

# 1. Standard form consumer contracts: the background and context

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## STANDARD FORM CONTRACTS: INTRODUCTION

The problems caused by the use of standard form contracts in consumer transactions have long been recognised. As early as 1943, Friedrich Kessler had used the term ‘contract of adhesion’ to describe the type of ‘take it or leave it’ contract that had become commonplace in many consumer transactions.<sup>1</sup> According to Kessler, the ‘increasingly important’ aspect of these standard contracts was that they were typically used by enterprises with strong bargaining power.

The weaker party, in need of the goods or services, is frequently not in a position to shop around for better terms, either because the author of the standard contract has a monopoly (natural or artificial) or because all competitors use the same clauses. His contractual intention is but a subjection, more or less voluntary to terms dictated by the stronger party, terms whose consequences are often understood only in a vague way, if at all. Thus, standardized contracts are frequently contracts of adhesion; they are ‘a prendre ou a laisser.’<sup>2</sup>

Standard form contracts have been problematic for courts and contract law scholars because they depart so radically from the classic contract law notion of a bargained-for agreement freely entered between the parties. In the contract of adhesion, the voluntariness of consent to the contract terms is questionable, and there is a danger of the stronger party imposing one-sided terms. Kessler warned that standard form contracts could enable businesses to ‘legislate by contract’ and that they could ‘thus become effective instruments in the hands of powerful industrial and commercial overlords enabling them to impose a new feudal order of their own making upon a vast host of vassals’.<sup>3</sup>

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<sup>1</sup> Friedrich Kessler, ‘Contracts of Adhesion – Some Thoughts about Freedom of Contract’ (1943) 43 *Columbia Law Review* 629.

<sup>2</sup> *Ibid.*, 632.

<sup>3</sup> Kessler (n. 1) 640.

By the end of the twentieth century, use of standard form contracts was widespread and accepted as part of everyday life both for routine transactions and for more important consumer agreements such as insurance, property, mortgages and credit.<sup>4</sup>

David Slawson, writing about standard form contracts in 1971, observed that

most persons have difficulty remembering the last time they contracted other than by standard form; except for casual oral agreements, they probably never have. But if they are active, they contract by standard forms several times a day. Parking lot and theatre tickets, package receipts, department store charge slips, and gas station credit card purchase slips are all standard form contracts.<sup>5</sup>

Slawson's observation remains accurate today. We could add, however, that most people may have difficulty remembering the last time they contracted other than by *electronic* standard form. The evolution of the digital age has caused the electronic standard form to become dominant and has resulted in increased use of standard form contracts. Nowadays, lengthy electronic contract terms accompany most online consumer transactions regardless of their size or significance. Consumers are accustomed to clicking to agree on websites for all kinds of goods and services including digital content, social networking sites, airline tickets, insurance policies and telecommunication services. Even simply using or browsing a website is now often subject to an electronic standard form contract.

### The Benefits of Standard Form Contracts

The rapid rise of the standardised mass contract was an inevitable response to the mass production that had accompanied the industrialisation of the nineteenth and twentieth centuries and was largely driven by economic efficiency. Rather than entering individual negotiations or modifications of terms with each customer, a business that used a standard form could substantially reduce the costs of transacting and this allowed for the efficient mass distribution of goods, also potentially resulting in cheaper goods and services for the consum-

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<sup>4</sup> See Kessler (n. 1) 631, noting that 'once the usefulness of these contracts was discovered and perfected in the transportation, insurance, and banking business, their use spread into all other fields of large scale enterprise, into international as well as national trade, and into labor relations'.

<sup>5</sup> David Slawson, 'Standard Form Contracts and Democratic Control of Law-Making Power' (1970) 84 *Harvard Law Review* 529.

er.<sup>6</sup> Other efficiencies also came to be associated with the use of the standard form, including, for example, the efficient management of risk.<sup>7</sup> Being in the best position to understand the risks they can bear most effectively, businesses can allow the exclusion of those that are difficult to calculate and make other risks uniform for all similar transactions, thus minimising the cost of the product or service. Standard forms also reduce agency costs in mass-market transactions by removing agents' authority to agree to any changes in the terms of the contract that might reallocate risks to the principal and result in related costs if those risks were to materialise.<sup>8</sup> Other advantages of standard forms relate to their strategic importance, for example as an integral part of a business model that may be used to meet a particular business need or to address problems within a particular industry.<sup>9</sup> Further, standard forms have been considered important in encouraging the development of particular trade norms or practices that might facilitate the growth of that trade where otherwise there might be undue restrictions.<sup>10</sup>

The benefits of standard form contracting thus came to be generally accepted – that they are efficient, that there are societal benefits associated with their use, and that their prevalence was essential to facilitate transactions in an economy that was dependent on mass production and distribution.<sup>11</sup> No different to its paper counterpart, the electronic standard form also allows businesses to reduce transaction costs and manage risk, and indeed use of

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<sup>6</sup> See Kessler (n. 1) 632 stating that 'In so far as the reduction of costs of production and distribution thus achieved is reflected in reduced prices, society as a whole ultimately benefits from the use of standard contracts.' Although other scholars have questioned the extent to which this passing on of reduced cost to the consumer is validated in practice. See Margaret Jane Radin, *Boilerplate, The Fine Print, Vanishing Rights, and the Rule of Law* (Princeton University Press 2013) 290 n. 21.

<sup>7</sup> Kessler (n. 1) 631.

<sup>8</sup> Todd D. Rakoff, 'Contracts of Adhesion: An Essay in Reconstruction' (1982–83) 96 *Harvard Law Review* 1173, 1223.

<sup>9</sup> See Nancy S. Kim, *Wrap Contracts: Foundations and Ramifications* (Oxford University Press 2013), 22–23, discussing the use of standard form contracts to extend credit, thereby enabling average consumers to purchase high-priced items such as sewing machines and cars that they otherwise could not afford and thereby fuelling the growth of industries producing those goods.

<sup>10</sup> Kim (n. 9) 25, discussing the development of standard terms allowing carriers to contract out of liability for negligent acts; and consumer standard software licences that permitted software developers to maintain control over the software after it was sold.

<sup>11</sup> For further discussion of the benefits of standard form contracting, see Kessler (n. 1); Rakoff (n. 8); Richard L. Hasen, 'Efficiency under Informational Asymmetry: The Effect of Framing on Legal Rules' (1990–91) 38 *UCLA Law Review* 391; Robert Hillman and Jeffrey Rachlinski, 'Standard-Form Contracting in the Electronic Age' (2002) 77 *NYU Law Review* 429.

the standard contract is essential to e-commerce given that one of its central characteristics and the reason for its efficiency is that there is no necessity for the business to use human agents to complete transactions.<sup>12</sup>

### Problems Associated with Contracts of Adhesion

Despite the benefits associated with the use of standard form contracts, the problems that Kessler first identified as being associated with use of business to consumer standard form contracts are now universally accepted. Consumers enter transactions where the terms are dictated by the stronger party and where there is little choice but to accept those terms or not to participate at all. The terms are likely to be one-sided with the supplier allocating rights and responsibilities to its advantage. Consumers are also unlikely to have read the standard terms before concluding the contract.<sup>13</sup> This is because the consumer recognises the realities of the situation: that there is no possibility to negotiate the terms, that the terms are long, and that the consumer is unlikely to understand them, that competing businesses usually offer the same or similar terms, and that the risks allocated to the consumer are unlikely to arise.<sup>14</sup>

These characteristics apply equally to traditional standard forms and to online standard form contracts. Like their paper counterparts, online standard form contracts contain terms drafted by one party to the transaction, that party having the power to offer these terms on a 'take it or leave it' basis. Online users also typically do not read the terms and different terms cannot be negotiated. Yet, there are significant differences between paper and electronic contracts that may adversely affect online adherents. The electronic environment offers possibilities to businesses to present terms to consumers in various ways that consumers may fail to notice. Terms of use, terms of service and other terms and conditions may be located in several different places, accessible via numerous hyperlinks. The burden rests on the consumer to track down the terms and reconcile the various provisions in each location. Because many consumers fail to notice them, businesses may increase the number of terms and this can be done without any corresponding increases in reproduction and distribution costs such as might occur in the world of paper contracting and that might otherwise be a deterrent.<sup>15</sup> Electronic standard forms are notoriously

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<sup>12</sup> Hillman and Rachlinski (n. 11) 476.

