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## The Reunification of Contract Law: The Objective Theory of Consumer Form Contracts

Michael I. Meyerson

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# The Reunification of Contract Law: The Objective Theory of Consumer Form Contracts

MICHAEL I. MEYERSON\*

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## I. INTRODUCTION

Standard form contracts have been in use for over two centuries, and the question of the proper construction of these contracts has haunted contract law ever since. Form contracts were first used in the

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\* Professor of Law, University of Baltimore School of Law. B.A. 1976, Hampshire College; J.D. 1979, University of Pennsylvania Law School. I would like to thank Professor E. Allan Farnsworth for graciously reading this Article in manuscript form. I would also like to thank both Emily R. Greenberg, Law Library Director at the University of Baltimore School of Law, and Morris L. Cohen, former Law Librarian and Professor at Yale Law School, for helping track down the full text of Professor Llewellyn's unpublished draft of his proposed 1941 revision of the Uniform Sales Act. Finally, I want to acknowledge that funding for this article came from the University of Baltimore School of Law's Summer Research Fund. Of course, all opinions expressed and mistakes made are my own.

latter half of the eighteenth century for marine insurance.<sup>1</sup> The insurance companies' reliance on forms marked a radical departure from the traditional negotiated contract:

No longer do individuals bargain for this or that provision in the contract . . . . The control of the wording of those contracts has passed into the hands of the concern, and the drafting into the hands of its legal advisor . . . . In the trades affected it is henceforth futile for an individual to attempt any modification, and incorrect for the economist and lawyer to classify or judge such arrangements as standing on an equal footing with individual agreements.<sup>2</sup>

In the contemporary debate, some economists and lawyers continue to equate form contracts with the negotiated, "individual contracts."<sup>3</sup> Other commentators, however, recognize that consumer form contracts create special risks and problems.<sup>4</sup> These difficulties have been attributed, with varying emphases, to unequal bargaining power, to the failure to negotiate the contract terms, to the "take-it-or-leave-it" basis of the transaction, and to the fact that inevitably most terms remain unread.<sup>5</sup>

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1. OTTO PRAUSNITZ, *THE STANDARDIZATION OF COMMERCIAL CONTRACTS IN ENGLISH AND CONTINENTAL LAW* 11 (1937). This book was the subject of Karl Llewellyn's famous 1939 book review, in which he first detailed his own view of form contracts. See K.N. Llewellyn, Book Review, 52 HARV. L. REV. 700 (1939); see *infra* text accompanying note 78.

2. PRAUSNITZ, *supra* note 1, at 18 ("It is the freedom of contract theory pushed to its extreme, thus reaching its climax and resulting in fetters to one of the parties concerned.").

3. See, e.g., RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 84-86 (2d ed. 1977); Stephen J. Ware, *A Critique of the Reasonable Expectations Doctrine*, 56 U. CHI. L. REV. 1461, 1467 (1989); Alan Schwartz & Louis L. Wilde, *Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis*, 127 U. PA. L. REV. 630, 652-55 (1979). This is not a unanimous view. For the theory that economic efficiency requires that the consumers' objective understanding control the unread written terms, see Michael I. Meyerson, *The Efficient Form Contract: Law and Economics Meet the Real World*, 24 GA. L. REV. 583 (1990); Lee Goldman, *My Way and the Highway: The Law and Economics of Choice of Forum Clauses in Consumer Form Contracts*, 86 NW. U. L. REV. 700 (1992).

4. The term "consumer form contract" in this context includes more than merely contracts associated with the purchase of consumer goods and services. Many, though not all, form contracts create similar problems concerning informed assent. See, e.g., *Martin v. Joseph Harris Co., Inc.*, 767 F.2d 296 (6th Cir. 1985) (small businesspeople such as family farmers); *Weaver v. American Oil Co.*, 276 N.E.2d 144 (Ind. 1971) (gas station franchisees); *Matuszak v. Houston Oilers*, 515 S.W.2d 725 (Tex. Ct. App. 1974) (contract presented to employees). Accordingly, any theory purporting to resolve the problems raised by form contracts must also cover agreements between employers and employees as well as between large and small businesses, where the situation indicates to the reasonable contract drafter that the other party has not assented to unread and unexpected terms. See, e.g., *Haspel v. Rollins Protective Service, Inc.*, 490 So. 2d 530, 533 (La. Ct. App. 1986), *writ denied*, 496 So. 2d 326 (La. 1986) (stating that "an artificial distinction between commercial enterprises and consumers is inappropriate . . . Sophistication and educational level, not commerciality, are the primary considerations"). Cf. Addison Mueller, *Contracts of Frustration*, 78 YALE L.J. 576, 576 n.1 (1969) (defining consumer as "a buyer of a small lot from a retailer").

5. See, e.g., *infra* text accompanying notes 23-41.

Unfortunately, a generally accepted solution to the issue has yet to be formulated. In 1970, Arthur Leff described the law of consumer form contracts as "a disaster." He wrote "the consumer-purchase transaction is still stumbling about, a diagnosed disease seeking a nostrum."<sup>6</sup> Since then, contract law has died,<sup>7</sup> and been resurrected,<sup>8</sup> reconstructed,<sup>9</sup> and transformed.<sup>10</sup> Doctrines of adhesion,<sup>11</sup> reasonable expectations,<sup>12</sup> and unconscionability<sup>13</sup> have all been advanced. Yet, the battle continues to rage.

This Article proposes a modest solution to the dilemma of form contracts. The Article's central thesis is that confusion continues to reign mostly because those seeking answers have searched too hard. The conceptual difficulties stem from one fundamental error: the common law presumption, often conclusive, that consumers who sign form contracts are aware of, understand, and assent to the unread, unexpected and un contemplated terms in the form contracts. This presumption of assent conflicts with the objective theory of contracts. Because the drafters of these contracts know not only that their forms will not be read, but also that it is reasonable for consumers to sign them unstudied, a reasonable drafter should have no illusion that there has been true assent to these terms. If the common law courts had merely recognized the self-evident—that objectively the drafter does *not* expect the consumer to learn of the contract terms—traditional contract theory would have produced logical results.

In short, courts correctly applying the objective theory to consumer form contracts will not assume automatically that there is objective agreement to all terms merely because they have been printed and a document has been signed. Rather, courts will try to determine how a reasonable drafter should have understood the consumer's agreement. The critical questions will be:

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6. Arthur A. Leff, *Contract as Thing*, 19 AM. U. L. REV. 131, 142 (1970). Thirteen years later one commentator stated that "[a]lthough there is a quite general perception that different law must be applied to contracts of adhesion, there is little agreement on what principles should control. The currently applicable law is characterized by a lack of intelligible doctrine and a lack of consistent results." Todd D. Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96 HARV. L. REV. 1173, 1175 (1983).

7. GRANT GILMORE, *THE DEATH OF CONTRACT* (1974).

8. Colin K. Kaufman, *The Resurrection of Contract*, 17 WASHBURN L.J. 38 (1977).

9. Rakoff, *supra* note 6, at 1176.

10. W. David Slawson, *The New Meaning of Contract: The Transformation of Contracts Law by Standard Forms*, 46 U. PITT. L. REV. 21 (1984).

11. Friedrich Kessler, *Contracts of Adhesion: Some Thoughts about Freedom of Contract*, 43 COLUM. L. REV. 629 (1943).

12. See, e.g., Robert E. Keeton, *Insurance Law Rights at Variance with Policy Provisions: Part Two*, 83 HARV. L. REV. 1281 (1970).

13. *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445 (D.C. Cir. 1965).

- 1) What terms would a seller reasonably expect were known and understood by the non-drafting party?
- 2) What subordinate terms were pointed out or explained by the seller?
- 3) What would the reasonable seller have assumed was the consumer's purpose in entering into the transaction?
- 4) Is a clause favoring the drafter reasonably tailored to accomplish a legitimate purpose?
- 5) Was information conveyed by the seller, either directly, by an agent or by advertisements, to create a reasonable expectation in the consumer?
- 6) Did the consumer communicate to the seller information indicating a particular understanding of the terms of the contract?
- 7) Does an unknown one-sided clause deal with issues beyond the realm of contemplation of the reasonable consumer at the time of contracting?

These questions focus attention on how a reasonable drafter should understand the assent of a consumer. This analysis does not automatically favor either the drafter or the consumer, but attempts to give both parties full freedom to contract *together*. It also may help bring the law of form contracts back into the mainstream of general contract law.

## II. THE OBJECTIVE THEORY OF CONTRACTS

In the ancient past, contracts required a "meeting of the minds" to be legally recognized.<sup>14</sup> It is now settled that no actual meeting of minds or subjective agreement is necessary, most obviously because the mind of a human is unknown and unknowable for the rest of the world.<sup>15</sup> A person's true feelings are secret; the existence of heart-felt agreement is forever uncertain.

Accordingly, the common law courts shifted their focus to a version of "objective reality." The true motivations and feelings of the contracting parties became irrelevant.<sup>16</sup> Instead, all that mattered was how words and actions would be understood by a reasonable

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14. E. Allan Farnsworth, "Meaning" in the Law of Contracts, 76 YALE L.J. 939, 943-44 (1967).

15. See generally MORTON HOROWITZ, THE TRANSFORMATION OF AMERICAN LAW 1780-1860 200 (1977) (The subjective theory "had the drastic limitation of making legal certainty and predictability impossible. Once contractual obligation was founded entirely on an arbitrary 'meeting of minds,' it endowed the parties with a complete power to remake law.").

16. See 1 SAMUEL WILLISTON, THE LAW OF CONTRACTS § 26 (1920) ("In the formation of contracts it was long ago settled that secret intent was immaterial; only overt acts being considered in the determination of such mutual assent as that branch of law requires.").

recipient of information. As Judge Learned Hand stated: "A contract has, strictly speaking, nothing to do with the personal, or individual, intent of the parties. A contract is an obligation attached by the mere force of law to certain acts of the parties, usually words, which ordinarily accompany and represent a known intent."<sup>17</sup>

To determine if *A* has made a legally enforceable promise to *B*, one must determine whether *B* "had reason to believe that the first party had that intention."<sup>18</sup> The intent of a speaker or writer is inferred from the perspective of what the listener or reader knew or should have known.<sup>19</sup>

Thus, if owners of property write and sign a piece of paper stating, "We hereby agree to sell to W.O. Lucy the Ferguson Farm complete for \$50,000, title satisfactory to buyer," a court can confidently find an intent to sell.<sup>20</sup> Similarly, if Lucy reads and accepts the document, the court may infer an intent to purchase the Ferguson Farm. This is a straightforward application of the rule that "[t]he law imputes to a person an intention corresponding to the reasonable meaning of his words and acts."<sup>21</sup>

Thus, traditionally there has been a so-called duty to read, which binds those who sign or accept a contract to the written terms even if they did not read or understand its content.<sup>22</sup> In cases involving negotiated contracts or experienced businesspeople, this duty to read is consistent with the objective theory because assent can reasonably be inferred from the act of signing a document in such circumstances. One expects the average businessperson to be able to learn the mean-

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17. *Hotchkiss v. National City Bank*, 200 F. 287, 293 (S.D.N.Y. 1911), *aff'd*, 201 F. 664 (2nd Cir. 1912), *aff'd*, 231 U.S. 50 (1913).

18. E. ALLAN FARNSWORTH, *CONTRACTS* 114 (1982). This rule governs transactions under the U.C.C. as well as the common law; *see, e.g.*, *City of Everett v. Estate of Sumstad*, 614 P.2d 1294, 1296 (Wash. Ct. App. 1980), *aff'd in part, rev'd in part*, 631 P.2d 366 (Wash. 1981). *See generally* U.C.C. § 1-103 ("Unless displaced by the particular provisions of this Act, the principles of law and equity, including the law . . . relative to capacity to contract, principle and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions."); *see also* *Morgan Guaranty Trust Co. v. American Sav. & Loan*, 804 F.2d 1487, 1495 (9th Cir. 1986) ("Judges have a duty to consider the equities of a case unless equitable principles have been displaced, and nothing short of an express code provision . . . demonstrates displacement.") (citations omitted).

19. JOHN D. CALAMARI & JOSEPH M. PERILLO, *THE LAW OF CONTRACTS* 26 (3d ed. 1987).

20. *Lucy v. Zehmer*, 84 S.E.2d 516, 517 (Va. 1954).

21. *Id.* at 521 (quoting *First Nat'l Exchange Bank v. Roanoke Oil Co.*, 192 S.E. 764, 770 (Va. 1937)).

22. For a discussion of the evolution of the duty to read doctrine, *see* John D. Calamari, *Duty to Read: A Changing Concept*, 43 *FORDHAM L. REV.* 341 (1974).

ing of the contract terms with relative ease and to voice any disagreement with such terms.

There are, however, circumstances where the significance of the same act is quite different. The law has long recognized that unsuspecting recipients of parcel room checks or ticket stubs do not accept, and thus are not bound by, the printed limitations on liability.<sup>23</sup> This principle, too, is consistent with the objective theory because the party printing the ticket, knowing the fine print will not be read, does not have a reasonable belief that the other party assented to the limitations. As the Massachusetts Supreme Judicial Court stated in rejecting a waiver of liability printed on the ticket to an amusement park attraction: "[A] person of average intelligence and alertness would be unlikely to observe it, and would enter the [ride] in the belief that he had all the rights of the ordinary business visitor with respect to so much of the premises as he was invited to use."<sup>24</sup> The court added that if such a limitation was to be enforceable at all, the ride's proprietor should have "employed adequate means to bring to [the patron's] attention the fact that his invitation was a qualified and conditional one."<sup>25</sup>

If the objective theory of contracts were correctly applied to consumer form contracts, a similar rule would result. In our current society, the average consumer is unlikely to observe most of the terms in form contracts. They may well know central terms, such as price and quantity, but generally they neither know nor understand subordinate terms, such as those describing recourse in case of breach.<sup>26</sup> Consumers, thus, contract with a reasonable belief that they do not relinquish the rights implied by law for the benefit of the ordinary contracting party.<sup>27</sup>

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23. See generally *Jones v. Great Northern Ry. Co.*, 217 P. 673 (Mont. 1923) (railroad ticket); *Healy v. N.Y. Cent. & H.R.R., Co.*, 138 N.Y. Supp. 287 (N.Y. 1912) (parcel room claim check); *Weisz v. Parke-Bernet Galleries, Inc.*, 325 N.Y. Supp. 2d. 576 (N.Y.C. Ct. 1971) (80-page auction house catalogue); *McAshan v. Cavitt*, 299 S.W.2d 1016 (Tex. 1950) (parking lot claim check).

24. *Kushner v. McGinnis*, 194 N.E. 106, 108 (Mass. 1935).

25. *Id.*

26. For a discussion of the differentiation between "central" and "subordinate" terms, see George L. Priest, *A Theory of the Consumer Product Warranty*, 90 YALE L.J. 1297, 1304-06 (1981). This differentiation is analogous to Llewellyn's distinction between a "few dickered terms" and "boilerplate clauses." See *infra* text accompanying note 85.

27. This view is in harmony with the presumption that a party to a contract will not knowingly give an unfair advantage to the other without receiving adequate compensation, which is another method of establishing a party's objective intent. See, e.g., *Brown v. McGraw-Hill Book Co.*, 269 N.Y.S.2d 35, 38 (N.Y. App. Div. 1966), *motion granted*, 228 N.E.2d 418 (N.Y. 1967), *aff'd*, 231 N.E.2d 768 (N.Y. 1967) ("It is not to be assumed that people act unreasonably to their own disadvantage . . ."); *Jacob & Youngs v. Kent*, 129 N.E.

It is no secret that consumers neither read nor understand standard form contracts.<sup>28</sup> The president of a car rental company hardly believes that renters at the airport rental counter read the front and back of the rental contract before receiving the keys.<sup>29</sup> It is equally unrealistic to state that a reasonable rental car executive would assume that a renter's signature reflects true assent to every term in the contract.<sup>30</sup> The only basis for such a belief would be if the current law mandates such a result *despite* the objective understanding of the rental car executive.<sup>31</sup> Any expectation that the contract terms written by the company's lawyers are enforceable against the consumer is "reasonable" not because the consumer's true intent was objectively ascertained but solely because of the legal rule.

One reason for a contract system founded on objective criteria of assent to ignore the reasonable interpretation of the consumer's intent might be to affect the consumer's behavior. However, consumers do

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889, 891 (N.Y. 1921) (Cardozo, J.) ("There will be no assumption of a purpose to visit venial faults with oppressive retribution.").

28. See, e.g., *Davis v. M.L.G. Corp.*, 712 P.2d 985, 992 (Colo. 1986) (automobile rental agent testifying that she had never seen any customer read the reverse side of the rental agreement); *Unico v. Owen*, 232 A.2d 405, 410 (N.J. 1967) ("The ordinary consumer goods purchaser more often than not does not read the fine print . . ."); *Holiday of Plainview, Ltd. v. Bernstein*, 350 N.Y.S.2d 510, 512 (N.Y. Dist. Ct. 1973) (stating that "it is true that defendant (as have many before him and probably many will after him) failed to read the entire contract").

29. See, e.g., *Elliot Lease Cars, Inc. v. Quigley*, 373 A.2d 810, 813 (R.I. 1977) (stating that "[i]t is common knowledge, and so should have been known to [the car leasing company] that the detailed provisions of insurance contracts are seldom read by consumers"); see also *Val Preda Leasing, Inc. v. Rodriguez*, 540 A.2d 648 (Vt. 1987) (finding that average consumer would not understand the numerous exceptions to the limitation on liability for damage to the rental car).

30. When the context of the transaction "is such as to preclude the reasonable expectation that the printing will be read or understood in any significant number of cases, the seller cannot claim that he nonetheless so expected. He therefore has no basis of asserting that he relied to his detriment on manifestations of mutual consent." W. David Slawson, *Standard Form Contracts and Democratic Control of Lawmaking Power*, 84 HARV. L. REV. 529, 544 (1971).

31. "A party who makes regular use of a standardized form of agreement does not ordinarily expect his customers to understand or even to read the standard terms." RESTATEMENT (SECOND) OF CONTRACTS § 211 cmt. b (1979). The principal drafter of this section of the Restatement (Second) argued that "Customers who adhere to standardized contractual terms ordinarily, 'understand that they are assenting to the terms not read or not understood, subject to such limitations as the law may impose.'" *Carpenter v. Suffolk Franklin Sav. Bank*, 346 N.E.2d 892, 900 (Mass. 1976) (Braucher, J.) (quoting RESTATEMENT (SECOND) § 237 cmt. b (Tentative Drafts Nos. 1-7 (1973))). This statement is unhelpful for two reasons. First, it is not at all clear that consumers "understand" that they are signing away substantive rights or procedural rights. Second, the term "subject to such limitations as the law may impose" is too broad, thus permitting "the law" to construe form contracts according to either the non-drafter's reasonable expectations or an objective interpretation of the non-drafter's intent.



not read form contracts both because it is unreasonable to do so and because businesses do not want consumers to read them prior to signing.<sup>32</sup>

Most consumers fail to read the form contracts that pass before them every day.<sup>33</sup> Consumers simply do not have the time to read them, as exemplified by the car-renter at the airport. They also generally lack the legal background to understand the subordinate clauses.<sup>34</sup> Additionally, because consumers know that the agent behind the counter is not authorized to rewrite the contract,<sup>35</sup> they conclude that there is little to be gained from reading a non-negotiable contract.

Moreover, businesses hardly want the consumer to read form contracts. If the purpose of using a form is to achieve uniformity in transaction, individualized negotiations will defeat that purpose.<sup>36</sup> Additionally, businesses, like consumers, are short of time and prefer not to have their turnover slowed by hordes of consumers pausing to peruse pages of legalese.<sup>37</sup>

Despite wishful commentary to the contrary,<sup>38</sup> there is no evi-

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32. For an economic analysis of why it is inefficient for consumers to read form contracts, see Meyerson, *supra* note 3, at 596-603.

33. The rationality of not reading the form contract is strengthened by the increased difficulty resulting from the use of excessively fine print and hopelessly convoluted language. "[C]ontracts of adhesion, most of which are editorial nightmares, proliferate. There is a dark suspicion that the same people who prepare these prepare tax forms and directions as to how to put together packaged Christmas toys." *Spence v. Omnibus Indus.*, 119 Cal.Rptr. 171, 173 n.1 (Cal. Ct. App. 1975).

34. See, e.g., Kaufman, *supra* note 8, at 45 ("Knowledge that certain words were used creates no knowledge of the reality intended to be created."); see also *Commercial Union Assurance Cos. v. Gollan*, 394 A.2d 839, 841 (N.H. 1978) ("Although insurers have had over one hundred years to hone their policies into forms that would not ferry the unwary reader on a trip into Wonderland, they regrettably often fully merit the criticism that Chief Justice Doe [deploring the prolixity of complex verbiage in policies, *DeLancey v. Insurance Co.*, 52 N.H. 581 (1873)] levelled at their predecessors.") (quoting *Storms v. United States Fidelity & Guar. Co.*, 388 A.2d 578, 580 (N.H. 1978)); *Unico v. Owen*, 232 A.2d 405, 410 (N.J. 1967) ("[I]t is unlikely that [the consumer] would understand the legal jargon, and the significance of the clauses is not explained to him.").

35. "Employees regularly using a form often have only a limited understanding of its terms and limited authority to vary them." *RESTATEMENT (SECOND) OF CONTRACTS* § 211 cmt. b (1979). See, e.g., *A & M Produce Co. v. FMC Corp.*, 186 Cal. Rptr. 114, 125 n.13 (Cal. Ct. App. 1982) (in response to the question whether there is negotiation over form terms, a salesperson stated: "I'm not empowered to do that, sir.").

36. "One of the purposes of standardization is to eliminate bargaining over details of individual transactions, and that purpose would not be served if a substantial number of customers retained counsel and reviewed the standard terms." *RESTATEMENT (SECOND) OF CONTRACTS* § 211 cmt. b (1979). See also M.J. Trebilcock, *The Doctrine of Inequality of Bargaining Power: Post Benthamite Economics in the House of Lords*, 26 U. Toronto L.J. 359, 364 (1976) (stating that consumer standard form contracts are used "to reduce transaction costs").

