University Jean Moulin Lyon III 2023 Comparative Contract Law		
Pages	**Topic**	**Reading**
	Topic 1	**Introduction and Overview**
1	01A	Laidlaw v. Organ, New French Civil Code 1104
1	01B	Rowan 2016 French Contract Law: Good Faith Negotiations
4	01C	Pre-contractual negotiations new 2016 French Civil Code Provisions
3	01D	Hadley v. Baxendale
2	01E	Winn, American Legal Realism as Pragmatism, Hadley and Civil Code
22	01F	Winn Briefing Cases Issue Spotter Exams UJM-L3 2021
3	01G	Winn Comp Contract Issue Spotter Hypotheticals 2021
36	Total	
	Topic 2	**Common Law versus Civil Law**
17	02A	Dainow, Introduction to Civil and Common Law
1	02B	Wells, Civil vs Common Law Chart
1	02C	Baker, Form of Writ
4	02D	Social and Economic Globalization
4	02E	World Bank Doing Business Report 2006 excerpt
6	02F	World Bank Doing Business Report 2016 excerpt
2	02G	2023 World Bank Launches New "Business Ready" Indicators
35	Total	
	Topic 3	**Comparative Contract Law**
30	03A	Farnsworth, Chapter on Comparative Contract Law
30	Total	
	Topic 4	**Bilateral Contracts**
8	04A	Leonard vs. PepsiCo
3	04B	Campbell Soup v. Wentz
2	04C	Hill v. Gateway
7	04D	Bragg v. Linden Labs
2	04E	Wood v. Lucy, Lady Duff Gordon
5	04F	Cause vs Consideration
27	Total	
	Topic 5	**Unilateral Contracts, Reliance**
3	05A	Meldrum: French Contract Law: Classification
4	05B	Bilateral vs Unilateral Contract Manufactured Difficulties
4	05C	Executing Contracts in France 2021
2	05D	Unilateral Contracts: French vs American Definition
2	05E	Restatement 2d Contracts Section 90 + Commentary
3	05F	Ruud vs. Great Plains Supply
18	Total	
	Topic 6	**Contracts of Adhesion, Arbitration**
20	06A	Winn & Webber, Unfair versus Unconscionable
5	06B	Brower v. Gateway
14	06C	New York Times Arbitration Everywhere
8	06D	Hubbert v. Dell
47	Total	
	Topic 7	**From Comparative Contracts to Global Governance**
5	07A	Gordley French Law Contrat Cadre 2001
3	07B	Honnold Framework Contracts under CISG
4	07C	Winn Framework Contract Summary 20-March-2020
11	07D	HBR New Approach to Contracts 2019
8	07E	Rise of Platform Economy EU Consumer Law 2019
20	07F	Winn Amazon Platform Private Regulator 2016
51	Total	
244	**Total**	

Art. 1104 Contracts must be negotiated, formed and performed in good faith. This is a matter of public policy.
Art. 1104 Les contrats doivent être négociés, formés et exécutes de bonne foi. Cette disposition est d'ordre public.

Laidlaw v. Organ
Supreme Court of the United States, 1817
15 U.S. 178

[Plaintiff Organ] filed his petition ... in the court below, stating, that on the 18th day of February, 1815, he purchased of [defendant Laidlaw] 111 hogsheads of tobacco, as appeared by the copy of a bill of parcels annexed, and that the same were delivered to him by the said Laidlaw & Co., and that he was in the lawful and quiet possession of the said tobacco when, on the 20th day of the said month, the said Laidlaw & Co., by force, and of their own wrong, took possession of the same, and unlawfully withheld the same from the petitioner, notwithstanding he was at all times, and still was, ready to do and perform all things on his part stipulated to be done and performed in relation to said purchase, and had actually tendered to the· said Laidlaw & Co. bills of exchange for the amount of the purchase money, agreeably to the said contract. . . . Wherefore the petition prayed that the said Laidlaw & Co. might be cited to appear and answer to his plaint, and that judgment might be rendered against them for his damages, etc. .....

[T]he cause was tried by a jury, who returned the following verdict, to wit: "The jury find for [the buyer Organ], for the tobacco named in the petition, without damages, payable as per contract." Whereupon the court rendered judgment "that [Organ] recover of [Laidlaw] the said 111 hogs-heads of tobacco . . . and ordered, that the marshal deliver the said tobacco to [Organ], and that he have execution for his costs aforesaid, upon [Organ's] depositing in this court his bills of exchange for the amount of the purchase money .... "

[Laidlaw] filed the following bill of exceptions, to wit: . . . [O]n the night of the 18th of February, 1815, Messrs. Livingston, White, and Shepherd brought from the British fleet the news that a treaty of peace had been signed at Ghent by the American and British commissioners, con-tained in a letter from Lord Bathurst to the Lord Mayor of London, published in the British newspapers, and that Mr. White caused the same to be made public in a handbill on Sunday morning, 8 o'clock, the 19th of February, 1815, and that the brother of Mr. Shepherd, one of these gentlemen, .and who was interested in one-third of the profits of the purchase set forth in [Organ's] petition, had, on Sunday morning, the 19th of February, 1815, communicated said news to [Organ]; that [Organ], on receiving said news, called on Francis Girault, (with whom he had been bargaining for the tobacco mentioned in the petition, the evening previous) said Francis Girault being one of the said house of trade of Peter Laidlaw & Co., soon after sunrise on the morning of Sunday, the 19th of February, 1815, before he had heard said news. Said Girault asked if there was any news which was calculated to enhance the price or value of the article about to be purchased; and that the said purchase was then and there made, and the bill of parcels annexed to the plaintiff's petition delivered to [Organ] between 8 and 9 o'clock in the morning of that day; and that in consequence of said news the value of said article had risen from 30 to 50 per cent. There being no evidence that the [Organ] had asserted or suggested anything to the said Girault, calculated to impose upon him with respect to said news, and to induce him to think or believe that it did not exist; and it appearing that the said Girault, when applied to, on the next day, Monday, the 20th of February, 1815, on behalf of [Organ], for an invoice of said tobacco, did not then object to the said sale, but promised to deliver the invoice to [Organ] in the course of the forenoon of that day; the court charged the jury to find for [Organ] ....

MARSHALL, C.J. The question in this case is, whether the intelligence of extrinsic circumstances, which might influence the price of the commodity, and which was exclusively within the knowledge of the vendee, ought to have been communicated by him to the vendor? The court is of opinion that he was not bound to communicate it. It would be difficult to circumscribe the contrary doctrine within proper limits, where the means of intelligence are equally accessible to both parties. But at the same time, each party must take care not to say or do anything tending to impose upon the other. The court thinks that the absolute instruction of the judge was erroneous, and that the question, whether any imposition was practised by the vendee upon the vendor ought to have been submitted to the jury. For these reasons the judgment must be reversed .. . .

Jane K. Winn
UJM-Lyon 3 2020

Solene Rowan, The new French law of contract, International & Comparative Law Quarterly (2007)

Freedom of contract is a longstanding and uncontroversial principle in French law. It did not however appear in the 1804 Code. The new Code recognises it explicitly for the first time. It is symbolically placed as the outset, as the very first rule immediately after the definition of contract, to mark its significance.

The principle of the binding force of contracts is also formally recognised and given a prominent place in the new Code. Article 1103 reuses almost identically the near sacrosanct wording of old article 1134, paragraph 1, that legally formed agreements have the force of law between the parties. This means that contracts must be given effect and adhered to: *pacta sunt servanda*, one must perform that which one has promised. It is a principle that is perceived to promote legal certainty and justify the centrality of specific performance as a remedy for breach.

More innovative is the new prominence given to the principle of good faith. In addition to its new location amongst the key principles that govern contracts, its scope has been expanded. Article 1104 provides that contracts must be 'negotiated, formed and performed in good faith'; this is described as 'a matter of public policy'. Whereas the 1804 Code simply stated that contracts should be performed in good faith, the reforms have codified case law that had extended the principle to the pre-contractual negotiations and formation stages.

Pre-contractual negotiations – a new codified French regime

reedsmith.com/en/perspectives/2017/02/precontractual-negotiations--a-new-codified-french

Authors: Andrew Tetley Aurélie Lopez

New French contract law provisions are now in force and apply to any contracts concluded after 1 October 2016.

In previous related client alerts, we outlined this legal revolution in France and described the new recognition of hardship under French contract law.

This client alert focuses on the new rules governing pre-contractual negotiations, which draw inspiration from notions of good faith. The new provisions in part codify existing case law, and in part effect a departure from the previous law.

Background

When the French civil code was first adopted in 1804, it did not specifically address pre-contractual negotiations. One explanation often given is that in the late seventeenth century, negotiation periods were generally short, so not worthy of legislative attention.

In due course, the subject matter gained the attention of French courts adjudicating claims relating to the breakdown of lengthy negotiations. The legislative gap was filled by the courts. Certain solutions developed by the courts have now been codified at articles 1112 et seq of the new French civil code. The French reform also introduces two general duties binding on the negotiating parties.

(a) Freedom to negotiate – subject to good faith

Article 1112 provides that parties have complete freedom to initiate, conduct and break off negotiations. However, this freedom is restricted by a specific requirement of good faith contained in article 1112 itself.
Prior to the reform, the French civil code only made reference to the requirement of good faith in the performance of contracts.

This requirement of good faith for pre-contractual negotiations is mandatory. Parties cannot contract out of it. However, the exact meaning of good faith in this context is likely to be a slippery concept until the courts have had the opportunity to decide some cases.

(b) Failure of negotiations – no loss of chance

While parties are free to break off negotiations, they may be liable if they wrongfully break them off. It is not the breaking off that is sanctioned here but the manner in which it is undertaken, examined through the prism of good faith.

However, adopting the approach previously developed by the French Cassation Court, article 1112 circumscribes recoverable losses in case of the wrongful breakdown of negotiations. Article 1112 specifically provides that in any assessment of damages, there can be no compensation for the loss of advantages expected from the contemplated contract that did not eventuate.

(c) General pre-contractual duty to inform

The reform formally introduces into French law a mandatory duty to inform during negotiations. This duty is applicable to any negotiating party, whether acting in a professional capacity or not. While a duty to inform already existed under French law in certain limited circumstances – for example, under consumer laws – the reform now introduces this duty as a general obligation under French law.

The new duty is to be found in article 1112-1 of the new French civil code. The duty arises where one party has information that is decisive to the other party's consent, and where the other party is legitimately ignorant or places its trust in that party.

The duty will extend to information that has a direct and necessary link to the content of the contract or the quality of the parties. However, the estimated value of the contracted service is excluded from the duty to inform. This exclusion codifies established French Cassation Court case law in this regard.

The party claiming a breach of the duty to inform bears the onus of establishing the duty in its favour. The respondent party then bears the onus of showing that it duly informed the claimant party.

A breach of the pre-contractual duty to inform is sanctioned by damages. It may also lead to annulment of the contract if it can be shown that the other party's consent was vitiated by the wrongful failure to inform.
The duty to inform is mandatory. Parties cannot limit or exclude it. However, certain legal authors have suggested that parties may nevertheless agree on what they consider as decisive information.

(d) General obligation of confidentiality

Influenced by the principles of European contract law and the UNIDROIT principles, the French contract law reform introduces a general obligation of confidentiality protecting pre-contractual negotiations.

Article 1112-2 of the new French civil code provides for a free-standing right that disclosure of confidential information obtained during negotiations, without consent, may form the basis for an action in damages.

Comment

The codification of established case law and the introduction of new principles applicable to pre-contractual negotiations are a welcome development. However, the new legal landscape will present challenges.

On good faith in negotiations, prior to the reform French law chimed with the view of the English judge Lord Ackner who, in 2005, succinctly stated that a duty to negotiate in good faith is "unworkable in practice".1 What does this new duty herald for commercial parties? Cards-on-the-table negotiations would appear to be called for. The development here joins with a noticeable legal trend towards transparency in commercial dealings.

On the duty to inform, this will be an interesting area to follow as the courts are given fact scenarios to rule upon. The new provisions open up a large potential area of dispute, but they also firmly entrench the notion that it is still possible to validly conclude a bad deal. On any particular set of facts, the balance here may be a delicate one for courts and tribunals called upon to rule on this issue.

On confidentiality, this is a welcome innovation. Fishing expeditions for information, masquerading as negotiations, will now attract clear sanction, subject always to the inevitable challenges of proof in such areas.

Overall, the single practical takeaway from the above changes is that sophisticated parties should be putting in place a pre-agreement to anticipated negotiations, at least for those negotiations with any degree of complexity. Some aspects of the new provisions can be contractually excluded if so desired. Others can be contractually tailored or their effects potentially mitigated or defined.

While no-one can predict with certainty how the courts will develop some of these concepts, the recent codification in this area cries out for parties to 'dress up' and define the rules of courtship for prospective commercial partnerships. Where negotiations sour, or subsequent contractual performance disappoints, a failure to dress up may lead to downsides much greater than simply not holding on to your new partner.

How Reed Smith can help you

Reed Smith can assist clients through the implementation of the new French civil code and, for example, adapt their general conditions of business to accommodate and address the new legal landscape in force since 1 October 2016.

More specifically, Reed Smith can assist clients through pre-contractual negotiations, tailoring pre-contractual agreements, carrying out due diligences, and drafting complex contracts. Reed Smith can also assist clients in advising generally and, where appropriate, commencing legal action in relation to negotiations, or breaches of the new duty to inform or of confidentiality obligations.

Client Alert 2017-058

Jane K. Winn
UJM-Lyon 3 2020

Hadley v Baxendale
9 Exchequer 341, 156 Eng. Rep. 145
Court of Exchequer, 1854

At the trial before Crompton, J. [this stands for "judge" not the judge's first name], at the last Gloucester Assizes [former name for local courts in England, from the French *s'assoir* meaning to be seated], it appeared that the plaintiffs carried on an extensive business as millers at Gloucester; and that on the 11th on May, their mill was stopped by a breakage of the crank shaft by which the mill was worked. The steam-engine was manufactured by Messrs. Joyce & Co., the engineers, at Greenwich, and it became necessary to send the shaft as a pattern for a new one to Greenwich. The fracture was discovered on the 12th, and on the 13th the plaintiffs sent one of their servants to the office of the defendants, who are the well-known carriers trading under the name of Pickford & Co., for the purpose of having the shaft carried to Greenwich. The plaintiffs' servant told the clerk that the mill was stopped, and that the shaft must be sent immediately; and in answer to the inquiry when the shaft would be taken, the answer was, that if it was sent up by twelve o'clock any day, it would be delivered at Greenwich on the following day. On the following day the shaft was taken by the defendants, before noon, for the purpose of being conveyed to Greenwich, and the sum of 2l. 4s. [i.e., £2, 4 shilling, worth approximately £220 in 2020] was paid for its carriage for the whole distance; at the same time the defendants' clerk was told that a special entry, if required, should be made to hasten its delivery. The delivery of the shaft at Greenwich was delayed by some neglect; and the consequence was, that the plaintiffs did not receive the new shaft for several days after they would otherwise have done, and the working of their mill was thereby delayed, and they thereby lost the profits they would otherwise have received.

On the part of the defendants, it was objected that these damages were too remote, and that the defendants were not liable with respect to them. The learned Judge left the case generally to the jury, who found a verdict with £25 [worth approximately £2,500 in 2020] damages beyond the amount paid into Court.

Whateley [lawyer for the defendant], in last Michaelmas [autumn] Term, obtained a rule nisi for a new trial [nisi = "unless" so this was a provisional ruling that the defendant got a new trial unless the plaintiff can show why it should not be allowed], on the ground of misdirection [i.e., the judge's instructions to the jury were incorrect].