<sup>13</sup> See further Ian Ayres and Alan Schwartz, 'The No-Reading Problem in Consumer Contract Law' (2014) 66 *Stanford Law Review* 545.

<sup>14</sup> For an account of the characteristics of a classic contract of adhesion, see Rakoff, 'Contracts of Adhesion: An Essay in Reconstruction' (n. 8) 1177.

<sup>15</sup> Nancy S. Kim, 'Situational Duress and the Aberrance of Electronic Contracts' (2014) 89 *Chicago-Kent Law Review* 265. See also Kim, *Wrap Contracts: Foundations and Ramifications* (n. 9) 58.

lengthy and complex. The digital form also allows businesses to experiment with presentation styles, graphics and font sizes in order to attract potential customers and perhaps arrange terms in ways to minimise consumer scrutiny. Transacting online also allows for businesses to collect information on consumer preferences and to measure the effects of their electronic marketing strategies.<sup>16</sup>

Added to this, electronic contract formation methods may be problematic. In so-called 'browse-wrap' contracts, users are said to have assented to terms simply by continuing to use the website after being given notice of terms. A user may not have any intention to be legally bound and may not be aware of the existence of contractual terms at all. In 'click-wrap' contracts, users consent to terms by clicking 'I agree'. Although an affirmative act of clicking is required, it has been observed that consumers are habituated to click-wrap agreements<sup>17</sup> and that they might not attach the same significance to the click as to a signature on a paper form.<sup>18</sup>

The typical characteristics of standard form contracts, whether online or in traditional form, give rise to concerns as to procedural fairness and as to the quality of consent to the standard terms; as well as to concerns that the trader may seek to exploit its stronger position to impose onerous obligations on the consumer. Traders may use standard terms that seek to alter or limit background legal rights such as widely drafted limitations or exclusions of liability; or terms that limit or exclude access to justice such as arbitration or jurisdiction clauses. Unilateral modification clauses are a notable feature of electronic standard form contracts that allow businesses to continuously modify terms with little notice to consumers. Notice is often simply posted on the business website with the burden of discovering modification of terms being left to consumers who will therefore often be unaware of changes.<sup>19</sup>

It has been observed that by imposing one-sided standard terms, the drafter of the terms is acting more like a lawmaker than a private contracting party.<sup>20</sup>

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<sup>16</sup> Hillman and Rachlinski (n. 11) 482.

<sup>17</sup> Rainer Böhme and Stefan Köpsell, 'Trained to Accept? A Field Experiment on Consent Dialogs', ACM Conference on Human Factors in Computing Systems (2010, Atlanta, Georgia) available at <http://dmrussell.net/CHI2010/docs/p2403.pdf>. This study finds that users tend to blindly accept terms whose presentation resembled a typical end-user licence agreement (EULA) because of the ubiquity of such agreements.

<sup>18</sup> Juliet M. Moringiello, 'Signals, Assent and Internet Contracting' (2004–2005) 57 *Rutgers Law Review* 1307.

<sup>19</sup> Kim, *Wrap Contracts: Foundations and Ramifications* (n. 9) 55, noting that in this respect electronic standard form contracts may fail to satisfy the evidentiary function.

<sup>20</sup> See Kessler (n. 1) 640; Rakoff (n. 8) 1237; Slawson (n. 5).

In the internet era, this observation takes on renewed significance. Business to consumer online contracting is nowadays carried out on a huge scale. The internet has opened vast new markets, allowing businesses to transact not just within national boundaries, but also across borders, with the potential for each business to reach millions of consumers. Invariably, internet transactions are carried out on suppliers' terms, and often those terms are standardised across particular sectors. This gives businesses the ability to use the mechanism of private contract to impose their own terms upon the mass market. In this way, businesses potentially have power to distort the regime of consumer protection that is put in place through public means.<sup>21</sup> This raises public policy concerns regarding the substantive content of standard contracts that go beyond the individual parties to the transaction. It raises questions as to how best to reconcile the traditional private law concerns about justice between the parties with the regulation of contracts in the public interest.

Being so far removed from the classic model of negotiation and mutual agreement, the standard form contract has posed fundamental challenges to contract law that legal scholars working in all jurisdictions have grappled with throughout the twentieth century, with various approaches being taken to provide protection for users of standard forms. This chapter discusses contract law theories on standard form contracts and the rationale for intervention to protect consumers. Much of the early scholarship on standard form contracts is written in the common law tradition, and much of it originated in the US where, in contrast to the EU, the debate did not result in the introduction of general public regulation of the substantive content of standard form contracts. This lack of regulation reflects a market-oriented approach to consumer protection which considers intervention as necessary only where competition in the market does not protect consumers, and contrasts with the EU model, the rationale for which is based around social as well as economic policy goals. Despite the different approaches, an examination of the varying perspectives of contract law theorists is highly useful in understanding the background to the introduction of the Unfair Contract Terms Directive (UCTD)<sup>22</sup> and issues arising in current law and practice that are discussed in later chapters.

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<sup>21</sup> See Radin, *Boilerplate, Vanishing Rights and the Rule of Law* (n. 6) 33, referring to the use of 'mass market boilerplate deletion schemes' as a process of 'democratic degradation'. See further discussion below, 'Standard Form Contracts and Public Policy'.

<sup>22</sup> Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts OJ L 95/29 (Unfair Contract Terms Directive).

## THE CONTEXT: THE DECLINE OF FREEDOM OF CONTRACT

One of the important questions for contract law was the extent to which controls could be imposed on standard form contracts without encroaching too much on the notion of party autonomy or freedom of contract. Prior to the advent of standardisation in the nineteenth century, contract was thought of primarily in terms of individualism.<sup>23</sup> In this environment, the principal relationships between individuals were viewed as competitive, and contract law developed its rules as to 'duty to read'.<sup>24</sup> People who willingly chose to bind themselves to documents that they had not read or understood were not protected by the law. The rule was adopted by the common law courts, becoming part of the general law of contract and was also applied in the context of standard forms.<sup>25</sup>

This era of individualism coincided with the high point of theories of natural law, freedom of contract and laissez-faire economics. Writing from the perspective of the English common law tradition, Atiyah explains freedom of contract as comprised in two concepts: first, it emphasised that contracts were based on mutual agreement, and second, it stressed that the creation of a contract was the result of a free choice unhampered by external control such as government or legislative interference.<sup>26</sup> Within this view, the function of contract law is simply to enforce contracts where they reflect the free will of the contracting parties; and to avoid any inquiry into the substantive justice of the contractual terms.