37. See, e.g., Kaufman, *supra* note 8, at 40-41.

38. Priest, *supra* note 26, at 1347.

dence that a small cadre of type-A consumers ferrets out the most beneficial subordinate contract terms, permitting the market to protect the vast majority of consumers. Obvious terms, such as pricing and warranties, may be subject to such comparison shopping. It is hard, however, to imagine a sufficient number of prospective consumers refusing to rent a car because the contract contains an unfair forum selection clause.<sup>39</sup>

If consumers do not read and comprehend the subordinate terms of standard form contracts, there can be no subjective agreement to the particular terms. Furthermore, merchants and sellers who know that consumers do not read these terms have no objective basis for claiming that the consumers agreed to those terms. If it is both unreasonable and undesirable to have consumers read these terms, courts should not fashion legal rules in a futile attempt to force consumers to read these terms or to punish those who do not.<sup>40</sup>

The common law of contracts, it seems, has strayed for the path of logical progression.<sup>41</sup> The wrong turn occurred when the perfectly logical assumption that a merchant's signature implied assent to negotiated terms was mistakenly applied to consumer form contracts. The courts abandoned the objective theory in search of a seductive consistency.

### III. CLASSIC CONTRACTS

The classical legal view of standard form contracts defies logic and invites great injustice. Essentially, under the twin banners of

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39. It is similarly ridiculous to believe that advertising permits competitors to inform consumers of unexpected harsh secondary terms. See Ware, *supra* note 3, at 1479. As one commentator noted, "it would be ludicrous for a seller to base an advertising campaign on the claim that, 'if you injure yourself on our cruise, you can sue us anywhere.'" Goldman, *supra* note 3, at 719.

40. Courts attempting to force consumers to read form contracts know that they will not succeed. This futility was recognized by the Nevada Supreme Court in *Farmers Ins. Exch. v. Young*, 832 P.2d 376, 379 n.2 (Nev. 1992). "Although we understand that many people may in fact not read their insurance policies, we conclude that the consumer has at least this responsibility. If we presume that consumers do not read policies, we would then force insurers to explain verbally every minute detail of a policy. We must assume that the insured party has at least read the policy and given a plain common-sense meaning to the policy's provisions." This is not a sound basis for a decision. Courts should not presume something they know is untrue. Besides, insurers need not explain "every minute detail," only unexpected terms or those which contradict the rest of the policy. See *infra* note 289 and accompanying text.

41. See generally POSNER, *supra* note 3, at 404-07.

"freedom of contract"<sup>42</sup> and "duty to read,"<sup>43</sup> the law has given drafters of form contracts the power to impose their will on unsuspecting and vulnerable individuals.

The 1918 case of *Morstad v. Atchinson T. & S.F. Railway Co.*<sup>44</sup> demonstrates the resulting hardship and injustice. A railroad worker, Andrew Morstad, was injured while unloading timber. He was taken to a bunk car and was lying on a bed "in an awful pain."<sup>45</sup> The railroad company foreman presented him with a form and said, "[H]ere is something you will have to sign before you go to the hospital."<sup>46</sup> Morstad, who was not wearing his reading glasses, signed the form without reading it. The form was a settlement contract whereby Morstad "agreed" to release the railroad from all liability in exchange for one dollar and transportation to the hospital.<sup>47</sup>

The New Mexico Supreme Court upheld the validity of the release, stating that "[Morstad] was guilty of such gross negligence in not informing himself of the contents of the contract that he is estopped to avoid the same. His lack of knowledge of the contents of the contract was due absolutely to his own negligence."<sup>48</sup> The court opined that "it is the duty of every person to read a contract before he signs the same, if he can read, and it is as much his duty to have the same read and explained to him before he executes it, if he cannot read or understand it."<sup>49</sup>

The court gave several policy rationales for this strict rule. Someone who signs a contract "owes it to the other party to read or have read, the contract . . . because the other party has a right to and does conform his own conduct to the requirements of the contract . . . ." <sup>50</sup> The court also noted that permitting Morstad to go beyond the written word would threaten to "destroy all of the efficacy

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42. See, e.g., *Gas House, Inc. v. Southern Bell Tel. & Tel. Co.*, 221 S.E.2d 449, 504-05 (N.C.1976) (upholding disclaimer of liability for negligent handling of yellow page advertising because each person is "free to contract according to [his] own judgment"); *contra* *College Mobile Home Park & Sales, Inc. v. Hoffmann*, 241 N.W.2d 174, 177 (Wis. 1976) (stating that "[t]he unconsidered application of the principle of freedom of contract . . . is not always justified when there are extenuating circumstances which may affect the degree to which that freedom actually exists").

43. See, e.g., *Hunter v. Texas Instruments, Inc.*, 798 F.2d 299, 303 (8th Cir. 1986) (stating that warranty disclaimer in tenth paragraph of twenty-one paragraphs on back of two-page contract "should have attracted the attention of a reasonable buyer").

44. 170 P. 886 (N.M. 1918).

45. *Id.* at 889.

46. *Id.*

47. *Id.* at 890.

48. *Id.*

49. *Id.* at 889.

50. *Id.*

of written contracts.”<sup>51</sup> The rule, the court noted in conclusion, “renders written contracts safe and secure, and just what they must be if the business of the world is to be carried on in an orderly fashion.”<sup>52</sup>

Classical courts upheld written language, even where the drafter discouraged a semi-literate individual from reading the paper by saying, “it was all a matter of form—it was immaterial.”<sup>53</sup> Judges confidently cited, “the well-settled principle that affixing a signature to a contract creates a *conclusive presumption*, except as against fraud, that the signer read, understood, and assented to its terms.”<sup>54</sup> Courts moralistically preached that if a person failed to read the contract, “he cannot set up his own carelessness and indolence as a defense.”<sup>55</sup>

This classical theory has no basis in either reality or justice.<sup>56</sup> Courts had to create a “conclusive” presumption that the signing party understood the terms because such a presumption was so counter-factual. The drafters of the contracts knew the signing party had not read the terms. There could be no problem of unfair surprise, since the objective understanding of the contract drafter mirrored the subjective reality of the non-drafter.

The other problem with the classical theory was that it permitted drafters of form contracts to abuse their power.<sup>57</sup> There were no safeguards against grotesquely one-sided agreements, drafted to be signed unread.

51. *Id.*

52. *Id.* The court gave Morstad the opportunity to prove that he received no consideration for the release. *Id.* at 890.

53. *Fivey v. Pennsylvania R.R. Co.*, 52 A. 472, 474 (N.J. 1902).

54. *Id.* at 473 (emphasis added).

55. *McNinch v. Northwest Thresher Co.*, 100 P. 524, 526 (Okla. 1909).

56. “It is obvious that analysis of the form lease in terms of traditional contract principles will not suffice, for those rules were developed for negotiated transactions which embody the intention of both parties.” *Galligan v. Arovitch*, 219 A.2d 463, 465 (Pa. 1966).

57. See, e.g., *Gray v. American Express Co.*, 743 F.2d 10, 19 (D.C. Cir. 1984) (calling form term “a snare and deceit”); *Spring Valley Gardens Ass’n v. Earle*, 447 N.Y.S.2d 629, 631 (N.Y. County Ct. 1982) (“[I]t is immediately apparent that [these leases] have been carefully, painstakingly designed to provide maximum protection for the landlords and to give only the most grudging, minimal recognition to the reasonable expectations of residential tenants.”). For a particularly angry judicial response to one such incident, see *John Deere Leasing Co. v. Blubaugh*, 636 F. Supp. 1569, 1571 (D. Kan. 1986), where the court described a form lease term imposing a penalty for defaulting as:

written in such fine, light print as to be nearly illegible . . . . The court was . . . required to use a magnifying glass to read the reverse side. The court found the wording to be unreasonably complex. It is as if the scrivener intended to conceal the thrust of the agreement in the convoluted language and fine print . . . . John Deere’s contention that the defendant had a duty to ascertain the meaning of all terms, in the face of the near concealment of this unusually harsh remedy, is inexcusably inadequate and need not be tolerated by any court. This court is surprised that a reputable company such as Deere would stoop to this.

In response to this problem, judges began resorting to subterfuge to reach the result that should have been obtained directly under basic principles of "objective appearances." Ambiguity, waiver, estoppel, and conditions to contract were used to sidestep unpleasant results, while the courts purportedly followed the path of the earlier decisions.<sup>58</sup>

Many of the finest legal scholars of the twentieth century have tried with limited success to correct these errors, each pointing out the inconsistency in legal reasoning and illustrating a part of the problem. More recently, serious attempts have been made to present a formal solution to the entire area by creating a separate rule for form contracts.<sup>59</sup> The collective wisdom has brought us to the point where contract law can now be reunified, where the objective theory of contracts is again applied to all contracts.

#### IV. THE EVOLUTION OF FORM CONTRACT THEORY

The first step in the creation of a unified theory of form contracts was the basic recognition that form contracts are fundamentally different from the classic individualized contracts that existed during the formation of the common law. In 1919, Edwin Patterson imported the phrase "contracts of adhesion" into American jurisprudence.<sup>60</sup> Patterson's translation of a French writer's analysis focused on the lack of bargaining associated with these contracts.

Doubtless, there are contracts and contracts, and we are in reality far from the unity of contractual type assumed by the law. Eventually the law must, indeed, yield to the shading and differences that have emerged from social relations. There are pretended contracts that have only the name, the juridical construction of which remains to be made. For these, in any event, the rules of individual interpretation should undergo important modifications, if only that one might call them, for lack of a better term, contracts of adhesion, those in which a single will is exclusively predominant, acting as a unilateral will which dictates its law, no longer to an individ-

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58. See, e.g., Llewellyn, *supra* note 1, at 702 ("[W]e have developed a whole series of semi-covert techniques for somewhat balancing these bargains."); Robert E. Keeton, *Insurance Law Rights at Variance with Policy Provisions*, 83 HARV. L. REV. 961, 972 ("The conclusion is inescapable that courts have sometimes invented ambiguity where none existed, then resolving the invented ambiguity contrary to the plainly expressed terms of the contract document."); see also *Marston v. American Employers Ins. Co.*, 439 F.2d 1035, 1039 (1st Cir. 1971) ("Not infrequently the linkage between results and rational analysis has been blurred to the point of invisibility.").

59. See *infra* text accompanying notes 189-90.

60. Edwin W. Patterson, *The Delivery of a Life-Insurance Policy*, 33 HARV. L. REV. 198, 222 (1919).

ual, but to an indeterminate collectivity, and which in advance undertakes unilaterally, subject to the adhesion of those who would wish to accept the law [loi] of the contract and to take advantage of the engagements imposed on themselves.<sup>61</sup>

In 1943, Friedrich Kessler presented the first full portrait of contracts of adhesion.<sup>62</sup> He saw several key components: 1) "form contracts" were typically used by businesses with a "strong bargaining power;" 2) the drafter either enjoyed a monopolistic position or used the same contract as its competitors; 3) the weaker party understood the legal consequences of the contract, "only in a vague way, if at all;" and 4) the terms of the contract were presented on a take-it-or-leave-it basis.<sup>63</sup>

Kessler argued these contracts were inconsistent with traditional notions of freedom of contract which have "delegated to individual citizens a piece of sovereignty which enables them to participate constantly in the law making process."<sup>64</sup> Without prescribing a particular legal treatment for form contracts,<sup>65</sup> Kessler complained that "our common law of standardized contracts is highly contradictory and confusing."<sup>66</sup>

The same year Kessler's article was published, William Prosser wrote an article discussing an important subtopic, disclaimers of the implied warranty of merchantability.<sup>67</sup> Although neglected by most studies of form contracts, Prosser's analysis offers a compelling understanding that is applicable to the entire field.

Prosser noted that a "disclaimer is not at all a pernicious thing in any case where it appears that the buyer really is willing to take his chances."<sup>68</sup> Thus, it is proper to enforce a contractual disclaimer when a buyer purchases second-hand goods or when the seller lacks

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61. RAYMOND SALEILLES, *DE LA DÉCLARATION DE VOLONTÉ* § 89 at 229-30 (1901) (translated in Edwin W. Patterson, *The Interpretation and Construction of Contracts*, 64 COLUM. L. REV. 833, 856 (1964)). The first case to rely on the terminology of "adhesion" was an insurance case, *Bekken v. Equitable Life Assurance Soc'y*, 293 N.W. 200, 212 (N.D. 1940).

62. Kessler, *supra* note 11, at 632.

63. *Id.* The California Supreme Court has defined an adhesion contract as "a contract entered into between two parties of unequal strength, expressed in the language of a standardized contract, written by the more powerful bargainer to meet its own needs, and offered to the weaker party on a 'take it or leave it basis' ". *Gray v. Zurich Ins. Co.*, 419 P.2d 168, 171 (Cal. 1966).

64. Kessler, *supra* note 11, at 641.

65. See W. David Slawson, *The New Meaning of Contract: The Transformation of Contracts Law by Standard Forms*, 46 U. PITT. L. REV. 21, 32 (1984).

66. Kessler, *supra* note 11, at 633.

67. William L. Prosser, *The Implied Warranty of Merchantable Quality*, 27 MINN. L. REV. 117 (1943).

68. *Id.* at 159.

knowledge of the quality of the goods and "makes it clear" that the sale is conditioned on the seller bearing no responsibility for their quality.<sup>69</sup> In other words, risks may properly be shifted to consumers, provided they knowingly accept them.

However, Prosser warned, when courts mechanically uphold a seller's contract disclaiming all warranties, "a dangerous power is placed in the hands of the seller."<sup>70</sup> Prosser argued the seller cannot reasonably suppose that a buyer "is willing to pay good money for whatever the seller will give him, and remain completely at the seller's mercy."<sup>71</sup> The seller knows that the typical buyer expects a particular item to be of generally acceptable quality. Even the most comprehensive disclaimer is contradicted by the contractual description of the goods being sold; their very name incorporates the general understanding that they are "goods of the kind sold on the market."<sup>72</sup>

Prosser proposed to limit the effectiveness of disclaimers of implied warranties to those instances where purchasers could be understood to have actually agreed to a disclaimer. Disclaimers would be ineffective whenever "the circumstances indicate that a reasonable person in the position of the buyer would, despite such general language, be in fact relying on the merchantable quality of the goods or their fitness for a particular purpose."<sup>73</sup>

One year after Prosser's article appeared, Arthur Corbin put another small piece of the form contract puzzle into place when he wrote his famous review of the parol evidence rule.<sup>74</sup> Corbin argued that the written words of a contract should not be interpreted to conflict with the contracting parties' intent. He urged judges to look behind the writing to ascertain the parties' desires from all the circumstances surrounding the contract. Corbin declared that merger clauses, express written contractual declarations that there are no unwritten promises, should not be reflexively enforced. Corbin stated that such clauses are properly understood as assertions of fact rather than conclusions of law. He added, "paper and ink possess no magic power to cause statements of fact to be true when they are actually untrue."<sup>75</sup> Therefore, the writing could not be conclusive because

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69. *Id.*

70. *Id.*

71. *Id.*

72. *Id.* at 160.

73. *Id.* at 165 (quoting the SECOND DRAFT OF THE REVISED UNIFORM SALES ACT § 15(6) (1941)). Prosser's support for the phrase "general language" is probably meant to be viewed the same as his earlier statement that "[a]ny general language of the disclaimer, no matter how comprehensive it may be [qualifies]." *Id.* at 160.

74. Arthur L. Corbin, *The Parol Evidence Rule*, 53 YALE L.J. 603 (1944).

75. *Id.* at 620.

"[a] statement in the writing that it contains all terms agreed upon and that there are no promises, warranties, or other extrinsic provisions, is a statement of fact that may actually be untrue."<sup>76</sup> Though the contractual language may be clear, courts should permit additional oral promises to be proven "where justice seems to require it."<sup>77</sup>

Despite the work of Prosser and Corbin, it was Karl Llewellyn who dominated the early analysis of standard form contracts. His writings, published from 1939 through 1960, continue to serve as the starting point for the current debate on this topic.

Llewellyn noted that form contracts replaced "item by item" negotiation with "standard clauses and terms, prepared often by one of the parties only."<sup>78</sup> This could be a positive development, he stated, because standardized contracts saved time and money.<sup>79</sup> The danger of the forms, however, was from the potential for abuse created by the one-sided control over contract terms. To prevent that harm, Llewellyn complained, courts used subterfuges, such as finding ambiguity where none existed or placing strained interpretations on clear language, to protect the non-drafting party. Llewellyn criticized this approach as ultimately ineffective, since it permitted skillful contract writers simply to draft new language to accomplish the same unfairness. Second, mangling legal rules limited the efficacy of the rules in other areas of contract law without guaranteeing just results for form contracts. Llewellyn cogently stated, "Covert tools are never reliable tools."<sup>80</sup>

Llewellyn's first attempt to clarify the law resulted in the following syllogism:

[F]ree contract presupposes free bargain; and . . . free bargain presupposes free bargaining; and that where bargaining is absent in fact, the conditions and clauses to be read into a bargain are not those which happen to be printed on the unread paper, but are those which a sane man might reasonably expect to find on that paper.<sup>81</sup>

This statement reads like a formulation of the modern doctrine of reasonable expectations.<sup>82</sup> It is not the words on the page that con-

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76. *Id.* at 621.

77. *Id.* at 643.

78. Llewellyn, *supra* note 1, at 700.

79. *Id.* at 701. "Nothing can approach in speed and sanity of readaptation the machinery of standard forms of a trade and for a line of trade, built to meet the particular needs of that trade."

80. *Id.* at 703.

81. *Id.* at 704.

82. See *infra* text accompanying notes 210-13.



trol, but the terms one would "reasonably expect" to find on the page.

Nonetheless, Llewellyn gave a great deal of deference to the drafter. Under Llewellyn's analysis, "utterly unreasonable clauses" would be struck down, but "a due presumption in favor of an expert's knowledge of what the condition of his trade may be calling for" would still be permitted.<sup>83</sup>

Llewellyn struck a similar balance in his last major discussion of form contracts in 1960.<sup>84</sup> He propounded his "answer" to the question posed by form contracts:

Instead of thinking about "assent" to boiler-plate clauses, we can recognize that so far as concerns the specific, there is no assent at all. What has in fact been assented to, specifically, are the few dickered terms, and the broad type of the transaction, and but one thing more. That one thing is a blanket assent (not a specific assent) to any not unreasonable or indecent terms the seller may have on his form, which do not alter or eviscerate the reasonable meaning of the dickered terms. The fine print which has not been read has no business to cut under the reasonable meaning of those dickered terms which constitute the dominant and only real expression of agreement, but much of it commonly belongs in.<sup>85</sup>

Llewellyn continued to believe that tradespeople knew which clauses were most appropriate and that forms were efficient and desirable. He added that courts reviewing form terms should remember that "there are still many which are sound particularizations of the deal to the business, very useful and wholly within reason; and those ought to be sustained and applied."<sup>86</sup>

Perhaps the most vigorous attack on Llewellyn's respect for non-negotiated terms came from Todd Rakoff, who argued that Llewellyn had "failed to understand that it is very often the lawyer's expertise, not the businessman's, that is revealed."<sup>87</sup> Rakoff asserted the goal of contract drafters was not to further the interest of the trade, but to protect their client's interests as best possible. Thus, he proposed that subordinate contract terms, which he called "invisible terms," be presumed unenforceable.<sup>88</sup>

Colin Kaufman countered that it was judges who should not be overly trusted in determining the content of form contracts.<sup>89</sup> He

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83. Llewellyn, *supra* note 1, at 704.

84. KARL N. LLEWELLYN, *THE COMMON LAW TRADITION: DECIDING APPEALS* (1960).

85. *Id.* at 370.

86. *Id.* at 366.

87. Rakoff, *supra* note 6, at 1205.

88. *Id.* at 1220-48.

89. COLIN K. KAUFMAN, *CORBIN ON CONTRACTS* (1992 Supp.).

feared that Rakoff's approach would result in a change from "an even-handed rule to a consumers only doctrine."<sup>90</sup> Kaufman contended that form contracts, growing out of business experience and expertise, serve a valid purpose. The role of the courts, he concluded, is to ensure the fairness of form terms: the contract is presumed fair, but the non-drafting party can defeat it by proving either that the drafter has received all the benefits of the terms or that the terms are not reasonably adapted to advance legitimate purposes.<sup>91</sup> In sum, Kaufman argued, "[t]he loss of 'freedom of contract' suffered by the customer in modern society does not require as a corollary that businesses must lose that same freedom, but only that they exercise that freedom in a fair manner."<sup>92</sup>

An alternate tack was suggested by both Arthur Leff<sup>93</sup> and David Slawson.<sup>94</sup> They each saw the problems of form contracts as a public law concern. Skeptical about the expertise of courts, each urged legislative and administrative control of the content of form contracts.<sup>95</sup>

In a subsequent article, Slawson argued such outside intervention might not be necessary if courts continued to adopt what he termed, "the new meaning of contract."<sup>96</sup> Under this approach, courts are not limited to the mere interpretation of contractual language. They are to find the contractual obligations imposed by form contracts based on all the circumstances.<sup>97</sup> The writing no longer controls. Instead, "under the new meaning [of contracts], the reasonable expectations *are* the contract."<sup>98</sup>

One final player in the academic debate was Robert Keeton, whose analysis of insurance contracts helped spawn the "doctrine of reasonable expectations."<sup>99</sup> Even though his analysis focused on insurance contracts, the reasoning and principles generally apply to consumer form contracts.<sup>100</sup>

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90. *Id.* at 368-89.

91. *Id.* at 358-67.

92. Colin K. Kaufman, *The Resurrection of Contract*, 17 WASHBURN L.J. 38, 71 (1977).

93. Leff, *supra* note 6, at 147-57.

94. Slawson, *supra* note 30, at 557-61. See also W. David Slawson, *Mass Contracts: Lawful Fraud in California*, 48 S. CAL. L. REV. 1, 14-20 (1974).

95. Leff, *supra* note 6, at 147-57; Slawson, *supra* note 30, at 533-36.

96. Slawson, *supra* note 10, at 71-74.

97. *Id.* at 23.

