we believe, should be implemented differently in different legal systems. The implementation should be carried out according to the existing doctrines of the legal system. In the United States, for example, where Chapter 7 provides an option for automatic discharge, the considerations for changing the system according to the discussion held above are different than those in a system in which automatic discharge is not possible, such as Israel. That said, we still believe that more emphasis should be put on reducing the practice of manipulation in advertising.