

Covert Marketing Advertising Law Review Paper

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Abstract: This paper examines the legal and ethical issues surrounding stealth marketing, especially in the current popular trend of influencer marketing on social media, and its effects on the trust and perception of consumers. The paper explores regulatory frameworks, focusing on the American FTC and the European UCPD, which govern self-regulation and disclosure requirements. This research adopts a literature review of the selected case studies and a review of general findings on advertising transparency, consumers' behavior, and general cultural responses to covert advertising. The comparative method was used to determine differences between the US state laws and EU laws regarding stealth marketing. The findings indicate that when commercial intent in marketing is concealed, consumer confidence and brand loyalty are compromised. Although younger generations and customers in non-Western countries may tolerate hidden advertising to an extent, integrity is vital for long-term brand development. The study also highlights the potential of AI-supported systems to assist in compliance and increasing transparency in social media advertising. The conclusions indicate that enhanced compliance with the legal provisions on transparency and the implementation of AI monitoring mechanisms in organizations offer much potential to improve consumer confidence and ensure brand responsibility in the global marketplace.

Keywords: Stealth Marketing, Consumer Trust, Influencer Marketing, Advertising Transparency, FTC and UCPD Compliance.

1. Introduction

In recent years, stealth marketing has gained widespread popularity as a highly controversial promotional strategy on social media platforms, particularly within the field of influencer marketing. By skillfully embedding brand content into influencers' everyday posts, it conceals commercial intent, making it difficult for consumers to determine whether content is an advertisement or a genuine recommendation. While stealth marketing can attract younger consumers more naturally, its lack of transparency has raised numerous ethical and legal concerns. The regulatory environment for stealth marketing varies significantly across regions, especially between the United States and Europe. The U.S. Federal Trade Commission (FTC) requires influencers to clearly disclose sponsored content to ensure consumer awareness, while the European Union's Unfair Commercial Practices Directive (UCPD) promotes transparency by preventing misleading advertising practices, though enforcement may differ among member states. Given these complexities, this paper will explore the impact of stealth marketing on consumer trust by comparing regulations in the U.S. and Europe, providing an

in-depth analysis of how these legal differences and cultural contexts influence consumer attitudes. Additionally, this research examines the potential of artificial intelligence to enhance transparency in social media advertising, supporting compliance and ethical standards.

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Stealth marketing, also known as covert marketing, refers to marketing methods in which brands promote products or services to consumers when customers do not recognize them as advertisements [1]. In recent years, this practice has been especially prominent in influencer marketing on social media, where the influencers integrate paid content with brands in their posts without being obvious about their association with the brands [2]. This lack of transparency serves some critical legal and ethical dilemmas concerning consumer trust and brand attitude. In the United States, the Federal Trade Commission (FTC) requires a very high level of disclosure to ensure consumers know they are being sold products through sponsored advertisements. On the other hand, the European Union's Unfair Commercial Practices Directive (UCPD) focuses on preventing potentially misleading advertisements/communications to consumers and regulates transparency differently than the US. This paper addresses the research question: What impacts does the practical application of stealth marketing have on consumer trust and perception of the brand? Therefore, this research aims to investigate the implications of unvoiced advertising on consumers and will look at US and EU transparency requirements to identify possible enhancements in the present rules to promote trust and accountability in advertising.

3. Literature Review

Stealth marketing raises many legal and ethical questions, particularly regarding misrepresenting products which can erode consumer trust. Consumers who feel deceived by hidden advertising are likely to respond negatively, harming the established trust between the brand and the consumer [1,3]. Evans et al. [3] highlights that hidden advertisement, particularly in influencers, is likely to trigger negative consumer responses once the concealed advertising is uncovered. Skiba et al. [4] further explain that consumers value truthful information from the influencers and feel misled when advertisements are disguised as organic content. This is further supported by Ashley and Leonard [5], who also observe that covert marketing harms consumer-brand relationships and degrades brand loyalty. Such insights concur with Martin & Smith [1], who posit that stealth marketing leverages social uses for business gains and is thus unethical because the consumers do not know that they are being sold content.