98. *Id.*

99. Keeton, *supra* note 58, at 966-74.

100. Since neither type of form contract is read by the typical consumer and neither results from negotiation but is presented on a take-it-or-leave-it basis by a drafter with greater bargaining power, the literal language on each printed page often will not reflect the objective understanding of the contract. See, e.g., Slawson, *supra* note 10, at 52 (asserting that the reasonable expectations doctrine "lacks any principled justification for being limited to

Judge Learned Hand had espoused an earlier version of the doctrine of reasonable expectations. He wrote that the common layperson's understanding of insurance terms, not the special industry meaning, should govern policy interpretation.<sup>101</sup> The content of the actual language used, however, firmly anchored this rule so that unambiguous language still controlled: "A man must indeed read what he signs, and he is charged, if he does not; but insurers who seek to impose upon words of common speech an esoteric significance intelligible only to their craft, must bear the burden of any resulting confusion."<sup>102</sup>

In 1970, Keeton reviewed many insurance cases relying on the insured's reasonable expectations, and he enunciated a new version of this principle: "The objectively reasonable expectations of applicants and intended beneficiaries regarding the terms of insurance contracts will be honored even though painstaking study of the policy provisions would have negated those expectations."<sup>103</sup> The use of the phrase "painstaking study" illustrates the lineage of the principle. Without mandating that policyholders "read what they sign," Keeton

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insurance policies"); see also *Gray v. American Express Co.*, 743 F.2d 10, 17 (D.C.Cir. 1984) (applying rules of construction for insurance contracts to ordinary contract); *Davis v. M.L.G. Corp.*, 712 P.2d 985, 989 n.4 (Colo. 1986) (stating that because car rental "was, like most insurance contracts, a 'form' contract prepared by the lessor and offered on a take-it-or-leave-it basis . . . 'we feel that the appropriate interpretive principles are those normally applicable to insurance contracts.' ") (quoting *Elliott Leases Cars, Inc. v. Quigley*, 373 A.2d 810, 812 (R.I. 1977)); *Uni-Serv Corp. v. Frede*, 271 N.Y.S.2d 478, 483 (N.Y. Civ. Ct. 1966), *aff'd*, 279 N.Y.S.2d 510 (N.Y. App. Term 1967) ("The rules for construction of ordinary contracts do not differ from those to be applied to insurance contracts . . . . In this case, the [credit card] contract was not negotiated and [was] exclusively prepared by plaintiff, so that rules for construction of insurance contracts are applicable."); *Allen v. Prudential Property & Casualty Ins. Co.*, 839 P.2d 798, 806 n.17 (Utah 1992) (finding it "difficult to conceive why the version of the reasonable expectations doctrine . . . should be limited solely to insurance contracts"). Insurance contracts do contain some common features, such as a right of cancellation. See William A. Mayhew, *Reasonable Expectations: Seeking A Principled Application*, 13 PEPP. L. REV. 267, 271-72 (1986). Also, insurance contracts are not received until after they have been made. Mark C. Rahdert, *Reasonable Expectations Reconsidered*, 18 CONN. L. REV. 323, 339-41 (1986). Nevertheless, these features are either not determinative of the objective understanding of consumers or are not unique to insurance contracts. See, e.g., *Carnival Cruise Lines v. Shute*, 499 U.S. 585 (1991) (where cruise line did not send contract until ticket paid).

101. *Gaunt v. John Hancock Mut. Life Ins. Co.*, 160 F.2d 599, 601 (2d Cir.), *cert. denied*, 331 U.S. 849 (1947) ("An underwriter might so understand the phrase, when read in its context, but the application was not to be submitted to underwriters; it was to go to persons utterly unacquainted with the niceties of life insurance, who would read it colloquially. It is the understanding of such persons that counts . . .").

102. *Gaunt*, 160 F.2d at 602.

103. Keeton, *supra* note 58, at 967. The first case to adopt explicitly a formulation similar to Professor Keeton's was *Smith v. Westland Life. Ins. Co.*, 539 P.2d 433, 441 (Cal. 1975).

implies that an unread contract containing an unexpected clause is binding if a "casual reading" would have indicated its meaning.

In fact, one of the greatest sources of confusion over the doctrine of reasonable expectations is whether court should indeed use it only for contracts that are ambiguous or also for all unread language.<sup>104</sup> If the doctrine of reasonable expectations is limited to ambiguous contracts, it is not a doctrine at all; it is nothing more than the traditional rule that ambiguous contracts be interpreted against the drafter.<sup>105</sup> Only if courts discard the fiction that consumers read form language, unambiguous or otherwise, will contracting parties realize their reasonable expectations.

The other major stumbling block for courts considering the doctrine of reasonable expectations is the fear that consumers will invent expectations *post hoc* to receive a gain not bargained for. Rejecting the doctrine of reasonable expectations, the Idaho Supreme Court warned that "the periphery of what losses would be covered could be extended by an insured's affidavit of what he 'reasonably expected' to be covered."<sup>106</sup>

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104. One commentator noted three separate responses: restricting the theory to ambiguous contracts only, utilizing the theory to determine whether a contract's "fine print" unfairly limits a party's more prominent expectations, and looking at all the circumstances to determine reasonable expectations. Ware, *supra* note 3, at 1467. Other commentators have noted only two dominant themes. See, e.g., Rahdert, *supra* note 100, at 335-36, 345 (analyzing weaker and stronger versions). There is an ongoing judicial debate concerning the subject. Compare Casey v. Highlands Ins. Co., 600 P.2d 1387, 1391 (Idaho 1979) (enforcing unambiguous insurance terms); Standard Venetian Blind Co. v. American Empire Ins. Co., 469 A.2d 563 (Pa. 1983) (same) with Lauvetz v. Alaska Sales & Serv., 828 P.2d 162 (Alaska 1991) (no ambiguity needed); Gordinier v. Aetna Casualty & Sur. Co., 742 P.2d 277, 282-83 (Ariz. 1987) (same). A Missouri appellate court has criticized its Supreme Court for requiring ambiguity. Compare Rodriguez v. General Accident Ins. Co., 808 S.W.2d 379, 382 (Mo. 1991) ("The 'reasonable expectations doctrine' requires that there be a contract of adhesion and ambiguity in the policy language") with Cobb *ex rel.* Lambert v. State Farm Mut. Auto. Ins. Co., 820 S.W.2d 602, 604 (Mo. App. 1991) (stating that requiring an ambiguity before applying the doctrine of reasonable expectations is "inconsistent with the definition of the doctrine as it applies even when 'a thorough study of the policy provisions would have negated these expectations.'") (quoting Robin v. Blue Cross Hosp. Serv., Inc., 637 S.W.2d 695, 697 (Mo. 1982)). See generally Roger C. Henderson, *The Doctrine of Reasonable Expectations in Insurance Law after Two Decades*, 51 OHIO ST. L.J. 823 (1990); Mayhew, *supra* note 100, at 278-86.

105. See National Bank v. Insurance Co., 95 U.S. 673, 679 (1877) ("It is its [the insurance company's] language which the court is invited to interpret, and it is both reasonable and just that its own words should be construed most strongly against [it]."); see also Ware, *supra* note 3, at 1469 (stating that because all courts interpret ambiguities against the drafter, limiting reasonable expectations to ambiguous contracts effectively means there is no new doctrine).

106. Casey v. Highlands Ins. Co., 600 P.2d 1387, 1391 (Idaho 1979); see also San Francisco Newspaper Printing Co. v. Superior Ct., 216 Cal. Rptr. 462, 465 (Cal. Ct. App. 1985) (stating that "failing to read the contract is no excuse, otherwise all contracts of adhesion would be unenforceable at the whim of the adhering party").

This concern is unwarranted and confuses objective with subjective expectations. The very concept of *reasonable expectations* imposes a requirement that the expectation have an objective foundation. The consumer must still show "some evidentiary basis beyond naked belief on the part of the person seeking coverage, i.e., that it be objectively determinable."<sup>107</sup>

Perhaps the real reason for the judicial reluctance to embrace the full doctrine of reasonable expectations is the fear of creating broad new exceptions to normal contract principles for a wide range of consumer transactions.<sup>108</sup> For example, when the Utah Supreme Court rejected the doctrine of reasonable expectations, it emphasized its concern with any "attempt to craft a new and potentially sweeping equitable doctrine."<sup>109</sup>

We need no new and sweeping doctrine for interpreting consumer form contracts. Properly applied, the venerable objective theory will achieve the goals of the doctrine of reasonable expectations, without grafting a new branch onto the jurisprudential tree.<sup>110</sup>

#### V. ROADS NOT TAKEN: THE U.C.C. AND THE SECOND RESTATEMENT

Twice has a solution to the dilemma of form contracts been close at hand. The drafters of both the Uniform Commercial Code (U.C.C.) and the Restatement (Second) of Contracts presented for consideration workable proposals consistent with the objective theory of contracts. It is no small irony that the champions of these proposals were two of the leading figures in twentieth century contract law,

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107. Henderson, *supra* note 104, at 839.

108. *Allen v. Prudential Property & Casualty Ins. Co.*, 839 P.2d 798, 806 (Utah 1992). The court describes its decision as one "to proceed interstitially with existing equitable doctrines rather than to adopt a new doctrine with unknown ramifications." *Id.* at 806; *see also* *Markline Co. v. Travelers Ins. Co.*, 424 N.E.2d 464, 465-66 (Mass. 1981) (declining without explanation to adopt the doctrine of reasonable expectations and stating "[w]e are not prepared to make this the first case in which this court adopts such an approach to the purchase of insurance.").

109. *Allen*, 839 P.2d at 806. Later in the opinion, the court describes its decision as one "to proceed interstitially with existing equitable doctrines rather than to adopt a new doctrine with unknown ramifications . . . ." *Id.* at 806. *See also* *Markline Co. v. Travelers Ins. Co.*, 424 N.E.2d 464, 465-66 (Mass. 1971) (declining to adopt the doctrine of reasonable expectations because, without further explanation, "[w]e are not prepared to make this the first case in which this court adopts such an approach to the purchase of insurance.").

110. Arguably, the Utah Supreme Court is, in fact, utilizing an objective theory. The court saw no reason not to use "estoppel, waiver, unconscionability, breach of the implied duty of good faith and fair dealing, and the rule that ambiguous language is to be resolved against the drafter . . . to protect against overreaching insurers . . . on a case-by case basis." *Allen*, 839 P.2d at 805-06 (footnotes omitted). If used properly, these doctrines all can serve to identify and protect the objective understanding of the consumer.

Professors Karl Llewellyn and E. Allan Farnsworth, and that both were soundly defeated in their attempt to rationalize this area of law.

In 1941, Llewellyn prepared two drafts for the proposed revision to the Uniform Sales Act.<sup>111</sup> The first draft, which has never been published in its entirety before,<sup>112</sup> contained a lengthy section devoted exclusively to form contracts.<sup>113</sup> In that section, Llewellyn explained again his view of form contracts and proposed a regulatory scheme to balance the competing interests. He entitled the section "DECLARATION OF POLICY, AND PROCEDURE WITH REGARD TO DISPLACEMENT OF SINGLE PROVISIONS OR GROUPS OF PROVISIONS BY AGREEMENT."

The section generally permitted the enforcement of "particularized terms," parts of a contract to which "both the parties have . . . directed their attention."<sup>114</sup> It declared, however, that assent to contract terms which "are not studied and bargained about in detail by both parties" should not be presumed unless those terms were fair.<sup>115</sup>

This section denied enforcement of form contracts containing unknown terms that altered the gap-filler provisions of the Code to the drafter's benefit, the so-called "jug-handled forms."<sup>116</sup> Llewellyn challenged the notion that fundamental contract principles required enforcing unfair form contract terms as written: "*The principle of freedom of bargain* is a principle of freedom of *intended bargain*."<sup>117</sup> When common-law courts first enunciated contract principles, Llewellyn noted, written contracts reflected the result of true bargaining, and accordingly, it was fair to presume that a signature meant agreement.<sup>118</sup> Modern form contracts, however, permitted bargaining on only a few terms such as "price, credit, date of delivery, description and quantity."<sup>119</sup> The rest of the contract is not negotiated and is assumed to be the "fair and balanced" terms implied by law.<sup>120</sup> A form contract that altered these terms could not be presumed, by

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111. I first learned of Llewellyn's first 1941 draft in Arthur A. Leff, *Unconscionability and the Code—The Emperor's New Clause*, 115 U. PA. L. REV. 485 (1967), which gives an extensive history of the drafting of U.C.C.'s § 2-302, the unconscionability provision.

112. For the full text of Section 1-C, see APPENDIX.

113. Karl N. Llewellyn, Unpublished First Draft of Revision to the Uniform Sales Act § 1-C (Sept. 1941) (This draft is contained in a letter dated September 5, 1941, from Karl Llewellyn to Professor Underhill of Yale Law School. The letter and draft are available at the Yale Law School library). See APPENDIX for full text of this document.

114. *Id.* § 1-C (1)(b).

115. *Id.* § 1-C (1)(d).

116. *Id.* § 1-C cmt. (A)(2).

117. *Id.* § 1-C cmt. (A)(3).

118. *Id.*

119. *Id.*

120. *Id.*

itself, to reflect the intent of the non-drafting party because "deliberate intent is not shown by a lop-sided form whose very content suggests that it has not been carefully read, and the circumstances of whose execution suggest that the matters under discussion and consideration were only the matters written or typed in."<sup>121</sup>

According to Llewellyn, fair form contracts served many socially valuable functions.<sup>122</sup> Usefulness alone, however, did not require that their abuses be tolerated. "The true principle is clear enough," he stated. "The substitution of private rule-making by one party, in his own interest, for the balance provided by the law, is not to be recognized without strong reason shown."<sup>123</sup>

The heart of Llewellyn's proposed law was to permit the enforcement of unbalanced form contracts only if the non-drafter had knowingly assented to them:

If the bloc as a whole is shown affirmatively to work a displacement or modification of the provisions of this Act in an unfair and unbalanced fashion not required by the circumstances of the trade, then the party claiming application of any particular provision in such bloc must show that the other party, with due knowledge of the contents of that particular provision, intended that provision to displace or modify the relevant provision of this Act in regard to the particular transaction.<sup>124</sup>

If the changes from the background law were balanced the contract would stand. To determine whether a fair balance existed, courts had to examine several circumstances, such as whether both parties helped prepare the contract, whether the displacement of provisions "as a whole runs disproportionately in favor of one party," and whether the new provisions reflect "fair expectation" in light of trade practices.<sup>125</sup>

Arguing that the proposed section would better fulfill the contracting parties' expectations and reduce the confusion caused by judicial attempts to avoid harsh form-contract terms, Llewellyn wrote that "the case for the provision stands . . . on the bewildering uncertainty which exists today as to when a court will read one-party language as it is written, and when it will find a way to avoid such

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121. *Id.* cmt. 3.

122. "[T]he expression of a body of fair and balanced usage is a great convenience, a gain in clarity and certainty, an overcoming of the difficulty faced by the law in regulating the multitude of different trades." *Id.* § 1-C.

123. *Id.*

124. *Id.* § 1-C (2)(a)(i).

125. *Id.* § 1-C (2)(c).

language."<sup>126</sup>

Nevertheless, the drafting committee rejected the proposal. Llewellyn's second draft of the year reported simply their conclusion that the "machinery for administration thus far developed is inadequate, and is too unreckonable to be in keeping with the lines of the Draft."<sup>127</sup> Two years later, the drafting committee proposed a much shorter version of the section with a far more limited scope. Courts were to presume all but "unconscionable" form terms as terms to which both parties had assented, regardless of whether the consumer was aware of them.<sup>128</sup> Eventually this section metamorphosed into the current 2-302 unconscionability provision.<sup>129</sup>

The current U.C.C., therefore, lacks the straight-forward approach Llewellyn suggested. Rather than simply acknowledging the lack of assent restricting the enforcement of unknown one-sided terms, the Code awkwardly focuses on the undefined and far more limited concept of unconscionability.<sup>130</sup>

Many courts have utilized the concept of unconscionability to deal with the harshness of form contracts.<sup>131</sup> Unfortunately, the doctrine of unconscionability is too weak a tool to effectively analyze these contracts. The principal difficulty arises from determining how bad is unconscionable.

The Official Comment circuitously indicates that a court may strike only those terms that are "so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract."<sup>132</sup> The classic definition of "unconscionable" terms, "such as

126. *Id.* § 1-C cmt. (7)(b).

127. THE REVISED UNIFORM SALES ACT 51-52 (Report and Second Draft 1941).

128. REVISED UNIFORM SALES ACT § 24 (1943).

129. As finally approved, U.C.C. § 2-302 (1) provides as follows:

If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

130. Karl Llewellyn, *Why a Commercial Code*, 22 TENN. L. REV. 779, 784 (1953). Perhaps, this is what Llewellyn was bemoaning when he wrote, "[T]here are so many beautiful ideas I tried to get in . . . but I was voted down." One might assume that Llewellyn was merely relieved to have even this small victory when he termed § 2-302 "perhaps the most valuable section in the entire Code." LAW REVISION COMM'N OF NEW YORK, 1 N.Y.L. REPORT AND RECORD OF HEARINGS ON THE UNIFORM COMMERCIAL CODE, Pub. L. No. 65, 121 (1954).

131. See, e.g., *Fontaine v. Industrial Nat'l Bank*, 298 A.2d 521, 523 (R.I. 1973) (striking as unconscionable clause in loan contract permitting repossession of car without demand for payment).

132. U.C.C. § 2-302 cmt. 1 (1989). The confused nature of this section is well-illustrated by the description in the Official Comment of the underlying purpose: "The principle is one of



no man in his senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other,"<sup>133</sup> fails to encompass the reality of modern form contracts. A wide range of unfairness and inefficiency would be permitted so long as the unread terms are not so extreme as to repulse people not under delusion.

Unconscionability will remain an important concept, even if the objective theory of contracts is used for form contract situations. A court must retain the ability, in an imperfect world, to deny force to grotesquely unfair terms. As Justice Felix Frankfurter wrote, "Is there any principle which is more familiar or more firmly embedded . . . than the basic doctrine that courts will not permit themselves to be used as instrument of inequality and injustice."<sup>134</sup>

Suppose, for example, the only electric company in town includes in the contract with its customers a confession of judgment provision. Even assuming consumers know of the term and reluctantly accept it, there would be something fundamentally wrong with a court permitting such a clause to bar billing disputes.<sup>135</sup>

Unconscionability should be saved for the extraordinarily unfair.<sup>136</sup> A more precise concept is needed for form contracts.

The drafters of the Restatement (Second) of Contracts acknowledged the overlap between the U.C.C.'s unconscionability provision and the developing law of form contracts and recognized the need for a specific separate analysis of form contracts.<sup>137</sup> As with the U.C.C.,

the prevention of oppression and unfair surprise . . . and not of disturbance of allocation of risks because of superior bargaining power." *Id.* As has been frequently noted, § 2-302 seems to encompass two forms of unconscionability: "oppression" implies a substantive harm while "unfair surprise" implies procedural trickery. *See, e.g.,* Leff, *supra* note 6. Arguably, a court needs both in order to strike a particular contract term.

133. *Hume v. United States*, 132 U.S. 406, 411 (1889) (quoting *Earl of Chesterfield v. Janssen*, 28 Eng. Rep. 82, 100 (1750)).

134. *United States v. Bethlehem Steel Corp.*, 315 U.S. 289, 326 (1942) (Frankfurter, J., dissenting).

135. This concept is illustrated by Professor Eisenberg's example of the "desperate traveller," who is rescued from death in the desert only upon promising to pay his rescuer two-thirds of his wealth or \$100,000 whichever is greater. Melvin A. Eisenberg, *The Bargain Principle and its Limits*, 95 HARV. L. REV. 741, 755-56 (1982).

136. Jeffrey Davis, *Revamping Consumer-Credit Contract Law*, 68 VA. L. REV. 1333, 1337 (1982) ("[Unconscionability] stands today primarily as a backstop to catch any creative new practices slippery enough to get past other protective devices, yet odious enough to fall within its timid scope.").

137. 47 A.L.I. PROC. 515, 523 (May 22, 1970) (Statement of Mr. Charles Hastings Willard). For an excellent discussion of the drafting of the RESTATEMENT (SECOND) OF CONTRACTS, see John E. Murray, Jr., *The Parol Evidence Process and Standardized Agreements under the Restatement (Second) of Contracts*, 123 U. PA. L. REV. 1342 (1975). Professor (now Judge) Robert Braucher was the first Chief Reporter for the RESTATEMENT (SECOND) OF CONTRACTS. After his appointment to the Supreme Judicial Court of

the path from visionary draft to final result is littered with missed opportunities.

A 1970 draft of the section devoted to standardized agreements stated, "[w]here the other party has reason to know that the party manifesting such assent believes or assumes that the writing does not contain a particular term, the term is not part of the agreement."<sup>138</sup> This language focused on the non-drafter's knowledge and expectations. Under this version, form terms were not enforceable if the drafter slipped into the contract terms the reasonable consumer would not have expected. The consumer had to be aware of and consent to unusual or novel terms. Consequently, only expected or explained terms would have been enforceable.

During the discussion of this section by the American Law Institute's review committee, opposition arose because it was feared that such a rule would impede freedom of contract. Charles Willard, a New York City lawyer, argued that "many of us have signed contracts containing provisions that we wish weren't in there, but on balance we thought: All right, we want the contract, and we have to take the good with the bad."<sup>139</sup> This reasoning ignores the reality that form terms are unread and often unexpected. Accordingly, consumers are not actually deciding whether they desire the contract enough to take the good with the bad terms. Nevertheless, Willard offered replacement language that eventually became the final version of Section 211(3): "Where the other party has reason to believe that the party manifesting such assent would not do so if he knew that the writing contained a particular term, the term is not part of the agreement."<sup>140</sup>

Professor Farnsworth argued that such a rule would permit enforcement of unexpected terms:

I'm troubled by the apparently simple form that contains a clause

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Massachusetts in 1971, he was replaced by Professor E. Allan Farnsworth. It was Professor Braucher who was the Chief Reporter when section 211, dealing with standardized contracts, was drafted.

138. RESTATEMENT (SECOND) OF CONTRACTS § 237(3) (Tent. Draft No. 5, 1970).

139. 47 A.L.I. PROC. 528 (May 22, 1970) (Statement of Mr. Charles Hastings Willard).

140. The remainder of RESTATEMENT (SECOND) OF CONTRACTS § 211 reads:

(1) Except as stated in Subsection (3), where a party to an agreement signs or otherwise manifests assent to a writing and has reason to believe that like writings are regularly used to embody terms of agreements of the same type, he adopts the writing as an integrated agreement with respect to the terms included in the writing.

(2) Such a writing is interpreted wherever reasonable as treating alike all those similarly situated, without regard to their knowledge or understanding of the standard terms of the writing.

RESTATEMENT (SECOND) OF CONTRACTS § 211 (1979).

in the back of it, perhaps a more or less innocuous clause, but one which, it turns out, because of later events is important to the person signing. It is quite possible, it seems to me, that under Mr. Willard's language it would not be clear that he would not have signed the agreement had he known that this clause was added; and yet under [the] original language it would not be a part of the contract.<sup>141</sup>

Professor Farnsworth was unable to convince other drafters to adopt his position. The final Restatement provision ignores the unfair form term that deals only with a secondary consideration or unlikely risk for the consumer. It has no effect unless the term is so egregious that it negates the entire contract. Thus, the evils of one-sided, unknown subordinate terms continue.