Keating and Dowdeswell [lawyers for the plaintiff] shewed cause [i.e., attempted to show why the defendant was not entitled to a new trial]. The plaintiffs are entitled to the amount awarded by the jury as damages. These damages are not too remote, for they are not only the natural and necessary consequence of the defendants' default, but they are the only loss which the plaintiffs have actually sustained. The principle upon which damages are assessed is founded upon that of rendering compensation to the injured party. This important subject is ably treated in Sedgwick on the Measure of Damages. . . The several cases, English as well as American, are there collected and reviewed. [Parke, B[aron]. The sensible rule appears to be that which has been laid down in France, and which is declared in their code—Code Civil, liv. iii. tit. iii. ss. 1149, 1150, 1151, and which is thus translated in Sedgwick: "The damages due to the creditor consist in general of the loss that he has sustained, and the profit which he has been prevented from acquiring, subject to the modifications hereinafter contained. The debtor is only liable for the damages foreseen, or which might have been foreseen, at the time of the execution of the contract, when it is not owing to his fraud that the agreement has been violated. . .]

Alderson, B[aron]. We think that there ought to be a new trial in this case; but, in so doing, we

deem it to be expedient and necessary to state explicitly the rule which the Judge, at the next trial, ought, in our opinion, to direct the jury to be governed by when they estimate the damages.

It is, indeed, of the last importance that we should do this; for, if the jury are left without any definite rule to guide them, it will, in such cases as these, manifestly lead to the greatest injustice. The Courts have done this on several occasions; and, in Blake v. Midland Railway Company, 18 Q.B. 93, the Court granted a new trial on this very ground, that the rule had not been definitely laid down to the jury by the learned Judge at Nisi Prius [court of original jurisdiction, "nisi prius" means something like "unless beforehand" in Latin]

"There are certain established rules," this Court says, in Alder v. Keighley, 15 M. & W. 117, "according to which the jury ought to find." And the Court, in that case, adds: "and here there is a clear rule, that the amount which would have been received if the contract had been kept, is the measure of damages if the contract is broken."

Now we think the proper rule in such a case as the present is this:-- 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.

Now, if the special circumstances under which the contract was actually made were 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. But, on the other hand, if these special circumstances were wholly unknown to the party breaking the contract, he, at the most, could only be supposed to have had in his contemplation the amount of injury which would arise generally, and in the great multitude of cases not affected by any special circumstances, from such a breach of contract. For, had the special circumstances been known, the parties might have specially provided for the breach of contract by special terms as to the damages in that case; and of this advantage it would be very unjust to deprive them.

Now the above principles are those by which we think the jury ought to be guided in estimating the damages arising out of any breach of contract. It is said, that other cases such as breaches of contract in the nonpayment of money, or in the not making a good title of land, are to be treated as exceptions from this, and as governed by a conventional rule. But as, in such cases, both parties must be supposed to be cognizant of that well-known rule, these cases may, we think, be more properly classed under the rule above enunciated as to cases under known special circumstances, because there both parties may reasonably be presumed to contemplate the estimation of the amount of damages according to the conventional rule. Now, in the present case, if we are to apply the principles above laid down, we find that the only circumstances here communicated by the plaintiffs to the defendants at the time of the contract was made, were, that the article to be carried was the broken shaft of a mill, and that the plaintiffs were the millers of the mill.

But how do these circumstances shew reasonably that the profits of the mill must be stopped by an unreasonable delay in the delivery of the broken shaft by the carrier to the third person? Suppose the

plaintiffs had another shaft in their possession put up or putting up at the time, and that they only wished to send back the broken shaft to the engineer who made it; it is clear that this would be quite consistent with the above circumstances, and yet the unreasonable delay in the delivery would have no effect upon the intermediate profits of the mill. Or, again, suppose that, at the time of the delivery to the carrier, the machinery of the mill had been in other respects defective, then, also, the same results would follow. Here it is true that the shaft was actually sent back to serve as a model for the new one, and that the want of a new one was the only cause of the stoppage of the mill, and that the loss of profits really arose from not sending down the new shaft in proper time, and that this arose from the delay in delivering the broken one to serve as a model.

But it is obvious that, in the great multitude of cases of millers sending off broken shafts to third persons by a carrier under ordinary circumstances, such consequences would not, in all probability, have occurred; and these special circumstances were here never communicated by the plaintiffs to the defendants. It follows therefore, that the loss of profits here cannot reasonably be considered such a consequence of the breach of contract as could have been fairly and reasonably contemplated by both the parties when they made this contract. For such loss would neither have flowed naturally from the breach of this contract in the great multitude of such cases occurring under ordinary circumstances, nor were the special circumstances, which, perhaps, would have made it a reasonable and natural consequence of such breach of contract, communicated to or known by the defendants. The Judge ought, therefore, to have told the jury that upon the facts then before them they ought not to take the loss of profits into consideration at all in estimating the damages. There must therefore be a new trial in this case.

Rule absolute. [i.e., defendant won, plaintiff did not show that that what the defendant wanted should not be allowed]

Jane K. Winn
UM-Lyon3 2020

American Legal Realism as a Form of Pragmatism

One of the themes of this course is that historical differences between the American common law legal system and the French civil law system often explains differences in modern American and French contract law. This is often, but not always, true.

The holding in *Hadley v. Baxendale* is a translation of this provision of the French Civil Code:

> Napoleonic Code 1804 Art. 1150
>
> > A debtor is only held to damages which were foreseen or which could have been foreseen at the time of the contract, when it is not by his willfulness that the obligation is not executed.
> >
> > Le débiteur n'est tenu que des dommages et intérêt qui ont été prévus ou qu'on a pu prévoir lors du contrat, lorsque ce n'est point par son dol que l'obligation n'est point exécutée.

Napoleon's Code Civil of 1804 was a codification of the Roman Emperor Justinian's *Corpus Juris Civilis* published in 529-534 CE, which in turn was a codification of Roman law dating back to the founding of the Roman Republic around 450 BCE.

In Section 4620 of the 1999 Encyclopedia of Law & Economics, Professor Eric Posner (son of the famous judge), described this holding in the following terms:

> The *Hadley* rule, which denies recovery for losses that the promisor could not ordinarily foresee, is thought to provide promisees with incentives to reveal how much they value performance, in order to give the promisor optimal with incentives to take care.

In other words, according to 20th century law & economic analysis, Section 1150 of the Napoleonic Code and the holding of *Hadley v. Baxendale* promote economic efficiency. The *Hadley* rule is still good law in the U.S. today and is still widely cited in judicial decisions.

How is it that the Second Consul of the French Republic Cambacérès (a lawyer) working with noted jurists Bigot-Préameneu Maleville, Portalis, and Tronchet under tremendous time pressure managed to come up with a rule that American social scientists still believe is the "right" rule 200 years later?

Founders of the American philosophy of Pragmatism might have an answer:

> "The opinion which is fated to be ultimately agreed to by all who investigate is what we mean by the truth, and the object represented in this opinion is the real." Charles Sanders Peirce (1839-1914)
>
> "Consider the practical effects of the objects of your conception. Then, your conception of those effects is the whole of your conception of the object." C.S. Peirce

In other words, American pragmatism rejects "Cartesian dualism" (meaning can be expressed as the opposition of two ideas such as subjective versus objective, public versus private) as well as Kantian essentialism (everything has a true nature which cannot be perceived directly but only through abstract thought) and Newtonian universalism (the world embodies timeless, universal laws of nature).

The only European philosopher to take American Pragmatism seriously is Jürgen Habermas. By contrast, American pragmatist philosopher John Dewey (1859-1952) spent two years in China (1919-1921) and had a major impact on how China perceived "modernization." Dewey believed that the mission of education should be to prepare citizens to participate in democracy, and that participating in democracy was a form of learning:

> An undesirable society is one that sets up barriers to free interaction among its members. Giving and taking orders produces results, but cannot by itself constitute sharing of purposes. To the extent that a society provides for participation of all its members on equal terms in articulating its values, and flexible readjustment of its institutions in a similar manner, then then that society is democratic. John Dewey, Democracy & Education (1916)

Justice Oliver Wendell Holmes (1841-1935) was an active member of the group of American intellectuals who established the American philosophy of Pragmatism at the end of the 20th century. Some of Holmes' contributions to American pragmatism took the form of cryptic but insightful observations about the nature of law:

> The prophecies of what the courts will do in fact, and nothing more pretentious, are what I mean by the law.[1]
>
> The common law is not a brooding omnipresence in the sky but the articulate voice of some sovereign or quasi sovereign that can be identified.[2]

One way to interpret these aphorisms would be to treat them rejecting the conventional wisdom that legal systems are made up of rules, and as asserting that legal systems are made up of people using legal rules as tools to try to solve social problems.[3] In other words, he focused squarely on the human agency of judges in describing how power is exercised within the legal system.

> You can give any conclusion a logical form. You always can imply a condition in a contract. But why do you imply it?[4]

This aphorism might be interpreted as Justice Holmes reminding us that there is always enough wiggle room in legal reasoning to make a case go one way or the other. Recognizing how much discretion judges have isn't the hard part about understanding how legal institutions work. The hard part is figuring out when judges will feel motivated to intervene and shift the outcome of a case in an unexpected direction (we will see an example of this in Justice Benjamin Cardozo's decision in *Lucy, Lady Duff-Gordon* case later in the course).

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[1] The Path of the Law 10 Harvard Law Review 457 (1897).

[2] Southern Pac. Co. v. Jensen, 244 U.S. 205, 222 (1917) (Holmes, J., dissenting).

[3] Professor Lasser of Cornell Law School reached a similar conclusion about French judges. Mitchel de S.-O.-l'E. Lasser, Judicial (Self-)Portraits: Judicial Discourse in the French Legal System 104 YALE L.J. (1995) https://digitalcommons.law.yale.edu/ylj/vol104/iss6/2

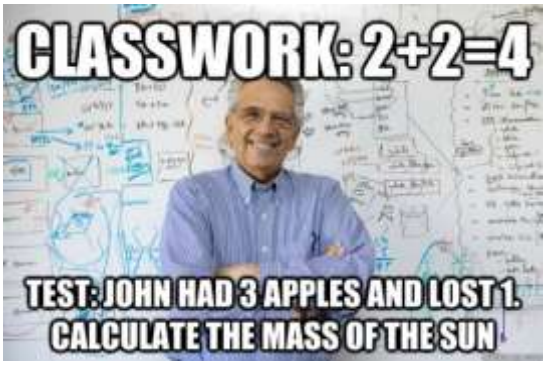
[4] The Path of the Law 10 Harvard Law Review 457 (1897).

Jane K. Winn
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21 March 2021 draft

Introduction to Briefing Cases and Answering Issue Spotter Exam Questions

I. The "Calculate the Mass of the Sun" Problem 1
II. Extract a Legal Rule from a Judicial Decision 2
A. Restatement 2d of Contracts, § 24 Offer Defined 2
B. How to Brief a Simulated Judicial Decision 4
C. Practice Briefing a Simulated Decision 8
III. Extracting the Holding from Real Cases 10
A. Restatement 2d Contracts § 164 Misrepresentation 10
B. A Real Judicial Decision that JD 1Ls Might Find Very Difficult to Brief 11
IV. Answering Exam Questions 13
A. How to Write an IRAC Exam Answer 15
B. Exam Question Based on *Taylor v. Miller* and on *Yaro v. Khan* plus Answer 17
C. Apply What You Have Learned: Exam Question Based on *Taylor v. Miller* and *Yaro v. Khan* 19
V. Outlining as the Bridge between Class and Exams 19

I. The "Calculate the Mass of the Sun" Problem



The meme about "Calculate the mass of the sun" test question in a STEM class makes a joke about how classwork/homework in STEM classes can seem pretty straightforward, but then exam questions in those classes seem much harder. If students point this out to the instructor, the instructor will feel surprised because the classwork/homework and the exam questions all seem equivalent to the instructor. That's because the instructor suffers from the "curse of knowledge" i.e., knows so much more about the subject than the students know that it is no longer possible to remember how things look from the student perspective.

In US law school, students may feel that briefing cases, Socratic method class discussions, and memorizing black letter law rules can seem pretty straightforward, but then issue spotter exam questions seem much harder. While law school instructors can see the connections between briefing cases, class discussion, memorizing rules and exam questions, they may have trouble making those connections explicit to students if they suffer from the "curse of knowledge."

The goal of this essay is to make those connections explicit.

II. Extract a Legal Rule from a Judicial Decision

A. Restatement 2d of Contracts, § 24 Offer Defined

This lesson will focus on one legal rule taken from a collection of rules named the Restatement (Second) of Contracts prepared by the American Law Institute (ALI), an influential non-profit organization founded in 1923 with the mission of improving the law. The ALI creates "restatements" of law by gathering together a panel of distinguished subject matter experts who gather together all the relevant state and federal judicial decisions then distill their holdings into a collection of clear, concise rules that resemble a statute. The first restatement of contract law was finished in 1932, but contract law continued to evolve through the process of judicial decision making, and in 1982, the second restatement of contract law was issued.

The ALI adds official commentaries to all of its restatements to insure that the rules are interpreted consistently. In order to distinguish the official rule from the commentary, it is conventional to print the text of the rule I bold. For this reason, it is common for American lawyers to refer to formal legal doctrine as "black letter law" (i.e., the part of the restatement text printed in bold).

In the Restatement (Second) of Contracts, here is the rule that defines what constitutes an offer to form a contract (in bold) followed by part of the official commentary:

> **An offer is the manifestation of willingness to enter into a bargain, so made as to justify another person in understanding that his assent to that bargain is invited and will conclude it.**
>
> Comment:
>
> a. Offer as promise. An offer may propose an executed sale or barter rather than a contract, or it may propose the exchange of a promise for a performance or an exchange of promises, or it may propose two or more such transactions in combination or in the alternative. In the normal case of an offer of an exchange of promises, or in the case of an offer of a promise for an act, the offer itself is a promise, revocable until accepted. There may also be an offer of a performance, to be exchanged either for a return promise (§ 55) or for a return performance; in such cases the offer is not necessarily a promise, but there are often warranties or other incidental promises.
>
> Illustration:
>
> 1. A says to B, "That book you are holding is yours if you promise to pay me $ 5 for it." This is an offer empowering B, by making the requested promise, to make himself owner of the book and thus complete A's performance. In that event there is also an implied warranty of title made by A.

In order for a plaintiff to win a lawsuit, the plaintiff must make out a "prima facie" case (prima facie is Latin for "at first sight.") A prima facie case says what the applicable legal rule is and shows that when that rule is applied to the facts of the dispute without considering the defendant's response, the result would be that the plaintiff wins.

In order to figure out whether or not the plaintiff has made out a prima facie case, it is first necessary to break the applicable legal rule down into "elements" (i.e., sub-rules that when combined make up the applicable legal rule). Then the plaintiff must assert that from within the facts of the dispute, the plaintiff can prove specific facts to justify the application of each element of the rule to this dispute.

In order to figure out whether a plaintiff can prove that an offer to form a contract was made, the plaintiff will need to break the rule in Restatement 2d Contracts § 24 into its constituent elements. There is no official, authoritative, definitive way to do this, but most people seem to think that Restatement 2d Contracts § 24 has three elements. (Note: if Restatement 2d Contracts § 24 were subdivided into more than three elements, then that would increase the number of facts that the plaintiff would have to prove to win the case.)

Before going on to the next section, please take a moment to try break the rule in Restatement 2d Contracts § 24 into three elements:

Element 1:

Element 2:

Element 3:

If you really tried to do this, then you should have discovered it really isn't obvious how this should be done. Although there do exist some legal rules for which all lawyers agree about how they should be broken into rules, those for which there is only partial consensus is much greater precisely because it can be quite difficult to break rules into elements.

