

# Santa Clara University

## The Economics of Reputational Information

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# What is Reputational Information?

- Reputational information = information about an actor's past performance that helps predict the actor's future ability to perform/satisfy preferences
- Examples:

Unmediated	Mediated
<ul style="list-style-type: none"><li>• Word of mouth</li><li>• Recommendation letters and job references</li><li>• Student evaluations</li></ul>	<ul style="list-style-type: none"><li>• Credit scores</li><li>• Investment ratings (bonds, mutual funds)</li><li>• GPAs</li><li>• Consumer product reviews and ratings (Amazon star ratings; Ratemyprofessor.com; Avvo; Ripoff Report; BBB)</li><li>• Voting systems? PageRank, Digg</li></ul>

# Why Reputational Information Matters

- The market's invisible hand is predicated on consumers rewarding good producers and punishing poor ones
  - Reputational information = invisible hand of the invisible hand
- Hypotheses
  - #1: Anomalies in reputational information supply and demand hinders invisible hand
  - #2: Inconsistent regulation of reputational information should be examined for unwarranted dichotomies

# Selected Reputational Information Regulations

- **Stimulate supply**
  - Whistleblower laws and other immunizations (ex: 47 USC 230)
  - Mandatory disclosure laws (ex: mandatory job references)
- **Suppress supply**
  - Defamation
  - Mandatory non-disclosure laws (ex: anti-blacklisting laws)
- **Stimulate demand**
  - Mandatory consulting of reputational information
- **Suppress demand**
  - Privacy laws

# Regulatory Dichotomies

- #1: Job references
  - Defamation/tortious omission but immunization for “good faith” references
  - But miscalibrated immunization suppresses job reference supply and drives hirers to alternative supply sources
- #2: Amazon product reviews
  - Individuals face defamation liability but Amazon protected by 47 USC 230
- Why the differences?
  - Mediation
  - Differential knowledge about legal consequences of reviewing
  - Defendant’s wealth
  - Relative bargaining power between reviewer/reviewee
  - Economic consequences of erroneous bad review
  - Number of legitimate reviewers
  - Objectivity of review criteria

# Correcting Undersupply

- **Why does reputational information remain non-public information?**
  - Benefits: usually only psychic rewards (pulls towards love it or hate it)
  - Costs: time, vendor retribution, norms against public criticism, privacy, legal risks
- **Possible regulatory solutions**
  - Recalibrate legal risks
    - Raise standards for legal claims
    - Give potential defendants more tools to counterattack bogus threats
    - Protect intermediaries facilitating production of reputational information
  - Make consumer adoptions/defections public information (ex: Beacon)
  - Increase channels for anonymous dissemination of reputational information
  - Government funding of reputational information production