The Comments to this Section of the Restatement, however, seem to permit a far more realistic approach. They assert that businesspeople who draft standardized agreements are aware that "[c]ustomers do not in fact ordinarily understand or even read the standard terms."<sup>142</sup> The Comments further state that customers "are not bound to unknown terms which are beyond the range of reasonable expectation."<sup>143</sup>

This has enabled courts purporting to rely on Section 211 to actually improve upon it. The Arizona Supreme Court, in ostensibly adopting the rule of Section 211, held that courts should "enforce a boilerplate term unless the drafter had reason to believe that the adhering party would not have assented to the particular *term* had he or she known of its presence."<sup>144</sup> Note that this formulation of Section 211's rule involves the far more precise inquiry of whether a given term in the form contract would have been assented to had it been read and understood. By contrast, the literal language of Section

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141. 47 A.L.I. PROC. 527 (May 22, 1970) (Statement of E. Allen Farnsworth).

142. RESTATEMENT (SECOND) OF CONTRACTS § 211 cmt. b (1979).

143. *Id.* § 211 cmt. f. This comment further develops the idea that non-assented to terms are non-binding,

[A] party who adheres to the other party's standard terms does not assent to a term if the other party has reason to believe that the adhering party would not have accepted the agreement if he had known the agreement contained the particular term. Such a belief or assumption may be shown by the prior negotiations or inferred from the circumstances. Reason to believe may be inferred from the fact that the term is bizarre or oppressive, from the fact that it eviscerates the non-standard terms explicitly agreed to, or from the fact that it eliminates the dominant purpose of the transaction. The inference is reinforced if the adhering party never had an opportunity to read the term, or if it is illegible or otherwise hidden from view.

*Id.*

144. *Gordinier v. Aetna Casualty & Sur. Co.*, 742 P.2d 277, 283 (Ariz. 1987) (emphasis added).

211 permits enforcement of such an unwanted term unless the term was so important and unfair that the consumer would have refused to assent to the *contract*. As one commentator notes, the actual words of Section 211 of the Restatement ultimately amount to "nothing more than an effort to deal with a species of unconscionability."<sup>145</sup>

## VI. OBJECTIVE ASSESSMENT OF SUBJECTIVE KNOWLEDGE

The objective theory of contracts has led to several rules for dealing with circumstances where one party is aware of the other party's lack of knowledge. Normally, when one party, by research or fortuitously, learns information that affects the value of the bargain there is no duty to share that information.<sup>146</sup> There are, however, instances where it is both economically efficient and just to prevent a party, who is aware of the other's misunderstanding or lack of knowledge, from taking unfair advantage or from imposing unexpected risks and burdens.<sup>147</sup>

Those who possess both superior information and the knowledge of another's relative ignorance will not be permitted to pretend that they are dealing with someone possessing adequate knowledge. The doctrines of known unilateral mistake and of foreseeable consequential damages, the U.C.C.'s "Battle of the Forms" rule, and even the tort law requirement that doctors obtain their patients' informed consent all share this underlying rationale. Close scrutiny of this theme permits not only a fuller understanding of the objective theory of contracts, but also illustrates its proper application to form contracts.

### A. *Known Misunderstanding or Unilateral Mistake*

Frequently, contracting parties disagree on the meaning of a term, but one party knows or should know of the other's differing belief. In such cases the courts will apply the meaning of the unknowing party.<sup>148</sup> Professor Farnsworth tells the story of Temures, a legal-

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145. Murray, *supra* note 137, at 1383.

146. See, e.g., *Laidlaw v. Organ*, 15 U.S. 178, 186-87 (1817).

147. It is well established in contract law that "where the peculiar talent or the industry of one man has given him a superiority of knowledge," it is permissible for him to withhold such information. GULIAN C. VERPLANCK, AN ESSAY ON THE DOCTRINE OF CONTRACTS 75 (Arno Press ed. 1972) (1825). Yet contracts that take advantage in any respect are presumed fraudulent when it is understood by the other that no advantage will be taken. *Id.* at 119. Verplanck argued that this reasoning applied to all sales and stated that if a seller's neighbor had such confidence that the seller would sell to him at market price and that the goods the seller offers were of merchantable quality, it would be unfair to take advantage of such confidence. *Id.* at 134.

148. In the words of the early nineteenth century author Verplanck, a contract is breached "when the thing done, or delivered, varies materially in kind, or quality, from the kind or

istic warrior who promised a garrison that "no blood would be shed if they surrendered."<sup>149</sup> Upon surrender, the garrison was buried alive, without so much as a loophole to breathe through. A modern court reviewing this agreement would find Temures guilty of a breach of contract because he should have been aware of the meaning that would likely be attached to his promise.

A similar situation arises when one party is aware of the other party's mistake. Suppose a subcontractor submits a bid to the contractor containing an obvious mathematical error. The contractor cannot happily accept the mistaken bid and pocket the windfall.<sup>150</sup> The law excuses the mistaken subcontractor from performance because the contractor had actual knowledge of the error. Moreover, courts often impute such knowledge to contractors who receive a range of bids of which one is markedly lower. The law does not reward the unquestioning contractor who rushes to accept an offer that is "too good to be true."<sup>151</sup> The subcontractor prevails because the contractor had "reason to know" of the error.

Both rules have long been accepted as wise policy. One commentator argued that the party who knows of an error is the "better mistake-preventer . . . because of his superior access to relevant information that will disclose the mistake and thus allow its correction."<sup>152</sup> In other words, neither Temures nor the contractor should prevail because a reasonable person in their positions should have understood the probable intent of their negotiating partners. Allowing those with easy knowledge of another's error to take advantage of that knowledge would be unjust.<sup>153</sup>

The same theory should apply to consumer form contracts. Drafters know the terms of their own contracts and consumers do not. Since the drafters are aware that consumers do not read their contracts, the drafters know that the contract will not inform con-

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quality . . . understood by the one party, and known to be so understood by the other." *Id.* at 148.

149. Farnsworth, *supra* note 14, at 946 (quoting WILLIAM PALEY, *PRINCIPLES OF MORAL AND POLITICAL PHILOSOPHY*, Book III, Part I, ch. V (12th ed. 1810)).

150. *Tyra v. Cheney*, 152 N.W. 835 (Minn. 1915). "One cannot snap up an offer or bid knowing that it was made in mistake." *Id.*

151. See Anthony T. Kronman, *Mistake, Disclosure, Information and the Law of Contracts*, 7 J. LEGAL STUD. 1, 7 (1978); see, e.g., *Geremia v. Boyarsky*, 140 A. 749, 750 (Conn. 1928) (granting rescission where plaintiff had "good reason to believe that a substantial error had been made"); FARNSWORTH, *supra* note 18, at 668 (stating that a bidder can avoid a contract if the difference from other bids was so great "as to make the mistake palpable").

152. Kronman, *supra* note 151, at 7-8.

153. The concept of "easy" knowledge is meant to distinguish the cases where the party with greater knowledge acquired such knowledge as the result "of a deliberate and costly search." *Id.* at 13.

sumers of their legal rights. Similarly, if a form contract contains a term that eviscerates the central purpose of the contract, contradicts representations made by the seller, or deals with secondary issues not considered by the typical consumer, the drafter should know that the written term is unexpected. Since the term is both unexpected and unknown to the consumer, the drafter also should know that the consumer is mistaken about the contents of the contract.

Drafters should not be permitted to take Temures-like advantage of consumers. As one court has stated, "[w]here a party permits another to sign a contract knowing that he is under a misapprehension as to its terms, there is equitable fraud which warrants reformation or rescision."<sup>154</sup>

### B. *The Rule of Hadley v. Baxendale*

The classic case of *Hadley v. Baxendale*,<sup>155</sup> recognizes the responsibility on a party with greater knowledge. In *Hadley*, a mill owner entrusted a broken engine shaft to a common carrier for delivery to a manufacturer as model for a replacement shaft. Due to the carrier's neglect, delivery took longer than expected, and the mill owner, who was unable to run the mill in the interim, suffered a loss of expected profits. The court denied recovery of lost profits and stated:

Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, i.e. according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it.<sup>156</sup>

The court explained that breaching parties should not be responsible for special circumstances of which they are unaware, because they can "only be supposed to have . . . in [their] contemplation the amount of injury which would arise generally."<sup>157</sup> The court also reasoned that those who face special losses have an obvious protection of

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154. *Grossman Furniture Co. v. Pierre*, 291 A.2d 858, 863 (N.J. Essex County Ct. 1972); see also *Miller v. Troy Laundry Machinery Co.*, 62 P.2d 975, 977-78 (Okla. 1936) (finding such exploitation to be constructive fraud); *Daskolopoulos v. European Am. Bank Trust Co.*, 481 N.Y.S.2d 100, 102 (N.Y. App. Div. 1984) (finding allegations sufficient to raise issue of fact as to whether plaintiff misunderstood the nature of lease obligations and whether defendants were aware of that misunderstanding).

155. 156 Eng. Rep. 145 (1854).

156. *Id.* at 151.

157. *Id.*

their interests by disclosing their unexpected situation. The court stated:

Now, if the special circumstances under which the contract was actually made was communicated by the plaintiffs to the defendants, and thus known to both parties, the damages resulting from the breach of such a contract, which they would reasonably contemplate, would be the amount of injury which would ordinarily follow from a breach of contract under these special circumstances so known and communicated.<sup>158</sup>

Thus, the rule of *Hadley* is that breachers are responsible only for consequential damages they "reasonably contemplate," either because such damages are "naturally occurring" or because they have been disclosed. In other words, the risk of loss assumed by the promisor is that which the reasonable person in the position of the promisor would foresee.

There are several sound reasons for such a rule. First, if promisors know of special circumstances, they can negotiate special contract terms.<sup>159</sup> Second, with adequate knowledge the eventual breacher might well have decided that the likely gain from the contract was not worth the risk of substantial damages, and thus would have foregone the deal. Finally, greater care in negotiation might be taken, commensurate with the greater risk. The rule of *Hadley* "induces the party with knowledge of the risk either to take any appropriate precautions himself or, if he believes that the other party might be the more efficient loss avoider, to disclose the risk to that party."<sup>160</sup>

The same logic applies where the drafter of a form contract inserts burdens and risks of which the consumer is unaware. Without knowing these terms, the consumer can neither negotiate different terms, avoid an unduly risky venture, nor utilize greater care in negotiations. It is incumbent upon the contract drafter, like the mill owner, to disclose the greater risks and permit consumers to assume the costs of just those losses within their "reasonable contemplation." Without the seller's disclosure of unexpected terms, consumers should be held to only such risks "as may reasonably be supposed to have been in the contemplation of *both* parties, at the time they made the contract. . . ."<sup>161</sup>

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158. *Id.*

159. The *Hadley* court stated that, "of this advantage it would be very unjust to deprive [the promisors]." *Id.*

160. Posner, *supra* note 3, at 61.

161. *Hadley*, 156 Eng. Rep. at 151 (emphasis added).

### C. *The U.C.C. and the Battle of the Forms*

Imagine a seller with two customers: a large business making multiple purchases and an individual consumer. Assume that both the business buyer and the consumer order goods from the seller. The business buyer sends a purchase order drafted by one of her attorneys while the consumer orders by telephone. Neither buyer mentions the implied warranty of merchantability in the order. Prior to shipment, the seller sends identical acknowledgement forms to both purchasers, disclaiming the implied warranty of merchantability in large capital letters. The business buyer forwards the form to her lawyer for filing; the consumer puts the form in a kitchen drawer. Neither of them reads the form. When the goods arrive defective, the seller raises the acknowledgement form as a defense. Who has the better chance of having the seller's unread limitation clause declared ineffective: the business buyer supported by a staff of lawyers or the solitary consumer?

While the answer for the case of the consumer is uncertain,<sup>162</sup> thanks to the "battle of the forms" section of the Uniform Commercial Code the business buyer will prevail because disclaiming the implied warranty of merchantability is a "material alteration" of the bargain.<sup>163</sup> This section was designed to cover situations where two parties, usually merchants, exchange forms without reading the other party's form. For those circumstances, the Code changes the common-law "mirror image" rule and permits a contract to be formed even if the forms contain non-identical terms.<sup>164</sup> If courts recognize such a contract, they need to determine which document's terms become part of the contract. Section 2-207 (2) provides that, between merchants, additional terms in the offeree's form become part of the contract unless they "materially alter" the bargain.<sup>165</sup>

This is a sensible rule, based on the reality that the forms are not read and on the sense that permitting an acceptor to alter the terms of the bargain unilaterally in an unexpected material way is unfair and uneconomical.<sup>166</sup> The Code's Official Comments state that if the offeree's terms "are such as materially to alter the original bargain,"

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162. See *infra* text accompanying notes 169-172.

163. U.C.C. § 2-207 cmt. 4 (1989). See, e.g., *Old Albany Estates, Ltd. v. Highland Carpet Mills, Inc.*, 604 P.2d 849, 853 (Okla. 1979) (holding such a disclaimer to be a new term materially altering the contract and thus not part of the bargain).

164. U.C.C. § 2-207 (1).

165. U.C.C. § 2-207 (2)(b). The new terms also do not become part of the contract if they are objected to in the offer itself, by restricting acceptance to only the terms of the offer, or by notification shortly after receipt of the return form. U.C.C. § 2-207 (2)(a), (c).

166. FARNSWORTH, *supra* note 18, at 161.



they do not become part of the contract "unless expressly agreed to by the other party."<sup>167</sup> The Comments also point out that "express awareness by the other party" is the only way enforcement of such terms would not result in "surprise or hardship."<sup>168</sup>

It would be illogical, if not plain silly, to prevent a consumer from making the same argument. Both the business buyer and the consumer had objectively reasonable expectations that the goods would be at least of "average" quality.<sup>169</sup> Neither read the seller's forms, which is what the seller would expect. If a disclaimer of warranty "materially alters" the bargain for the experienced business buyer, it must surely do the same for the consumer. If anyone is to be penalized for not reading the acknowledgement form, it should be the merchant buyer with her cadre of lawyers, not the untrained, inexperienced consumer.

The judicial experience with Section 2-207 is useful to determine which terms are presumably within the consumer's objective understanding of the merchant's form. In addition to refusing to enforce disclaimers of warranties, courts applying Section 2-207 have also refused to enforce clauses that limit the remedy for breach of warranty to replacement,<sup>170</sup> require the buyer to pay the seller's attorneys' fees,<sup>171</sup> mandate the seller's choice of law,<sup>172</sup> or compel arbitration.<sup>173</sup>

If courts do not enforce such terms, absent knowing assent, against a merchant engaging in the battle of the forms, they certainly should not enforce them against the unarmed consumer. Consumers, no less than merchants, are entitled to enter contracts free from surprise and hardship.

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167. U.C.C. § 2-207 cmt. 3.

168. U.C.C. § 2-207 cmt. 4.

169. This was Professor Prosser's argument in favor of enforcing disclaimers of the warranty of merchantability only with actual assent. *See supra* text accompanying notes 67-73.

170. *Reliance Steel Prods. Co. v. Kentucky Elec. Steel Co.*, 35 U.C.C. Rep. Serv. 1430 (E.D. Pa. 1983).

171. *Johnson Tire Serv., Inc. v. Thorn, Inc.*, 613 P.2d 521 (Utah 1980).

172. *General Instrument Corp. v. Tie Mfg. Inc.*, 517 F. Supp. 1231 (S.D.N.Y. 1981); *see also Pacamor Bearings, Inc. v. Molon Motors & Coil, Inc.*, 477 N.Y.S.2d 856 (N.Y. App. Div. 1984). *But see Coastal Indus., Inc. v. Automatica Steam Prods. Corp.*, 654 F.2d 375, 379 (5th Cir. 1981) (holding choice of New York law did not materially alter the contract because "[t]he application of New York law comports with the objective intent of the parties . . . in that New York law bears a reasonable relation to the sales transaction in issue").

173. *Coastal Indus.*, 654 F.2d at 379; *see also Duplan Corp. v. W.B. Davis Hosiery Mills, Inc.*, 442 F. Supp. 86, 89 (S.D.N.Y. 1977); *Marlene Indus. Corp. v. Carnac Textiles, Inc.*, 380 N.E.2d 239 (N.Y. 1978). *But see Diskin v. J.P. Stevens*, 652 F. Supp. 553 (D. Mass. 1987) (holding that arbitration clause does not materially alter the contract when trade usage indicates that arbitration is common).

### D. *Informed Consent*

To facilitate understanding of the relationship between knowledge and assent one can draw a useful comparison with the tort law requirement that physicians obtain a patient's informed consent before commencing treatment. This requirement predates the American Revolution,<sup>174</sup> and is based on the principle that "[e]very human being . . . has a right to determine what shall be done with his own body."<sup>175</sup>

Courts have consistently recognized that "[t]rue consent to what happens to one's self is the informed exercise of a choice, and that entails an opportunity to evaluate knowledgeably the options available and the risks attendant upon each."<sup>176</sup> The patient's "right of self decision . . . can be effectively exercised only if the patient possesses enough information to enable an intelligent choice."<sup>177</sup>

Medical knowledge is not presumed to be in the possession of the non-expert patient. "The doctrine of informed consent takes full account of the probability that unlike the physician, the patient is untrained in the medical science, and therefore depends completely on the trust and skill of his physician for the information on which he makes his decision."<sup>178</sup> Patients are not responsible for ferretting out the necessary relevant information, because few patients have the knowledge and ability to "identify the relevant questions in the absence of prior explanation by the physician. Physicians and hospitals have patients of widely divergent socio-economic backgrounds, and a rule which presumes a degree of sophistication which many members of society lack is likely to breed gross inequities."<sup>179</sup>

To ensure that consent to medical procedures is true informed

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174. "[I]t was improper to disunite the callous without consent; this is the usage and law of surgeons . . . ." Slater v. Baker & Stapleton, 95 Eng. Rep. 860, 862 (K.B. 1767) (quoted in LaCaze v. Collier, 434 So. 2d 1039 (La. 1983)).

175. Schloendorff v. Society of N.Y. Hosp., 105 N.E. 92, 93 (1914) (Cardozo, J.). Some courts have premised the doctor's duty to disclose information on a fiduciary-type relationship with a patient. See, e.g., Woods v. Brumlop, 377 P.2d 520, 524 (N.M. 1962). One can argue that a lawyer drafting a form contract who is aware that the consumer will not rely on legal counsel in determining whether to sign the contract also has a fiduciary-type obligation not to overreach against the uncounseled consumer.

176. Canterbury v. Spence, 464 F.2d 772, 780 (D.C. Cir. 1972); see also Sard v. Hardy, 379 A.2d 1014, 1019 (Md. 1977) (stating that effective consent "must have been an 'informed' consent, one that is given after the patient has received a fair and reasonable explanation of the contemplated treatment or procedure.").

177. Canterbury, 464 F.2d at 786; see also Pegram v. Sisco, 406 F. Supp. 776, 779 (W.D. Ark. 1976).

178. Sard, 379 A.2d at 1020.

179. Canterbury, 464 F.2d at 783 n.36.

consent, doctors must disclose material risks.<sup>180</sup> This requirement squares with the objective theory of contracts. A reasonable physician should not assume that a patient consents to medical procedures unless the doctor has provided the information necessary to permit an informed choice.<sup>181</sup>

The objective theory protects the physician as well. If the information is presented in an appropriate manner, it is irrelevant whether an individual patient subjectively understands the situation, since "the physician discharges the duty when he makes a reasonable effort to convey sufficient information, although the patient, without fault of the physician, may not fully grasp it."<sup>182</sup> Similarly, the information the doctor must convey is based on what the doctor would reasonably assume the patient did *not* know: "There is no obligation to communicate those [dangers] of which persons of average sophistication are aware. Even more clearly, the physician bears no responsibility for discussion of hazards the patient has already discovered . . . ."<sup>183</sup>

Courts reviewing consumer form contracts should apply similar principles. A consumer's true assent should be understood as the informed exercise of a choice, which is effectively exercised only if the consumer possesses enough information to make an intelligent choice.

As with medical knowledge, knowledge of legal rules cannot be presumed for the layperson. As patients are generally uneducated about medical procedures, few consumers possess the legal acumen even to identify the relevant questions. Consumers should only be held to have consented to unread terms of which they have been informed.

Drafters of form contracts must not be permitted to presume assent to unexpected terms unless they adequately disclosed such terms. In the world of contracts, as in the realm of medicine, true assent by the non-expert requires informed consent.

## VII. EARLY JUDICIAL ATTEMPTS AT A UNIFIED THEORY

In the 1950s, courts began to consider directly the issue of form contracts as a category unto themselves. While courts did not change the classic framework, some judges began arguing for a "realistic" resolution of these cases.

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180. *Sard*, 379 A.2d at 1022. "A material risk is one which a physician knows or ought to know would be significant to a reasonable person in the patient's position . . . ."

181. See *Rogers v. Lumberman's Mut. Casualty Co.*, 119 So. 2d 649, 652 (La. Ct. App. 1960) (characterizing general consent to all procedures "as found necessary" to be "almost completely worthless").

182. *Canterbury*, 464 F.2d at 780 n.15.

183. *Id.*

In *Siegelman v. Cunard White Star*,<sup>184</sup> the Second Circuit enforced language from a cruise line's contract limiting the time for passengers to file suit to one year. In dissent, Judge Frank urged the court to consider the cruise contract a "contract of adhesion" and argued that courts should refuse "to enforce directly . . . highly unfair provisions of all so-called 'contracts of adhesion' where there was no possibility of real bargaining."<sup>185</sup> Contending that the consumer did not really assent to the unknown terms in the form contracts, Judge Frank stated "[i]n such a standardized or mass-production agreement, with one-sided control of its terms, when the one party has no real bargaining power, the usual contract rules, based on the idea of 'freedom of contract,' cannot be applied rationally. For such a contract is 'sold not bought.'"<sup>186</sup>

A few years later, an Illinois appellate court criticized its own state's Supreme Court for upholding lease provisions exempting landlords from liability to tenants.<sup>187</sup> The lower court argued that when standard forms are offered on a take-it-or-leave-it basis, "there remains little of the element of liberty to contract as one chooses, which is the essence of the public policy of freedom of contract."<sup>188</sup> The court argued that "this fragment of a liberty" must not trump the state's policy that people should be liable for harm they inflict through the negligent performance of their duties.