If it is hard for judges and lawyers to agree on how a rule should be broken into elements so the facts of the case can be organized according to whether or not they justify the application of the rule to a given dispute, it is even harder for citizens serving on juries who lack any formal legal training. In an effort to reduce some of this confusion, some states have published standard jury instructions in an effort to make it easier for judges and lawyers to explain what facts must be proven in order for a plaintiff to prevail over a defendant.

But even standard form jury instructions designed to make it easier for juries to engage in legal reasoning may not explicitly break legal rules down into elements. For example, here is the 2019 edition of the Washington State Pattern Jury Instructions for the issue of "mutual assent" in contract law:

> In order for there to be mutual assent, the parties must agree on the essential terms of the contract, and must express to each other their agreement to the same essential terms.

This is the only standard jury instruction in Washington State designed to help jurors figure out what facts a plaintiff must prove in order to establish that an offer to form a contract was made. But ask you can see, this rule refers to mutual assent rather than offer, and even for mutual assent, does not make it very clear what facts a plaintiff would have to prove to prevail.

California has taken a different approach. It started with the "black letter rule" provided by Restatement 2d Contracts § 24 then made it explicit how that rule might be broken into three elements:

> Judicial Council of California Civil Jury Instructions § 307 Contract Formation—Offer (2020 edition)
>
> Both an offer and an acceptance are required to create a contract. [*Name of defendant*] contends that a contract was not created because there was never any offer. To overcome this contention, [*name of plaintiff*] must prove all of the following:
>
> 1. That [*name of plaintiff*] communicated to [*name of defendant*] that [*he/she/nonbinary pronoun/it*][1] was willing to enter into a contract with [*name of defendant*];
>
> 2. That the communication contained specific terms; and
>
> 3. That, based on the communication, [*name of defendant*] could have reasonably concluded that a contract with these terms would result if [*he/she/nonbinary pronoun/it*] accepted the offer.
>
> If [*name of plaintiff*] did not prove all of the above, then a contract was not created.

One goal of this essay is to teach you a system for starting with primary legal materials that look more like the Washington State standard jury instructions then converting them into something that looks more like the California standard jury instructions. In this essay, rules presented in a form similar to that used by Washington State to describe mutual assent will be referred to as "amalgamated" in the sense of being made up of many different elements while rules in a form similar to that used by California to describe what constitutes an offer will be referred to as "basic" in the sense of having been broken down into their constituting elements.

Law students need to have some method for boiling amalgamated rules down into basic rules in order to answer "issue spotter" exam questions. This is because while it may be possible to use an amalgamated version of a legal rule in a legal research memo, that version of a rule is too complex and bulky to use when writing answers to exam questions within the allotted time.

B. How to Brief a Simulated Judicial Decision

The challenge law students face as they prepare to take law school issue spotter exams is not just how to break down the relatively of clear, concise rules found in ALI restatements into elements, but also how to extract legal rules from judicial decisions so that the legal rule can be broken down into elements.

Sometimes it is easy to extract a clear legal rule from a judicial decision, but often it is not easy. (If it were always easy, there would be no need for the ALI to create restatements.) This essay begins explaining how the process of extracting a legal rule from a judicial decision works by using a simulated (fake) judicial decision designed to make the embedded rule very easy to find. In the next section, the process will be repeated with a real judicial decision.

In this simulated decision, the judge makes the application each element of Restatement 2d Contracts § 24 to the facts of the dispute absolutely explicit. In real judicial decisions, judges usually do not make each step in their analysis so explicit.

[1] "It" here would be the correct pronoun for referring to legal persons such as a corporation or government agency.

Tina Taylor, Plaintiff v. Matthew Miller, Defendant

312 New Dakota Dist. Ct. 1234 (2014)

Goode, J.

This case arises out of an alleged agreement to sell a Saint Bernard dog for $2,000. On May 1, 2014, Tina Taylor filed suit in Gilbert County claiming she had formed a contract for the purchase and sale of Matthew Miller's St. Bernard and that Miller had breached the contract by refusing to turn over the dog and accept the purchase price when she tendered it. On May 15, Miller filed a reply, denying that any contract had ever been formed. Having considered the evidence submitted and legal arguments made by the parties at trial, the Court now finds that no contract was formed.

Taylor and Miller were next-door neighbors in Helston, New Dakota for many years, and shared a fondness for dogs. Taylor owns a poodle named Cupcake and Miller owns a St. Bernard named Heidi which is the dog at issue in this case. In addition to seeing each other in and around their houses, Taylor and Miller often performed dog-sitting services when one or the other of them was out of town, and often ran into teach other in a nearby public park when out walking their dogs. It was in the context of this friendship that Taylor learned some months ago that Miller would be moving away from Helston to Phoenix, Arizona in April 2014. Miller shared with Taylor his concern that Heidi would have trouble adapting to the hot climate of Phoenix, Arizona.

Sometime around March 1, 2014, Miller and Taylor ran into each other in the park while out walking their dogs. They sat down together on a park bench and discussed Miller's preparations for his upcoming move to Phoenix. Miller and Taylor both agree that Miller said, "I'd consider leaving Heidi here in Helston if I knew she'd be loved and I got paid the $2,000 that I originally paid for her when she was a puppy." They also both agree that Taylor replied, "Sounds good to me."

On March 31—the day before Miller was scheduled to move to Phoenix—Taylor appeared at Miller's front door with $2,000 in cash and asked Miller to give Heidi to her. Miller was surprised by Taylor's tender of $2,000 and request for Heidi. He explained that he'd checked with other dog owners in Phoenix and learned that it was possible for St. Bernard's to adapt to the climate with minor accommodations, and so decided to take Heidi with him when he moved. Taylor was surprised by Miller's response, and retorted, "A deal is a deal. You need to take the $2,000 and give me Heidi before you leave because that's what we agreed to do." After Miller persisted in his refusal to take the money or turn over the dog, this lawsuit followed.

In order to create a contract, the parties must manifest to each other their mutual assent to the same bargain at the same time. The issue presented in this case is whether the statement by Miller, "I'd consider leaving Heidi here in Helston if I knew she'd be loved and I got paid the $2,000 that I originally paid for her when she was a puppy" was his offer to sell Heidi to Taylor for a loving home and $2,000.

The Restatement (Second) of Contracts § 24 defines an offer in the following terms, "…the manifestation of willingness to enter into a bargain, so made as to justify another person in understanding that his assent to that bargain is invited and will conclude it." In order to prevail, Taylor will have to show that:

Miller was manifesting his willingness to enter into a contract when he spoke and not simply reporting current thoughts about how best to help Heidi cope with his impending move to Phoenix;

Miller's manifestation of willingness to enter into a contract contained specific terms that were communicated to Heidi; and

Taylor was justified in understanding that her assent to a bargain was invited.

Illustration 1 to § 24 provides an example of a simple sentence that constitutes an offer to form a contract: "That book you are holding is yours if you promise to pay me $5 for it." If we compare what Miller said to this sentence, it is clear that he was merely expressing his current thinking about how best to help his dog cope with his impending move, not inviting Taylor to form a purchase and sale contract for a dog. He said he would "consider leaving Heidi" if he knew she'd be loved and he got his $2,000, not that he would definitely give her up if Taylor promised to love her and pay $2,000.

Contract law permits the parties to establish a legal framework governing their respective rights and obligations, and courts in this state do not lightly reach the conclusion that the parties intended to establish such a framework. In the event of ambiguity surrounding the parties' intentions to form a contract based on the undisputed language of their communications and in the absence of special circumstances that would give an unexpected meaning to the parties' words, we must find that no contract was formed.

Because the Court concludes that what Miller said was not an offer, we do not need to reach the issue of whether the terms communicated to Taylor were specific enough and whether what Taylor said in response constituted an acceptance. However, it is worth noting that even if Taylor had been justified in thinking that Miller was offering to form a contract, her statement "Sounds good to me" would not constitute language clearly signifying acceptance of an offer. Rather, like Miller's original statement, it is information about how Taylor felt after hearing Miller's thoughts about how to help Heidi cope with his impending move.

For the foregoing reasons, the Plaintiff's claim of breach of contract is denied and judgement is entered for the Defendant.

***

There is no universal consensus among law school instructors about the best way to brief a case to prepare for class. The situation is complicated further by the fact that many law school instructors believe, given the lack of consensus among faculty members, it is probably best for each student to work out for themselves their own system for briefing cases. This essay takes the opposite approach: given the lack of consensus, this essay teaches one specific method for briefing cases that focuses on what matters most to students (e.g., getting the best grades possible as efficiently as possible) rather than what may be of more interest to instructors (e.g., sophistication and depth of class discussion). This essay is designed to give you a benchmark you can use to measure the quality of other methods of preparing for class discussion and exams that you learn about later rather than persuade you that this is the best method for all students to use.

If there is no universal consensus regarding how a case should be briefed for class discussion or outlining purposes, there is even less consensus regarding how "issue statements" should be drafted. The very

wooden, mechanical formula used here is designed to make it possible for students to engage in "deliberate practice"[2] until they feel confident they can distinguish an issue statement from other elements of legal reasoning.

In order to create a "case brief" the following information needs to be extracted from the case:

Title & Citation:

Facts: [Background Facts] [Key Facts]

A "key" fact is a fact that if it were changed, the outcome of the case (who wins and who loses) of the case would be reversed. The rule element that is matched up with the key fact is the "rule element in dispute." The combination of the key fact(s) and rule element in dispute form the pivot around which the analysis in the case turns.

Background facts are merely helpful in understanding the nature of the dispute, and should be kept to an absolute minimum in a case brief.

Legal Rule Broken Down into Elements: [E1] [E2] [E3]

Rule Element in Dispute: the parties usually agree that the plaintiff has in fact proven most of the facts required to make out most of the elements of a prima facie case, but disagree about whether or not the facts require to apply a specific element have been proven. Because the plaintiff cannot win unless the plaintiff proves that the court is justified in applying every single element of the rule, not just most elements, the failure to establish just one element is enough to defeat a plaintiff. The rule element associated with the disputed fact is the "rule element in dispute" and the disputed fact is the "key fact."

Legal Issue: [Whether/When] [Rule element in dispute] [Party1] [Party2][Key fact] (organized in some way that makes sense linguistically)

For the sake of clarity and consistency, legal issues will be expressed using a rigid formula in this essay. The formula is:

WHETHER is the first word of the issue in order to express a question for a judge to answer

After WHETHER comes a short sentence that incorporates the rule element in dispute and identifies the parties to the dispute

WHEN marks the transition from applicable law to key facts

Holding/Decision: [Yes/Maybe/No]

Rationale/Justification: This is optional, not all judicial decisions provide an explicit rationale/justification. A judge may add a rationale/justification to make the reasoning more persuasive, but the ruling is effective even if no rational/justification is provided.

Applying this case brief formula to the simulated (fake) judicial decision presented above, here is the result:

Title & Citation: Taylor v. Miller, 312 New Dakota Dist. Ct. 1234 (2014)

[2] See generally, Deliberate Practice https://en.wikipedia.org/wiki/Practice_(learning_method)#Deliberate_practice

Facts: [Background][3] Miller and Taylor each had a dog and knew each other well; Miller was planning to move away and was worried his dog Heidi would not be happy in the new location.

[Key fact] Miller said to Taylor "I'd consider leaving Heidi here in Helston if I knew she'd be loved and I got paid the $2,000 that I originally paid for her when she was a puppy."

[Background] But he later decided to take Heidi with him when he moved. When Taylor tried to give him $2,000 and take Heidi, Miller refused to give up the dog.

Legal Rule broken down into elements: [E1: An offer is a manifestation of intention to be bound to a bargain] [E2: specific terms are transmitted] [E3 a similar manifestation of intention to be bound from the other person.]

Issue: [Whether/When] **WHETHER** [Party1] a dog owner] [Rule element in dispute] manifests intent to be bound to sell a dog to [Party2] his friend **WHEN** [Key fact] he said "I'd consider leaving my dog here with you if I knew she'd be loved and I got paid the $2,000 that I originally paid for her when she was a puppy"?

Holding: [Yes/Maybe/no] NO

Rationale: "In the event of ambiguity surrounding the parties' intentions to form a contract based on the undisputed language of their interaction and in the absence of special circumstances that would give a special meaning to the parties' words, we must find that no contract was formed."

C. Practice Briefing a Simulated Decision

Before moving on to real judicial decisions, here is another simulated (fake) judicial decision you can use to test you own understanding of how to use the case brief formula:

Yves Yaro, Plaintiff v. Kate Khan, Defendant

321 New Dakota Dist. Ct. 1432 (2015)

Goode, J.

This case arises out of an alleged agreement to sell a painting for $8,000. On March 10, 2015, Yves Yaro filed suit in Gilbert County claiming he had formed a contract for the purchase and sale of Kate Khan's Sebastian Barrow painting and that Khan had breached the contract by refusing to accept the purchase price and deliver the painting. On March 20, Khan filed a reply, denying that any contract had ever been formed. Having considered the evidence submitted and legal arguments made by the parties at trial, the Court finds a contract was formed, and orders Khan to deliver the painting in exchange for Yaro's payment of $8,000.

Yaro and Khan have known each other for many years, having been class mates at New Dakota State University where Khan majored in electrical engineering and Yaro majored in art history. In 2014, Khan's widowed uncle Milton Mayer passed away, and having no children of his own, left his entire estate to Khan. Among the things Khan inherited from her Uncle Milton was the Sebastian Barrow painting, No. 3 in Red. As part of the process of settling Uncle Milton's estate, the painting had been appraised at $8,000,

[3] The distinction between background and key facts is not one that is made outside of helping students prepare for law school exams because it is not a part of legal reasoning per se. So students should *NEVER* add [Background] or [Key fact] labels to their work on actual law school exams.

and the parties agree that this appraisal accurately reflects the painting's current market value. Yaro, who is an accomplished art dealer in River City, New Dakota, had returned to Helston, New Dakota on January 28, 2015 to attend a 10th college reunion planning committee meeting. While he was in Helston, he stopped by to visit Khan who was now living in Uncle Milton's house which she had inherited and was in the process of remodeling.

When Yaro was in Khan's house, he noticed the Sebastian Barrow painting and asked Khan whether or not she'd be interested in selling it. Khan told Yaro that she had never been fond of the painting because it was in the style of abstract impressionism which she did not like and furthermore, the red color now clashed with the turquoise and coral colors she was using for the redecoration. Yaro said he'd be happy to pay the appraised value any time Khan wanted to sell, but Khan said that it was too soon after Uncle Milton's death for her to part with any of his possessions.

On February 1, Khan emailed the following question to Yaro after he had returned to River City, "Redecorating is more expensive than anticipated. Will you buy the Barrow for $8,000 as discussed?" Yaro immediately replied by email, "Yes." But when Yaro showed up at Khan's house in Helston the following day with $8,000 in cash, Khan told him she'd figured out a different way to pay for the redecorating and didn't want to sell the painting after all. Yaro responded by filing this lawsuit on March 10.

In order to create a contract, the parties must manifest to each other their mutual assent to the same bargain at the same time. *Taylor v. Miller, 312 New Dakota Dist. Ct. 1234 (2014)* The issue presented in this case is whether the question contained in the February 1 email by Khan, "Redecorating is more expensive than anticipated. Will you buy the Barrow for $8,000 as discussed?" constitutes her offer to sell the Sebastian Barrow No. 3 in Red painting to Yaro for $8,000.

The Restatement (Second) of Contracts § 24 defines an offer in the following terms, "…the manifestation of willingness to enter into a bargain, so made as to justify another person in understanding that his assent to that bargain is invited and will conclude it." In order to prevail, Khan must demonstrate:

- Khan was manifesting her willingness to sell the painting to Yaro and not merely making an inquiry that might later lead to an offer to form a contract;
- Yaro was justified in understanding that his assent to a bargain was invited; and
- Yaro's assent to the bargain would form a binding contract.