As societal conditions changed, however, this era of individualism also declined and there was a period of gradual decline in belief in freedom of contract. Atiyah traces this decline as occurring from 1870 to 1980 and attributes this to three factors. First, the emergence and widespread use of the standard form contract, second the declining importance attached to free choice and intention as grounds of legal obligation<sup>27</sup> and third, the emergence of the

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<sup>23</sup> See Michel Rosenfeld, 'Contract and Justice: The Relation between Classical Contract Law and Social Contract Theory' (1984) 70 *Iowa Law Review* 769.

<sup>24</sup> David Slawson, 'The New Meaning of Contract: The Transformation of Contracts Law by Standard Forms' (1984–1985) 46 *University of Pittsburgh Law Review* 21, 28.

<sup>25</sup> An early manifestation of the rule in English common law is to be found in *Lewis v Great Western Railway* (1877) 3 QBD 195. See also *L'Estrange v Graucob* [1934] 2 KB 394.

<sup>26</sup> S.A. Smith and P.S. Atiyah, *Atiyah's Introduction to the Law of Contract* (6th edn, Oxford University Press 2006), 10.

<sup>27</sup> The objective approach to questions of agreement and intention had steadily gained acceptance in the common law. This meant that contract law was not concerned with finding subjective agreement but rather looked at whether the parties' conduct and

consumer as a contracting party.<sup>28</sup> Decreasing individualism gave rise to an increase in the use of standard forms as larger commercial enterprises began to emerge, with more complex bureaucratic structures, more averse to individualised transactions with consumers.<sup>29</sup>

By the mid twentieth century, standard form contracts were recognised as one of the major problems of contract law.<sup>30</sup> Atiyah notes that the vast majority of the most important contracts made by the average citizen were made on terms that were essentially imposed on him, and ‘most astonished the average citizen would be if he understood those contracts, let alone agreed to them in any real sense’.<sup>31</sup> Inequalities in bargaining power, social and economic pressures (often pressures of poverty) and the use of standard forms now meant that there was no real freedom of choice in many situations.

In this period, the UK economy began to experience huge growth of monopolies and restrictive practices, which exacerbated the problem. These developments restricted freedom of choice and caused many to doubt the efficacy and justice of freedom of contract. Atiyah also refers to a change in political values. Between 1870 and 1980, collectivist and socialist values became widespread in England. ‘The idea that free and voluntary exchange was the secret to economic prosperity, and indeed perhaps to a generally freer and more contented society, went into steep decline.’<sup>32</sup>

Gradually, it was understood that the weak, poor and vulnerable needed protection by the law. If left to make their own contracts they would ‘inevitably be worsted by rich and powerful contracting parties on the other side’.<sup>33</sup> In the UK, Parliament began to intervene in many ways to prohibit certain types of contract or to regulate certain contract terms. Employment legislation was passed to confer rights on employees, hire-purchase legislation was enacted, and landlord and tenant legislation was passed to enhance tenants’ rights. The Unfair Contract Terms Act 1977 was enacted to restrict the use of exemption clauses in contracts. By the middle of the twentieth century, the judges were also influenced by this type of legislation and showed themselves willing to try

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language would lead a reasonable person to assume that they had agreed. See *Smith v Hughes* (1870–71) LR 6 QB 597.

<sup>28</sup> Smith and Atiyah (n. 26) 10.

<sup>29</sup> Slawson, ‘The New Meaning of Contract’ (n. 24) 28.

<sup>30</sup> P.S. Atiyah, *The Rise and Fall of Freedom of Contract* (Clarendon Press 1985); P.S. Atiyah, *Essays on Contract* (Oxford University Press 1990); Smith and Atiyah (n. 26).

<sup>31</sup> Smith and Atiyah (n. 26) 12.

<sup>32</sup> Ibid., 20.

<sup>33</sup> Ibid., 23.

to assist the weaker party to a contract by implying suitable terms into a contract or adopting a construction of the terms favourable to the weaker party.<sup>34</sup>

Other countries in Europe at this time were also following this trend towards intervening in the market to protect perceived weaker parties to transactions, according to ideas of social justice and the welfare state. Most European countries had also enacted employment legislation and landlord and tenant legislation; and there was increasing awareness of consumers' rights and various interventions to protect consumer transactions, including laws regulating standard terms.<sup>35</sup>

This trend was not followed everywhere. The US, for example, did not develop a European-style welfare state and significant differences in political culture and legal tradition resulted in diverging approaches, with the US having much less state regulation of markets. Solutions to the problem of standard form contracts tended to focus either on industry-specific disclosure rules, or the development of common law principles. By the mid 1960s most states had enacted the Uniform Commercial Code into law. The Code introduced the doctrine of unconscionability,<sup>36</sup> which was designed to avoid the incorporation and legal enforcement of one-sided, oppressive or unfair contracts or clauses. State legislatures, however, had not established guidelines for use of the doctrine so the task of interpreting and developing these mitigating doctrines fell to the courts and the judges to develop on a case-by-case basis. In Europe, on the other hand, statutory regulation became the focus from the 1970s onwards, although European countries adopted a variety of different regulatory approaches to the regulation of standard form contracts.<sup>37</sup>

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<sup>34</sup> Ibid., 30.

<sup>35</sup> For example, French law on unfair terms was introduced in the *loi Scrivener* in 1978 (now consolidated in the Code de la Consommation). Germany introduced regulation of unfair terms in 1976 in the AGB-Gesetz, although it was not limited to consumer contracts. The Italian legal system was the first in Europe to adopt rules to control unfair terms in standard contracts through Articles 1341 and 1342 of the Italian Civil Code 1942. See further Paolisa Nebbia, *Unfair Contract Terms in European Law: A Study in Comparative and EC Law* (Bloomsbury 2007) 5.

<sup>36</sup> Article 2.302. Article 2.302 is limited to contracts for the sale of goods, but the unconscionability doctrine has been included in other uniform Acts such as those dealing with consumer credit and property law as well as in the Restatement (Second) of Contracts.

<sup>37</sup> See Thomas Wilhelmsson, 'Various Approaches to Unfair Terms and their Background Philosophies' (2008) *XIV Juridica International Law Review* 51.

## LEGAL THEORIES OF STANDARD FORM CONTRACTS

Throughout the twentieth century, many contract law scholars attempted to develop analytical frameworks to address the challenges associated with standard forms. Initially, commentators considered the issues within an exclusively private law framework, confining their analysis to the response of the courts within the context of the individual contracting parties, whereas later scholars began to expand the analysis and argue that standard form contracts should be viewed from a public interest perspective. In Europe, from the 1970s, legislatures and courts were focusing on social justice and protecting consumers as weaker parties in the contractual relationship. Despite the differences in approach to regulation that emerged between the US and EU, many of the contributions of US scholars were influential in the subsequent development of the law and are also helpful in understanding the underlying rationale for the regulation of standard form contracts, which is discussed later in this book as it relates to the UCTD.<sup>38</sup>

### Blanket Assent

In the US, in 1960, Karl Llewellyn proposed his famous theory of ‘blanket assent’ to standard form contracts in which he suggested that in standard form contracts the buyer assents to the few ‘dickered’ or bargained-for terms, but also gives a blanket non-specific assent to any other terms that are neither ‘unreasonable’ nor ‘indecent’.<sup>39</sup> Llewellyn suggested that the adherent to the form contract assents in the sense of placing confidence in the drafting party to fill in the terms of the deal, much like handing over a blank cheque. He noted that most standard form terms are legitimate and reasonable, and therefore, they ought to be sustained and applied. He further proposed that a workable guide for the courts could be sought to allow judges to distinguish between those reasonable terms and ‘clauses of oppression or outrage’.<sup>40</sup>

Some subsequent scholars also took the view that specific knowledge of all the terms of a standard form was not necessary. Randy Barnett, for example, theorised that if consent to be legally bound is the basis of contractual enforcement, then in principle, a person can consent to be bound by unread terms

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<sup>38</sup> See Chapter 2.