Soon thereafter, courts began to create rules explicitly governing form contracts. The two most influential cases were *Henningsen v. Bloomfield Motors*<sup>189</sup> and *Williams v. Walker-Thomas Furniture Co.*<sup>190</sup>

In *Henningsen*, the New Jersey Supreme Court refused to enforce a form term severely limiting the warranty protection for a new automobile.<sup>191</sup> Critics of this case point to the court's reliance on the fact that there were only a few car manufacturers and that they all

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184. 221 F.2d 189 (2d Cir. 1955).

185. *Id.* at 205 (Frank, J., dissenting). He noted, "The one party dictates its provisions; the other has no more choice in fixing those terms than he has about the weather." *Id.* at 204.

186. *Id.* at 204.

187. The Illinois Supreme Court upheld such a clause in *O'Callaghan v. Waller & Beckwith Realty Co.*, 155 N.E.2d 545 (Ill. 1958).

188. *Simmons v. Columbus Venetian Stevens Bldg.*, 155 N.E.2d 372 (Ill. App. Ct. 1958).

189. 161 A.2d 69 (N.J. 1960).

190. 350 F.2d 445 (D.C. Cir. 1965).

191. The warranty clause, in fine print on the back of contract, limited warranty protection to the first ninety days or 4000 miles, whichever came first, and required that the consumer prepay shipping charges for transporting the defective automobile to the manufacturer. *Henningsen*, 161 A.2d at 74. The clause concluded that "this warranty being expressly in lieu of all other warranties expressed or implied, and all other obligations or liabilities on its part." *Id.*

used the same disclaimer.<sup>192</sup> The real lesson of *Henningsen* has been its recognition that the paradigm of free bargaining is absent from consumer form contracts. The dealer presented the contract to the Henningsens "without authority to alter it; his function is ministerial—simply to deliver it."<sup>193</sup> The fine print on the back of the contract "was such as to promote lack of attention rather than sharp scrutiny" and even if a consumer saw the language, the ordinary layperson would not "realize what he was relinquishing in return for what he was being granted."<sup>194</sup> Accordingly, the general principle that those who do not read contracts cannot escape from unknown terms has "prove[n] to be inadequate under the impact of later experience."<sup>195</sup> The unilaterally imposed contract terms "resemble a law rather than a meeting of the minds."<sup>196</sup> Thus, based on "public policy," the Henningsens recovered for the damage caused by the defective automobile, despite the contract's disclaimer.<sup>197</sup>

The *Williams* court used the doctrine of unconscionability to justify its refusal to enforce a densely written "add-on" clause, which allowed the seller to repossess every item previously sold to a consumer in the event of a single default.<sup>198</sup> This case has also been subject to criticism, especially for its discussion of the particular consumer's lack of education and status as a welfare recipient.<sup>199</sup> Nonetheless, *Williams* is important for any understanding of form contracts, because it stands on the fact that the consumer not only was unaware of the add-on clause, but that the seller knew of this unawareness. The court concluded that when a consumer signs such a "commercially unreasonable" contract, "with little or no knowledge of its terms," it cannot be said "that his consent, *or even an objective*

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192. The court limited its holding due to the "unique" status of the 1960 American automobile industry, where oligopolistic conspiracies prevented effective bargaining:

The status of the automobile industry is unique. Manufacturers are few in number and strong in bargaining position. In the matter of warranties on the sale of their products [they] present a united front. From the standpoint of the purchaser, there can be no arms length negotiating on the subject.

*Id.* at 94. But courts rely on the case when form contracts are used, even in the absence of oligopolistic conditions. See, e.g., *Higel v. General Motors Corp.*, 544 P.2d 983, 989-90 (Colo. 1976) (discussing *Henningsen* as applying to disclaimers of warranties in a "consumer sale.").

193. *Henningsen*, 161 A.2d at 87.

194. *Id.* at 92.

195. *Id.* at 84.

196. *Id.* at 86.

197. *Id.* at 94-95.

198. The clause stated that "all payments now and hereafter made by [purchaser] shall be credited pro rata on all outstanding leases, bills and accounts due the Company by [purchaser] at the time each such purchase is made." *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445, 447 (D.C. Cir. 1965). The court accurately termed this a "rather obscure provision." *Id.*

199. *Id.* at 448-49.

*manifestation of his consent*, was ever given to all the terms.”<sup>200</sup> Thus, the reasonable merchant cannot assume assent to an unknown, unreasonable term and cannot demand its enforcement.

Since these early attempts to solve the form contract dilemma, courts throughout the country have begun to interpret form contracts based on the reasonable understanding of the consumer rather than on the actual terms known only to the drafter. While courts use a wide range of formulations to reach their conclusions, their common ground is a realistic application of the objective theory of contracts.

### VIII. THE OBJECTIVE THEORY OF CONSUMER FORM CONTRACTS

The typical consumer neither reads nor comprehends the terms of a form contract.<sup>201</sup> More significantly, because drafters know that consumers are unaware of the terms of the contract they cannot reasonably believe that consumers have agreed to the unknown terms. What, then, should a reasonable drafter believe consumers are thinking when they sign the contract?

As a general rule, consumers should only be bound by those contract terms that they know and comprehend.<sup>202</sup> The central or dickered terms of a contract properly bind the consumer because the consumer is obviously aware of them.<sup>203</sup>

Similarly, when a consumer reads and comprehends subordinate terms or when the seller points out and explains a complex term, the seller should be able to treat the consumer's assent as an assent to the discussed term.<sup>204</sup> Absent policy reasons to the contrary, such as a

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200. *Id.* at 449 (emphasis added).

201. See *supra* text accompanying notes 28-29.

202. All contract provisions, however, are subject to unconscionability analysis. See *supra* text accompanying notes 129-32.

203. See, e.g., LLEWELLYN, *supra* note 84, at 370.

204. See *Meyers v. Guarantee Sav. & Loan Ass'n*, 144 Cal. Rptr. 616, 620 (Cal. Ct. App. 1978) (stating that because borrower “admitted to having read and understood the contract, his subjective expectations were not objectively reasonable”). Professor Keeton has argued to the contrary. “If the enforcement of a policy provision would defeat the reasonable expectations of the great majority of policyholders to whose claim it is relevant, it will not be enforced even against those who know of its restrictive terms.” ROBERT E. KEETON, *INSURANCE LAW: BASIC TEXT* § 6.3(b), at 358 (1971). He reasoned that a policyholder who takes the time to read and understand the policy should not be penalized for doing so. *Id.* Keeton's argument flies in the face of the objective theory of contracts. A consumer who knows of and understands a term and then assents to a contract can reasonably be held to have agreed to that term by not objecting to it. This rule does not put a premium on ignorance. See *Weaver v. American Oil Co.*, 276 N.E.2d 144, 155 (Ind. 1971) (Prentice, J., dissenting). First, since very few consumers read their contracts, the number of consumers affected is minuscule. Second, the contract drafter, by pointing out unusual terms, can avoid the consumer's ignorance as well as the drafter's advantage therefrom.

merchant's promise not to enforce a term, unconscionably onerous terms,<sup>205</sup> or inherently coercive situations,<sup>206</sup> knowledgeable consumers should be held to their agreements.

The degree of disclosure required of the seller is that which enables a reasonable consumer to understand both the meaning and effect of a term. One court stated that obtaining the consumer's knowing assent "could easily have been done in this case by explaining to plaintiff in laymen's terms the meaning and possible consequences of the disputed clause."<sup>207</sup> Even if an individual consumer does not understand the clause, the drafter can reasonably rely on an objectively adequate disclosure.

In cases where a consumer does not know or understand the terms of a form contract, courts must examine the circumstances surrounding the transaction to determine the consumer's objective understanding. Because the consumer is clearly acquiring *something*, courts can look to the "purpose" for the acquisition: Why would one likely make such a purchase? Consumers share a basic understanding of what is to be expected from a particular product or service. For example, if a consumer calls and orders a pizza to be delivered and the store sends over a piece of cooked dough covered with pineapple rather than tomato or cheese, the consumer may rightfully reject the delivery.

Next, courts should determine whether the business seller or service provider had reason to assume that the item or service being

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205. See *supra* text accompanying note 132.

206. Examples of coercive situations include a doctor's waiting room just prior to surgery, see *infra* text accompanying note 319, or a monopolistic environment, see, e.g., *Henningsen v. Bloomfield Motors*, 161 A.2d 69, 94 (N.J. 1960). It has been argued that notice will not assist consumers who are not free to bargain. See *Mueller, supra* note 4, at 581. Outside of coercive situations, a consumer with understanding and knowledge can indeed leave a take-it-or-leave-it proposition. For example, if a consumer tells a film processor that she greatly values a roll of film and is told that the store does not guarantee its work, if the film is later lost or ruined, the developer should not be responsible for damages beyond replacement of the film. A consumer who proceeds to make a contract on such terms should be held to assume the risk of loss. Cf. *Mieske v. Bartell Drug Co.*, 593 P.2d 1308 (Wash. 1979) (no clear notice given). For a discussion of *Mieske*, see *infra* text accompanying notes 268-71. However, merchants must not be permitted to entice a consumer into a deal and then spring an unfair term on the consumer at the last minute when backing out of the contract would be impractical, expensive, or difficult. The test should be whether a reasonable person in the drafter's position would understand that voluntary assent had been given.

207. *Johnson v. Mobil Oil Corp.*, 415 F. Supp. 264, 269 (E.D. Mich. 1976); see also *Wheeler v. St. Joseph Hosp.*, 133 Cal. Rptr. 775, 786 (Cal. Ct. App. 1976) ("The hospital's admission clerk need only direct the patient's attention to the arbitration provision, request him to read it, and give him a simple explanation of its purpose and effect, including the available options."). This standard is similar to that for informed consent to medical procedures, which requires "a reasonable effort to convey sufficient information . . ." *Canterbury v. Spence*, 464 F.2d 772, 780 n.15 (D.C. Cir. 1972).

acquired was not expected to perform to industry standards.<sup>208</sup> Absent solid evidence to the contrary, courts should find that the reasonable consumer does not intend to waste money by paying "market price" for unmarketable goods or services. If you hire someone to mow your lawn, you expect the work done to be of "reasonable quality."

Courts also need to expect that the consumer is likely to have spoken with a salesperson or agent and may well have seen advertisements for the product or service. Statements made by both seller and consumer contribute to the average customer's understanding of contractual rights and remedies.

Other important considerations, however, are usually totally absent from a consumer's contemplation at the time of contracting. For example, consumers rarely consider even the possibility of a subsequent legal action. Courts and sellers should realize that consumers do not knowingly assent to terms that effectively discard their legal rights.

Such considerations do not interfere with true freedom of contract. Merchants remain free to create the bargain they desire as long as the consumer knowingly assents. The affirmative duty placed on the seller to inform consumers of unexpected terms creates a contracting situation far closer to the paradigm of the classic "bargaining table" than any anachronistic duty-to-read rule. As one court observed:

Such a requirement does not detract from the freedom to contract, unless that phrase denotes the freedom to impose the onerous terms of one's carefully-drawn printed document on an unsuspecting contractual partner. Rather, freedom to contract is enhanced by a requirement that both parties be aware of the burdens they are assuming.<sup>209</sup>

Only through a realistic application of the objective theory to form contracts can both sellers and consumers exercise the free will essential to the freedom of contract. A growing number of courts recognize this principle. Some courts utilize the "doctrine of reasonable expectations,"<sup>210</sup> while others discuss "contracts of adhesion"<sup>211</sup> or "unconscionability."<sup>212</sup> Another group unfortunately resorts to

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208. See Prosser, *supra* note 67, at 160.

209. *Johnson*, 415 F. Supp. at 269.

210. See *Ware*, *supra* note 3, at 1467. See also *Puritan Life Ins. Co. v. Guess*, 598 P.2d 900, 904 (Alaska 1979).

211. *Graham v. Scissor-Tail, Inc.*, 623 P.2d 165, 176 (Cal. 1981).

212. See, e.g., *Collins v. Uniroyal, Inc.*, 315 A.2d 16, 18 (N.J. 1974).



judicial subterfuge,<sup>213</sup> which so offended Llewellyn, to reach the same result. Nevertheless, a review of how these courts enforce the objective understanding of the parties, rather than mechanically applying the literal written language, brings the modern practice into sharper focus.

### A. *The Purpose of the Contract*

Every contract has a purpose. Under contract law, the undisclosed subjective purpose of the parties is irrelevant. Instead, courts are concerned with "objective" purpose. Where there is a "common" or "obvious" reason for the transaction, courts rarely permit unknown contract terms to defeat that purpose.

Consider the case of a consumer renting an automobile who paid extra for a "physical damage waiver" (PDW) or a "collision damage waiver" (CDW), whereby the rental car company agreed to waive all claims against the renter for damage to the car.<sup>214</sup> The car was subsequently damaged in an accident, and the renter was issued a traffic citation. The rental company argued that the renter was liable because he had violated a contract clause prohibiting the use of the car "in violation of any laws or ordinances applicable to the operation . . . of the vehicle."<sup>215</sup> Because the unread clause would defeat the obvious purpose behind the purchase of the PDW, the court rejected this contention, stating:

Clearly, consumers . . . elect PDW coverage with the reasonable expectation that if they are involved in an automobile accident, they are protected from damage liability, regardless of fault. To permit the insertion of technical language in a standard form contract that would nullify PDW coverage whenever the operator's simple negligence results in a traffic violation defeats the purpose of purchasing such coverage.<sup>216</sup>

Similarly, the Vermont Supreme Court refused to enforce unambiguous contractual language eliminating collision damage waiver protection for *inter alia* falling asleep at the wheel.<sup>217</sup> The court rea-

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213. See *Grossman Furniture Co. v. Pierre*, 291 A.2d 858, 863 (N.J. Dist. Ct. 1972) (equitable fraud); *Brakeman v. Potomac Ins. Co.*, 371 A.2d 193 (Pa. 1977) (forfeiture); *Elliot Leases Cars, Inc. v. Quigley*, 373 A.2d 810, 813 (R.I. 1977) (finding ambiguity in a contract containing "an admittedly unequivocal provision"); *Smith v. The Peoples Bank of Elk Valley*, No. 01A01-9111-CV-00421, 1992 Tenn. App. LEXIS 477, at \*10 (Tenn. Ct. App. June 3, 1992) (public interest); *Exxon Corp. v. Brecheen*, 526 S.W.2d 519, 525 (Tex. 1975) (public policy).

214. *Syme v. Marks Rentals, Inc.*, 520 A.2d 1110 (Md. Ct. Spec. App. 1987).

215. *Id.* at 1114.

216. *Id.*

217. *Val Preda Leasing, Inc. v. Rodriguez*, 540 A.2d 648 (Vt. 1987). One of 16 exceptions

soned that while "[t]he contract appears to absolve the renter of liability for damage to the car if the renter purchases the CDW . . . [t]he exceptions swallow the protection."<sup>218</sup> The court stated, "It is only after reading and digesting those sections that the reader would realize the full import of the limitations on the rental company's waiver."<sup>219</sup> Because the unread exception contradicted the very concept of the CDW, the court refused to enforce the exception and thereby defeat the purpose of the contract.<sup>220</sup>

Protecting the purpose of the contract frequently requires striking unknown disclaimers of implied warranties.<sup>221</sup> When someone purchases a new machine designed to make concrete blocks, for example, absent contrary discussion, the objective understanding is that the machine will successfully make concrete blocks.<sup>222</sup> In *Myers v. Land*,<sup>223</sup> the Kentucky Supreme Court refused to uphold contractual language that denied the existence of implied warranties in the sale of such a machine. The court noted:

Though the present disclaimer of warranty is clear in its terms, we cannot overlook the fact that it is to be found in a long and formi-

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to the CWP listed on the back page, the provision provided that the "[v]ehicle shall not be used or operated by any person . . . who is not sufficiently alert or capable or properly or safely driving vehicle." *Id.*

218. *Id.* at 650, 652.

219. *Id.* at 650.

220. *Id.* at 652. The Supreme Court of Nevada likewise refused to deprive a driver of liability protection after the driver made an improper left turn which resulted in an accident, arguing that such an interpretation would "read a very material limitation into the waiver agreement." *Automobile Leasing & Rental, Inc. v. Thomas*, 679 P.2d 1269 (Nev. 1984). The court reasoned that "[t]he ordinary reader would not assume that an unqualified promise of this nature only covered accidents not caused by the negligence of the operator of the automobile. Indeed just the opposite is true. [A collision waiver] is generally understood to cover whatever accidents occur, regardless of the negligence of the operator." *Id.* at 1271 (quoting *Elliott Leases Cars, Inc. v. Quigley*, 373 A.2d 810, 812 (R.I. 1977) (limiting scope of collision insurance restriction)). *Accord* *Davis v. M.L.G. Corp.*, 712 P.2d 985 (Colo. 1986); *Lauvetz v. Alaska Sales and Serv.*, 828 P.2d 162 (Alaska 1991).

221. *See, e.g.*, *A & M Produce Co. v. FMC Corp.*, 186 Cal. Rptr. 114, 125 (Cal. Ct. App. 1982) ("Since a product's performance forms the fundamental basis for a sales contract, it is patently unreasonable to assume that a buyer would purchase a standardized mass-produced product from an industry seller without any enforceable performance standards."); *Steele v. J.I. Case Co.*, 419 P.2d 902, 903 (Kan. 1966) (striking limit on warranty liability for sale of farm equipment where seller knew "the urgency of harvest" and the limitation was never "called to the buyer's attention"); *Berg v. Stromme*, 484 P.2d 380, 385 (Wash. 1971) ("The purported disclaimers of warranty . . . highlight the absurdity of a rule of law which elevates these bland and substantially meaningless terms and conditions above the individually and expressly negotiated terms and conditions . . ."). Of course, a buyer is always free to purchase knowingly an item without a warranty. *See* *Klein v. Asgrow Seed Co.*, 54 Cal. Rptr. 609, 617 (Cal. Ct. App. 1966) ("When two parties bargain on an equal basis and the buyer is willing to buy a pig in a poke there is no policy of the law to prevent such a transaction.").

222. *Myers v. Land*, 235 S.W.2d 988 (Ky. 1950).

223. *Id.*

dable document prepared by the seller and that it was doubtless unnoticed or its import uncomprehended by the buyer. *Anyone brought up to believe that for every wrong there is a remedy will pause before saying that the seller will escape all liability by merely putting in an order blank a statement to the effect that there is no assurance that the buyer will get a machine that will work.* We have paused for the moment and have readily concluded that the avoidance of liability under such a circumstance is not permitted by the law.<sup>224</sup>

Numerous insurance cases hold that because the insured is attempting to purchase protection against a particular contingency undisclosed terms should not be permitted to defeat this expectation.<sup>225</sup> In *Puritan Life Insurance Co. v. Guess*,<sup>226</sup> a consumer entered into a contract for life insurance after paying a \$100 premium and getting a receipt.<sup>227</sup> The consumer was unaware that this was a so-called "conditional receipt," which provided coverage only after a medical examination. The Alaska Supreme Court held that insureds who pay a premium reasonably expect coverage for their money. The court therefore refused to enforce the "conditional receipt" language because it would have defeated the logical purpose of the payment. The court placed the burden of showing adequate disclosure on the insurer, stating:

[W]e require that the insurer's agent, who negotiates the application, personally draw to the attention of the applicant any limiting condition. The insurer has the burden of showing that it had taken appropriate steps to inform the applicant for insurance of such conditions, and that the applicant, therefore, could not have had a reasonable expectation that he was immediately protected.<sup>228</sup>

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224. *Id.* (emphasis added). See also *Martin v. Harris Joseph Co.*, 767 F.2d 296 (6th Cir. 1985) (refusing to enforce disclaimer of warranty on seeds sold to farmer); *Chandler v. Aero Mayflower Transit Co.*, 374 F.2d 129, 137 (4th Cir. 1967) (refusing to enforce written limit on moving company's liability "unless the shipper had been given reasonable notice by the carrier that he actually had a choice of 'higher or lower liability by paying a correspondingly greater or lesser charge.'") (citations omitted); *Mallory v. Conida Warehouses, Inc.*, 350 N.W.2d 825, 828 (Mich. Ct. App. 1984) (same); *Testo v. Russ Dunmire Oldsmobile, Inc.*, 554 P.2d 349 (Wash. Ct. App. 1976) (striking warranty disclaimer for used car); *Klein*, 54 Cal. Rptr. at 615-17 (same).

225. See, e.g., *Federal Ins. Co. v. Century Fed. Sav. & Loan Ass'n*, 824 P.2d 302, 306 (N.M. 1992) (holding that "a policy provision excluding liability should be disregarded or stricken because it is repugnant to—i.e., contradicts—a provision extending coverage to certain losses").

226. 598 P.2d 900, 902 (Alaska 1979).

227. *Id.* at 902.

228. *Id.* at 906; see also *Collister v. Nationwide Life Ins. Co.*, 388 A.2d 1346, 1352 (Pa. 1978) (stating that "if nothing is said about the complicated and legalistic phrasing of the receipt, and the agent accepts an application for insurance together with the first premium

Similarly, those purchasing theft burglary insurance reasonably expect coverage against "a bona fide third party burglary,"<sup>229</sup> and those purchasing life insurance reasonably expect coverage against unintentional death,<sup>230</sup> and a couple purchasing automobile insurance together reasonably expects to be insured regardless of which spouse is driving.<sup>231</sup> In the automobile insurance case, the court added:

The possibility remains that these limitations were called to [the husband's] or [the wife's] attention, that [the husband] and not [the wife] was the named insured for a specific reason, such as the request of either, or that for some other reason the transaction was accomplished in accordance with the understandings or wishes of the parties. If [the insurance company] can prove this, we will enforce the limitation of coverage against [the wife].<sup>232</sup>

Of course, looking to the purpose of a transaction can also work in favor of the seller.<sup>233</sup> In *Estrin Construction Co. v. Aetna Casualty & Surety Co.*,<sup>234</sup> a contractor purchased general liability insurance for a construction project. When a wall collapsed, the contractor attempted to recover under the policy for its own losses.<sup>235</sup> The insurance company refused to pay, citing a clause that excluded payments for property damaged while in the "care, custody or control" of the contractor.<sup>236</sup> The court ruled for the insurance company, stating that "[t]he dominant purpose of such a standard liability insurance policy . . . is to insure against liability to *others*, not to oneself. The exception, therefore, subserves the dominant purpose of the transaction, rather than avoids that purpose."<sup>237</sup>

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payment, the applicant has reason to believe that he is insured. Otherwise, he is deceived.") (quoting *Toevs v. Western Farm Bureau Life Ins. Co.*, 483 P.2d 682, 685 (Idaho 1971)).