Illustration 1 to § 24 provides an example of a simple sentence that constitutes an offer to form a contract: "That book you are holding is yours if you promise to pay me $ 5 for it." If we compare what Khan said to this sentence, it is clear that she was making a similar offer to form a contract, and not merely making an inquiry that might later lead to an offer.

Although courts in this state do not lightly reach the conclusion that the parties intended to use contract law to establish a new legal mandate governing their respective rights and obligations, once it is clear that the parties have entered into a contract, then they are bound to perform as agreed. In this case, Khan and Yaro had known each other for many years, and Khan was well aware that Yaro was a professional art dealer who made a living buying and selling paintings. On January 28, Khan and Yaro engaged in a detailed discussion regarding a fair price for the painting, Yaro's interest in purchasing it and Khan's ambivalence about selling it. On February 1, Khan sent an email explaining why she had overcome her ambivalence about selling it, and asking Yaro whether he was still willing to buy it for the appraised

value as discussed on January 28. Because the exchange of emails took place within the general circumstances of the parties' long acquaintance and the specific circumstances of the parties' January 28 discussions, it is clear that Khan was offering to sell the painting to Yaro for $8,000. Yaro unambiguously accepted the offer by reply email, forming the contract.

When Yaro arrived in Helston the following day to pay Khan the $8,000 in cash and take delivery of the painting, Khan informed Yaro that she'd had a change of heart about selling the painting because she'd figured out a different way to pay for remodeling Uncle Milton's house. The fact that Khan later experienced seller's remorse does not change the status of her email the day before, nor invalidate the contract that was formed when Yaro accepted her offer.

For the foregoing reasons, the court finds that Defendant breached the purchase and sale agreement with the Plaintiff and the Plaintiff is awarded possession of the painting in exchange for payment of $8,000.

Yaro Khan Brief

Title & Citation:

Facts: [Background] [Key]

Legal Rule Broken Down into Elements: [E1] [E2] [E3]

Legal Issue: [Whether/When] [Rule element in dispute] [Party1] [Party2] [Key fact(s)]

Holding/Decision: [Yes/Maybe/No]

Rationale:

III. Extracting the Holding from Real Cases

The two simulated judicial decisions above were designed to be easy to brief. Real judicial decisions are often very difficult to brief because the judge do not always make every step in their legal reasoning explicit. The reason judges may skip some steps in the legal reasoning is that judges expect the lawyers reading the decision to be able to infer the missing steps. But if a student has just begun to study law or is not already familiar with the rule being applied, then it can be very hard to infer the missing steps. The case below illustrates very clearly how judges can skip a lot of steps in the legal analysis.

A. Restatement 2d Contracts § 164 Misrepresentation

The holding in the case below is based on a legal rule that is closely related to the following black letter law rule.

> Restatement of Contracts 2d § 164 (1): If a party's manifestation of assent is induced by either a fraudulent or a material misrepresentation by the other party upon which the recipient is justified in relying, the contract is voidable by the recipient.

Misrepresentation is the formal legal term for what people who have not attended law school call "lying." "Voidable" here means that the party who is the victim of the misrepresentation may choose whether or not to perform the contact. If the victim chooses not to perform, then any performance on either side of the contract has to be reversed in order to put the parties in a position that is as close as possible to where

they were before the contract was formed. The plaintiff in the case below is not asking to have the contract voided, however, but instead is asking the other party to pay for repairs to the house.

Although at 42 words, the Restatement of Contracts 2d § 164 (1) is not much longer than Restatement 2d Contracts § 24 at 33 words, most lawyers would consider it to be a much more complex rule with many more elements. Here are the California Civil Jury Instructions for this kind of claim by a plaintiff:

> [*Name of plaintiff*] claims that [*name of defendant*] made a false representation that harmed [*him/her/nonbinary pronoun/it*]. To establish this claim, [*name of plaintiff*] must prove all of the following:
>
> 1. That [*name of defendant*] represented to [*name of plaintiff*] that a fact was true;
>
> 2. That [*name of defendant*]'s representation was false;
>
> 3. That [*name of defendant*] knew that the representation was false when [*he/she/nonbinary pronoun*] made it, or that [*he/she/nonbinary pronoun*] made the representation recklessly and without regard for its truth;
>
> 4. That [*name of defendant*] intended that [*name of plaintiff*] rely on the representation;
>
> 5. That [*name of plaintiff*] reasonably relied on [*name of defendant*]'s representation;
>
> 6. That [*name of plaintiff*] was harmed; and
>
> 7. That [*name of plaintiff*]'s reliance on [*name of defendant*]'s representation was a substantial factor in causing [*his/her/nonbinary pronoun/its*] harm.

So a plaintiff would have to find "key facts" for each of these seven elements. If the plaintiff can provide a plausible interpretation for doing so, it may be possible to recycle some facts so that they can be used as "key facts" for more than one element. Nevertheless, it should be clear the plaintiff will have a lot of facts to prove in order to make out a claim for intentional misrepresentation.

B. A Real Judicial Decision that JD 1Ls Might Find Very Difficult to Brief

Here is a famous case in which the judge ruled against the plaintiff, holding that the plaintiff had not offered enough key facts to justify the application of the intentional misrepresentation rule. This real decision is actually shorter than the simulated decisions in the preceding section, something which is very unusual. Yet we just saw that the "black letter rule" that the court is applying is more complex. A law student might reasonably wonder how all that complexity could be reduced to the following short opinion. A law student trying to brief this decision might be even more frustrated trying to identify the actual sentence in this case that constitutes the "holding" of the case.

Neil W. Swinton v. Whitinsville Savings Bank

311 Mass. 677 (1942)

Qua, J. The declaration alleges that on or about September 12, 1938, the defendant sold the plaintiff a house in Newton to be occupied by the plaintiff and his family as a dwelling; that at the time of the sale the house "was infested with termites, an insect that is most dangerous and destructive to buildings"; that the defendant knew the house was so infested; that the plaintiff could not readily observe this condition upon inspection; that, "knowing the internal destruction that these insects were creating in said house," the

defendant falsely and fraudulently concealed from the plaintiff its true condition; that the plaintiff at the time of his purchase had no knowledge of the termites, exercised due care thereafter, and learned of them about August 30, 1940; and that, because of the destruction that was being done and the dangerous condition that was being created by the termites, the plaintiff was put to great expense for repairs and for the installation of termite control in order to prevent the loss and destruction of said house.

There is no allegation of any false statement or representation, or of the uttering of a half truth which may be tantamount to a falsehood. There is no intimation that the defendant by any means prevented the plaintiff from acquiring information as to the condition of the house. There is nothing to show any fiduciary relation between the parties, or that the plaintiff stood in a position of confidence toward or dependence upon the defendant. So far as appears the parties made a business deal at arm's length. The charge is concealment and nothing more; and it is concealment in the simple sense of mere failure to reveal, with nothing to show any peculiar duty to speak. The characterization of the concealment as false and fraudulent of course adds nothing in the absence of further allegations of fact. *Province Securities Corp. v. Maryland Casualty Co. 269 Mass. 75, 92, 168 N.E. 252*.

If this defendant is liable on this declaration every seller is liable who fails to disclose any nonapparent defect known to him in the subject of the sale which materially reduces its value and which the buyer fails to discover. Similarly it would seem that every buyer would be liable who fails to disclose any nonapparent virtue known to him in the subject of the purchase which materially enhances its value and of which the seller is ignorant. See *Goodwin v. Agassiz, 283 Mass. 358, 186 N.E. 659*. The law has not yet, we believe, reached the point of imposing upon the frailties of human nature a standard so idealistic as this. That the particular case here stated by the plaintiff possesses a certain appeal to the moral sense is scarcely to be denied. Probably the reason is to be found in the facts that the infestation of buildings by termites has not been common in Massachusetts and constitutes a concealed risk against which buyers are off their guard. But the law cannot provide special rules for termites and can hardly attempt to determine liability according to the varying probabilities of the existence and discovery of different possible defects in the subjects of trade. The rule of nonliability for bare nondisclosure has been stated and followed by this court in *Matthews* v. *Bliss*, 22 Pick. 48, 52, 53, *Potts v. Chapin, 133 Mass. 276*, *Van Houten v. Morse, 162 Mass. 414, 38 N.E. 705*, *Phinney v. Friedman, 224 Mass. 531, 533, 113 N.E. 285*, *Windram Manuf. Co. v. Boston Blacking Co. 239 Mass. 123, 126, 131 N.E. 454*, *Wellington v. Rugg, 243 Mass. 30, 35, 36, 136 N.E. 831*, and *Brockton Olympia Realty Co. v. Lee, 266 Mass. 550, 561, 165 N.E. 873*. It is adopted in the American Law Institute's Restatement of Torts, § 551. See Williston on Contracts (Rev. ed.) §§ 1497, 1498, 1499.

The order sustaining the demurrer is affirmed, and judgment is to be entered for the defendant. *Keljikian v. Star Brewing Co. 303 Mass. 53, 55-63, 20 N.E.2d 465*.

So ordered.

When a lawyer familiar with the law of intentional misrepresentation reads this decision, the lawyer infers that the plaintiff did not prove any facts to justify the application of rule element 1 (the defendant made a representation to the plaintiff that was false). This means the defendant has to win, so the court did not feel under any obligation discussing rule elements 2-7. But the court omitted more than just rule elements 2-7. The court did not bother to state the relevant black letter law at all.

The first paragraph provides background information about the case and the third paragraph provides a rationale for the ruling. So all the "apply rule to facts" legal reasoning is found in the second paragraph.

If you try to put the legal reasoning in this case in the standard formula introduced above, you will likely find it is not easy to do:

Title & Citation:

Facts: [Background] [Key]

Legal Rule Broken Down into Elements: [E1] [E2] [E3]

Legal Issue: [Whether/When] [Rule element in dispute] [Party1] [Party2]

Holding/Decision: [Yes/Maybe/No]

Rationale:

Now imagine how difficult it would be for a student to brief that case if the student had not been told in advance that the relevant "black letter law" was Restatement of Contracts 2d § 164 (1), had not been provided with the example of the California Civil Jury Instructions to guide the process of breaking the rule into elements, and had not been told to focus on the second paragraph and pay less attention to the first and third paragraphs.

It should now be clear why the process of briefing cases as a way to prepare for law school class discussions can be a very difficult, time consuming and frustrating process. The case brief formula presented in this essay was developed as a strategy to reduce the effort required of law students to brief cases while at the same time increasing the value of the briefs students create for reviewing for exams.

IV. Answering Exam Questions

American law school "issue spotter" exams are quite different from the kind of exams used in other fields of study in American colleges and universities. They are designed to test students on their mastery of problem solving skills similar to those that students studying engineering are supposed to master, but they do not rely on science and mathematics to establish the correct solution. They are designed to test students on their mastery of textual interpretation skills similar to those that students studying history or literature are supposed to master but the range of solutions accepted as correct is narrower than in the humanities.

American law schools developed this distinctive style of testing student progress in learning to "think like a lawyer" in order to simulate some of the most essential skills required to practice law after graduation. While lawyers in practice must investigate both the facts of a dispute and possible legal issues that might be raised, law school faculty members provide students with simplified, cartoonish fact patterns describing fictitious disputes. Students are tested on their ability to identify the "black letter law" they have learned in class that is most relevant to the hypothetical facts in the exam question.[4] In other words, the skill that is being tested with "issue spotter" exams is how well a student can reason by analogy from

[4] The term "black letter law" comes from the legal publishing convention of using a bold font for the legal rule itself and normal font for the commentary on the doctrine.

the cases discussed in class to fact patterns describing disputes that are similar to those cases in some ways and different in others.

The two hardest parts of answering a law school issue spotter exam question are:

1. Choosing the correct legal rule from among all the legal rules in the course syllabus to apply to the facts; and
2. Explaining how the most relevant element of the rule applies to the key facts of the exam hypothetical.

In a short essay like this, there is no way to explore strategies for meeting the first part in depth because that requires students to have studied an entire collection of legal rules. This essay focuses on only one rule (what constitutes an offer to form a contract), so it only offers strategies for dealing with the second part

But it is possible to illustrate the kind of reasoning required to solve problems related to finding the correct legal rule with a very simple example. Assume you are taking the exam for a mini-course that includes only these three simple rules:

1. Don't leave the house without turning on the home security alarm.
2. Don't leave the house without making sure the oven is turned off.
3. Don't leave the house without locking the door.

Assume you have an issue spotter exam question that includes the following facts:

> Student removed the travel mug from the microwave, turned on the alarm and locked the front door before leaving the house.

Which of the three rules is most relevant to the facts in this question?

Because the fact of turning on the alarm and locking the door were stated explicitly in the fact pattern, those rules are relevant and the legal outcomes are not controversial. (A law school instructor may expect a student to explain why certain issues are not relevant, but if included, this part of the students answer should be very brief because common law legal reasoning focuses on controversies, not on things everyone agrees on.)

The ambiguous part of the fact pattern is whether a "microwave" is an "oven" or not. The conventional meaning of "don't leave the house without turning off the oven" refers to a traditional convection oven that would waste a huge amount of energy of left running all day or might even catch fire and burn the house down. Microwave ovens turn themselves off automatically, so they cannot normally be left running all day. Thus the interesting issue raised by these facts is whether or not a microwave oven is within the scope of Rule 2, and if so, whether Student has complied with it even without taking a separate step of "turning it off."

Another issue spotter exam question designed to test a student's mastery of these three rules might be:

> Student turned off the oven, turned on the alarm and locked the front door before leaving the house, but left the window open.

Which of the three rules is most relevant to the facts in this question? At the most superficial level, the key facts required to show that Student complied with all three rules have been stated explicitly in the fact pattern. So all three rules are equally irrelevant, and this could be noted in passing.

The hard part of this question is what to say about the window, which is a more difficult problem than treating a microwave oven as equivalent to a traditional oven. The student will need to make an analogy between the security alarm, the oven or the door. If a student says that there are no rules about windows, that answer would not get a good grade because the student did not draw any analogies. But if a window can be analogized to a door, then the argument could be made that leaving the window open is equivalent to not locking the door. That answer would get a good grade because it demonstrates the student's ability to use reasoning by analogy as a tool for solving problems.

These two small examples have the same basic structure as "issue spotting" on a real law school exam. After a student has learned several dozen different "black letter rules" in a class, figuring out which of those rules are relevant and which are not relevant based on the simplified, cartoonish fact patterns in exam questions can be very, very difficult.

A basic and important strategy for "issue spotting" on a real exam is to write a brief "scratch" outline before starting to write out the actual answer. In this context, "scratch" means brief notes that make sense to the writer but are not complete sentences. One benefit of writing a "scratch" outline is that it gives a student the opportunity to isolate the most ambiguous parts the question that are likely to be of the most interest to an instructor using the exam to assess students' ability to grapple with ambiguity.

Some other basic strategies for creating a course outline that makes it easier to "spot issues" will be discussed in the following section.

A. How to Write an IRAC Exam Answer

This essay provides a brief introduction to using the simple, mechanical "Issue-Rule-Apply-Conclusion" formula can be used to write answers to issue spotter exam questions. Just as there is no universal consensus regarding how to brief cases or write issue statements, there is also no universal consensus regarding the best way to answer issue spotter exams. Most law school faculty members teaching in law school today did well on issue spotter exams in law school with little or no explicit instructions about how to take them, so they may have trouble understanding why their own students want explicit instructions. Some faculty members actually oppose teaching law students how to use the IRAC formula for answering issue spotter questions because they believe it can only capture the most basic elements of common law legal reasoning, thus interferes with students' ability to express more subtle nuances in their analysis.