The European Union and the United States pursue different approaches to managing transparency problems in stealth marketing. The US Federal Trade Commission has very stringent laws regarding sponsorship disclosures, as demonstrated by *Lord & Taylor's* case, which it penalized for not revealing that it was paying the influencers [4]. This case provides an understanding of what may happen in unnoticed marketing, as the FTC intervention was meant to prevent consumers from being misled [6]. In the UK, the Committee of Advertising Practice (CAP), demands that influencers must put hashtags that display paid advertisements. CAP is regulated by the Advertising Standards Authority (ASA), which makes sure all the advertisements are clearly recognizable, especially on social media [7]. Comparatively, while FTC more focused on transparency, CAP is focused on consumer protection and the principles of fair competition [7]. Pierre [8] discusses that similar to the concept seen in the US, CAP-regulated advertising that lacks transparency means a lack of consumer trust in specific campaigns from brands that people anticipate to be honest. Generally, studies confirm that hidden advertising in the US or the UK is legally prohibited and ethically ambiguous, potentially damaging the consumer's brand perception and organizational reputation in the long run.

4. Analysis: US Advertising Law and Stealth Marketing

FTC has established extensive policies to regulate advertising disclosures, mainly concerning deceptive practices in influencer marketing and all forms of undercover advertising. These regulations originate from the FTC Act, which prohibits misleading or unfair practices that impact commerce [4]. The FTC requires that individuals who receive goods or cash in exchange for promoting a product must make the relationship clear to avoid deceiving the audience. This is relevant when in influencer marketing, some differences between promotional and non-promotional messages can be discerned well. For instance, disclosures such as “sponsored” or “#ad” tags must be prominent and cannot be hidden by other tags, ensuring that they are easily noticeable to the average consumer.

The FTC has been particularly vocal about the approval of advertisement endorsements, particularly in some incidents in the United States, such as a case that involved *Lord & Taylor* in 2016. *Lord & Taylor* raised concerns when it offered 50 fashion influencers money to go on Instagram in the same dress from the DesignLab [7]. The influencers were asked not to disclose their sponsorship. The FTC ruled that this failure to disclose breached its guidelines, leading to a resolution that barred the company from engaging in similar practices in the future [7]. To the FTC, this case supported its argument that any brand that wishes to use influencers should make everything known to customers. This case marked a significant turning point in influencer marketing and set a precedent for transparency in sponsored posts. They stressed the significance of specifics and required actions to guarantee and strengthen them to be more transparent [7]. Therefore, to counteract the rise in influencer advertising, the FTC increased its focus on influencer advertising and prompted all disclosure rules on all platforms.

Another important example is the *Warner Bros Home Entertainment* case of 2017. The organization paid several of the most popular YouTubers to recommend a video game without visible disclosure of the fact that they were paid to do so [9]. The FTC concluded this as a violation of this rule under its guidelines. Therefore, Warner Bros entered a legal settlement that would prevent it from deceiving the consumer's overpaid sponsorship [9]. The case aligns with the FTC's proposal regarding independent assurance that all influencers disclose the sponsorship details themselves. The broader impact of this case is beyond Warner Bros as it has set a precedent in that any internet site or social media platform, including those using influencer content, has to respect the principles of keeping user transparency rules [9]. The FTC restored post-case enforcement by issuing more warnings and settlements, evidencing the rise of the crackdown and the necessity for brands to monitor influencers' compliance to avoid sanctions.