229. *C & J. Fertilizer, Inc. v. Allied Mut. Ins. Co.*, 227 N.W.2d 169, 177 (Iowa 1975). *See also Mills v. Agrichemical Aviation, Inc.*, 250 N.W.2d 663, 668 (N.D. 1977) ("It is not unreasonable for a buyer to have a reasonable expectation that when he buys and pays for 'farm liability' insurance, it will cover liability arising out of any of his normal farming operation, unless excluded operations are called to his attention.").

230. *See, e.g., Jones v. Crown Life Ins. Co.*, 150 Cal. Rptr. 375 (Cal. Ct. App. 1978). *See generally Silverstein v. Metropolitan Life Ins. Co.*, 171 N.E. 914, 915 (N.Y. 1930) ("A policy of insurance is not accepted with the thought that its coverage is to be restricted to an Apollo or a Hercules.").

231. *Gordinier v. Aetna Casualty & Sur. Co.*, 742 P.2d 277, 281 (Ariz. 1987).

232. *Id.* at 285.

233. *See, e.g., Home Fed. Sav. & Loan Ass'n v. Campney*, 357 N.W.2d 613, 621 (Iowa 1984) (holding that a due-on-sale clause in a home mortgage did not contradict the dominant purposes of the transaction—either purchasing a house or permitting the buyers to sell the property later at a profit).

234. 612 S.W.2d 413 (Mo. Ct. App. 1981).

235. *Id.* at 415.

236. *Id.*

237. *Id.* *See also Continental Ins. Co. v. Bussel*, 498 P.2d 706 (Alaska 1972). In *Bussel*, a liability insurance policy was held not to include death benefits owed by an employer to

The goal of the objective theory of form contracts is not to reward the consumer,<sup>238</sup> but to effectuate the reasonable understanding of the contracting parties. Unread and undisclosed form terms should not defeat the purpose of a contract. Courts, accordingly, should read restrictive terms in the context of the overall purpose of the contract. Where the restrictive term effectively defeats the essential purpose of the contract, the restrictive term must give way.

### B. *The Purpose of the Clause*

Just as every contract has a purpose, so does every clause. Although clauses may have multiple or even different purposes for each party, there should always be an answer to the question "Why is this clause in the contract?" The focus of this inquiry will often be to determine what contingency the clause was intended to cover or what risk was sought to be avoided.

Even a clause with a valid purpose may be illegitimate if its reach exceeds its purpose. If two parties with equal knowledge hammer out a deal, negotiations will tend to lead to clauses that serve intended purposes without unreasonably harming either party.<sup>239</sup> In a non-negotiated form contract, there is no such check on overbroad provisions far exceeding legitimate purposes. Sellers should realize that consumers signing form contracts implicitly assume that the contract terms serve legitimate purposes without causing unnecessary harm. Courts should therefore enforce obscure or hidden form terms only to the extent that the terms serve legitimate interests.<sup>240</sup>

For example, courts permit a form contract clause to reduce the statutory time for filing causes of action because legitimate interests are at stake. The shortening of a statute of limitations can help insurance companies protect against fraudulent claims that cannot be refuted due to lost witnesses, misplaced evidence, and faded memories.<sup>241</sup> Such a clause, though, should only block a valid claim when it

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employees: "The policy itself is entitled, 'Liability Insurance Policy' as contrasted with the title of a life insurance policy." *Id.* at 710.

238. Proponents of the classical duty-to-read school often try to discredit those arguing for the objective theory by charging that their true goal is mindless one-sided boosterism for consumers and against business. *See, e.g.,* Ware, *supra* note 3, at 1466 ("Advocates saw in the reasonable expectations doctrine a unifying principle that would resolve more cases in favor of the insured and would do so in an open and principled manner.").

239. Confidence that negotiations will produce rational contract terms is highest in the idealized, perfectly competitive market. *See* Eisenberg, *supra* note 135, at 746-48.

240. As long ago as 1884, the Pennsylvania Supreme Court declared that "where the reason of a [contract] condition does not apply this court has refused to apply it." *Grandin v. Rochester German Ins. Co.*, 107 Pa. 26, 37 (1884).

241. *Zuckerman v. Transamerica Ins. Co.*, 650 P.2d 441, 445 (Ariz. 1982).

serves its valid purposes. The Arizona Supreme Court has held that a clause limiting the time for the filing of a cause of action is enforceable only if "the insurer has shown prejudice by reason of the delay in filing suit."<sup>242</sup> The court reasoned that:

The provision is not one which is bargained for and its application in the face of an otherwise valid claim defeats the reasonable coverage expectations of the insured; in the absence of prejudice to the insurer, caused by the late filing of suit, enforcement leads to an effectual forfeiture of the claim, thus creating an inequitable result.

. . . Where the conditions do no more than provide a trap for the unwary, the insurer will be estopped to raise them. We thereby grant the consumer his reasonable expectation that coverage will not be defeated by the existence of provisions which were not negotiated and in the ordinary case are unknown to the insured . . . . *The clause will be enforced when the reasons for its existence are thereby served and will not be applied when to do so would be to defeat the basic intent of the parties in entering into the insurance transaction.*<sup>243</sup>

The California Supreme Court reasoned similarly when it examined a bank's six dollar charge for processing checks drawn on commercial accounts without sufficient funds to cover the checks (NSF checks).<sup>244</sup> The depositor argued the fee was unconscionable because it was twenty times greater than the actual thirty cent cost to the bank for processing NSF checks.<sup>245</sup> The court held that in order to determine the enforceability of the fee "inquiry into its basis or justification is necessary."<sup>246</sup>

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242. *Id.* at 443, 448; *accord* *Brakeman v. Potomac Ins. Co.*, 371 A.2d 193, 197 (Pa. 1977); *see also* *Jones v. Bituminous Casualty Corp.*, 821 S.W.2d 798, 801 (Ky. 1991) (holding that an insurer cannot withdraw coverage on the ground that a provision requiring prompt notification of an accident was not met, unless the insurer can show that it was prejudiced).

243. *Zuckerman*, 650 P.2d at 447-48 (emphasis added); *accord* *Burne v. Franklin Life Ins. Co.*, 301 A.2d 799, 803 (Pa. 1973) (holding that condition in life insurance policy limiting recovery to deaths occurring within 90 days from date of an accident was inapplicable where there was no dispute over cause of death); *see also* *Jones v. Mountain States Tel. & Tel. Co.*, 670 P.2d 1305, 1312 (Idaho Ct. App. 1983) (construing insurance policy provision requiring an accident to be the "sole cause" of an injury as meaning the "dominant cause" of the injury); *Smith v. Municipal Mut. Ins. Co.*, 289 S.E.2d 669, 671-72 (W. Va. 1982) (construing insurance contract provision stating that mailing is adequate notice, as requiring actual notice).

244. *Perdue v. Crocker Nat'l Bank*, 702 P.2d 503 (Cal. 1985).

245. *Id.* at 512.

246. *Id.* at 513. The court noted that "the bank charges the same fee whether it honors or rejects an NSF check. The fee, consequently, cannot be intended as compensation for the credit risk arising from paying such a check, or for the interest on the amount loaned." The court remanded the case so that the parties could present evidence on "the commercial setting, purpose, and effect" of the NSF charge. *Id.* at 514. *See generally* *Capital Associates, Inc. v. Hudgens*, 455 So. 2d 651, 653-54 (Fla. 4th DCA 1984) (striking as unconscionable an acceleration clause permitting jukebox lessor to recover \$12,000 in unaccrued rent for

In *C & J. Fertilizer, Inc. v. Allied Mutual Insurance Co.*,<sup>247</sup> the insured assumed he was covered when his warehouse was robbed. There were tire treads showing where the burglars used a truck to haul away goods. The insurance policy, though, provided coverage only if there were "visible marks made by tools, explosives, electricity or chemicals upon, or physical damage to, the *exterior* of the premises."<sup>248</sup> The insurance company denied recovery because the only damage was to an *interior* door.<sup>249</sup> The Iowa Supreme Court held that the purpose of the policy limitation was a "requirement of visual evidence (abundant here) indicating the burglary was an 'outside' not an 'inside' job."<sup>250</sup> Because the evidence indicated an "outside" job, there was no legitimate reason strictly to enforce the provision against the insured.

This analysis does not mean that the consumer always wins. If a form clause is appropriately tailored to fulfill its purpose, it should, and will, be enforced. For example, the Educational Testing Service (ETS) reserves, in its contract with those taking the Law School Admission Test, the unilateral right to cancel a test-taker's score upon suspicion of cheating.<sup>251</sup> This was upheld because ETS's ability to cancel a score it reasonably believed did not reflect a candidate's aptitude for law school increased the test's predictive ability and thus served the legitimate interests of ETS, law schools, and the public in general.<sup>252</sup> This was not viewed as an unfair, unbalanced clause. Because ETS offered the applicant the right to take a free retest with a commitment that, if the retest score was close, the original score would be reinstated, the form term was "eminently fair and reasonable under the circumstances."<sup>253</sup>

Restricting the reach of overbroad terms in form contracts more accurately reflects the objective understanding of the consumer. Moreover, such restriction serves as an effective proxy for the face-to-face negotiation envisioned by traditional contract law.

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equipment resold for \$1,000); *Spring Valley Gardens Assoc. v. Earle*, 447 N.Y.S.2d 629, 631 (Rockland County Ct. 1982) (striking \$50 late fee for ten-day delay in paying \$405 monthly residential rent).

247. 227 N.W.2d 169 (Iowa 1975).

248. *Id.* at 171 (emphasis added).

249. *Id.*

250. *Id.* at 177.

251. *K.D. v. Educational Testing Serv.*, 386 N.Y.S.2d 747 (S. Ct. N.Y. County 1976). The provision was in a booklet presented to all LSAT takers and read, "We reserve the right to cancel any test score if, in our sole opinion, there is adequate reason to question the validity. Before exercising this right, we will offer you an opportunity to take the test again at no additional fee." *Id.* at 749.

252. *Id.* at 752.

253. *Id.*

### C. *The Information Exchanged*

Even in a form contract situation there is often communication between the parties. Statements are made by the seller, the seller's agent, or the consumer. Additionally, important information is often conveyed to consumers through mass advertising. This exchange of information contributes to the consumer's objective understanding of the contract.<sup>254</sup>

In *Computerized Radiological Services, Inc. v. Syntex Corp.*,<sup>255</sup> a group of radiologists purchased a CAT scanner.<sup>256</sup> In order to close the deal, the seller promised that, although the current scanner only screened heads and took 60 seconds to scan, the capability to screen the entire body in 30 seconds would be available "shortly."<sup>257</sup> Although these improvements were not forthcoming, the seller argued there was no breach of warranty because the one-year warranty against defects provided for in the contract was "expressly in lieu of all other obligations or liabilities."<sup>258</sup> The judge held that the express warranty promised by the seller survived the disclaimer. The court stated that "[t]o agree with defendant that its boiler plate language . . . bars proof of express warranties made before plaintiff signed that form, would be to reweave the fabric of the agreement to suit defendant's own ends."<sup>259</sup>

Statements by insurance agents also contribute to the insured's understanding of the fabric of the agreement. In *Harr v. Allstate Insurance Co.*,<sup>260</sup> an applicant for homeowner's and fire insurance

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254. For example, one court held that in-state students at the University of New Hampshire who received letters informing them of the possibility of mid-semester tuition increases were bound by a contract term giving the University the right to increase tuition at any time, while out-of-state students who did not receive the mailing were not so bound: "Absent notice by the University of the potential increase, a reasonable student would not have anticipated additional charges for tuition to occur mid-semester." *Gamble v. University Sys. of N.H.*, 610 A.2d 357, 362 (N.H. 1992).

255. 595 F. Supp. 1495 (E.D.N.Y. 1984).

256. The cost of the CAT (Computerized Axial Tomography) Scanner was \$347,000. *Id.* at 1500.

257. *Id.* at 1501, 1506.

258. *Id.* at 1506.

259. *Id.* at 1507; see also U.C.C. § 2-313, cmt. 1 (1990) (stating that express warranties "rest on 'dickered' aspects of the individual bargain, and go so clearly to the essence of that bargain that words of disclaimer in a form are repugnant to the basis of dickered terms."); *Miller v. Troy Laundry Mach. Co.*, 62 P.2d 975, 977 (Okla. 1936) (stating that when an express oral warranty is contradicted by a written disclaimer, the buyer "may relabel his action as one in fraud and thus escape the parol evidence rule."); *Grossman Furniture Co. v. Pierre*, 291 A.2d 858, 863 (N.J. Essex County Ct. 1972) ("Where a party permits another to sign a contract knowing that he is under a misapprehension as to its terms, there is equitable fraud which warrants reformation or rescission.").

260. 255 A.2d 208 (N.J. 1969).



sought to include his business merchandise on his policy. Before leaving on a trip, he telephoned his insurance agent and requested coverage for the merchandise. The agent replied, "Mr. Harr, we can cover you for \$7500 and you are *fully covered*. Go to Florida . . . and have a good time."<sup>261</sup> While Mr. Harr was in Florida, disaster struck. Even though the merchandise was damaged by water from bursting pipes, which the language of the policy unambiguously excluded from coverage, the court ruled that the agent's statements were part of the contract:

[W]here an insurer or its agent misrepresents, even though innocently, the coverage of an insurance contract or the exclusions therefrom, to an insured before or at the inception of the contract, and the insured reasonably relies thereon to his ultimate detriment, the insurer is estopped to deny coverage after a loss on a risk or from a peril actually not covered by the terms of the policy. This proposition is one of elementary and simple justice. By justifiably relying on the insurer's superior knowledge, the insured has been prevented from procuring the desired coverage elsewhere. To reject this approach . . . would be an unfortunate triumph of form over substance.<sup>262</sup>

The court recognized that this rule will impose new and possibly unintended risks on the insurer. Nonetheless, that too was equitable because:

If the insurer is saddled with coverage it may not have intended or desired, it is of its own making, because of its responsibility for the acts and representations of its employees and agents. *It alone has the capacity to guard against such a result by the proper selection, training and supervision of its representatives.*<sup>263</sup>

Similarly, a seller has the capacity to guard against misrepresentations in its advertisements that raise consumer expectations. In *Collins v. Uniroyal*,<sup>264</sup> tire advertisements provided a guarantee against blowouts stating, "[i]f it only saves your life once, it's a bargain."<sup>265</sup>

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261. *Id.* at 212.

262. *Id.* at 219; *see also* *Brown v. Glens Falls Ins. Co.*, 818 S.W.2d 1, 13 (Tenn. 1991) ("Technical distinctions, created by the insurer within its field of expertise and exclusive control, should not dictate the fortunes of innocent insureds who reasonably rely upon the misrepresentations of agents of the insurer.").

263. *Harr*, 255 A.2d at 219 (emphasis added); *see also* *Brown*, 818 S.W.2d at 13 ("[T]he insurer is in a better position to minimize the frequency of occasions in which the reasonable expectations of an insured are not supported by the policy language. By training its agents in the language of its policies, and by simplifying the policy language itself, the insurer can reduce the frequency of misrepresentations and increase the difficulty of proving reasonable reliance."); *Peninsular Life Ins. Co. v. Wade*, 425 So. 2d 1181, 1183-84 (Fla. 2d DCA 1983).

264. 315 A.2d 16 (N.J. 1974).

265. *Id.* at 18.

The estate of a purchaser, who was killed in an accident caused by a blowout, was permitted to sue for damages despite a contract clause limiting damages to replacement of the tire.

The court stressed that the tire manufacturer's advertised statements created an objective understanding that the manufacturer was assuming a far higher responsibility than normal:

The seller should be held to realize that the purchaser of a tire buying it because so warranted is far more likely to have made his purchase decision in order to protect himself and the passengers in his car from death or personal injury in a blowout accident than to assure himself of a refund of the price of the tire in such an event. *That being the natural reliance and reasonable expectation of the purchaser flowing from the warranty*, it appears to us patently unconscionable for the manufacturer to be permitted to limit his damages . . . .<sup>266</sup>

Statements made by the consumer prior to contracting are also relevant to the objective interpretation of form contracts because they contribute to the seller's understanding of the consumer's knowledge and purpose. Under the objective theory of form contracts, when a consumer's statements indicate a particular belief, the seller's silence can be viewed as acquiescence, regardless of written contractual language to the contrary.

Cases involving film processors' disclaimers of liability are an example of this principle. Film processors generally limit their liability because "no film processor would expose itself to liability for the unknown content of film without having to so greatly increase the cost to the public as to price the service out of the market."<sup>267</sup> A Florida court upheld these limitations, but stressed that the consumer actually read and understood this clause.

In contrast, the Washington Supreme Court refused to uphold a similar disclaimer of liability in *Mieske v. Bartel Drug Co.*<sup>268</sup> A consumer brought in thirty-two movie reels, covering many years of family life, for splicing. She was given a receipt stating, "We assume no responsibility beyond retail cost of film unless otherwise agreed to in writing."<sup>269</sup> Although unaware of the clause, she said to the store

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266. *Id.* (emphasis added).

267. *Fotomat Corp. v. Chanda*, 464 So. 2d 626, 630 (Fla. 5th DCA 1985).

268. 593 P.2d 1308 (Wash. 1979). A similar result, based on course of dealing, was reached in *Karol v. New Hampshire Ins. Co.*, 414 A.2d 939, 940 (N.H. 1980) (ignoring exclusion of film processing loss where film-maker asked insurer for "broad coverage" against film production losses).

269. *Mieske*, 593 P.2d at 1310.

manager, "don't lose these. They are my life."<sup>270</sup> After the store lost the film, the court upheld a jury verdict for \$7,500.

This is an appropriate result. The manager knew or should have known from the consumer's statement that she placed special value on the film and would hardly be satisfied with receiving twenty-five rolls of blank film or replacement. Once the manager knew of her special circumstances from her statements, he had an affirmative duty to inform her of the disclaimer of liability if he wished to retain the limitation.<sup>271</sup> If the manager feared losing the customer's business, he could have taken special precautions, perhaps for an added charge. The manager who knew of the special nature of the film, not the customer who was unaware of the liability disclaimer, should suffer for the manager's silence.

#### D. *Beyond the Realm of Contemplation*

When parties negotiate a transaction, they focus on the central terms, such as price and quantity, and are likely aware of certain subordinate topics, such as warranty and credit terms. There are certain issues, however, that are so far removed from the purpose of the deal that they are not within the realm of contemplation of a party who neither drafted nor read the written contract. Just as one cannot accept an offer of which one is unaware,<sup>272</sup> consumers should not be held to have objectively assented to such terms.

In *Weaver v. American Oil Co.*,<sup>273</sup> the Indiana Supreme Court refused to enforce a term in a lease between an oil company and a filling station operator that not only held the oil company harmless for its own negligence, but actually required the operator to indemnify the oil company for damages caused by the *oil company's* negligence. The oil company did not contend that the operator knew of this term, or that he should have known he was assuming financial responsibility for the company's negligence. Rather, the company argued that the unread clause should control. The court refused to enforce the clause absent explicit agreement by both parties to the term. The court stated: "We do not mean to say or infer that parties may not make contracts exculpating one of his negligence and providing for indemnification, but it must be done *knowingly* and *willingly* as in insurance

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270. *Id.*

271. *Fotomat Corp.*, 464 So. 2d at 631 ("When the customer is made aware of the provision for limitation of liability and nevertheless proceeds with the transaction, he has assented to an agreement for which there is a commercial need . . .").

272. CALAMARI & PERILLO, *supra* note 19, at 73.

273. 276 N.E.2d 144 (Ind. 1971).

contracts made for that purpose.”<sup>274</sup>

A contract’s subordinate clause permitting a bank to retain and use a mortgagor’s prepaid interest and tax premiums without paying interest was struck down for similar reasons in *Derenco, Inc. v. Benj. Franklin Federal Savings and Loan Association*.<sup>275</sup> The court pointed out that approving a bank’s interest-free use of the mortgagor’s money would result in a “gratuitous windfall” because:

[a]t the time of the making of the contract, there would have been *no reason for borrowers to assume*, in the absence of their being otherwise informed, that [the bank] would have any interest other than that which was necessary to accomplish the purpose of the deposits.

. . . .

[W]hen he is not paid interest nor told that deposited funds will be put to the institution’s use, but instead is told that they will be put into a reserve account, we believe *it is doubtful that he would expect* the money to be used for the benefit of such institution.<sup>276</sup>

Banks have long been relieved of the duty to pay a publicly announced reward to a samaritan who assists in the capture of a bank robber when she is unaware of the reward, because there “is no mutual agreement of the minds as is essential to a contract.”<sup>277</sup> There is similarly no mutual agreement of the minds as to contract provisions beyond the scope of the consumer’s contemplation. Accordingly, form clauses disclaiming a residential landlord’s implied warranty of habitability,<sup>278</sup> imposing substantial liquidated damages

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274. *Id.* at 148. Interestingly enough, the court wrestled with the concept of objective, as opposed to subjective, assent: “The party seeking to enforce such a contract has the burden of showing that the provisions were explained to the other party and *came to his knowledge* and there was in fact a *real and voluntary meeting of the minds and not merely an objective meeting.*” *Id.* at 148.

The court confused the “objective meeting” of the minds with a “legally imposed” meeting. The latter comes when the courts enforce an unknown clause, even though it was not contemplated by the consumer, because of a black-letter rule that signed contracts should be enforced as written. By contrast, the “objective” meeting of the minds over the indemnity clause never occurred in *Weaver*, as the court itself noted, because both the filling station operator was unaware of the term and the oil company knew that the operator’s signature represented “a mere formality.” *Id.* at 146. Although the court thought its holding violated the objective theory of contracts, in reality the decision enforces the objective understanding of the non-drafter’s intent: “The law should seek the truth or the subjective understanding of the parties in this more enlightened age. The burden should be on the party submitting . . . [the] printed form to show that the other party had knowledge of any unusual or unconscionable terms contained therein.” *Id.* at 147.

275. 577 P.2d 477 (Or. 1978).

276. *Id.* at 488, 490 (emphasis added).

277. *Broadnax v. Ledbetter*, 99 S.W. 1111, 1112 (Tex. 1907).

278. See, e.g., *Teller v. McCoy*, 253 S.E.2d 114, 130 (W. Va. 1978) (“[I]t is fair to presume that no individual would voluntarily choose to live in a dwelling that had become unsafe for

for default on a lease of farm equipment,<sup>279</sup> and permitting a pawnbroker to trespass on a borrower's property and intentionally (and tortiously) damage property<sup>280</sup> have all been struck down.