The best way to think about the IRAC formula is as a kind of drill to get good at different parts of a complex skill, so no one should expect it to capture all the "thinking like a lawyer" skills being taught in law school. For example, someone working on their tennis skills may practice by hitting a tennis ball against a wall even though in a real tennis game, no one hits a ball against a wall. To learn ballet, dancers practice using a wooden bar but do not use a bar when actually dancing. Students learning to play piano practice playing scales but then play music, not scales, when performing for an audience.

The name for this kind of drill in learning theory is "scaffolding." If the IRAC formula is only used as "scaffolding" to help law students get oriented to the distinctive characteristics of common law legal reasoning, then at least some faculty objections to teaching students exam formulas like IRAC can be seen as a failure to distinguish between novice and expert learning styles.[5] As soon as a student has grasped how to present his or her analysis of an issue spotter exam question clearly and concisely, then the mechanical IRAC formula can be discarded and the student can develop his or her own style of answering issue spotter questions.

Here is a brief overview of what is supposed to be going on in different parts of an IRAC issue spotter answer:

Issue: This issue statement is equivalent to the issue statement in a case brief except that it summarizes the student's reasoning about the facts of the exam question rather than the court's reasoning about the facts of the case. Just as with briefing a case, the "Whether/When" formula may provide students with a useful framework for learning to combine rules and facts into an issue statement at the appropriate level of abstraction/concreteness.

Rule: This is where a student summarizes the relevant legal rule that the student believes can resolve the issue presented by the facts of the exam question. It might be a paraphrased Restatement rule or it might be the paraphrased holding of a case discussed in class. Just as the court in Swinton v. Whitinsville Savings Bank case did not mechanically spell out all the elements of the black letter rule it was applying, law students may be able to adjust their descriptions of the relevant legal rule in light of their relevance to the issue being analyzed and still receive full credit.

Apply Rule to Facts: This step involves showing how key facts may be inside or outside the scope of a rule. It requires reasoning by analogy from the facts of cases taught in class to the facts of the exam question. For most issue spotter exam answers, the "apply the rule to the facts" step is the most important, yet many beginning law students completely omit it or give it short shrift.

> If legal reasoning were more like formal deductive logic, then it would be OK to skip the "apply rule to facts" step or give it short shrift. But in common law legal reasoning, applying rules to facts is the radioactive core of the reasoning process.
>
> In order to help students slow down and grapple with the ambiguity and messiness of applying rules to facts, the process for answering exam questions presented in this essay asks students to use the formula, "On the one hand…[apply rule to facts producing outcome X]; on the other hand…[apply same rule to same facts described differently producing outcome NOT X]."
>
> As with all other forms of scaffolding—such as training wheels on bicycles—the goal is to get rid of this structure as soon as the student feels confident they understand the ideas behind it.

Conclusion: In this step, the student loops back to the question posed by the instructor at the end of the issue spotter fact pattern, generally with a "Yes" or "Maybe" or "No" answer. For most law school exams, the conclusion of the analysis that gets students the most points from the instructor will be maybe because that requires the students to argue both pro and con positions for the same question, then decide which is

[5] John D. Bransford et al. eds., How People Learn: Brain, Mind, Experience, and School, Chapter 2: How Experts Differ from Novices.

more persuasive. Compared to most undergraduate programs in America or legal education programs in other countries, American legal education is fairly unique in its insistence in rewarding students for concluding that there may be no clearly right or wrong answers to exam questions.

B. Exam Question Based on *Taylor v. Miller* and on *Yaro v. Khan* plus Answer

In its classic form, an issue spotter fact pattern on a law school or bar exam may be quite long, covering one or two full pages. When an instructor uses that classic form of issue spotter exam question, then the student is being tested on how well he or she sequences the discussion of many different issues in addition to how well he or she analyzes each issue. The skill of prioritizing and sequencing the discussion of many different legal issues is outside the scope of this introduction, so the issue spotter exam questions used here present only one main issue related to whether or not what someone said constitutes an offer to form a contract.

Here is a short, simple issue spotter exam question based on Restatement 2d § 24, *Taylor v. Miller* and *Yaro v. Khan*:

> Wilma Wilson was a member of the Good Shepherd Church, and also sang in the choir every Sunday. When the members of the Good Shepherd Church choir met for their regular Wednesday evening practice, Pastor Pete Perkins stopped by to ask all the choir members to think about donating money or goods to sell for the upcoming church fundraiser the following Sunday. After choir practice, Wilma mentioned to another choir member named Bert Black that she had inherited an 18th century copy of the Church of England Book of Common Prayer that she could donate for the fundraiser, but she didn't know whether anyone would want to buy it. Bert was a collector of rare books, so he told her that he would be interested in buying it from her, and then Wilma could donate the money he paid to the church fundraiser. Wilma replied, "It was recently appraised so I know that $2,000 would be a fair price. Can you bring that amount in cash on Sunday before the service?" Bert responded, "I'll do it, no problem!" The following Saturday, when Wilma's niece Nancy Nettles stopped by to visit her, Wilma mentioned her plan to sell the Book of Common Prayer and donate the proceeds to the sale to the church fundraiser. Nancy told Wilma that she should leave the book in her will to one of her grandchildren because it was a family heirloom and just donate the money instead because she could afford it. The next day, when Bert tried to hand Wilma $2,000 in cash before the church service, Wilma told him she'd changed her mind and hadn't brought the book. Can Bert demand that Wilma sell him the book for $2,000? Why or why not?

*****

Using the IRAC template as scaffolding:

Issue: WHETHER Wilma made an offer to form a contract **WHEN** she said, "I know that $2,000 would be a fair price for the book. Can you bring that amount in cash on Sunday before the service?" after Bert told her at choir practice on Wednesday that he wanted to buy the book?

Rule: An offer is an expression of willingness to enter into a contract communicated with specific terms and mad with the intention of granting another person the power to form a contract by accepting it.

Application: [On the one hand,] What Wilma said could be interpreted as merely sharing information about the terms that would be acceptable to her if she decided to sell the book to Bert. That would be

similar to what Miller said to Taylor about being willing to consider leaving his dog in Helston for $2,000 and a loving home in *Taylor v. Miller*.

[On the other hand,] Wilma indicated a definite price, a definite time and a definite place when she would sell the book after Bert expressed clearly his interest in buying the book which looks a lot like an offer. This seems similar Restatement 24 illustration about selling a book if someone promised to pay $5 for it and Khan's offer to sell a painting for $8,000 in *Yaro v. Khan*.

Conclusion: [Maybe Yes or Maybe or Maybe No] Bert can probably make Wilma sell him the book for $2,000 because Wilma specified a price, date and location when she would sell it to him after he told her how much he wanted to buy the book.

*****

Many faculty members in American law schools associate the use of a formal IRAC system for answer exam questions with commercial bar preparation services. When they see labels like Issue Rule Analysis Conclusion in a law student's exam, they take this as evidence that the student has been reviewing for the exam using commercial bar prep materials instead of the student's own notes of class discussions that this instructor led. Viewed from this perspective, it suggests the student believes commercial bar prep materials are a more reliable source of information than their own instructor, an inference likely to annoy the instructor and result in a lower grade.

So IRAC analysis is probably best used only for the "scratch" outline part of answering issue spotter exam questions, and should not be transferred over to the student's real answer.

Answering the exam question above using the IRAC analysis as the framework but without showing any of the IRAC scaffolding might look like this:

Bert wants to treat his conversation at choir practice with Wilma as an enforceable contract, not a mere social interaction. In order to force Wilma to sell the book, he will have to prove that she made an offer and he accepted it. Rstmt 2d defines an offer as an expression of willingness to enter into a contract made with the intention of granting another person the power to form a contract by accepting it. What Wilma said could be interpreted as mere descriptions of possible actions she might take in the future. *Taylor v. Miller*. But Wilma told Bert the exact dollar amount he'd have to pay in cash and a definite time and place he'd need to pay it after he told her how much he wanted to buy the book. That looks more like Wilma was giving Bert an opportunity to form a contract on those terms. *Yaro v. Khan*. If what Wilma said was an offer, then when Bert said was clearly an acceptance. So while Wilma might be able to get out of selling the book to Bert, it seems more likely that a court would interpret what she said as an offer to form a contract.

*****

If you compare the two answers, you will notice that the "one the one hand, on the other hand" discussion was shorter in the less structured answer. Most law school issue spotter exams contain more issues than a student could possibly discuss clearly during the time allowed even using the quicker, less structured form, so faculty members do not expect students to go into each issue in very much detail. So a student's goal is to make sure the person grading your exam can see that you considered more than one possible outcome before reaching a conclusion, not to spell out all possible answers in equivalent detail. In

the less structured answer, the student could mention briefly in passing that what Bert said was clearly an acceptance. If a student applied the IRAC formula in a mechanical way, that would have required a whole separate IRAC analysis which would be overkill for such a simple, easy issue.

C. Apply What You Have Learned: Exam Question Based on *Taylor v. Miller* and *Yaro v. Khan*

Here is a short, simple issue spotter exam question you can use to try your hand at composing an answer in IRAC form. After you've used the IRAC form to isolate the main issues and key facts, you can then try rewriting answer in the more flowing, less structured form preferred by most faculty members.

> When Harry and Vickie Holmes came home on Friday night from dinner at a local restaurant, Harry mentioned to Vickie that he thought the dress she had worn that evening was very attractive. "This old rag?" Vickie responded, "I should get rid of it." After changing into her pyjamas, Vickie set the dress out on the back porch to take to the dry cleaners. The next day, Harry and Vickie were having a yard sale. They got up early in the morning, set out all the things they planned to sell on their drive way and marked them with price tags. Many people came to check out the yard sale, so both Harry and Vickie were busy negotiating prices and taking payment from buyers. Linda Lindal looked up from the things for sale on the driveway and spied Vickie's dress on the back porch next to the drive way. She asked Harry what the price was for the dress. Harry replied, "I might be able to sell it for $10, let me see," and went ask Vickie whether it was OK to sell the dress. When Harry came back with Vickie, Linda already had the dress in her hand and $10 out to pay for it. Vickie said, "I'm so sorry, that dress is not for sale," but Linda insisted that Harry had already agreed to sell it to her. If Linda has really fallen in love with Vickie's dress and isn't willing to let the matter drop, can she demand that Harry and Vickie sell it to her for $10? Why or why not?
>
> *****

Using the IRAC template as scaffolding:

> **Issue: [**Whether/When]
>
> **Rule:**
>
> **Apply:** [On the one hand…; on the other hand…]
>
> **Conclusion:** [Maybe Yes or Maybe or Maybe No]
>
> *****

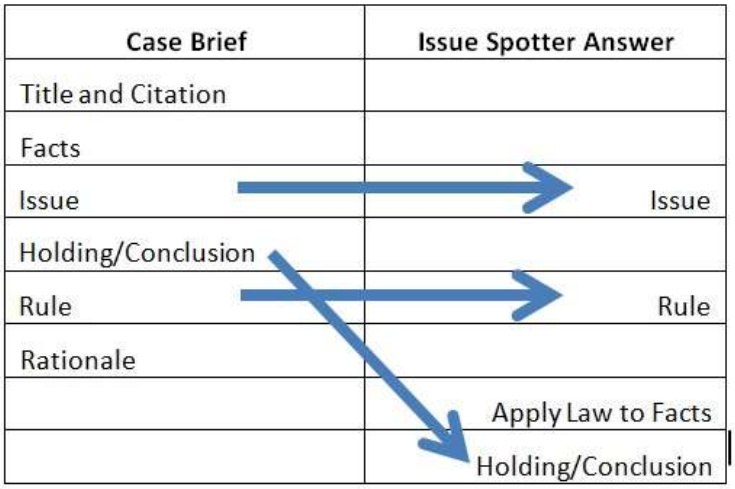
Answering the exam question without showing the IRAC scaffolding:

V. Outlining as the Bridge between Class and Exams

Now that you have been provided with wooden, mechanical formulas for both case briefs and IRAC exam answers that you can use for scaffolding/deliberate practice, we are finally ready to see how an American

law school course outline can be created from case briefs and used to support issue spotting for exam answers.

Here's simple comparison showing which elements case briefs and IRAC exam answers have in common, and which elements are different:



The description of the issue, the relevant black letter rule and the conclusion share a common structure while case briefs lack an "apply rule to facts" section. It is important to understand why this is so: a judicial decision presents only the winners version of the facts as background information and ignores alternative interpretations that would make its conclusion seem less persuasive. Dissenting opinions are more likely to have some explicit apply rule to facts analysis as part of the process

of explaining why the majority did not do that step correctly. But sometimes dissenting decisions merely present the opposite interpretation to the majority, leaving the reader with the impression that the majority and dissent might not be talking about the same dispute.

Given that students do not really get many opportunities to practice the apply rule to facts part of legal reasoning when reading cases, why should they be expected to know how to perform that step? The answer is that law school instructors believe that they are demonstrating how to do the apply rule to facts set during Socratic Method class discussion.[6]

By comparing what goes into case briefs and issue spotter exams in a bit more detail, the common structural elements are more visible.

[6] Once I explain this to most law students, they can appreciate that it may be true, but they acknowledge that they had not understood that was what was going on in class discussion before I pointed it out. But if most law students cannot explicitly make the connection between class discussion and apply rule to facts analysis on exams, then they cannot engage in deliberate practice when studying for exams.

Case Brief

- Title & Citation
- **Key Facts 1, 2, 3**
- **Rule** [not usually included]
- **WHETHER** [**rule element in dispute**] [party 1] [party 2] **WHEN** [**key fact**]
- **Holding:** [YES] [MAYBE] [NO]
- Rationale [*why is this outcome fair?*]

Issue Spotter Exam Question: Issue-Rule-Apply-Conclusion Answer

- **WHETHER** [**rule element in dispute**] [party 1] [party 2] **WHEN** [**key fact**]
- **Rule**
- **Apply rule to facts:**
  - One the one hand **Key Facts 1, 2** + **Rule Element**
  - On the other hand **Key Facts 2, 3** + **Rule Element**
- **Conclusion:** [YES] [MAYBE] [NO]

Compare Brief to IRAC

Case Brief	IRAC
Title & Citation	
Key Facts 1, 2, 3	
Rule [not usually included]	
WHETHER [**rule element in dispute**] [party 1] [party 2] **WHEN** [**key fact**]	**WHETHER** [**rule element in dispute**] [party 1] [party 2] **WHEN** [**key fact**]
	Rule
	Key Facts 1, 2 + **Rule Element** **Key Facts 2, 3** + **Rule Element**
Holding: [YES] [MAYBE] [NO]	**Conclusion:** [YES] [MAYBE] [NO]

Because the best kind of American law school course outline is the one that makes it possible for a student to get the highest possible grade on an issue spotter exam, the structure of the outline should be create by reverse engineering the exam answer, not by simply piling up class discussion notes. This is because most class discussion notes are organized as historical record of what happened in class and what was discussed in cases. But what is tested in law school is problem solving, and a detailed description of what happened in class and in cases is not a tool that can easily be used to solve issue spotter problems because it is too cumbersome.

The wooden, mechanical case brief formula taught at the beginning of this essay was created by reverse engineering the parts of issue spotter exam answers that get the most points. So the formula may have seemed arbitrary and restrictive compared to a more natural way of writing about what happens in cases.

The wooden mechanical formula for briefing cases is harder to create than a more natural description of what happens in cases, but the extra time and effort invested in distilling cases assigned for class to only those elements that can be used as tools to answer issue spotter exam questions pays big dividends toward the end of a course when a student begins studying for exams.

The first draft of a student's course outline does not need to consist of much more than cutting and pasting the case briefs created for class discussion into a single document. In addition, statutes and restatement sections cited in cases and discussed in class should be added.