<sup>39</sup> Karl N. Llewellyn, *The Common Law Tradition: Deciding Appeals* (reprint edition, William S. Hein & Co. 1996).

<sup>40</sup> *Ibid.*, 366.

contained, for example, in a sealed envelope.<sup>41</sup> According to Barnett, as long as there are limits on what the obligation can be, and as long as the terms are not 'radically unexpected', the terms can be enforceable.<sup>42</sup> Omri Ben-Shahar also shares this view of form contracts, arguing that people can agree to buy a surprise, e.g. a lottery ticket; or they can agree to buy a car or a cell phone where some of the features are discovered only later through experience or use.<sup>43</sup> According to Ben Shahar, it is understood in these cases that agreement is not lacking due to the surprise; rather, the buyer is providing blanket assent to the known and unknown features of the deal.<sup>44</sup>

Other scholars, however, have been firmly opposed to the notion of blanket assent. Todd Rakoff, in his classic article on contracts of adhesion, argued that Llewellyn's approach extended the idea of assent to such an extent that it was 'fictitious or forced'.<sup>45</sup> David Slawson was also critical of Llewellyn's theory, believing that it was wrong on policy grounds.<sup>46</sup> According to Slawson, the purpose of requiring that someone consent to something in order that it is considered to be legitimate, is that his consent provides him with an understanding of what he is allowing to happen, and in some situations, with control over what it will be. So, for example, consent is by law a defence to almost any tort, but the law does not consider the consent to be valid unless the person was reasonably expected to have understood what he was consenting to.<sup>47</sup>

Slawson also used the analogy of democratic government, where political tradition requires that government be 'with the consent of the governed',<sup>48</sup> and argued that no one would consider that consent to have been obtained if the candidates had merely stated that if elected, they would not do anything unreasonable or indecent. 'Government with only the "blanket assent" of the governed would be a democracy in name only.'<sup>49</sup> Applying these principles to contract law, he finds that the notion of blanket assent is too broad to give the adhering party the understanding and control that he ought to have.<sup>50</sup>

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<sup>41</sup> Randy Barnett, 'Consenting to Form Contracts' (2002–03) 71 *Fordham Law Review* 627, 636.

<sup>42</sup> *Ibid.*, 637.

<sup>43</sup> Omri Ben-Shahar, 'The Myth of the Opportunity to Read in Contract Law' (2009) 5 *European Review of Contract Law* 1.

<sup>44</sup> *Ibid.*

<sup>45</sup> Rakoff (n. 8) 1206.

<sup>46</sup> David Slawson, 'The New Meaning of Contract' (n. 24).

<sup>47</sup> *Ibid.*, 35.

<sup>48</sup> *Ibid.*

<sup>49</sup> *Ibid.*

<sup>50</sup> *Ibid.*

Margaret Jane Radin, writing more recently, has also been strongly critical of the idea of blanket assent.<sup>51</sup> For those who are not contract theorists, she compares the approach with ‘buying a pig in a poke’<sup>52</sup> and views it as part of a process of ‘devolution or decay of the process of voluntariness’<sup>53</sup> where ‘agreement gets reduced to consent, then further reduced to assent. Next assent becomes “blanket assent” to unknown terms, provided they are what the consumer – an abstract general construct of a “consumer” – might have expected.’<sup>54</sup> According to Radin, one of the problems with the approach is the ambiguity of the term ‘expectation’ which ‘makes for murky and unpredictable jurisprudence’.<sup>55</sup> The notion that expectation amounts to consent to particular terms is also problematic for Radin where ‘boilerplate consistently shrinks legal rights to the vanishing point’.<sup>56</sup> Radin refers to this problem as ‘normative degradation’ for the legal system and questions attempts by scholars such as Llewellyn and Barnett to use traditional contract theory to expand the notion of consent to justify enforcing boilerplate schemes.

### Visible and Invisible Terms

Writing in 1983, Todd Rakoff suggested a model based on the notion that the standard terms in a contract of adhesion should be considered presumptively unenforceable.<sup>57</sup> Within this model, he distinguishes between ‘visible’ and ‘invisible’ terms. The visible terms are those which a large portion of adherents may be expected to have bargained for and known about, such as the price term. These terms are the ones that the adherent agrees to. The rest, according to Rakoff, are not agreed to and should be presumed to be unenforceable and replaced by terms supplied by statutory regulation or by the courts. Where a drafting party argues that an ‘invisible’ term should be enforced, the court must first decide what background law would apply in the absence of the form term. If the result of applying the background law and the form term is the same, then the court must ignore the form term and apply the background law. If the form term and the background term are different, then the reasons supporting the form terms must be considered relevant, and the drafter bears

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<sup>51</sup> Radin, *Boilerplate: The Fine Print, Vanishing Rights, and the Rule of Law* (n. 6).

<sup>52</sup> *Ibid.*, 84.

<sup>53</sup> *Ibid.*, 82.

<sup>54</sup> *Ibid.*

<sup>55</sup> *Ibid.*, 85.

<sup>56</sup> *Ibid.*, 30. ‘Boilerplate’ is commonly used in the US to refer to fine-print standard terms and conditions.

<sup>57</sup> Rakoff, ‘Contracts of Adhesion: An Essay in Reconstruction’ (n. 8).

the burden of providing the necessity of the enforcement of the term on the basis of public interest.

Rakoff's approach, whilst novel, also attracted criticism from commentators, largely based on the impracticality of its scheme. Barnett, for example, while acknowledging that the distinction between visible and invisible terms was 'highly useful',<sup>58</sup> nevertheless was dubious as to whether courts and legislatures can write terms that better serve the interests of the contracting parties than the drafter of the form. Barnett also argues that the imposition of more favourable terms contrary to the form terms would raise the cost of the transaction and this may disadvantage the party who is supposed to benefit from the intervention. Additionally, Barnett sees the terms that are imposed on parties as even more removed from the transaction than a form, moving an agreement even further from the consent of the parties, 'toward a regime in which the legal system supplies the terms that others think best'.<sup>59</sup>

Rakoff's approach may not have been universally accepted, but his idea of separating standard forms into visible and invisible terms is echoed in the treatment of so called 'core terms' under the UCTD, where those terms are exempt from the scope of the Directive's unfairness test as long as they are transparent.<sup>60</sup> Like Rakoff's theory, the rationale for the exemption is that these core terms (such as the price and subject matter) are 'visible' to the consumer and are actually agreed upon. The other terms of the contract are 'invisible' and therefore are subject to controls imposed by the legislation. The notion is also akin to Llewellyn's description of 'dickered' terms as those that are actually agreed between the parties, in contrast to the ancillary terms for which there is presumed to be blanket assent unless they are unreasonable or 'indecent'.

### Standard Form Contracts and Public Policy

Whereas Llewellyn's theory had attempted to develop an analysis of standard form contracts within the private law framework, other commentators began to look at the question in the light of public policy. Slawson, for example, writing in 1971, viewed the process of contracting as essentially law-making.<sup>61</sup> Further, he finds that much of the 'law' made by standard form contracts is not democratic in nature because only one of the two 'citizens' has meaningfully consented to the terms of the contract.<sup>62</sup> Similarly, Radin likens 'mass-market

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<sup>58</sup> Barnett, 'Consenting to Form Contracts' (n. 41) 634.