The underlying principle is that consumers should "not be intimidated or tricked . . . by booby trap clauses hidden away in a printed form . . . ." <sup>281</sup> The further a form term is from the central purpose of the contract, the easier it should be for courts to find a lack of objective manifestation of assent by the consumer.

## IX. SPECIAL CASES

While the range of possible form contract terms is virtually limitless, there are two areas that warrant special consideration under the objective theory. In the usual non-negotiated consumer form contract, merger clauses and terms affecting the consumer's access to courts create an extraordinary risk of defeating the consumer's objective understanding. Moreover, the unexpectedly harsh effect of such clauses is so contrary to the average consumer's expectations that enforcement of the clauses may lead to great injustice. Accordingly, courts reviewing such clauses must take special care to interpret these clauses under the objective theory of contract.

### A. *Merger Clauses*

A merger (or integration) clause purports to limit the contractual agreement to whatever terms appear on the document.<sup>282</sup> When knowingly agreed upon, a merger clause serves to confirm each party's understanding of their respective obligations and helps courts in determining the intent of the parties.<sup>283</sup>

In a typical consumer form contract, an unread merger clause not only fails to mirror the consumer's intent, but directly contradicts the understanding created by the merchant because it prevents prior statements from becoming part of the contract. For example, a salesperson makes a promise to induce the consumer to enter into a contract. The consumer reasonably relies on the statement and signs the contract. The unread merger clause defeats the consumer's reason-

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human habitation.") (quoting *Bowles v. Mahoney*, 202 F.2d 320, 326 (D.C. Cir. 1952)); see also *Henriouille v. Marin Ventures, Inc.*, 573 P.2d 465, 468-70 (Cal. 1978); *Old Town Development Co. v. Langford*, 349 N.E.2d 744, 786-87 (Ind. Ct. App. 1976).

279. *John Deere Leasing Co. v. Blubaugh*, 636 F. Supp. 1569, 1574-75 (D. Kan. 1986).

280. *Southwestern Inv. Co. v. Mannix*, 557 S.W.2d 755, 763 (Tex. 1977).

281. *Old Town Development Co.*, 349 N.E.2d at 785.

282. See *supra* text accompanying notes 75-77.

283. See, e.g., FARNSWORTH, *supra* note 18, at 457-58.

able expectation created by the seller's statements.<sup>284</sup> Not only is this unfair, but it also permits sellers to prevail despite their own knowledge of the consumer's reliance on their statements in entering the contract.

Following the teachings of Professor Corbin,<sup>285</sup> courts generally do not enforce consumer form merger clauses.<sup>286</sup> In the words of the Washington Supreme Court, "a merger clause will not be enforced where it does not in fact express the true intentions of the parties."<sup>287</sup> For sellers who wish to avoid incorporating statements by their sales agents into the contract, the remedy is the proper selection, training, and supervision of sales agents and the adequate informing of consumers.<sup>288</sup>

### B. Access to Courts

One broad area that is virtually never contemplated by consumers signing form contracts is the selection of the legal forum and rules that will govern any future litigation. Consumers do not consider these matters because: 1) the consumer generally does not foresee the breakdown of the contract; 2) very few contracts in fact end in litigation; 3) there is no discussion at the time of contract, and certainly no advertisement, addressing these issues; and 4) many subtle legal issues are unknown and misunderstood by most laypersons.<sup>289</sup> An unread term restricting consumers' access to judicial relief in case of breach of contract cannot be within their objective understanding of the agreement. Courts must ensure that enforcement of an unbalanced clause does not make the court itself a party to injustice.

## 1. CONFESSIONS OF JUDGMENT

A confession of judgment concedes liability on the part of the

284. *Seibel v. Layne & Bowler Inc.*, 641 P.2d 668, 671 (Or. Ct. App. 1982) (stating that "it would be unconscionable to permit an inconspicuous merger clause to exclude evidence of an express oral warranty").

285. See *supra* text accompanying notes 74-77.

286. See, e.g., *Central Jersey Dodge Truck Ctr., Inc. v. Sightseer Corp.*, 608 F.2d 1106, 1110 (6th Cir. 1979); *Anderson & Nafziger v. G.T. Newcomb, Inc.*, 595 P.2d 709, 714 (Idaho 1979); *Rinaudo v. Bloom*, 120 A.2d 184, 189 (Md. 1956); *Seibel*, 641 P.2d at 671.

287. *Berg v. Stromme*, 484 P.2d 380, 385 (Wash. 1971).

288. See, e.g., *Harr v. Allstate Ins. Co.*, 255 A.2d 208, 219 (N.J. 1969).

289. See John E. Murray, Jr., *Unconscionability: Unconscionability*, 31 U. PITT. L. REV. 1, 74 (1969) (stating that "the pain and suffering of attempting to read and understand every printed form would be greater than the pain [suffered] as a result of occasionally being bound by unread and uncomprehended printed terms"); Alex Y. Seita, *Uncertainty and Contract Law*, 46 U. PITT. L. REV. 75, 133 (1984) ("Because the vast majority of contracts are successfully completed, a reasonable consumer should pay little attention to the terms of a contract unless he values the contract highly or is alerted to potential problems.").

confessor prior to the alleged wrong-doing. The clause binds the signer to whatever charge the contract drafter chooses to levy, whether truthful or not. As one court stated:

[T]he confession of judgment clause was the essence of a material, risk-shifting term. It was designed to summarily discard the due process guarantees which our system of jurisprudence so highly cherishes. It is difficult to conceive of a clause which alters risks in a more drastic fashion than one which dispenses with the signer's day in court.<sup>290</sup>

The above quote is from a case where a wife signed two notes confessing judgment for monies her husband had embezzled from his employer.<sup>291</sup> She was told at the signing that she would only be responsible for \$160,000, which she knew her husband would be able to repay immediately.<sup>292</sup> After the \$160,000 was paid, the employer, citing the language of the second note, sued the wife for an additional \$212,000.<sup>293</sup> The court refused to enforce the second note because the wife

did not understand the terms of the second judgment note. The harsh allocation of risk was not manifested in a manner reasonably comprehensible to her. She had never before seen a judgment note and was crying for part of the time when she read the documents presented to her, although she tried her best to read them.<sup>294</sup>

Confessions of judgment in form contracts are simply not expected. Moreover, the results of these terms are extraordinarily harsh. Without a consumer's knowing and voluntary assent to such terms, the drafter cannot reasonably believe that the consumer assented to the clause. As Professor Murray stated:

Perhaps confession of judgment clauses are so pernicious that they should be declared illegal. In the absence of illegality, however, the only concern of the court should be whether the party against whom the clause is supposed to operate knew about it and, once his apparent assent is manifested, whether he had any choice at all in relation to it, i.e., whether his apparent assent was genuine.<sup>295</sup>

## 2. ATTORNEY FEES

Another pernicious clause frequently found in form contracts requires the consumer to pay the attorney fees of the contract drafter.

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290. *Germantown Mfg. Co. v. Rawlinson*, 491 A.2d 138, 146 (Pa. Super. Ct. 1985).

291. *Id.* at 140.

292. *Id.*

293. *Id.*

294. *Id.* at 147.

295. Murray, *supra* note 289, at 19-20.

The requirement to pay the other party's attorney fees for litigation over the contract, whose obligation has not yet been performed let alone breached, is not within the consumer's contemplation. Such a term should never be enforced absent knowing and genuine assent by the consumer.

Courts have long recognized the harmful effects of such clauses. In 1892, the Supreme Court of North Carolina refused to enforce a clause in a promissory note stipulating that "in case this note is collected by legal process the usual collection fee shall be due."<sup>296</sup> The court stated that "such a provision is a stipulation for a penalty or forfeiture, tends to the oppression of the debtor and to encourage litigation, is a cover for usury, is without any valid consideration to support it, contrary to public policy, and void."<sup>297</sup>

This tendency to oppress inherent in fee clauses is well-illustrated by the case in which a New York City landlord, after losing the case, attempted to collect attorney fees from a tenant.<sup>298</sup> The court denied recovery, stating that "[a]n award of counsel fees to a non-prevailing party would be an absurd and oppressive result."<sup>299</sup> The landlord was also denied attorney fees for the administrative hearings at which he prevailed. The court stated that "[t]he threat of onerous attorneys' fees in the event of an adverse determination might well have a chilling effect upon parties taking their grievance to the administrative body expressly established to adjudicate those grievances."<sup>300</sup>

Short of simply refusing to enforce form attorney fee clauses, the New York legislature may have created the best alternative for common law courts. New York State law now requires that where a lease provides for recovery of legal fees by a prevailing landlord, a tenant who prevails will also be eligible for attorney fees.<sup>301</sup>

In a consumer form contract, attorney fee provisions are far from the contemplation of the non-drafting party. The best response to such a provision would be to find it unenforceable because of the lack of objective manifestation of assent.<sup>302</sup> Alternatively, prevailing con-

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296. *Tinsley v. Hoskins*, 16 S.E. 325, 325 (N.C. 1892).

297. *Id.* (quoting *Merchants' Nat'l Bank v. Sevier*, 14 F. 662, 663 (C.C.E.D. Ark. 1882)).

298. *East 55th St. Joint Venture v. Litchman*, 469 N.Y.S.2d 1013 (N.Y.C. Civ. Ct. 1983), *aff'd*, 487 N.Y.S.2d 256 (N.Y. Sup. Ct. 1984).

299. *Id.* at 1018.

300. 487 N.Y.S.2d at 258.

301. N.Y. REAL PROPERTY LAW § 234 (McKinney 1989 and 1993 Supp.).

302. One example of an attorney fee clause that was subject to true assent was the promise by the owners of major league baseball teams to pay for the former baseball commissioner's attorney fees in case of litigation between the owners and the commissioner. Jim Henneman, *Owners Seem Prepared to Knock Vincent Out of Commission*, BALTIMORE MORNING SUN, Sept. 3, 1992, at D6.



sumers should be permitted to recover attorney fees whenever prevailing sellers would. Otherwise, intimidation and litigation is encouraged without gain for true freedom of contract.

### 3. JURY TRIAL

The Seventh Amendment to the United States Constitution provides the right to a jury trial in civil litigation.<sup>303</sup> One court stated that "[t]his is a valuable, cherished right; it is integral to our system of justice."<sup>304</sup> While this right can be waived, the relinquishment must be knowing and voluntary.<sup>305</sup>

Form contracts should not surreptitiously wrest away a right granted by the framers of the Constitution. As one court stated:

[Drafters] have a very heavy burden of proving that the plaintiffs knowingly, voluntarily and intentionally agreed upon the jury waiver provision . . . . A constitutional guarantee so fundamental as the right to jury trial cannot be waived unknowingly by mere insertion of a waiver provision on the twentieth page of a twenty-two page standardized form contract . . . . In fact, the defendants have failed to show that the plaintiffs had any choice other than to accept the contract as written. . . . Absent proof to the contrary, such an inequality in relative bargaining positions suggests that the asserted waiver was neither knowing nor intentional.<sup>306</sup>

The Alabama Supreme Court similarly refused to enforce a jury trial waiver in a form contract between a pharmacist and his employer, a department store, because "it does not appear that the waiver . . . was intelligently or knowingly made."<sup>307</sup> An unread form

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303. U.S. CONST. amend. VII ("In Suits at common law, . . . the right of trial by jury shall be preserved . . .").

304. *Dreiling v. Peugeot Motors of Am., Inc.*, 539 F. Supp. 402, 403 (D. Colo. 1982).

305. See, e.g., *K.M.C. Co. v. Irving Trust Co.*, 757 F.2d 752, 755 (6th Cir. 1985) (holding that waiver must be "done knowingly, voluntarily and intentionally"); *National Equip. Rental, Ltd. v. Hendrix*, 565 F.2d 255 (2d Cir. 1977) ("[T]he Seventh Amendment right to a jury is fundamental and . . . its protection can only be relinquished knowingly and intelligently."). For a discussion of waiver of Fourth Amendment rights, see *Smyth v. Lubbers*, 398 F. Supp. 777, 788 (W.D. Mich. 1975) ("[A] blanket authorization in an adhesion contract that the College may search the room for violation of whatever substantive regulations the College chooses to adopt and pursuant to whatever search regulation the College chooses to adopt is not the type of focused, deliberate, and immediate consent contemplated by the Constitution."); cf. *Fuentes v. Shevin*, 407 U.S. 67, 95 (1972) (holding unenforceable contractual provision waiving due process rights when there was "no showing whatever that the appellants were actually aware or made aware of the significance of the fine print now relied upon as a waiver of constitutional rights.").

306. *Dreiling*, 539 F. Supp. at 403 (refusing to enforce a jury trial waiver in a contract between an automobile manufacturer and a dealer).

307. *Gaylord Dep't Stores, Inc. v. Stephens*, 404 So. 2d 586, 587 (Ala. 1981). The court described the contract as a "form contract with boiler plate provisions. The jury waiver provision is buried in paragraph thirty-four in a contract containing forty-six paragraphs . . . ."

contract clause does not evince a knowing and willing waiver of the Constitutional right to trial by jury. Consequently, courts should be leary of enforcing such clauses absent concrete objective evidence of the consumer's assent.

#### 4. ARBITRATION

Arbitration can be an efficient and economical means for resolving disputes. The Supreme Court has held that the Federal Arbitration Act<sup>308</sup> "establishes a federal policy favoring arbitration, requiring that '[a court] rigorously enforce agreements to arbitrate.'"<sup>309</sup> Thus, the Court has upheld form terms in brokerage contracts that required arbitration of claims relating to S.E.C. Act violations,<sup>310</sup> antitrust laws,<sup>311</sup> and RICO suits.<sup>312</sup>

The Supreme Court, however, has not issued an opinion on unread form arbitration clauses. The Court has not stated that arbitration clauses are more easily enforceable than other contract clauses, merely that they should not be especially disfavored.<sup>313</sup> In a similar vein, the Court held that the Arbitration Act reflects Congress's intent to make "arbitration agreements as enforceable as other contracts, but not more so."<sup>314</sup> Thus, if other unread form contract

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*Id.*; see also *Fairfield Leasing Corp. v. Techni-Graphics, Inc.*, 607 A.2d 703, 705 (N.J. Super. Ct. Law Div. 1992) ("A constitutional guarantee so fundamental as the right to jury trial cannot be waived unknowingly by mere insertion of a waiver provision on the twentieth page of a twenty-two page standardized form contract."). A form jury waiver was enforced, however, when the non-drafter was represented by counsel who read the form prior to signing. *Chase Commercial Corp. v. Owen*, 588 N.E.2d 705 (Mass. App. Ct. 1992).

308. 9 U.S.C. § 1 (1988). Section 2 reads:

A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.

309. *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 226 (1987) (citations omitted).

310. *Scherk v. Alberto-Culver Co.*, 417 U.S. 506 (1974).

311. *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985).

312. *Shearson/American Express*, 482 U.S. at 242.

313. Absent a well-founded claim that an arbitration agreement resulted from the sort of fraud or excessive economic power that 'would provide grounds for the revocation of any contract,' the Arbitration Act 'provides no basis for disfavoring agreements to arbitrate statutory claims by skewing the otherwise hospitable inquiry into arbitrability.[']

*Id.* at 226 (quoting *Mitsubishi Motors Corp. v. Soler Chrysler Plymouth, Inc.*, 473 U.S. 614, 627 (1985)).

314. *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 404 n.12 (1967). The Court added that courts were not barred from reviewing whether arbitration clauses were fraudulently procured, because to "immunize an arbitration agreement from judicial challenge

clauses are struck down under the objective theory, unread arbitration clauses should meet a similar fate.

In fact, the Supreme Court seems willing to accept such a contention. In upholding a brokerage form arbitration agreement, the Court stated, "Although petitioners suggest that the agreement to arbitrate here was adhesive in nature, *the record contains no factual showing sufficient to support that suggestion.*"<sup>315</sup> The Court did not say it was irrelevant whether the contract was adhesive, merely that conclusory statements to that effect are insufficient to attack an arbitration clause. The clear implication is that if such a factual showing of adhesion had been made, the arbitration clause would have been treated quite differently.<sup>316</sup>

For example, the Nevada Supreme Court held that a medical clinic's arbitration clause was unenforceable because the clinic did not explain it to the patient.<sup>317</sup> Relying on the objective theory of contracts, the court stated that the patient "did not give an informed consent to the agreement and that no meeting of the minds occurred."<sup>318</sup>

Even if a patient does read an arbitration clause, depending on the circumstances, the reading alone may not constitute sufficient evidence of a meeting of the minds. Especially when the form is presented to a patient just before a medical procedure is to begin, courts should be reluctant to find objective assent.<sup>319</sup>

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on the ground of fraud in the inducement would be to elevate it over other forms of contract." *Id.*

315. *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477, 484 (1989) (emphasis added).

316. While the Court did not say precisely what sort of factual showing would be sufficient, its appreciation of the problem is apparent. *See Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, 627 (1985) (stating "courts should remain attuned to well-supported claims that the agreement to arbitrate resulted from the sort of fraud or overwhelming economic power that would provide grounds 'for the revocation of any contract.'").

317. *Obstetrics & Gynecologists v. Pepper*, 693 P.2d 1259, 1261 (Nev. 1985).

318. *Id.*; *see also Gray v. Zurich Ins. Co.*, 419 P.2d 168, 174 (Cal. 1966) (stating that arbitration provisions were contrary to the reasonable expectation of the non-drafting party, absent "plain and clear" notification of the existence of such clauses); *Sanchez v. Sirmons*, 467 N.Y.S.2d 757, 760 (N.Y. Sup. Ct. 1983) ("In order to be binding, the arbitration provision should have been called to the petitioner's attention and she should have been given a reasonable explanation of its meaning and effect, including an explanation of any other available options."); *Strong v. Oakwood Hosp. Corp.*, 325 N.W.2d 435, 438 (Mich. Ct. App. 1982) (agreement to arbitrate must be made "in an intelligent, knowing and voluntary manner").

319. It is only the unusual patient who faces surgery without fear and trepidation.

The anxiety produced by thoughts of soon entering the operating room, an unfamiliar setting, and the ever present possibility of an untoward result, create an inappropriate atmosphere in which to thrust upon a patient for the first time the burden of analyzing documents containing an arbitration provision

Even if arbitration was reasonably expected by the non-drafting party,<sup>320</sup> neither the arbitration provision nor the arbitration tribunal must favor the contract drafter.<sup>321</sup> A one-sided arbitration provision gives only one party the right to demand arbitration. For example, a physician's contract required that all claims arising from the doctor-patient relationship be arbitrated, except claims for money due for services rendered.<sup>322</sup> Because only doctors might have a claim for payment for their services, the court refused to enforce the arbitration clause and stated: "An arbitration agreement will not be enforced unless it is 'mutually binding.' Where an arbitration clause is not mutually binding, but rather grants one party a unilateral right to arbitrate, the court will not enforce such agreement."<sup>323</sup>

To be enforceable, an arbitration clause must also place the decision in the hands of an impartial arbiter who is neither personally nor institutionally biased. The California Supreme Court acknowledged that contracting parties could agree to select non-neutral arbitrators, but absent equal bargaining and true consent, required that any arbitration must meet "minimum levels of integrity."<sup>324</sup>

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inconspicuously embodied therein. A patient being wheeled into the operating room should not have to contemplate the pros and cons of litigating the surgeon's mistakes before a tribunal of arbitrators rather than before a jury in a court of law.

*Sanchez*, 467 N.Y.S.2d at 761; *see also* *Tunkl v. Regents of the Univ. of Cal.*, 383 P.2d 441, 447 (Cal. 1963) ("The admission room of a hospital contains no bargaining table where, as in a private business transaction, the parties can debate the terms of their contract.").

320. *See, e.g.*, *Preston v. Kruezer*, 641 F. Supp. 1163, 1172 (N.D. Ill. 1986); *Finkle & Ross v. A.G. Becker Paribas, Inc.*, 622 F. Supp. 1505, 1511-12 (S.D.N.Y. 1985); *Hope v. Dean Witter Reynolds Org., Inc.*, 226 Cal. Rptr. 439, 445-47 (Cal. Ct. App. 1986).

321. *See, e.g.*, *Madden v. Kaiser Found. Hosp.*, 552 P.2d 1178, 1186 (Cal. 1976) (upholding arbitration clause that "bears equally" on both parties).

322. *Miner v. Walden*, 422 N.Y.S.2d 335 (N.Y. Sup. Ct. 1979).

323. *Id.* at 339; *accord* *Mendes v. Automobile Ins. Co.*, 563 A.2d 695, 699 (Conn. 1989) (rejecting clause limiting appeals); *Worldwide Ins. Group v. Klopp*, 603 A.2d 788 (Del. 1992) (striking clause authorizing appeal of only high arbitration awards); *Schmidt v. Midwest Family Mut. Ins. Co.*, 426 N.W.2d 870, 875 (Minn. 1988) (same); *Pepin v. American Universal Ins. Co.*, 540 A.2d 21, 23 (R.I. 1988) (same); *see also* *Dwyer v. Biddle*, 83 N.Y.S.2d 138, 138 (N.Y. App. Div. 1948) ("There is no satisfactory showing of a reciprocally enforceable written contract of the parties containing the claimed arbitration clause.").

324. *Graham v. Scissor-Tail, Inc.*, 623 P.2d 165, 176 (Cal. 1981).

[W]e must note that when as here the contract designating such an arbitrator is the product of circumstances suggestive of adhesion, the possibility of overreaching by the dominant party looms large; contracts concluded in such circumstances, then, must be scrutinized with particular care to insure that the party of lesser bargaining power, in agreeing thereto, is not left in a position depriving him of any realistic and fair opportunity to prevail in a dispute under its terms.

*Id.* Thus, the court refused to order arbitration which would have been conducted by the union of one of the contracting parties. *Id.* at 177.