Before writing a second draft, the student should find some of the instructor's old exam questions and start testing the quality of the outline by trying to draw analogies between key facts in cases and what look like they might be key facts in the issue spotter exam. As it becomes apparent while trying to write out practice exam answers that there are gaps in the outline's coverage, the student can go back to class discussion notes, find information that is relevant to answering issue spotter exam questions, and add that to the outline.

As law students become more adept at writing course outlines that are "optimized" to contribute to their exam success, they will become aware of how helpful it would be if law school instructors provided not just old exam questions but also some kind of guidance about how they assess law student performance on exams. While some law school faculty members provide such information, the practice remains relatively rate. As a result, law students who wish to test the quality of their course outlines by using them to help write practice exam answers are forced to turn to generic, commercial study aids that may not track that closely what their instructors taught in class.

The American Bar Association concluded that law school faculty members should be providing more information to law student about how they assess academic success, and in 2015 it changed its rules for the accreditation of law schools to encourage faculty members to do just that.[7]

[7]ABA Section of Legal Education Managing Director's Guidance Memo: Standards 301, 302, 314 and 315 (June 2015) https://www.americanbar.org/content/dam/aba/administrative/legal_education_and_admissions_to_the_bar/governancedocuments/2015_learning_outcomes_guidance.pdf

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Comparative Contract Law: Issue Spotter Practice Exam Questions

Practice Exam Question for Offer and Acceptance

On Monday, Carlos Consumer got laid off from his job in Seattle and decided to move back to New York City to live with his parents until he could find a job there. His parents bought him a plane ticket for New York for Sunday morning. On Tuesday, he ran an ad in Craigslist listing his used Chevrolet Malibu sale because he wasn't going to need it after he returned to New York City. The text of the ad said, "Used Chevy Malibu 2 door runs great 55,000 miles will sacrifice to sell fast $2,000 cash or best offer, no reasonable offer refused." After he received a flood of email responses to his ad, he realized he'd made a mistake in the price. He deleted the first ad, and replaced it with an ad that gave the price as $12,000 instead. He arranged a meeting with someone who wanted to test-drive the car before buying it. After the test drive, the buyer said he wanted the car, and offered Carlos $2,000 in cash. Can Carlos refuse to accept $2,000 in cash for his car?

Practice Exam Question for Laidlaw v. Organ

On March 1, Bill Bingham offered his house in Old Town for sale for $200,000 by listing it on the website "Sell-Your-House.com and putting a sign in front of his house saying "for sale by owner." On March 2, Alice Alford visited the house, walking from room to room with Bill. Alice offered to buy the house for $190,000 in cash if the closing could be scheduled on March 20. Bill objected that wasn't enough time to complete all the formalities, but when Alice said she was willing to skip the formalities, Bill accepted her offer and they both signed a standard purchase and sale agreement reflecting those terms. The closing took place on March 20 as scheduled and Alice moved in on March 21. When Alice went to bed the night of March 21, she was horrified to discover that the house was full of termites that came out as soon as all the lights were turned off. Alice immediately obtained an estimate of the cost of an exterminator to remove the termites from the house and repair the hidden damage that they had already caused to the wood in the house, and learned it would cost $50,000. Can Alice demand that Bill pay her the $50,000? Why or why not?

Practice Exam Question for Leonard v. PepsiCo

After the heiress Ruby Russell died, her heirs gave her valuable collection of paintings to Imperial Art Galleries to auction off. Because the paintings were so valuable, Imperial Art Galleries was very careful about who it invited to make sure that only people who could afford to buy the art attended. It required anyone wishing to attend to register and provide proof that they would be able to pay at least $100,000 in cash if they won any of the sales. Kayla King and Tyler Tindall were wealthy individuals who had purchased valuable paintings in Imperial Art Galleries auctions in the past, so they were invited to attend and had no trouble proving that they could afford to buy more valuable paintings. On the day of the auction, Kayla and Tyler had lunch at a nearby restaurant and ended up drinking a whole bottle of wine together. They were in fine spirits when they arrived at the auction after lunch. During the auction, they began pretending to make bids on various pieces by sticking their fingers in their ears and up their noses before collapsing in barely suppressed giggles. At the end of the auction, however, they were

shocked to learn that Imperial Art Galleries said that Kayla owed $300,000 and Tyler owed $400,000 for paintings they had bid on and won. If Kayla and Tyler refuse to pay for the paintings, can Imperial Art Galleries force them to pay? Why or why not?

Practice Exam Question for Hadley v. Baxendale

Transformative Tech was a company that developed products designed to leverage machine learning, artificial intelligence, cloud computing and Internet of Things technologies. In 2017, they introduced the Digimi voice-activated personal digital assistant. The Digimi virtual assistant is designed to compete with Apple's Siri, Amazon's Alexa, Microsoft's Cortana or the Google Home Assistant. The Digimi virtual assistant transmits spoken messages by means of a wireless internet connection to the Transformative Tech machine learning/artificial intelligence search engine which runs on the Transformative Tech cloud computing system. Ethan purchased a Digimi virtual assistant on February 1, and used it as his alarm clock. In Metropolis, the city maintained an "intelligent transportation system." Metropolis installed dynamic message signs at all the bus stops that showed the current estimate for how many minutes until the next bus on a particular route would arrive at the stop. These estimates were prepared by analyzing information transmitted from transponders on all the busses and from traffic probe sensors positioned all around the city. Transformative Tech collected all the data from Metropolis's intelligent transportation system and analyzed it to prepare its own estimates of arrival times for busses at bus stops. Every morning when he was getting ready to go to work, Ethan would ask, "Digimi, when will the Bus 24 arrive at the bus stop on the corner?" Digimi would answer Ethan's question by telling him how many minutes away the next bus was, allowing Ethan to reduce the amount of time he spent standing at the bus stop near his house. On May 1, Ethan needed to leave home very early to get to a job interview. He had made it through the first three interviews, and he knew he was only competing against one other person for the job of his dreams. But Ethan overslept and then missed the bus because a software glitch in Transformative Tech's cloud computing system caused Digimi to fail to wake Ethan up and then gave him incorrect information about when the next bus was coming. If Ethan does not get the job of his dreams because he showed up 90 minutes late for the final interview, do you think he can demand that Transformative Tech compensate him for his loss? Why or why not?

Practice Exam Question for Campbell Soup v. Wentz

In 2016, the German automobile maker BMW decided to cash in on nostalgia for old British sports cars by producing a limited edition Triumph Roadster, an updated version of a classic English sports car originally produced in the 1940s (Mini and Rolls Royce automobiles in the UK are actually produced by BMW). The annual production run was limited to 3,000—one for each BMW dealer around the world. Tiffany Tyler owned and operated the Tyler BMW dealership in Arcadia. She decided to allow all of her customers who wanted to buy one of the limited edition Triumph Roadsters to submit their name plus a deposit of $10,000 and then she would draw the name of the lucky customer who would get the Roadster for the list price of $50,000 from a bowl. Tiffany drew the name of Erica Evans and after cashing Erica's check for the $10,000 down payment sent Erica a letter congratulating her on winning the drawing and reminder her that she would need to pay the balance of $40,000 on December 1 when the car was expected to arrive. On December 1, when Erica arrived with the balance of $40,000 in cash, she was informed by Tiffany that she had decided to give the Triumph Roadster to her own mother instead. After Tiffany refused to take the $40,000 and give her the car, Erica was hopping mad. If Erica consults lawyer, what do you think she will find her options are?

Practice Exam Question for Ruud v. Great Plains Supply

Anna Adams was a successful corporate executive who owned a beautiful cottage by Lake Tranquil in the mountains. Jeffrey was her favorite child even though he was never successful or dynamic like his mother. Except for handouts he got from his mother, he eked out a pitiful existence as a street musician. What he really loved was painting, but he was never able to sell any of his paintings to anyone but his mother. Anna's daughter Nancy was a high-powered attorney. Anna didn't like to admit it even to herself, but Nancy got on her nerves whenever they spent very much time together. Jeffrey and Nancy's father had passed away many years ago and Anna never remarried. Under Anna's will, which Nancy had reviewed, Anna left everything to both children 50/50. Anna wanted to use the cottage for as long as she lived, and then to give it Jeffrey when she died, but she didn't want Nancy to find out about it because that would just provoke a big fight about how Anna always loved Jeffrey better than Nancy. So Anna and Jeffrey entered into a written agreement that Anna would transfer ownership of the cottage to Jeffrey when she was too old to use it anymore or when she died, whichever came first. In return, Jeffrey agreed not to tell his sister Nancy about the transfer and both Anna and Jeffrey signed the agreement. A few years later, Anna died, and Nancy became the executor of her will. Jeffrey showed Nancy the agreement and asked Nancy to transfer the cottage to him, but Nancy refused, saying that they would share the cottage 50/50 along with all of Anna's other property. (Assume that Nancy's position is justified based on the language in Anna's will under US property law if the agreement between Anna and Jeffrey is not enforceable.) Can Jeffrey force Nancy to transfer the cottage to him?

Practice Exam Question for Hill v. Gateway & Brower v. Gateway

E-Money Direct provides online payment services for online auctions. It experienced explosive growth for several years, and soon had 50 million accounts. One term in its standard user agreement provided that "In its sole discretion, EMD may at any time make any changes it deems necessary in the terms and conditions of the services it provides to its customers." In order to open an EMD account, users were shown the entire 5,000 word standard form contract that included this term and had to click on "I agree." Professional criminals noticed that EMD had relatively lax security procedures, and began using EMD to "launder" money earned from drug dealing and other nefarious activities, and to steal money from other account holders. Suddenly faced with the threat of prosecution for aiding in criminal activities, and mounting fraud losses, EMD rushed to implement new security procedures to correct the problem, and revised its user agreement to allow it to place freezes for an indefinite period on any accounts it believes may be involved in illegal activity. EMD placed freezes on thousands of account without notice, and left them on because it lacked the staff to investigate so many cases and had no procedures for allowing innocent customers to ask to have their accounts unfrozen. As a result, many individuals in the business of buying and selling things in online auctions found they were unable to accept or make payments for online auctions because their EMD accounts had been frozen. If thousands of innocent EMD customers sue, demanding compensation for the losses they suffered as a result of having their accounts frozen in error and being unable to get them unfrozen in a timely manner, are they likely to recover? Why or why not?

JOSEPH DAINOW

The Civil Law and the Common Law: Some Points of Comparison

Introduction

The interest of jurists in legal systems other than their own and in comparative law has been a matter of long tradition. At any rate, during the twentieth century and especially from about thirty years ago, there has been an extraordinary growth of this interest. Now, with the Common Market and all the other expanding programs of international trade and commerce, it is impossible to overemphasize the importance of understanding the nature and function of legal systems of other countries.

In the legal history of Western Europe and of the countries that received their legal systems from these sources, one finds the establishment of the two great legal systems which are often made the basis of comparative law studies. This does not overlook the other legal systems outside of the continental civil law and the common law of the Anglo-Saxon countries. There are of course not only the different legal systems of the Asiatic countries but also within the European continent itself there is the legal system which has long been in effect in the Scandinavian countries, and there are also the more recent developments in the Soviet countries.

All legal systems have the same purpose of regulating and harmonizing the human activity within their respective societies, and in each society the legal system forms part of the culture and civilization as well as of the history and the life of its people. The events of their respective history have led toward certain fundamental similarities and differences in their legal systems. In the countries of Western civilization, the two best-known systems are the civil law and the common law, particularly as exemplified in France and in England.

The concentration in this article on the civil law and the common law is not intended to derogate from the importance and values of other legal systems. At the same time, it must also be recognized that there are many differences, for example, between the laws of France and Germany, as well as between England and the United States. Nevertheless, in each of these two great systems, civil law and common

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law, there are certain characteristics and general attributes that can serve as bases for a general comparison.

There are different ways of trying to explain civil and common law as legal systems. One way might be to examine the elements of resemblance or the points of difference, or even the history of their respective establishment and the methods of their development. A comparison could also be made from the point of view of their social and economic objectives and the methods used to accomplish these ends. All these points of view have a measure of truth, and they should really be appreciated all at once. On the other hand, there are those people who say that there no longer exists any real difference between the civil law and the common law by reason of the parallel developments that have taken place in order to satisfy the same societal needs in general conditions which are similar—the differences which remain being only matters of degree rather than nature. There are also some places in which the civil law and the common law have been functioning together in what may be called a "mixed jurisdiction," like Louisiana, Quebec, Scotland and South Africa. For the present kind of a study, the essential approach is to search for an *understanding* of these two systems, and especially to identify and understand the fundamental differences in their structures, in their methods of thought and in their attitudes towards the law as a legal system.

I. History and Development

A legal system is a living organism; it breathes, it grows, it evolves, it is part of the life of the people for whom it functions. Consequently, the first step in the direction of an understanding of the civil law and of the common law is to glance briefly over their respective history and development.

A. *The civil law*

The term "civil law" is derived from the Latin words "*jus civile,*" by which the Romans designated the laws that only the Roman citizens or "*cives*" were originally privileged to enjoy. For the other people there was the "*jus gentium.*" It is sometimes said that the countries of the civil law are those which received their legal system from the Roman law. While this in effect is true, it is only part of the story. Furthermore, this reference to Roman law can be appreciated better in the light of an examination of the nature of its development along with its historical and social evolution during a period of at least one thousand years, from the beginning of the formal written law in the Twelve Tables up to the completion of Justinian's codifications and compilations.

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To indicate briefly the salient points which stand out against this background: there was an ancient period with a very narrow legal system which had strict and limited procedural forms. When its insufficiencies caused excessive hardship, there was established the office of the *"praetor,"* whereby liberal influences could make themselves felt and be given concrete application. The strict ancient law, the *"jus civile,"* was tempered and at the same time supplemented by the justice and the equity of the new remedies and procedures developed by the *praetors.*

As public regard grew for the small number of highly skilled jurists, their opinions were often sought for clarification and guidance. The outstanding quality of their achievement brought them and their successors a constantly increasing recognition. In this manner, they served not only as technical interpreters of the written text, but their knowledge and their wisdom also became indispensable elements in the development of the law. In the course of time these jurists came to enjoy the very highest prestige in the law; emperors and magistrates not only sought their consultation and advice but in general followed and adopted their opinions.

During this time, not a matter of years or generations but of centuries, some efforts were made to co-ordinate and group the rules of law; there were also attempts to compile the results of a very large number of actual case decisions, especially the most significant ones.

It was against this background, and to be understood in the light of it, that Emperor Justinian brought together the great jurists of his day and had them compile the body of law that immortalized his name.

During the ensuing centuries and in the Middle Ages, the Roman law was eclipsed in many parts of Europe. However, it reappeared at different times and in various ways, it was modified and reinterpreted, and by the eighteenth and nineteenth centuries it had acquired the profound appreciation of European jurists and scholars. Roman law was at one of the peaks of its prestige when the several political unifications of Western Europe led to the unification of the private law in the national movements of codification, especially in France and in Germany.

The essential characteristics of these legislative codifications fixed the basis and determined the nature of the legal systems of which they were the expression.

B. *The common law*

The common law, as a legal system, is associated with its origin and development in England, where the social and economic and political history as well as the foundation of its law stem from the

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feudal system and its incidents. One aspect of this system was that the settlement of disputes was conducted on a purely local level, each region acting independently and without knowledge of what the others were doing. The rights and obligations of individuals flowed from the nature of their personal status within the system.

When the king sought to establish a more important central power, he ran into serious conflict with the local authorities. Nevertheless, in his quality of sovereign judge and source of justice, and to discharge his responsibility for the preservation of peace, he established his own courts with judges who went on circuit throughout the entire country. Even though these were not courts of general jurisdiction, but only competent in certain kinds of cases, they were not well received at first. Suffice it for present purposes to say that the king's courts were the victors in the ensuing struggle for authority. By means of their decisions they created the first uniform rules and the first basis of uniformity in the legal order, by establishing general norms which were common throughout the whole country. It was a form of general law or common law for all parts of the realm; hence the name, common law.