<sup>59</sup> Ibid.

<sup>60</sup> See Chapter 3.

<sup>61</sup> David Slawson, 'Standard Form Contracts and Democratic Control of Lawmaking Power' (n. 5).

<sup>62</sup> Ibid., 530.

systems of form contracts' to a form of undemocratic law-making, replacing the law of the state with the 'law' of the firm.<sup>63</sup> Along with the problem of consent in mass-market standard forms (normative degradation), Radin sees this as a situation where systems of contracts can delete rights that are granted through democratic processes (democratic degradation).<sup>64</sup>

Slawson's proposed solution to this undemocratic law-making is a framework derived from administrative law principles. According to his analysis, the standard form is not the contract. Instead, the contract is deemed to be composed of terms on which the parties did agree, such as the price and other basic terms, plus the expectations that the context of the transaction would imply. The remaining standard terms are delegated to the supplier to provide. They would then be scrutinised by the courts for consistency with the negotiated terms, in the same way as administrative regulations which must be consistent with their enabling legislation. The benchmark for assessment would be 'non-authoritative standards' that would serve to demonstrate that the terms were in the public interest'.<sup>65</sup> This, according to Slawson, would serve both to improve the law and to make it democratic, despite its non-democratic origins.

Some commentators, such as Rakoff, found flaws in the public law analogy (particularly in the attempt to legitimise the delegating to private parties to decide where the public interest lies).<sup>66</sup> Slawson, writing in 1985,<sup>67</sup> was himself critical of some aspects of his administrative law analogy.<sup>68</sup> Nevertheless, the contribution was very influential, not least in his forceful conclusion that standard forms as they are commonly used are not contracts, that the parties' contract should be deemed to be composed of terms to which they did agree plus the expectations that the context of the transaction would imply.

Radin also argues that where businesses use mass-market standard forms, they should not be referred to as contractual agreements, but instead should be viewed through a tort law framework such as product liability.<sup>69</sup> For these types of forms, which involve rearranging the adhering party's background legal rights, Radin argues that it is too difficult to stretch contract's justificatory rationales. She proposes a new tort, 'intentional deprivation of basic legal rights', the remedy for which would be that the offending terms should be declared invalid *in toto*, and recipients instead should be governed by back-

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<sup>63</sup> Radin, *Boilerplate: Fine Print, Vanishing Rights and the Rule of Law* (n. 6) 16.

<sup>64</sup> *Ibid.*, 15–16.

<sup>65</sup> Slawson (n. 5) 533.

<sup>66</sup> Rakoff (n. 8) 1213.

<sup>67</sup> Slawson, 'The New Meaning of Contract: The Transformation of Contracts Law by Standard Forms' (n. 24).

<sup>68</sup> *Ibid.*, 40.

<sup>69</sup> Radin (n. 6) 209–216.

ground legal default rules.<sup>70</sup> Radin also generally criticises the US preference for private market solutions that evolve to address particular problems, and advocates regulating the substance of terms through a rules-based approach such as black-listing some terms or sets of terms.<sup>71</sup> Overall, she calls for abandoning the attempt to regulate mass-market boilerplate (standard forms) within contract law, and instead to see it as being similar to product safety regulation or as a *sui generis* regime to regulate overreaching in standard forms.

Radin's reference to 'democratic degradation' and her call to escape from a contract law framework for the regulation of mass-market standard forms is interesting when placed in the context of the inherent conflict in the UCTD between its contextual unfairness test seeking to restore balance between private contract parties and its role in protecting the public interest through collective litigation and public administrative action. Radin refers to the 'almost polar opposite positions' of US and EU law with regard to the acceptability of onerous clauses in consumer contracts.<sup>72</sup> She refers to the EU's 'comprehensive regulatory solution'<sup>73</sup> and approves of a more rules-based approach of black-listing or grey-listing certain terms in order to counteract the democratic degradation caused by mass-market boilerplate schemes that divest consumers of basic rights. Although the UCTD does provide the rules-based approach that Radin calls for, there are significant challenges associated with applying its contextual unfairness test in collective litigation or to monitor the market in order to eliminate widespread use of unfair terms such as those 'mass-market boilerplate deletion schemes' referred to by Radin. Later chapters explore this tension at the heart of the UCTD and how the conflict can be overcome in order to optimise protection for consumers against the threat of unfair terms in mass-market contracts, a threat that has become ever more pressing against the backdrop of the digital transformation and the huge numbers of European consumers that are potentially at risk from such mass-market rights deletion schemes.

## Contract as Thing

Radin was not the first to make the analogy between regulating standard terms and regulating defective products. In a series of articles between 1967 and 1970, Arthur Leff introduced and developed the notion of 'contract as thing'.<sup>74</sup>

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<sup>70</sup> Ibid., 212.

<sup>71</sup> Ibid., 219 *et seq.*

<sup>72</sup> Ibid., 240.

<sup>73</sup> Ibid., 233.

<sup>74</sup> Arthur Allen Leff, 'Unconscionability and the Code – The Emperor's New Clause' (1966–67) 115 *University of Pennsylvania Law Review* 485; Arthur Allen

According to this theory, consumer adhesion contracts should not be thought of as contracts, but instead should be viewed as part of the product. Once this is established, it is easier to discuss what governmental regulatory decisions ought to be made about the quality of these ‘products’. According to Leff, thinking in this way might influence the regulation of the transaction, and provide a better conceptual framework for direct governmental quality controls. When products are dangerous or worthless, the government does directly intervene, therefore there is no reason, according to Leff, why intervention should not take place directly with respect to contract as things.<sup>75</sup> Leff acknowledged that a limitation of the approach is that it is not easy to tell when things should be regulated and what kind of clauses ought to be illegal. He therefore advocated not directly regulating quality but increasing the availability and quality of the information on which buying decisions are based.<sup>76</sup>

### Law and Economics

Leff’s view of the contract as the product was later developed and extended by other US scholars in the ‘law and economics’ school, who used the idea to justify information-based regulation of standard terms.<sup>77</sup> These scholars also ascribe to the view that the traditional notion of the consumer consenting to terms as part of the contractual transaction does not apply, and that the terms should be treated as part of the product, with governmental quality control in the form of increased information about the product (including the terms).

A law and economics analysis of standard form contracts focuses on market efficiency rather than on inequality between the parties. Under this analysis, in a perfectly functioning market, contracts will only contain efficient terms and the parties are free to enter contracts to enhance their welfare. The traditional starting point of the law and economics analysis is ‘rational choice’ theory, an economic principle that assumes that individuals always make decisions providing them with the greatest benefit and that provide maximum self-interest.<sup>78</sup>

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Leff, ‘Unconscionability and the Crowd – Consumers and the Common Law Tradition’ (1969–70) 31 *University of Pittsburgh Law Review* 349; Arthur Allen Leff, ‘Contract as Thing’ (1970) 19 *American University Law Review* 131.

<sup>75</sup> Leff, ‘Contract as Thing’ (n. 74) 147.

<sup>76</sup> Ibid.

<sup>77</sup> See for example, Douglas G. Baird, ‘The Boilerplate Puzzle’, (2006) 104 *Michigan Law Review* 933.

<sup>78</sup> For discussion of the background to rational choice theory, see Russell Korobkin and T.S. Ulen, ‘Law and Behavioural Science: Removing the Rationality Assumption from Law and Economics’ (2000) 88 *California Law Review* 1051; see also Russell Korobkin, ‘Bounded Rationality, Standard Form Contracts, and Unconscionability’ (2003) 70 *University of Chicago Law Review* 1203.