The FTC strengthened its scope in 2019 with the *Cure Encapsulations, Inc.* case that focused on incentivizing reviews without disclosure. *Cure Encapsulations* influenced Amazon users and received positive reviews regarding its weight-loss supplement by employing such customers as paid advertisers [10]. The FTC settlement highlighted complete compliance – particularly on internet markets – and reiterated the agency's position on ethical advertising. This case and others like *Teami* in 2020 showed that FTC is committed to supervising endorsements from diverse social platforms, including short-form content. FTC fined *Teami* for their involvement of celebrities like Cardi B marketing detox teas without clear warnings led to and then reinforced rules regarding influencers [11]. The courts have given it as a common understanding that both influencers and brands have legal responsibilities over sponsored collaborations that have no disclosures, leading social media outlets such as Instagram and Amazon to encourage better policies to prevent consumers from being ripped off [11]. Generally, FTC actions have certainly tightened the regulatory framework.

The prosecution measures show that the FTC pursues violators and that its jurisdiction over markets extends to influencers involved in stealth marketing. These steps were taken proactively to prevent future litigation and draw attention to paid social media advertising issues. A poll by

Mediakix in 2019 showed that 92.8% of the celebrities on Instagram were in breach of the FTC disclosure regulations [11]. Thus, the FTC legal foundation and the enforcement actions are valuable for establishing clear and comprehensible advertising and consumer protection.

5. Analysis: EU Advertising Law and Stealth Marketing

In the European Union, stealth marketing is regulated under the Unfair Commercial Practices Directive (UCPD), which requires that all advertisements, regardless of medium, be truthful and transparent. A notable example is the case of Instagram influencers penalized in Italy early this year through the help of UCPD. The Italian Competition Authority (AGCM) received numerous complaints from influencers and brands that lack proper disclosure of sponsored content [12]. This led to a directive requiring brands and influencers to use hashtags such as ‘#sponsored,’ which set the precedent for how influencer marketing regulations should appear throughout the EU [11]. A European survey of customers in 2020 revealed that 47% of the participants could not trust the brand again if it participated in covert advertising, showing that advertisers should continue to uphold the trust of consumers [13].

The United Kingdom is governed by the Committee of Advertising Practice (CAP) together with its enforcing agency, the Advertising Standards Association (ASA) [7]. Similarly, the *ASA v. The Love Island Influencers* case highlighted the importance of transparency, as participants in the reality show failed to disclose their sponsorships on Instagram [12]. Another survey conducted in 2021 by the ASA showed that 65% of the influencer posts did not adhere to the set guidelines on advertisement transparency [13]. The ASA’s intervention and CAP enforcement also cautioned influencers in the *Britvic Soft Drinks Ltd.* case, particularly on newer platforms like TikTok, where they violated the rules by promoting products with inadequate disclosure [10].

In Germany, the *YouTube Creators Case* offered additional empirical findings on the effects of non-disclosure. According to a study by the German Regulatory Authority for Commercial Broadcasting in 2019, 76% of YouTubers violated the law by not properly labeling their affiliate links [10]. The German Federal Court of Justice stated that even small compensation, like affiliate commissions, should be reported to consumers to avoid mislead them [12]. These cases, based on empirical evidence, also clearly show the European Union’s shift towards the issue of transparency. EU regulators seek to safeguard consumer confidence and uphold ethical advertising practices throughout the digital domain by strengthening these regulations under UCPD and CAP.

6. Impact of Advertising Transparency on Consumer Trust

The level of transparency in advertising influences consumers' trust in influencers and digital advertising. When sponsorship or paid endorsement is not stated, consumers may feel that they are being misled, significantly reducing their trust in both the content creator and the sponsor. Goldman [14] suggests that when consuming certain content, the consumer is disappointed or betrayed when they learn that it is a paid advertisement. This sense of deception erodes consumers' trust, which is vital in maintaining regular business between the consumer and the advertised. Goodman [15] further states that covert advertising simultaneously elicits trust and reduced credibility and arouses doubts about subsequent advertisements. When consumers realized being lured into consumption by covert advertisements, they may become wary about advertising in the future, posing a challenge for brands and influencers to regain consumers' trust.

Transparency promotes conditions improves openness, thus enhancing consumer confidence. The findings have suggested that consumers feel more in control of the content when they are notified or alerted that a post or advert is, in fact, a commercial one [13,16]. These measures enables the consumers give their verdict on the content without feeling exploited for some undisclosed purpose.