This growth and consolidation of the court system in England took place chronologically much earlier than the evolution of Parliament. After the law-making function of legislation had come into its own importance, there were stages during which there was a deep jealousy on the part of the courts. Since a parliamentary enactment had to be applied by the courts, each statute was by its nature an encroachment on the domain of the common law which embodied the protection of the rights of the people. Whenever the legislation was directly applicable to a particular situation, the courts were obliged to render their decisions in accordance with the text, but whenever any question or doubt could be raised, the statute was given a narrow interpretation so as to minimize its encroachment upon the common law and to preserve a maximum of authority in the courts.

These two historical conflicts, and the way in which they were resolved, provide considerable insight for an understanding of the nature of the common law as a legal system.

A third subject which should be mentioned is the development of the system known as "equity," apart and distinct from "law" but supplementary to it. To make remedies available for harsh situations, to establish new procedures, and in order to meet all sorts of new problems, recourse was had to the authority of the King in his sovereign capacity; he delegated this function to an official called the Chancellor of the Royal Court. In the course of time, this became the Court of Chancery, through which there developed a substantial body of col-

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lateral and independent law. Thus, English law consisted at the same time of "law" and "equity."

One can hardly overlook noting the strong resemblance to Roman law, where the praetorian law developed alongside but independently of the *"jus civile."* Furthermore, the more recent movement in England and the United States to combine "law" and "equity" may resemble, more than documentation has thus far established, the definitive consolidations which were eventually effectuated in the Roman law.

It is not entirely unreasonable to consider the English development of equity and its ultimate fusion with law as stages in the evolution of English law through which the Roman law passed many centuries ago. The legal system of the common law is much younger, having had only a few hundreds years of existence. During the first centuries of the history of Roman law, the development was equally pragmatic, based on experience and adjustment; there, also, the sources of law were rather in specific decisions and imperial decrees than in systematic compilations of legislative texts. The first systematic exposition of the Institutes of Gaius in the third century in actuality presented the essence of seven centuries of legal evolution.

The history and the evolution of equity in English law strikingly resemble the development of praetorian justice in Roman law. It may very well be asked whether the common law is not in the process of passing through the stages of development which the civil law experienced long ago, and whether the future of the common law might not in some measure be anticipated in the history of the civil law.

In both the "law" and "equity" branches of the common law, the established body of legal rules came essentially from judicial decisions. According to the declarative (or customary) theory, these decisions were merely the concrete expression or evidence of the common law which, so to speak, had a permanent and universal existence. According to the creative (or judicial) theory, the modern and more frank position is to recognize that the decided cases were the very source and the essence of the law.

II. Legislation and Judicial Decisions

From the foregoing it can be seen that two vital and essential points of reference for a comparison of the sources of positive law in the civil law and the common law are "legislation" and "judicial decisions." To reverse the phrase, in common-law thinking the distinction would be "case law" and "enacted law." It is necessary to examine each of these topics in the two legal systems.

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A. *Legislation as the basis of the civil law*

Generally, in civil law jurisdictions the main source or basis of the law is legislation, and large areas are codified in a systematic manner. These codes constitute a very distinctive feature of a Romanist legal system, or the so-called civil law. Although in the form of statutes duly enacted by the proper legislative procedure, these codes are quite different from ordinary statutes.

A civil code is a book which contains the laws that regulate the relationships between individuals. Generally it contains the following topics: persons and the family, things and ownership, successions and donations, matrimonial property regimes, obligations and contracts, civil responsibility, sale, lease, and special contracts, as well as liberative prescription (statute of limitations) and acquisitive prescription (adverse possession). A code is not a list of special rules for particular situations; it is, rather, a body of general principles carefully arranged and closely integrated. A code achieves the highest level of generalization based upon a scientific structure of classification. A code purports to be comprehensive and to encompass the entire subject matter, not in the details but in the principles, and to provide answers for questions which may arise.

The nature of such a code naturally calls for a liberal interpretation in order that it may serve as the basis of decision for new situations. The same method of liberal interpretation likewise prevails for the ordinary statutes in a civil law jurisdiction. There is a great respect and high regard for legislation as the basic source of the law.

A significant feature about legislation in modern civil law is the importance attached to the preparatory works and the draftsmen's comments, as well as the parliamentary discussions in connection with its initial formulation. This is especially true of the codes, and particularly during the earlier periods of their interpretation. Thus, in France the history of the drafts, the observations of the courts, the debates and the changes, were indispensable to the interpretation of the *Code Napoleon*.

B. *Judicial decisions as the basis of the common law*

Looking at the law in England, the picture is a totally different one. During the formative period of English legal history, there was no strong central legislative body, but there were the powerful king's courts.

When a court decided a particular case, its decision was not only the law for those parties, but had to be followed in future cases of the same sort, thereby becoming a part of the general or common law. Thus, the common law, as a body of law, consisted of all the

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rules that could be generalized out of judicial decisions. New problems brought new cases, and these enriched the rules of the common law.

Actually, the common law was conceived as being all-inclusive and complete; if a rule had not already been formulated, it was the judge's responsibility to declare it. Thus, judicial decisions were both the source and the proof of the law, pronounced in connection with actual cases.

What gave stability and continuity to this system was the doctrine of "precedent." Once a point had been decided, the same result had to be reached for the same problem; the judge was obliged to "follow" the earlier decision, the precedent. However, since courts are jealous of their prerogatives, the rule of precedent was applied only to the *"ratio decidendi"* or the exact point which was indispensable and necessary to reach a decision. Non-essential points were classified as *"obiter dicta"* and were not binding.

If a new situation resembled a prior case but was not exactly the same, then two possibilities were open to the judge. If he felt that it would be the socially desirable result to have the same solution, he could "apply" the rule of the earlier case. However, if the judge felt the other way, he could "distinguish" the previous decision and leave its application limited to the specific fact situation which it controlled. In extreme situations, a court could brand an earlier case as erroneous and "overrule" it, thereby providing a new precedent for the point involved.

The first two of these techniques, following precedent and applying the rule, assured stability and continuity of the law with the corollary of a reasonable protection of the parties involved and the security of legal relationships. The latter two techniques, distinguishing and overruling, made room for flexibility and permitted adjustment to new conditions.

In the development of the common law, in short, the focal point has been the judge.

C. *Legislation in the common law*

Of course, there is also legislation in the common-law countries. The first striking feature about this legislation is that statutes are usually not formulated in terms of general principles but consist rather of particular rules intended to control certain fact situations specified with considerable detail. Recently there have been some notable exceptions, and it might be asked whether this is the beginning of a movement toward codification.

In considering the place of legislation in the common law, it is necessary to remember the historical fact that the growth of Parlia-

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ment was a popular expression to counterbalance the power of the king. For their part, the king and the efficient organization of the king's courts manifested a jealous and sometimes hostile attitude towards Parliament and its increasing power. The judges refused to place any value on legislative history or preparatory works, and they sought by all means to minimize the infringement of their "common law." This resulted in the adoption of very strict methods of statutory interpretation.

In turn, to counteract these restrictive judicial tactics, the drafting of bills for legislative consideration became an art in the expression of succinct detail in order to assure maximum fulfillment of the legislative intent in specific situations.

By way of contrast, in the system of the civil law and of codified law, legislation occupies the most highly respected place as a source of law. The attitude of the courts is not only one of liberal and extensive interpretation of texts. Even in totally new kinds of cases, civil law courts generally look for a legislative text and its underlying principles which they can use in one way or another as a basis for their new decision.

D. *Judicial decisions in the civil law*

It is sometimes said that in civil law jurisdictions the function of the court is merely to apply the written law. This is a very curtailed statement, and it would mean a very narrow judicial function. Actually, when a court applies a law, it has to interpret that law; in the process of interpretation the court may well extend the scope of the law considerably beyond that originally contemplated. By this method of interpretation and by filling in gaps where the written law is silent or insufficient, the civil law court can be considered as "making" law, interstitially.

In this manner, the utilization of prior decisions is mainly on points of interpretation of the written texts, whereas in the common law, the decisions are themselves the source of law and "make" law "from the whole cloth," as it were.

In the civil law system, courts are not bound to follow previous judicial decisions. Each new decision must be grounded on the authority of the legislative text which provides the basis of continuity and stability. This does not preclude the same result in a later case, because the same text and the same reasons lead to the same conclusion. However, there is no binding rule of precedent; each case must be decided on the primary authority of legislation, and the reasons for the decision must be stated. A court may not render a judgment in the nature of a general rule.

In some countries like France and Belgium, the practice has been

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consolidated that when a certain point has been consistently decided in the same way by an appreciable number of cases, it becomes *"jurisprudence constante"* and is considered binding in future cases. This serves to stabilize the interpretation of the law.

In addition, after a second *"cassation"* (judgment of lower court annulled and case remanded for retrial) by the highest court of appeal in these two countries, the lower tribunal is obliged to accept the solution indicated.

There is also an increasing tendency among attorneys to cite cases as well as codes and other legislative texts.

Finally, for some topics there are very few legislative provisions, for example, in France, in connection with the civil responsibility for delicts and quasi-delicts. Thus, the elaboration of more detailed rules is necessarily delegated to judicial decisions in particular cases.

E. *Comparative comments*

In comparative studies of civil law and common law, it is sometimes concluded on the basis of the foregoing observations that the net result is approximately the same in both systems. In effect, while the common law starts with a case-law basis it also includes legislative encroachments, and while the civil law starts with a legislative basis, it incorporates developments of case-law. While this is a correct statement, it is fraught with the errors and pitfalls of partial truth.

As sources of positive law, legislation and judicial decisions have their place in both systems, but their relative importance is very different. It is not conducive to an understanding of the civil law and the common law to say that the difference is merely one of degree.

Despite the fact that legislation infiltrates into the common law, and regardless of the increasing importance of judicial decisions in a civil law country, the fundamental difference in the nature of the two systems continues to express itself in many other ways. The statutes in England and judicial law-making in France have not brought about any change in the classification of the respective legal systems. On the contrary, the importance of the difference between the civil law and common law is confirmed by an examination in the two systems of their doctrinal materials, legal education and modes of research, as well as in the organization and functioning of their judicial systems.

III. Doctrinal Materials, Legal Education and Research

As a result of the relative importance of legislation and judicial decisions in the civil law, on the one hand, and in the common law, on the other, there follow a number of other essential consequences,

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among which must be mentioned the nature and place of doctrinal materials, legal education and research.

A. *Doctrinal materials*

In civil law countries, the treatises and commentaries of legal writers are generally expressed in the form of systematic expositions and in discussions about broad legal principles. These works formulate general theories about the basic codes and legislation, in relation to the evolution of the legal system as a whole.

In common-law countries, there is not as large a quantity of doctrinal writings, and these are likely to consist of analyses of decided cases with the object of classifying them and distinguishing the rules they represent. The evolution of the law is traced by means of individual points progressively established in a series of judicial decisions. The purpose of these doctrinal writings is thus to compile the decided cases, and then to establish and evaluate their distilled essence. The cases are classified and arranged in a manner which will show up the evolution of the law. As authorities in their pleadings and in their judgments, the attorneys and the judges primarily cite previous cases rather than works of doctrine.

In the civil law, the doctrine is an inherent part of the system and is indispensable to a systematic and analytical understanding of it. The doctrine is not a recognized source of law, but it has exercised a great influence in the development of the law. It molds the minds of students, it gives direction to the work of the practitioners and to the deliberations of the judges, and it guides the legislators towards consistency and systematization.

B. *Legal education*

There is naturally a direct reciprocal influence between the nature of a legal system and the pattern of legal education. The nature of the former promotes the method of the latter, which in turn perpetuates the original character of the system. The program of law studies and the method of legal education establish and fix the fundamental understanding and the mode of thought which condition the individual for his entire professional career.

Legal education for the civil law is centered on legislation, codification and doctrine, on a very high level of abstraction. The great respect for legislation is basic to the judge's approach even when he uses a statute as his starting point for a liberal interpretation of it.

In contrast, legal education for the common law is founded on the primacy of the decided cases; it emphasizes the important role of the king's courts in the development and unification of law, and it

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inclines toward a strict interpretation of statutes in order to minimize the legislative encroachment on the judicial prerogative.

Thus, the great names of the civil law are the names of professors who wrote the treatises and created the doctrine, *e.g.,* Bartolus, Domat, Pothier, Savigny, Ihering, Planiol, Capitant, Laurent and Depage. By contrast, the heroes of the common law are the outstanding judges who contributed most to its development, like Coke, Hardwicke, Mansfield, Marshall, Story, Holmes and Brandeis.

In England, the training of young jurists was long considered to be a function and responsibility of the practicing bar; the Inns of Court still provide an indispensable stage in the preparation of barristers. The university role in legal education is relatively recent. On the Continent, the study of law was always a part of the higher education of the universities. In the United States, legal education has been established as a program of university instruction, and there has also been a growing recognition of the doctrinal writings of outstanding law professors.

In the specific courses of study in England and in the United States, the law student finds himself engaged in the discussion of actual and hypothetical practical problems. He learns very carefully the cases which have acquired great importance, and he develops a skill in analyzing judicial decisions in order to identify the narrow holding of a judgment which is entitled to the application of *stare decisis* as a precedent, while at the same time learning to distinguish it from other cases.

In civil law countries, the student starts his study with codes and textbooks. He learns about the Justinian codifications and their influence on his present-day legal system. He is taught general principles and how to think in abstractions. It becomes part of his being to appreciate classification and co-ordination of subject matter, and to take for granted a comprehensiveness of the law as systematic and a whole. It is only recently in countries like France and Belgium that the law student has been required to read some decided cases, and he usually attaches only secondary importance to the judicial decisions. He concentrates on the codes, the treatises, and the notes taken during the formal lectures by his professors.

Of course, the common-law student does not completely ignore law books of general import and philosophical speculation. At the same time, the civil law student now has occasion to come to know and to appreciate certain judicial decisions, especially in the new programs of *"travaux pratiques,"* which often include the study and discussion of actual cases and practical problems. Nevertheless, it is necessary to recognize that the training and formation of the law student are inevitably predicated upon the nature of the legal system.

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Thus, we return to the original affirmation that judicial decisions determine the nature of the common law system, while legislation is the basic characteristic of the civil law.

C. *Research*

The same affirmation can be made in connection with the methods of legal research. In the civil law system, inquiry usually begins with the codes and other legislation, then it seeks out the commentators and the treatises, and only in third place do cases come in for consideration and evaluation. Furthermore, without the rule of precedent and the principle of *stare decisis,* prior judicial decisions are not necessarily accepted as weighty authorities. Actually, each new decision rests primarily on the original code or legislative text.

In the common law, as such, research is focused essentially on prior judicial decisions, as a result of the very nature of the system. Of course, legislation is controlling where applicable, and it has to be examined to determine questions of applicability, but here again the judicial interpretations become the binding authority whereas in the civil law tradition, each case is related back essentially to the legislative authority.

Neither in the civil law nor in the common law is the indicated method of research an exclusive one. However, in each system there is a basic approach and method of thought that is distinctive in its emphasis.

IV. Judges and Courts

The differences in the nature of the legal systems of the civil law and the common law also manifest themselves with reference to their respective judges and courts. Of course, the essential objective is everywhere the same: to answer questions of law and to resolve disputes. However, in order to understand the two systems properly, there are disparities which must be recognized and evaluated. For more specific identification of ideas, it is useful to consider five points of reference: the training and recruitment of judges, the method of arriving at decisions, the personalization of opinions or the collegiality of judgments, the manner of writing opinions, and the attitude of the judge in case of silence and insufficiency of the written or established law.