According to these theorists, intervention is only justified when the market is not competitive and the business has monopoly power, or when the consumer is not, or has not the ability to become, informed about the terms in the contract.<sup>79</sup> The informed consumer is therefore a cornerstone of this theory, and recent debate has centred around the extent to which consumers are able to or are willing to inform themselves as to standard form contract terms.

### **Information Asymmetry and the No-Read Problem in Consumer Standard Form Contracts**

It is by now established that the vast majority of consumers enter contracts without reading the terms.<sup>80</sup> This has been confirmed by a number of empirical studies surveying and testing user behaviour.<sup>81</sup> Evidence can also be found in a number of examples of website providers including highly unusual clauses in their contract terms without attracting the attention of users.<sup>82</sup> Further, the

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<sup>79</sup> Alan Schwartz and Louis L. Wilde, 'Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis' (1979) 127 *University of Pennsylvania Law Review* 630.

<sup>80</sup> Ayres and Schwartz, 'The No-Reading Problem in Consumer Contract Law' (n. 13).

<sup>81</sup> See for example, Robert A. Hillman, 'Online Consumer Standard Form Contracting Practices: A Survey and Discussion of Legal Implications' in Jane K. Winn (ed.), *Consumer Protection in the Age of the 'Information Economy'* (Routledge 2006); see also Yannis Bakos, Florencia Marotta-Wurgler and David R. Trossen, 'Does Anyone Read the Fine Print? Consumer Attention to Standard-Form Contracts' (2014) 43 *Journal of Legal Studies* 1 (finding that in a survey of 45,091 households, only one or two out of every thousand retail software shoppers choose to access the licence agreement, and those few that do, spend too little time, on average, to have read more than a small portion of the licence text).

<sup>82</sup> In 2010, GameStation, an online gaming store, posted terms and conditions with the following term: 'Should we wish to exercise this option, you agree to surrender your immortal soul, and any claim you may have on it, within 5 (five) working days of receiving written notification from gamestation.co.uk or one of its duly authorised minions.' The clause went on to provide that the clause could be nullified by clicking on a link. The link led to a page stating that the clause was an April Fool and congratulating the user on being 'so vigilant' and offering a £5 voucher. Over 7000 customers entered transactions on the site that day, and each of them clicked a box confirming that they had read and understood the terms and conditions. No customer clicked on the link, suggesting that none had read the terms carefully. '7,500 Online Shoppers Accidentally Sold their Souls to Gamestation', [www.huffingtonpost.com/2010/04/17/gamestation-grabs-souls-o\\_n\\_541549.html](http://www.huffingtonpost.com/2010/04/17/gamestation-grabs-souls-o_n_541549.html). Similarly, UK-based Wi-Fi company Purple inserted a joke clause in their terms and conditions requiring customers to agree to 1000 hours of community service, 'including but not limited to, cleaning toilets at festivals, scraping chewing gum off the streets and manually relieving sewer blockages'. Purple also offered a prize for anyone who actually read the terms and conditions. Only one person

literature suggests that buyers are ‘rationally ignorant’.<sup>83</sup> Consumers faced with a list of complex legal terms will recognise that it will take time to read and will be difficult to understand. The consumer will realise that the transaction costs of doing this will be out of proportion to the dangers of agreeing to imbalanced terms. Some suppliers try to increase these transaction costs further by using fine print and obscure presentation.<sup>84</sup> As noted above, this is exacerbated in electronic contracts where suppliers may make use of technology to experiment with presentation techniques that deter reading.<sup>85</sup> Even if they decide to devote time to reading, consumers recognise that they probably won’t understand the terms, which are often couched in legalese.<sup>86</sup> Consumers also recognise that there would be little to gain from reading the standard terms because there is no possibility to negotiate or influence the content of the terms, a fact which is particularly emphasised in electronic transactions where there is no human agent to interact with.<sup>87</sup> Consumers may also conclude that terms are standardised throughout particular industries and therefore that there is little point in comparing terms. They also believe that if the market is reasonably competitive, it is likely that the terms in the standard form contract allocate risks in an efficient manner and that most businesses will not include exploitative terms as this would entail risking reputational damage.<sup>88</sup> Given these factors, it is in fact rational for even a conscientious consumer to pay little, if any attention to standard contract terms.<sup>89</sup>

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claimed the prize, whilst 1000 customers agreed to the terms; [www.theguardian.com/technology/2017/jul/14/wifi-terms-and-conditions-thousands-sign-up-clean-sewage-did-not-read-small-print](http://www.theguardian.com/technology/2017/jul/14/wifi-terms-and-conditions-thousands-sign-up-clean-sewage-did-not-read-small-print).

<sup>83</sup> Melvin Aron Eisenberg, ‘The Limits of Cognition and the Limits of Contract’ (1994–95) 47 *Stanford Law Review* 211; G.K. Hadfield and others, ‘Information-Based Principles for Rethinking Consumer Protection Policy’ (1998) 21 *Journal of Consumer Policy* 131; Hillman and Rachlinski, ‘Standard-Form Contracting in the Electronic Age’ (n. 11); Geraint Howells, ‘The Potential and Limits of Consumer Empowerment by Information’ (2005) 32 *Journal of Law and Society* 349.

<sup>84</sup> Michael J. Meyerson, ‘The Efficient Consumer Form Contract. Law and Economics Meets the Real World’ (1990) 24 *Georgia Law Review* 583.

<sup>85</sup> Hillman and Rachlinski (n. 11) 49.

<sup>86</sup> Meyerson (n. 84) 598. See also Hillman and Rachlinski (n. 11) arguing that in electronic contracts the problem of legal jargon is exacerbated by the fact that the legal jargon must be read from a computer screen, is unlikely to be printed out by the user and that e-consumers cannot be expected to comparison shop among terms that they do not understand.

<sup>87</sup> Hillman and Rachlinski (n. 11) 43.

<sup>88</sup> *Ibid.*, 18.

<sup>89</sup> Meyerson (n. 84) 600.

The fact that terms are rarely read means that in effect they are invisible, and firms have little or no incentive to compete to offer high quality terms.<sup>90</sup> Even in a market which is price-competitive, if few consumers read the fine print, it is unlikely that a firm will try to offer higher quality terms, and firms will have more incentive to offer low prices than to compete in relation to the quality of the fine print. This will result in the proliferation of low-quality standard contract terms on the market.

This problem was outlined by Akerlof in his ‘market for lemons’ analysis,<sup>91</sup> which described how information asymmetry between buyers and sellers in the used car market can result in a reduction in quality of the goods traded, leaving only ‘lemons’ or poor-quality goods on the market. The rationale can also be applied to standard contract terms. If the only incentive is to compete on price and nothing else, firms will shift more costs onto customers through harsher terms. Customers, unaware of terms unless a problem arises, do not complain and as a result there is a race to the bottom with a trend towards ‘low cost, harsh term contracts’.<sup>92</sup>

### The Informed Minority Hypothesis

Many economic analysts argued that the problems of information asymmetry were overstated and that market forces could still discipline businesses using standard forms.<sup>93</sup> According to some analysts, if there is a minority of ‘informed, sophisticated and aggressive’<sup>94</sup> consumers in any given market who read and understand the standard terms, this would be enough to discipline the seller to behave as if all consumers were informed. Thus, if there is a critical mass of some consumers who read, this could correct the market failure.