Similarly, according to Gürkaynak et al. [7], when the consumers know the truth, they appreciate such disclosures, making them to perceive the brand positively. According to Pierre [8], trust is an accountable yet susceptible feature of the relationship between the consumer and brands. The transparent disclosure of sponsorships assists in maintaining trust as it ensures that consumers are not fooled into interacting with commercial content.

7. Impact of Stealth Marketing on Consumer Brand Attitudes

The stealth marketing is often seen as questionable and intrusive in its approach to consumers, significantly impacting consumer perceptions of brand loyalty and overall impressions. Consumers who encounter unidentified disguised as native content tend to develop negative sentiments and change attitudes toward the specific brand [17]. Ashley and Leonard [5] establish that when consumers are aware of covert marketing strategies, their trust in the brand reduces dramatically. In the long run, the sense of betrayal is detrimental to the brand, as consumers become hesitant to engage with brands they perceive as untrustworthy [18]. When consumers realized that the brand's earlier interactions with them were fake, they could not trust the brand again, even if it started being genuine [18].

Besides, more vocal or reactive consumers can gain access to hidden advertisements and create negative brand perceptions not only for themselves but for the general market. Research by Milne et al. [6] suggests that consumers change their attitudes regarding a specific brand and the overall industry when they discover that a particular company is violating their privacy using underhanded marketing tactics. For instance, if a highly followed influencer is caught flogging products while being a paid sponsor, the consumers may generalize this literature and consider all brands equal to be a deception [13]. Such a ripple effect can drastically affect a brand image because the negative feelings evoked by stealth marketing tactics are long-lasting and lead to reduced purchase motivation and involvement.

8. Consumer Behavior Across Demographics

Consumer attitudes towards stealth marketing differ significantly in terms of age differences, which is primarily between the young and the older generations. Since the current generations, Gen Z and millennials, who have grown up with influencer marketing and social media advertising, tend to be more tolerant of surprise marketing techniques. Skiba et al. [4] argue that youth can regard sponsored content as something natural and are less likely to detect deception when they come across either explicit or hidden advertisements. However, this does not mean that they are not concerned about transparency. Despite the young consumer segment's greater acceptance of stealth marketing, clear disclosures still enhance their trust and brand perception [4]. On the other hand, older consumers are less used to covert marketing than younger ones and more often consider it deceptive and manipulative. When it comes to older audiences, Evans et al. [3] discovered that they tend to experience a negative emotional response to discovering undisclosed sponsorships and that this behavior is linked with dishonesty. To better tailor their transparency efforts and marketing strategies, brands must understand these demographic differences to address different consumer groups' disparate expectations effectively.

9. Cultural Differences in Perceptions of Transparency

Consumers also depict different attitudes toward transparency in advertising across various cultures. Western consumers, especially from the US and Europe, where organizations are regulated regarding the level of transparency by the FTC and CAP, fully expect such ads to be labeled. However, in regions such as Asia and Latin America, there is greater tolerance for covert marketing practices.

Zhang and Benyoucef [2] pointed out that in some Asian markets, users may have low concerns about undisclosed sponsorships due to entertainment and content values. Of course, the values of transparency remain crucial, although they do not value it as Western nations. While transparency remains essential, it is valued differently depending on the region [2]. The implications of this are that brands operating in different cultural contexts may have to adapt their transparency strategies to meet local consumer expectations. For instance, in countries with more lax transparency regulations, consumers may not exhibit the same degree of distrust towards covert marketing as in the US and Europe [2]. Information to this effect demonstrates that brands need to be aware of how transparency is viewed regionally in a unique way and adapt marketing approaches to maintain consumer confidence.