## 5. FORUM SELECTION CLAUSES

Contracting parties sometimes try to control the costs of future litigation by including a term requiring that all litigation be filed in a designated forum.<sup>325</sup> These forum selection clauses serve to prevent future conflicts regarding the correct forum and permit a rational business to consolidate legal action in one locale.<sup>326</sup>

The major danger inherent in these clauses is that they can force consumers to enforce their rights in far removed fora, which may effectively bar such enforcement. As one court said, such a clause

represents a recurring fantasy of shipowners and cargo defense lawyers. Ideally, if a choice of forum clause in a bill of lading would name the place for the resolution of the controversy, for example, Timbuktu or Byelorussia, then the expense and discomfort of pursuing the matter there would, of course, affect the exercise of the rights of the otherwise innocent cargo owner. Certain claims, because of the amount involved or other considerations regarding evidence and witnesses would not be pursued.<sup>327</sup>

In *Paragon Homes Inc. v. Carter*,<sup>328</sup> a Maine corporation, doing home improvements on a house in Brockton, Massachusetts, inserted into its form contract a clause designating New York as the proper forum.<sup>329</sup> The New York courts refused to enforce the clause, stating that the clause

was inserted by the plaintiff in its printed form of contract for the purpose of harassing and embarrassing the defendants in the prosecution or defense of any action arising thereunder. This is not a case involving parties situated on an equal basis . . . . The procurement of defendants' consent to New York as the forum for legal redress is . . . without justification, grossly unfair and unconscionable.<sup>330</sup>

By contrast, the United States Supreme Court upheld a forum selection clause in a consumer form contract in *Carnival Cruise Lines v. Shute*.<sup>331</sup> Consumers from the state of Washington had purchased, through a local travel agent, tickets for a cruise from California to

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325. Some courts hold that choice of law clauses should be treated the same as those designating choice of forum. *Sembawang Shipyard, Ltd. v. Charger, Inc.*, 955 F.2d 983, 986 (5th Cir. 1992).

326. For an excellent discussion of forum selection clauses, see Goldman, *supra* note 3.

327. *Underwriters at Lloyd's of London v. M/V "Steir"*, 773 F. Supp. 523, 524 n.1 (D.P.R. 1991).

328. *Paragon Homes, Inc. v. Carter*, 288 N.Y.S.2d 817 (N.Y. Sup. Ct.), *aff'd*, 295 N.Y.S.2d 606 (N.Y. App. Div. 1968).

329. *Id.* at 818.

330. *Id.*

331. 499 U.S. 585 (1991).

Mexico. The tickets contained a forum selection clause designating Florida, the location of the cruise line's corporate headquarters, as the forum.<sup>332</sup> Ms. Shute suffered an injury while sailing in international waters, and she sued the cruise line in Washington upon her return. The Supreme Court upheld the forum selection clause, stating that it had not been inserted into a form contract merely to discourage litigation.<sup>333</sup> Instead, the selection of Florida was a good faith selection given that the cruise line's principal place of business was Florida and that many of its cruises left from Florida. Moreover, because a ship carries passengers from many locales, the cruise line might rationally wish to consolidate all potential claims in a single site.<sup>334</sup>

One factor limiting the precedential scope of *Carnival* in future consumer form cases is that the cause of action occurred in international waters.<sup>335</sup> Unlike the situation where consumers purchase goods for use in their homes, the cruise occurred far from either party's domicile. The forum selection clause was especially appropriate in that situation "given the fact that Mrs. Shute's accident occurred off the coast of Mexico—[this dispute was not] an essentially local one inherently more suited to resolution in the State of Washington than in Florida."<sup>336</sup>

The Court also concluded that, even though this was a form contract over which there had been no bargaining, there were no contractual irregularities to defeat enforcement of the term.<sup>337</sup> The Court deliberately declined to address the most important issue in interpreting form contracts, whether consumers are truly aware of subordinate provisions of such contracts.

The reason for this omission is that the consumers in their brief expressly waived any contention that they had not received adequate notice of the clause: "The respondents do not contest the incorporation of the provision nor that the forum selection clause was reason-

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332. Clause 8 stated:

It is agreed by and between the passenger and the Carrier that all disputes and matters whatsoever arising under, in connection with or incident to this Contract shall be litigated, if at all, in and before a Court located in the State of Florida, U.S.A., to the exclusion of the Courts of any other state or country.

*Id.* at 587-88.

333. *Id.* at 595.

334. *Id.*

335. "We begin by noting the boundaries of our inquiry. First, this is a case in admiralty, and federal law governs the enforceability of the forum-selection clause we scrutinize." *Id.* at 590.

336. *Id.* at 594.

337. "Common sense dictates that a ticket of this kind will be a form contract the terms of which are not subject to negotiation, and that an individual purchasing the ticket will not have bargaining parity with the cruise line." *Id.* at 593.

ably communicated to the respondents, as much as three pages of fine print can be communicated. The issue is whether the forum selection clause should be enforced, not whether Respondents received the ticket."<sup>338</sup> The apparent irony of the phrase "as much as three pages of fine print can be communicated" was ignored by the Supreme Court, which took this admission at face value: "[W]e do not address the question whether respondents had sufficient notice of the forum clause before entering the contract for passage. Respondents essentially have conceded that they had notice of the forum-selection provision."<sup>339</sup> Therefore, the Court explicitly declined to consider the issue of the adequacy of Carnival Cruise Lines' disclosure of the forum selection term.

*Carnival* does not stand for the proposition that mere inclusion of a term in a form contract amounts to adequate notice. The consumers here conceded notice, and the Supreme Court merely took them for their word. The district court in *Generale Bank v. Choudhury*<sup>340</sup> therefore misread *Carnival* when it asserted that an undisclosed form term which "could have been read" was "reasonably communicated" to consumers.<sup>341</sup> The lower court upheld the forum selection clause in a promissory note, even though the debtor argued he did not have notice of the clause. The court stated that the debtor signed the promissory notes, and that he "could have been made aware of the forum-selection clause had he read those documents."<sup>342</sup> The court erroneously concluded that *Carnival* mandated that "[g]iven that the forum-selection clause was 'reasonably communicated' to Choudhury through delivery of the promissory notes which he signed, Choudhury had constructive notice of that

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338. Brief for Respondents at 26, *Carnival Cruise Lines* (No. 89-1647). This was a tactical decision [in hindsight, a poor one], as they chose to focus their legal energies on arguing that the unequal bargaining power was sufficient to defeat enforcement of the forum selection clause. In fairness, this strategy did work in the Court of Appeals, where the Ninth Circuit stated: "Even if we assume that the Shutes had notice of the provision, there is nothing in the record to suggest that the Shutes could have bargained over this language." 897 F.2d 377, 389 (9th Cir. 1990). The appellate court did say this assumption was "doubtful," because the consumers did not have the opportunity to review the terms until mailed to them, *id.* at 389 n.11, but proceeded on this "doubtful" contention anyway.

339. 499 U.S. at 590. The admission of having read the contract was counter-factual, as Justice Stevens argued in dissent that "only the most meticulous passenger is likely to become aware of the forum selection provision." *Id.* at 597 (Stevens, J., dissenting). The term was included as the eighth of twenty-five numbered paragraphs, on a form which was not delivered until consumers had already purchased their ticket, and which barred refunds for those who wished to get out of the deal. *Id.*

340. 779 F. Supp. 303 (S.D.N.Y. 1991).

341. *Id.* at 305 n.1.

342. *Id.* at 305.

clause.”<sup>343</sup>

The Supreme Court did not adopt the principle of “constructive notice.” The significance of *Carnival* for determining the enforceability of form terms in general is far more narrow. The Court stressed that its holding should be read in light of two limiting facts: the non-local nature of the dispute and the fact that the consumers did “*not claim lack of notice of the forum clause.*”<sup>344</sup> Therefore, as in the arbitration cases,<sup>345</sup> the Supreme Court has indicated that cases by consumers who were unaware of specific form terms are distinguishable from cases where consumers admit notice. Before enforcing an unread form forum-selection clause, courts should apply the objective theory of contract and insist on a showing that the consumer was aware of the clause and its effects.

One pre-*Carnival* court explicitly referred to this concept in refusing to enforce a forum selection clause in a farmer’s lease of water drilling equipment.<sup>346</sup> The court transferred the case to Washington, where the transaction had occurred, despite the clause selecting New York as the forum and stated “[t]here was absolutely nothing about these transactions which could alert reasonable persons that disputes arising out of the agreements would be adjudicated 3,000 miles away in New York.”<sup>347</sup> In a particularly appropriate application of the objective theory, the court stated: “[i]f the finder of fact determines that [the non-drafter] did not know of the lease’s provisions, and that they were not brought to his attention, . . . he might not be bound by those *provisions to which he did not assent—i.e. on which the parties’ minds did not meet.*”<sup>348</sup>

## X. CONCLUSION

The classical common law presumption that consumers read form contracts has led both to injustice and to an irrational bifurcation of contract law. Modern courts have attempted to correct this misstep by adhering to the fundamental principle that a consumer’s assent to a contract should be determined by how a reasonable person

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343. *Id.* (footnotes omitted).

344. *Carnival*, 499 U.S. at 595 (emphasis added). Later in the opinion, the Court again stressed the consumer’s concession: “Finally, respondents have conceded that they were given notice of the forum provision and, therefore, presumably retained the option of rejecting the contract with impunity.” *Id.*

345. See *supra* text accompanying notes 315-16.

346. *Leasing Serv. Corp. v. Broetje*, 545 F. Supp. 362 (S.D.N.Y. 1982).

347. *Id.* at 369.

348. *Id.* at 366 n.3 (emphasis added).



in the other party's position would ascertain the consumer's intent as manifested through words and deeds.

Accordingly, we can now see the outline of the objective theory of consumer form contracts. Courts no longer assume that the unknown subordinate written terms are automatically assented to merely because they are included in an executed contract. Rather, courts should examine both what the consumer actually knew and what knowledge is properly attributable to the consumer.

Courts applying the objective theory should examine what contract terms were actually negotiated or explained. Next, courts must explore the purpose for which the product or service is being acquired, the legitimate purposes for which subordinate clauses were included, the content of the communication between the consumer and the salesperson, and the effect of mass advertisements. Finally, courts must consider which topics were likely beyond the scope of the consumer's contemplation.

This correction of a misdirected common law rule is consistent with the role of common law courts. As Benjamin Cardozo explained:

A rule which in its origin was the creation of the courts themselves, and was supposed in the making to express the *mores* of the day, may be abrogated by the courts when the mores have so changed that perpetuation of the rule would do violence to the social conscience . . . . This is not usurpation. It is not even innovation. It is the reservation for ourselves of the same power of creation that built up the common law through its exercise by the judges of the past.<sup>349</sup>

The creation of a new rule for form contracts is at hand. If accurately applied, the objective theory will both end the unnatural growth of divergent contractual theories and permit true freedom of contract.

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349. BENJAMIN N. CARDOZO, *The Growth of the Law*, in SELECTED WRITINGS OF BENJAMIN NATHAN CARDOZO: THE CHOICE OF TYCHO BRAHE 185, 246 (Margaret E. Hall ed., 1947).

## APPENDIX

KARL LLEWELLYN'S UNPUBLISHED 1941 FIRST DRAFT OF  
REVISION TO THE UNIFORM SALES ACT: (section on  
form contracts)

SECTION 1-C. (New to Sales Act.) DECLARATION OF POLICY,  
AND PROCEDURE WITH REGARD TO DISPLACEMENT OF  
SINGLE PROVISIONS OR GROUPS OF  
PROVISIONS BY AGREEMENT.

(l) (a) The principles declared in this Act represent a fair and balanced allocation of rights and liabilities between parties to sales and contracts to sell, as such allocation has been developed out of the best case-law and mercantile practice to cover each point to which the two parties have not directed their careful and deliberate attention.

(b) When both the parties have so directed their attention to a particular point that the coverage of that point in a manner in addition to or at variance from this Act may fairly be regarded as the deliberate desire of both, and as reflecting a considered bargain on that particular point, the provision of the contract on that point is called in this Act a "particularized term of the bargain"; and the legislature recognizes that policy in general requires the parties' particular bargain to control. Wherever a provision of the Act is not subject to such modification by agreement, or is subject to such modification only within stated limits, that fact is expressly stated in the Act.

(c) The legislature also recognizes that particular trades and situations often require extensive special regulation in a manner departing from the general provisions of this Act, and that speed and convenience in transacting business may require such extensive departures to be incorporated into a general form-contract, or into "rules" to which particular transactions are made subject, although the details of such "rules" or forms are not so deliberated on and bargained about by the two parties when they are closing an individual transaction as to become particularized terms of the bargain.

(d) On the other hand, the legislature recognizes that where a group or bloc of provisions are not studied and bargained about in detail by both parties, then actual assent to the incorporation of such a group or bloc into a particular transaction is not in fact to be assumed where the group or bloc of provisions, taken as a whole, allocates rights and obligations in an unreasonably unfair and unbalanced fashion. The legislature recognizes that assent, without deliberation and bargaining, to the incorporation into a transaction of a group or bloc of provisions varying from the general law rests upon the presup-

position that such a group or bloc of provisions will prove to be a reasonably fair and balanced one; and the legislature recognizes that this holds true in fact, whether or not such a group or bloc of provisions are printed upon the contract-form used, and whether or not a formal recital of acceptance of such a group or bloc of provisions is found thereon.

(e) The policy of the legislature is to aid and foster any considered and deliberate action to the parties, or of representatives of the parties' interests, in substituting for the general rules of this Act a fair and balanced set of provisions more particularly fitted to the needs of any particular trade or type of situation. The policy of the legislature is also to avoid any seeming portion of a bargain which does not truly represent bargaining, but under which one party seeks to displace the rules of this Act without particular deliberation and bargaining over each clause, in favor of a set of provisions which lack reasonable balance and fairness in their allocation of rights and obligations.

(2) (a) It is therefore the declared policy of the legislature that where a number of points purport to be covered in bloc by a transaction, as by a form-contract, or by reference to a set of "rules", and a number of the provisions concerned are at variance with the provisions of this Act, then the circumstances of the case shall determine whether the bloc of provisions is or is not substituted as such for the provisions of the Act. It is the declared policy that the court shall examine the bloc of provisions in the light of the situation.

(i) If the bloc as a whole is shown affirmatively to work a displacement or modification of the provisions of this Act in an unfair and unbalanced fashion not required by the circumstances of the trade, then the party claiming application of any particular provision in such bloc must show that the other party, with due knowledge of the contents of that particular provision, intended that provision to displace or modify the relevant provision of this Act in regard to the particular transaction.

(ii) If the bloc as a whole is shown affirmatively to work a fair and balanced allocation of rights and duties in view of the circumstances of the trade, its incorporation into the particularized terms of the bargain is presumed from the presence of the bloc of provisions or of a clear incorporation thereof on the document of contract.

(iii) If no affirmative showing is made either way, then the whole bloc of provisions may be incorporated into the transaction by any circumstance which would justify treat-

ing a single provision as one of the particularized terms of the bargain.

(b) The question under this subsection is for the court [or for a special merchants' jury under Section 51-C.]

(c) In weighing fair balance and in weighing particular intention, the court may properly consider the circumstances of preparation of any contract-form, or set of "rules", and, in particular

(i) whether both buyers and sellers of the type involved in the particular transaction have had a voice in such preparation; and

(ii) whether the displacement of provisions of this Act sought by the form or "rules" as a whole runs disproportionately in favor of one party as against the other.

(iii) whether clauses sought to be substituted for provisions of this Act are in consonance with fair expectation, in the light of the circumstances of the trade.

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#### COMMENT ON SECTION 1-C.

##### A. *General.*

This section undertakes to clarify one of the most confused situations in the law of the field, while doing justice to each line of known need.

(1) *The balanced "Association" type of "Rules"*. General provisions in an Act cannot do particular justice to the particular conditions of the wholesale trade in grain, or furs, or dried fruit, or fresh produce. What general provisions can do, is to leave usage of trade free to modify or displace the general provisions. But *proof* of usage of trade, especially before a jury, is expensive and uncertain. Even before a jury of merchants, the results of proof of such usage of trade must abide the event, and some upsets are inevitable. Moreover, usage may be unclear, or in process of change, or different as between the market the seller knows and the market familiar to the buyer. It is, therefore, wisdom for those engaged in a particular trade to get together on a clear and specialized articulate statement in advance of such usages or changes in usage as they wish incorporated into their transactions. This the section recognizes and seeks to encourage.

(2) *The "jug-handled" type of "Rules" or form*. A private codification, however, has dangers. It may heap all the advantages sought on one side, and heap all the burdens on the other. And this has proved true not only of many form-contracts prepared by single sell-

ers (or buyers), but also of "rules" prepared by groups, when it happened that the interests or thinking of the group ran predominantly to one single side of the sales transaction.

(3) *The principle of freedom of bargain* is a principle of freedom of *intended* bargain. It requires what the parties' have bargained out to stand as the parties have shaped it, subject only to certain overriding rules of public policy. "Written" bargains, in the days when the rules about them crystallized, were bargains whose detailed terms the two parties had looked over; and the rule was proper, that a signature meant agreement. When, however, parties bargain today, they *think* and *talk* of such matters as price, credit, date of delivery, description and quantity. These are the bargained terms. The unmentioned background is assumed without mention to be the fair and balanced general law and the fair and balanced usage of the particular trade. Displacement of these balanced backgrounds is not to be assumed as intended unless deliberate intent is shown that they shall be displaced; and deliberate intent is not shown by a lop-sided form whose very content suggests that it has not been carefully read, and the circumstances of whose execution suggest that the matters under discussion and consideration were only the matters written or typed in.

(4) *The courts have groped* for a guide through these two situations, being bothered by an assumed need for a single rule which would either include even the most lop-sided form, or else would exclude even the fairest one, when the parties had not given particular and deliberate attention to its incorporation. Some of the earlier cases in which lop-sided forms produced shock were dealt with in part on principles of public utilities (the clauses freeing the railroad from its own negligence, or limiting the telegraph company's liability; the baggage-check clauses). More recently, in addition to sometimes strained construction "against the party preparing the document", court after court has given expression to the desire for balance by requiring, over and above what is needed to make out consideration, some type of further "mutuality" in the expressed obligation.

(5) *The true principle is clear enough*: the expression of a body of fair and balanced usage is a great convenience, a gain in clarity and certainty, an overcoming of the difficulty faced by the law in regulating the multitude of different trades; on the other hand, the substitution of private rule-making by one party, in his own interest, for the balance provided by the law, is not to be recognized without strong reason shown. This is the result in accordance with which the best case-law has moved, in many individual cases, but without the coherent general formulation here provided.

(6) *The one-sided group of clauses which are fair, but are needed to give protection against bad law.*

Many groups of clauses in very frequent use in the Sales field are utterly one-sided, but are, for all that, entirely fair because they correct in a reasonable way an unfortunate condition of the law. The most frequent of these are seller's clauses protecting against various types of business impossibility, and protecting against the obligation of delivery on credit to a buyer who has become a dubious risk. Such groups of clauses give no difficulty under the present Act, however; for the Act explicitly recognizes the impossibility clauses and provides the requisite balance to them in Section 50; and it explicitly recognizes the propriety of either party's desire for security against uncertainty of performance, in Section 45. In addition, any coverage by contract which appeals to the court as producing reasonable balance in matters not covered by the Act—such as, for instance, reasonable priority or rationing provisions in regard to outstanding commitments—would require to be regarded as pro tanto crystallizations of entirely reasonable trade practice or need. *See paragraph 2 (c) (iii).*

(7) *Will such a provision produce uncertainty in the construction of contracts in Sales transactions?*

There are two compelling reasons for the conviction that such a provision will not produce uncertainty in the construction of Sales transactions.

(a) It will not *produce* uncertainty, because there *is* uncertainty. It is at the present moment impossible to tell what a court will do with a contested provision in a lop-sided Sales contract. Draftsmen have to draft on a gamble.

(b) It will *lessen* the existing uncertainty, because it gives the draftsman a reasonable guidance as to what he may reasonably expect to sustain, and gives the court a reasonable guidance through the confused and conflicting precedents.

In addition, the provision may fairly be hoped, over the years, to lessen uncertainty not only in court, but in transactions, by encouraging the reduction of trade usage to written form. But the case for the provision stands not on this, but on the bewildering uncertainty which exists today as to when a court will read one-party language as it is written, and when it will find a way to avoid such language.

#### B. *Detail.*

(1) *Legislative Finding of Fact and Declaration of Policy.*

(a) The finding of fact and declaration of policy are, historically, almost an inherent part of statutes; their desue-

tude for a period was due in good part to their abuse. But when not abused, they have peculiar value.

(b) For from the technical standpoint they *are* inherent in a statute. It is humanly impossible to construe a statute without envisaging some situation to which the statute is conceived to be addressed; and it is also humanly impossible without envisaging a purpose or a set of purposes toward which the statute is directed.

The situation and the purposes thus have to be set up, either by the legislature or by the court. If they are left to be gathered by the court as best it can gather or imagine them, different courts are likely to see them differently. Both the need for uniformity and the need for clarity urge that the situation and the purposes be stated with care, to guide all lawyers and courts alike.

No less is the general relation between the Act and sets of special rules which purport to displace it the proper subject of a general declaration of policy. The matter turns on the entire situation and the entire purpose of the Act. All but a few of the individual sections and sub-sections are subject as of course to be displaced one by one, by specific bargain; the question here goes to the displacement of the whole balanced background of all specific bargain, and the substitution therefor of another whole background. Only a declaration of policy can make reasonably clear what kind of substitution of background the Act seeks to encourage, and what kind it seeks to discourage.

(2) *Question for the court.* The total estimate of the effect of a body of provisions, in terms of balance, is a job for which a court is peculiarly fitted. The question of whether the provisions fit the circumstances of a particular trade is one which a special merchants' jury can best judge, under Section 51-C. But the merchant runs some risk of accepting a provision merely as it is written because it is so written; and he has little training in sizing up a transaction from both ends at once, to reach a view of balance. As against this stands the fact that the issue to be tried is the issue of balance; and given that focus of attention, the merchants' jury would seem an adequate tribunal.

*But many cases, under the section, would be wholly for the court; notably purchases by consumers of articles commonly bought on complex forms. And if the policy of the section be approved, it may need explicit extension to cover contracts companioning the sales con-*

tract, as in the case of the sometimes startling purchase-money mortgages.

(3) *Constitutionality*. There are a number of reasons for feeling that no constitutional questions are involved in this section.

(a) Severe legislative restriction on minimum terms of particular types of transaction, where abuses have appeared, are familiar, and constitutional. Standard insurance policies are one instance; the Wisconsin statute on warranty and remedy in sales of farm machinery is another.

(b) The section is built in terms of testing the reality of consent, not in terms of limiting freedom of contract. Reality of consent has always been subject to testing by appropriate legal measures. The measures of the section are appropriate and reasonable, fit the facts of life, and show their theory on their face.

(c) The section builds a way through a confusion of case-law which itself leaves little doubt that Courts would welcome a clue to combining certainty and justice in these cases. Legislation felt by courts to be helpful in the work of the courts is very rarely held unconstitutional.