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<sup>90</sup> V.P. Goldberg, ‘Institutional Change and the Quasi-Invisible Hand’ (1974) 17 *Journal of Law and Economics* 461.

<sup>91</sup> George A. Akerlof, ‘The Market for “Lemons”: Quality Uncertainty and the Market Mechanism’ (1970) 84 *Quarterly Journal of Economics* 488.

<sup>92</sup> Goldberg (n. 90) 483. See also Michael Schilling, ‘Directive 93/13 and the “Price Term Exemption”: A Comparative Analysis in the Light of the “Market for Lemons” Rationale’ (2011) *International and Comparative Law Quarterly* 933.

<sup>93</sup> Alan Schwartz and Louis L. Wilde, ‘Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis’ (1979) 127 *University of Pennsylvania Law Review* 630; George Priest, ‘A Theory of the Consumer Product Warranty’ (1981) 90 *Yale Law Journal* 1347; Michael J. Trebilcock, ‘Rethinking Consumer Protection Policy’ in Charles E.F. Rickett and Thomas G.W. Telfer (eds), *International Perspectives on Consumers’ Access to Justice* (Cambridge University Press 2003); Clayton Gillette, ‘Rolling Contracts as an Agency Problem’ (2004) *Wisconsin Law Review* 679.

<sup>94</sup> Trebilcock (n. 93) 93.

Indeed, in the online context, because e-consumers communicate easily about the type of terms used, the informed minority could be even more efficient at disciplining businesses.<sup>95</sup> Many law and economics analysts advanced this theory to oppose regulatory intervention in defence of party autonomy and freedom of contract.<sup>96</sup>

The ‘informed minority’ hypothesis was not, however, universally accepted. Many critics questioned whether such an informed minority could be created or could have the stated effect of disciplining the market. Ben-Shahar,<sup>97</sup> for example, doubts whether a small subset of readers could induce the necessary discipline upon the drafters of the standard form even if they have access to the terms and can read them thoroughly. Instead, he argues that sophisticated strategies would develop to ‘separate this group and give it the terms it is looking for without letting these terms trickle through also to the non-reading majority’<sup>98</sup> and perhaps even requiring non-readers to cross-subsidise those advantages for the readers. Hillman suggests that e-commerce would facilitate this separation into groups and enable businesses to gather data on consumer internet behaviour.<sup>99</sup> Eisenberg<sup>100</sup> argues that the informed minority will not have any effect unless a significant number of customers participate in the search for optimal terms. Typically, that will not occur because most customers will find it irrational to engage in search and deliberation on any given form.

The most persuasive counterargument to the informed minority analysis appears in an influential empirical analysis of end user licence agreements by Bakos, Marotta-Wurgler and Trossen.<sup>101</sup> In their study, the authors tracked the internet browsing behaviour of 48,154 monthly visitors to 90 online software companies. They found that only one or two out of every thousand retail software shoppers chose to access the terms of the agreement and most of those that did spent too little time to have read more than a small portion of the text. The authors therefore cast doubt on the relevance of the informed minority mechanism. As virtually no customers read the fine print, information about the nature of the agreement could neither spread nor impact the firm’s reputation, providing little incentive for firms to compete over the licence terms.

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<sup>95</sup> Robert A. Hillman, ‘Online Boilerplate: Would Mandatory Website Disclosure of E-Standard Terms Backfire’ (2005–2006) 104 *Michigan Law Review* 837, 843.

<sup>96</sup> See for example, Gillette (n. 93); Douglas Baird, ‘The Boilerplate Puzzle’ (n. 77); Priest (n. 93).

<sup>97</sup> Omri Ben-Shahar, ‘The Myth of the “Opportunity to Read” in Contract Law’ (2009) 5 *European Review of Private Law* 1.

<sup>98</sup> Ibid.

<sup>99</sup> Hillman (n. 95) 843.

<sup>100</sup> Eisenberg, ‘The Limits of Cognition and the Limits of Contract’ (n. 83).

<sup>101</sup> Bakos and others (n. 81).

Information asymmetry, the market for lemons problem and the unlikelihood of an ‘informed minority’ on a significant scale emerging to discipline the market, are factors that combine to provide a rationale for regulatory intervention that focuses on the provision of information as the key to correcting market failure. If consumers are properly informed (e.g. as a result of mandatory disclosure or improving accessibility and transparency), then this may restore the ability of consumers to make informed rational decisions. Information duty-based regulation is often favoured by law and economics scholars, as it preserves the parties’ freedom of contract – sufficiently informed consumers can correct the market failure and help themselves while still guaranteeing party autonomy. This type of regulation focuses on procedural fairness, i.e. ensuring that the process leading to the conclusion of the contract is fair. As long as the process is transparent and consumers are properly informed about the terms, then they can act in a self-reliant way to protect their interests.<sup>102</sup>

But this regulatory technique assumes that consumers are sophisticated and capable enough to understand the information which is provided in order to make the appropriate decision. Many consumers can respond properly to such information disclosure; however, this will depend on the way that the information is presented and the complexity of the product or service.<sup>103</sup>

### **Behavioural Economics and the Limits of Consumer Cognition**

Increasingly, there are insights from studies in behavioural economics that challenge the assumptions of the law and economics school and which suggest that there are certain limits on human cognition and bounds on behaviour which cause individuals to rely on heuristics and biases to cope with decision-making.<sup>104</sup> Many of these biases affect the way that consumers assess

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<sup>102</sup> See Chris Willett, ‘The Functions of Transparency in Regulating Contract Terms: UK and Australian Approaches’ (2011) 60 *International and Comparative Law Quarterly* 355.

<sup>103</sup> See Stephen Weatherill, *EU Consumer Law and Policy* (2nd edn, Edward Elgar Publishing 2013) 143, arguing that the more complex the product or service and the more complex the nature of the information, the less likely that the consumer will be able to respond to it in an intelligent way, thus weakening the pressure on traders to improve the quality of products and services.

<sup>104</sup> For background, see Christine Jolls and others, ‘A Behavioral Approach to Law and Economics’ (1997–98) 50 *Stanford Law Review* 1471; Russell Korobkin and T.S. Ulen, ‘Law and Behavioural Science: Removing the Rationality Assumption from Law and Economics’ (n. 78); Russell Korobkin, ‘Bounded Rationality, Standard Form Contracts, and Unconscionability’ (n. 78); Eisenberg, ‘The Limits of Cognition and the Limits of Contract’ (n. 83); Michael G. Faure and Hanneke A. Luth, ‘Behavioural Economics in Unfair Contract Terms’ (2011) 34 *Journal of Consumer Policy* 337;

standard terms. Consumers, for example, have limited capacity to process information and tend to rely on mental shortcuts to guide them in complex decisions about risks.<sup>105</sup> When making decisions, consumers may rely on partial information that is just enough to make them comfortable with their choice and are therefore unlikely to consider whether assessment of remote risks in the standard terms is important to the decision whether to enter the contract or not.<sup>106</sup> People also tend to have trouble balancing many factors in decision-making and tend to reduce their decisions to a small number of factors. In assessing standard terms, consumers therefore tend to reduce decisions to factors such as price and subject matter.<sup>107</sup> In addition, the ‘sunk cost effect’ means that where consumers have invested time and effort in the search for a product or service, they are reluctant to reverse and walk away because they find unattractive terms late in the process.<sup>108</sup> Consumers also tend towards selective optimism or overconfidence and may underestimate certain risks and tend to generalise information based on selective examples that particularly suit them. They believe that adverse events are more likely to apply to others and not themselves and therefore tend to believe that they can safely ignore risks of adverse events covered in the standard terms.<sup>109</sup>

As a result of these types of biases, even where consumers are provided with information about the nature of the transaction, they may not necessarily make decisions that maximise their welfare. There is also potential for businesses to exploit these biases to their advantage to impose one-sided terms and discourage reading. This may be particularly the case in the online environment, where strategies can more easily be used to deter reading. Hillman, for example refers to the ‘subtle manipulations’ whereby businesses can experiment with different website presentation styles, making use of data collected on the effects of marketing on consumer behaviour and allowing internet businesses to measure the effects of different styles of presentation.<sup>110</sup> The effects of rational ignorance and behavioural bias in the online environment are discussed further in Chapter 5.