10. Long-term Impact of Stealth Marketing on Consumer Loyalty

Knowledge of the impact of stealth marketing on consumer loyalty gives insight into how undisclosed advertising affects brand perception in the long run. While short-term reactions to covert sponsorships are often negative, the long-term impact on consumer loyalty is even more severe. Pierre [8] stated that constant exposure to covert advertising can lead to a reduction of trust and that regaining trust once the covert advertising is stopped may not be easy. When consumers feel that they have been misled, they are likely to have a negative attitude towards the brand, and they may disengage from the brand. Moreover, it is important to note that transparency may not remedy the harm on its own. Some of the adverse effects can be reduced through timely disclosures. However, according to the findings of Milne et al. [6], repeated exposure to stealth marketing results in long-term brand distrust and, consequently, reduced consumer loyalty and purchase intention. These implications suggest that brands should avoid engaging in covert marketing strategies since the negative effects may overshadow the benefits of undisclosed advertising. This is because if a brand fails to remain consistent in its transparency, it is likely to develop a negative attitude toward the brand.

11. The Role of AI in Ensuring Transparency

In response to the growing demand for advertising transparency, artificial intelligence (AI) and machine learning have emerged as key technologies for enhancing monitoring and compliance. The brands and the regulators have started using artificial intelligence-driven content monitoring platforms to check whether the disclosure limits have been met. These tools assist in determining whether an influencer post contains the requisite disclosure and identifying content that does not meet the levels of transparency. Gürkaynak & Kama [7] explain that with AI technology, brands will be able to reduce human-related issues in enforcing advertising rules while it will also be easier for a brand to observe a large amount of digital content in real-time. Such a process can be automated to guarantee that any piece of content with sponsorship information has been tagged, which helps to enhance the amount of trust consumers have in the content. These systems also provide regulators such as the FTC with far more effective mechanisms for tracking compliance across platforms such as Instagram or comparable platforms like YouTube and TikTok, where the amount of influencer-generated content is so immense that monitoring is all but impossible to do manually. Apart from making brands legal-compliant with the legal cases of AI use, the integration of AI into digital promotions enhances a favorable advertisement area that benefits both customers and marketers.

12. Conclusion and Recommendations

There are significant legal and ethical challenges associated with stealth marketing, particularly regarding its impact on consumer trust and brand perception. The first significant effect of masked ads is to erode trust, which impacts brand credibility among consumers as well as their loyalty. To

address these issues, global standards for advertising disclosures should be strengthened. A universal policy requiring consistent disclosure labels like #ad or #sponsored across platforms would help consumers easily recognize sponsored content. This approach could be enforced through collaboration between governments, regulatory authorities, and social media applications. For instance, Instagram and YouTube can use automated ad labels or algorithm changes to identify sponsored content. This would make sure that the ad disclosures are not only visible but also impossible to ignore. Besides, social media platforms might promote content that complies with disclosure regulations while hiding or reducing others that do not meet the standards. Furthermore, brands and influencers should be incentivized to comply with transparency rules through the imposition of fines for non-disclosure and rewards for adherence to best practices.

Nonetheless, applying the ad-label policy is not easily feasible across countries with various legal frameworks. While there are specific regulations under the Federal Trade Commission (FTC) rules in the USA, other areas might have fewer rigid rules or no definite guidelines regarding the transparency of advertisements. To fill these gaps, multinational firms should assume a more active and flexible role, employing more targeted and direct disclosures in potentially less transparent nations while continuing to act transparently within the global marketplace. For instance, in the US, brands could use more specific ad labels and disclaimers, which are usually in the form of pop-ups or other visual notifications. In regions with less stringent regulations, multinational companies should take proactive steps to ensure transparency by voluntarily adopting global best practices. In addition to policies, organizations ought to harness techniques such as ad verification that guarantee adherence to the policies. Influencers must also integrate practices suitable for these moderating expectations, such as cognitively acknowledging and representing brand collaborations conspicuously. Thus, by adopting the norms of global transparency and applying innovative technologies, firms can establish a more solid base for consumer trust when operating in environments with diverse legal frameworks.

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