These behavioural studies suggest that the idea of the self-reliant informed consumer being enough to discipline the market is not a realistic prospect.

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Hillman and Rachlinski (n. 11); Howells, ‘The Potential and Limits of Consumer Empowerment by Information’ (n. 83).

<sup>105</sup> Hillman and Rachlinski (n. 11) 450.

<sup>106</sup> This is known as ‘satisficing’. See Eisenberg (n. 83) 214; see also Faure and Luth (n. 104) 344; Hillman and Rachlinski (n. 11) 451.

<sup>107</sup> Hillman and Rachlinski (n. 11) 452; Faure and Luth (n. 104) 344.

<sup>108</sup> Faure and Luth (n. 104) 348.

<sup>109</sup> *Ibid.*, 344.

<sup>110</sup> Hillman and Rachlinski (n. 11) 481–482.

This is borne out by the empirical studies that have tested user behaviour and confirm that consumers do not read the fine print.<sup>111</sup> There are also useful empirical studies on the effectiveness of disclosure duties. Marotta-Wurgler, for example, finds that enhanced accessibility does not lead to enhanced reading.<sup>112</sup> She makes the conclusion that disclosure duties alone are not likely to improve terms or increase readership. Even where consumers read the terms, they were equally likely to purchase the product regardless of the one-sidedness of those terms. This could perhaps be accounted for by the consumer being over-optimistic about the potential risks in the terms materialising. Donnelly and White,<sup>113</sup> in their empirical study of the Irish online market, investigate the practical effect of information provision requirements of Directive 97/7 on distance selling.<sup>114</sup> They find that even where online suppliers complied with the information requirements on websites, consumers were not able to make use of that information for various reasons, including lack of accessibility or organisation of the information, and use of unclear or incomprehensible language.<sup>115</sup>

The insights of behavioural economics together with the findings of empirical studies have resulted in renewed debate about information-based regulation of standard term contracts and the nature and form of information disclosure. A traditional law and economics analysis of standard term contracts proposes improving the provision of information as a method of correcting the market failure caused by the no-reading problem in consumer contract law. This would include both providing default rules and imposing information duties, including mandatory disclosure of information and increasing transparency and accessibility. The strong message emanating from the behavioural analysis, however, is that attempts to correct market failures through information duties alone may not be entirely effective. Even relatively transparent procedures in contracting can lead to unfair results because of behavioural/psychological factors. This inevitably leads to the conclusion that substantive control of the content of standard terms is a necessary element of any regulatory regime. The

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<sup>111</sup> See above, 'Information Asymmetry and the No-Read Problem in Consumer Standard Form Contracts'.

<sup>112</sup> Florencia Marotta-Wurgler, 'Will Increased Disclosure Help? Evaluating the Recommendations of the ALI's Principles of the Law of Software Contracts' (2011) 78 *University of Chicago Law Review* 165.

<sup>113</sup> Mary Donnelly and Fidelma White, 'The Effect of Information Based Consumer Protection: Lessons from a Study of the Irish Online Market' in C. Twigg-Flesner and others (eds), *Yearbook of Consumer Law 2008* (Ashgate 2008) 20.

<sup>114</sup> Council Directive 97/7/EC of 4 June 1997 on the protection of consumers in respect of distance contracts OJ L144, now repealed and replaced by Council Directive 2011/83/EU of 25 October 2011 on consumer rights OJ L304/64.

<sup>115</sup> Donnelly and White (n. 113) 22.

analysis also highlights the need for legal regulation in the form of information duties to be shaped in a way that is sensitive to such concerns about how consumers really behave.<sup>116</sup>

### **Inequality of Bargaining Power**

The idea of inequality of bargaining power was referred to in early scholarship on standard form contracts. Kessler, writing in 1943, referred to the use of standard forms by ‘enterprises with strong bargaining power’<sup>117</sup> and likened the use of standard forms by such enterprises to private law-making by contract. For Kessler, the weaker position of the consumer stemmed from the ‘take it or leave it’ nature of the form and from their lack of ability to shop around for better terms due to the trader’s monopoly position and because all competitors use the same clauses. Under this rationale, inequality of bargaining power stems from disparity in economic power, particularly in non-competitive markets. But inequality of bargaining power is not confined to situations where traders have monopoly positions.<sup>118</sup> Even in competitive markets, consumers may be considered to be in a weaker position as regards their level of knowledge in relation to the transaction. Further, as discussed above, it is acknowledged that consumers suffer from bounded rationality in relation to standard form terms, causing them to pay little attention to the fine print. To counteract the risk of the imposition of terms on the weaker party involving questionable consent and/or possibly substantively objectionable terms, legislative intervention is therefore justified based on both procedural and substantive factors.

In European countries, as discussed above, the response to standard forms was influenced by the rise of the welfare state and the willingness of states to intervene to protect the weaker party to transactions. Towards the end of the twentieth century, some commentators were discussing the question of ‘welfarism’ in contract law and whether there was a link between the modern welfare state with its concern to secure the needs of the citizens and interventionism in contract law to protect the weaker party to the contract.<sup>119</sup> For some of these scholars, this meant protection of the weaker party through interventions such as mandatory rules; for others it meant promoting individual

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<sup>116</sup> See Stephen Weatherill, *EU Consumer Law and Policy* (n. 103) 143.

<sup>117</sup> Kessler (n. 1) 640.

<sup>118</sup> Hugh Beale, ‘Review: Inequality of Bargaining Power’ (1986) 6(1) *Oxford Journal of Legal Studies* 123.

<sup>119</sup> Roger Brownsword, Geraint Howells and Thomas Wilhelmsson (eds), *Welfarism in Contract Law* (Dartmouth 1994).

autonomy through improving the possibility for market-rational consumers to make informed choices.<sup>120</sup>

The discussion also encompassed the idea that the classic contract law principle of freedom of contract was narrowly concerned with procedural fairness; whereas modern law intervenes to ensure substantive fairness and in doing so incorporates recognisably welfarist elements such as adjusting the contract where lack of balance has resulted from inequality of bargaining power. These discussions were taking place against the backdrop of the introduction of the UCTD and this prompted debate concerning both the extent to which the Directive's justification lay in welfarist concerns, and the effectiveness of legal intervention in achieving welfarist values. The debate highlighted the challenge of achieving a harmonised European contract law measure that would strike a balance between a market-oriented approach that respects ideas of private autonomy and freedom of contract, and an approach that includes principles of social justice such as, for example, intervening to protect the weaker party to the contract from terms that are considered substantively unfair. The background to the introduction of the Directive and the debate surrounding its underlying rationale and justification are discussed further in Chapter 2.

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<sup>120</sup> See also Thomas Wilhelmsson, 'Varieties of Welfarism in Contract Law' (2004) 10(6) *European Law Journal* 712, discussing different types of welfarism in contract law.