A. *The training and recruitment of judges*

The training and the recruitment of judges and the nature of their tenure are very important factors in determining their modes of

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thought, their methods of work and the ways in which they decide cases.

In the common-law countries, there is no particular training for judges apart from the fact that it is necessary to be an attorney or barrister with a number of years of experience and reputation. After having succeeded as a practitioner, one is either appointed by the government, as in England, or elected by the people, as in many American states. The background of his experience in practice conditions his mode of thought and his method of work in discharging his responsibilities as a member of the court. In a legal system based essentially on decided cases, the judges must necessarily be practical, and the elevation of a member of the bar to a seat on the bench is the perfectly natural procedure. It is to be expected that their manner of thinking, working and deciding legal questions should be a continuation of what it was when they were attorneys and barristers.

In certain civil law countries like France, there is a greater difference between the judicial function and the practice of law. The lawyer and the judge both have the same legal education at the university level; after that, however, each individual must make his choice of career, and goes into the practical apprenticeship training for the branch of the legal profession he has selected. Going directly from law study into a judicial association, the future judge approaches the law primarily through the theoretical education which he has received. He finds himself with other people who envision the law in the same way as he does, that is, as a comprehensive body of legal principles coordinated at a high level of generalization and abstraction.

B. *The method of deciding cases*

For their point of departure, civil law judges search the legislation for the controlling principle and the rules which govern the subject; this principle or rule is then applied or interpreted according to the particular facts of the case in dispute. The reasoning process is to go from the general principle to the special case.

On the contrary, common-law judges search in the previous decisions for a similar case, and are guided accordingly. If a statute is involved and the text is clear, the judge abides by its provisions; but if doubt or ambiguity can avoid the statute's applicability, there is again resort to a search of previous decisions for common-law authority as a basis of decision. From another point of view, it can be said that in a common-law country the judge must give effect to a clearly-stated statutory rule, while the judge in a civil law country is sometimes given wide discretionary powers through broadly stated legislation.

Another point of interest is that the common-law jury trial in civil cases left the determination of facts to the jury, so that the judicial

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technique of reducing the power of the jury was to broaden the scope of "matters of law" which fell within the judge's power. In the civil law, a jury in civil cases is either very rare or nonexistent, so that the judge is in complete control of all phases of the trial.

All this does not prevent the common-law judge from discussing general principles nor the civil law judge from taking cases into consideration. However, they do so with a difference in point of view and in method that is very significant even in situations which bear substantial resemblance to one another.

C. *The personal or collective character of decisions*

In the continental countries, judges enjoy a desirable prestige and security, but their emoluments are perhaps more modest than elsewhere. By reason of the usual collegial system of their organization and procedure, the judges always remain anonymous; consequently, the bench does not attract the strongest personalities of the profession. In England, Canada, the United States, and other countries of the common law, opinions are identified with their judicial authors; there can be dissenting or concurring opinions, and each judge has the possibility of setting forth his own point of view. In this manner, the personality of a great jurist makes itself felt and appreciated, and such a person makes a substantial contribution to the development of the law.

D. *The manner of writing opinions and decisions*

When it comes to the writing of judicial opinions and decisions in the two systems, the difference is very striking. In the common law, there is first a more or less organized exposition of all the facts that led to the controversy and that furnish the base for the analysis of the legal problem. Then an examination is made of the previous cases which resemble the present one, especially those cases which have been cited by the parties in the litigation. All these have to be analyzed and evaluated in order to determine which are analogous to the case in hand and which are to be distinguished. Finally, the court decides which precedents are in point, and it is on the basis of their authority that the new decision is grounded.

In the civil law, decisions are much shorter; it would seem that the higher the court in the judicial hierarchy, the shorter its judgment. A meager outline of the essentially relevant facts is followed by a succinct statement of the applicable principles and rules of law; then there is the conclusion which results from the application of the law to the facts of the particular case. There is a strict prohibition against the rendition of a judgment in the form of a general ruling. Thus, it

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is evident how much the manner of writing opinions reflects the basic mode of thought for legal problems and for their solution.

Again, while the respective judges have different approaches in the selection of relevant authorities, it would not be correct to leave the impression of a complete differentiation between the two systems. On the one hand, the court reports of the common law may well contain important discussion and substantial development of general principles. On the other hand, in civil law countries, the record files of the judge or of the *Ministère Public* often contain all the details and the facts of the dispute. Nevertheless, as already noted in other contexts, the point of departure and the method of approach are altogether different, again reflecting the difference in the nature of the two legal systems.

E. *Silence or insufficiency of the written or established law*

Another important item of difference between the common law and the civil law is found in the attitude of the judge in the event of the silence or insufficiency of the written or established law, the unprovided-for case. This does not present any problem for the common-law judge; he is then entirely within his field if he finds or makes the rule of decision. By contrast, for him the difficulty arises when there is a pertinent legislative text not to his liking; the challenge then is to restrict the scope of its application.

On the other hand, by reason of the legislative basis of the civil law, the judge in this system finds himself in an embarrassing situation when the written law is silent or insufficient on an essential issue. The judge cannot refuse to adjudicate under penalty of being guilty of a denial of justice. The various civil law countries have adopted different formulas to guide and instruct the judges in this respect. Article 1 of the Swiss Civil Code authorizes the judge to render the decision which he would make if he were legislator; in France and in Belgium, he is given only the instruction to adjudicate. Article 21 of the Louisiana Civil Code indicates that the judge must decide equitably according to natural law and reason or accepted usage. In Germany, the tradition is that the judge must fill gaps in the written law; one way of doing this is to make use of customary law as a source of law, or else to resort to general principles.

Whatever the explanation given (to fill in gaps or to effectuate the presumed intent of the parties), or the technique used (interpretation or analogy, recourse to custom or general principles), the civil law judges are not always limited to a mere application of the law; in effect they are obliged to make law. Does this not then have the effect of eliminating the important distinction between the common law and the civil law?

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The answer must be in the negative! In the first place, in a Romanist legal system, the written law is the supreme source of law; it is only in the case of silence or insufficiency of the written law that the judge is obliged to be creative. This mode of judicial legislation by the civil law courts represents only the exception, only a very small fraction of the totality of the law; whereas, in the common-law countries, the principal mass and all the residuary areas of the law are what is called "judge-made law" because the essential source of this law is in the decided cases.

In the second place, the common-law judge directly creates the rules of law; this is the significant aspect of his function and of his official authority. When a civil law judge establishes new rules of law, he does so either by virtue of an exceptional legislative delegation or in most instances by virtue of his power of interpretation of the legislative text. In this latter case, it is still in the written law that he seeks the applicable general principles or the bases of a reasoning by analogy.

In the third place, the system and the character of completeness of the codes in civil law countries seriously restrict the scope of this judicial function.

Finally, in the extent to which it is exercised, this creative function of the judicial authority remains marginal and insufficient to change the nature of the legal system.

In summary, the history, the sources and the nature of its development are never effaced from a well-established legal system.

Conclusion

Even though it be admitted that the civil law and the common law started from opposite extremes, it is sometimes said that as a result of the movements each has made in the direction of the other, there is no longer much difference between them. The same social needs, and similar economic and technical conditions, have led to the adoption of similar solutions for their legal problems. If it is true that the results are so close to each other, the methods used to reach them are nevertheless extremely divergent, and the matter is not that simple.

Conversely, neither would it be correct to say that there has been no *rapprochement* between these two great systems. The place and function of legislation and judicial decisions in the civil law, on the one side, and in the common law, on the other, are not so strict as to be mutually exclusive.

Each system possesses strong characteristics of a distinct and comprehensive nature that establish its own individuality. This does not prevent a country having one of these legal systems from borrowing or incorporating some of the traditional features of the other. However, when this happens, the extent of incorporation is relatively so slight

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that it does not have the effect of altering the fundamental nature of the system, which remains in the final analysis what it has always been.

The matter of "mixed jurisdictions," where major areas of both civil law and common law have come together into a living continuity, as in Louisiana, Quebec and Scotland, is another topic and one of great interest. However, it is much too extensive for more than mere mention at this time.

It is apparent that the purpose of these comments has not been to reach a relative evaluation of these two great legal systems. In its own ethnic and historical framework, each system has served well the society in which it functions; each has demonstrated its ability to satisfy the social and economic needs of a society in constant change. Each has also maintained a balance between the elements of flexibility and adaptation, on the one hand, while assuring the essential attributes of stability and security, on the other.

In every country, a legal system is a part of the life and the culture of the people for whose needs it has developed. Its evolution, including its susceptibility to outside influences, cannot be dissociated from its own characteristics. This should never be lost from sight; this is what makes for the usefulness of comparative study in a world where international relations and activities are taking an increasingly important place.

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COMPARISON:
***COMMON LAW* versus *CIVIL LAW* SYSTEMS**

System Features:	Common Law Systems	Civil Law Systems
Continuity of Legal system	Evolutionary	Arbitrary
Major Source of Law	Custom & Practice	Legislative Statutes
Reliance on precedent	Yes (Strong)	No (Weak)
Judicial role in law-making	Active & Creative	Passive and Technical
Role of Legal Scholarship	Secondary and Peripheral	Extensive and Influential
Judicial Review of Statutes & Executive Actions	Yes	No
Major Decision Stage	Trial	Investigation & Examination
Trial Format	Accusatorial/confrontational	Inquisitorial/collaborative
Use of Argument & Debate	Extensive & fundamental	modest & restricted
Style of Legal Reasoning	Inductive	Deductive
Trial Emphasis on:	Procedural Correctness	Factual Certainty
Evidentiary Rules	Formal and restrictive (exclusionary rule)	None (all evidence considered)
Role of lawyers during trial	Primary	Secondary
Functions of lawyers	Debate and oppose	advise and inform
Judge's role during trial	Referee/umpire	Director/examiner
Selection of judges	Political appointment from practicing lawyers	Merit advancement from judicial specialists
Status of Judges	Political VIPs	Mid-level civil servants
Citizen trial participation	Juries (Grand & Petit)	Members of Judicial Panels
Appellate review focus	Procedural	Procedural & substantive
Unity of Court Structure	Unified Court Structure	Diffused Court Structures (multiple specialized courts)

Appendix I
Specimen Writs[1]

Original Writs

A: 'PRAECIPIMUS TIBI' FORMS

i) *Writ of right patent*[2]

Edwardus Dei gratia Rex Angliae, dominus Hiberniae, et dux Aquitaniae, Edwardo comiti Lancastriae salutem. Praecipimus tibi quod sine dilatione plenum rectum teneas A. de B. de uno mesuagio et viginti acris terrae cum pertinentiis in I., quae clamat tenere de te per liberum servitium unius denarii per annum, pro omni servitio, quod W. de T. ei deforciat. Et nisi feceris, vicecomes Nottingham faciat, ne amplius inde clamorem audiamus pro defectu recti. Teste meipso apud Westmonasterium octavo die Octobris anno regni nostri duodecimo.

ii) *Replevin*[3]

Rex vicecomiti Nottingham salutem. Praecipimus tibi quod juste et sine dilatione replegiari facias B. quendam equum suum quod D. cepit et injuste detinet, ut dicitur, et postea eum inde juste deduci facias, ne amplius inde clamorem audiamus pro defectu justitiae. Teste etc.

iii) *De nativo habendo*[4]

Rex vicecomiti S. salutem. Praecipimus tibi quod juste et sine dilatione facias habere A. B. nativum et fugitivum suum cum omnibus catallis suis et tota sequela sua ubicumque inventus fuerit in balliva tua nisi sit in dominico nostro, qui fugit de terra sua post coronationem domini Henrici Regis filii Regis Johannis. Et prohibemus super forisfacturam nostram ne quis eum injuste detineat. Teste etc.

1 Note that in both appendices the Latin spellings have been standardised for ease of interpretation. The diphthong 'ae' (used in some printed precedents) was always written 'e' in the original documents.

2 Fitzherbert, *Natura Brevium*, fo. 1 G, but with royal style and *teste* from 87 SS 108. In the remaining precedents below, the full style and *teste* are omitted.

3 Ibid., fo. 68 D.

4 Ibid., fo. 77 E.

Appendix I
Specimen Writs (Translations)

Original Writs

A: 'PRAECIPIMUS TIBI' FORMS

i) *Writ of right patent*[1]

Edward, by the grace of God king of England, lord of Ireland, and duke of Aquitaine, to Edward earl of Lancaster, greeting. We command you that without delay you do full right to A. of B. in respect of one messuage and twenty acres of land with the appurtenances in J. which he claims to hold of you by the free service of one penny a year for all service, and of which W. of T. deforces him. And if you will not do so, let the sheriff of Nottingham do it, that we may hear no more complaint about this for want of right. Witness my self at Westminster on the eighth day of October in the twelfth year of our reign.

ii) *Replevin*

The king[2] to the sheriff of Nottingham, greeting. We command you that justly and without delay you cause to be replevied to B. a certain horse of his which D. took and unjustly detains, as it is said, and afterwards cause him to be justly dealt with therein, that we may hear no more complaint about this for want of justice. Witness etc.

iii) *De nativo habendo*

The king to the sheriff of S., greeting. We command you that justly and without delay you cause A. to have B. his villein and fugitive, with all his chattels and all his brood, wheresoever he may be found in your bailiwick except in our demesne, who fled from his land since the coronation of the lord King Henry, son of King John. And we prohibit, upon our forfeiture, that anyone detain him unjustly. Witness etc.

1 Cf. B. & M. 13, 16.

2 Real writs always began with the full name and style of the king: see note 2 on opposite page.

Jason Beckfield and David Brady, Social and Economic Aspects of Globalization, William A. Darity, Jr., ed., International Encyclopedia of the Social Sciences (2008)

Since the 1970s and 1980s, the increasing intensity of international economic exchange, the rising prominence and influence of international organizations, the diffusion of cultural products across national boundaries, the spanning of social ties across international borders, and global environmental problems have all placed globalization prominently on the agenda of social science. The definition of globalization remains contested, but globalization can be conceptualized as a multidimensional process of international network formation. (Globalization could also be understood as an ideology, but this would more accurately be termed globalism.) The network metaphor clarifies the concept of globalization by highlighting both the nodes (e.g., people, organizations, and states) and the relations (e.g., trade, investment, organization membership, consumption, and migration) that are central to the globalization process. Thinking about globalization as multidimensional network formation is also a useful heuristic for understanding the established facts and unresolved debates surrounding the phenomenon. Moreover, it helps differentiate the multiple levels of analysis inherent in the process: globalization involves local, regional, national, international, and world levels of social life.

Below, this entry employs the network heuristic to discuss the central issues in the social science of globalization. The discussion begins by exploring relatively settled terrain: the multiple dimensions of globalization. From there, the entry moves to rockier ground: the questions of whether globalization is really new, how extensive it is, and precisely what effects it has.

FIVE DIMENSIONS OF GLOBALIZATION

Cross-national connections are created in the economic, political, cultural, social, and environmental domains. Although these dimensions necessarily overlap, it is analytically useful to distinguish them. Economic globalization results when corporations go multinational, either by selling their products in other countries, buying corporations located in foreign countries, or opening branch offices or subsidiaries outside their home country. Multinational corporate expansion, and the consumption of foreign-sourced goods and services, aggregate into exports, imports, and investment relations among national economies. Political globalization, or the formation of international connections among elected officials, bureaucrats, judges, social movement activists, and states, has also generated intense interest. Political globalization results in part through the formation of intergovernmental organizations (IGOs) like the United Nations and the World Trade Organization, and international nongovernmental organizations (INGOs) like the International Committee of the Red Cross. For instance, Anne-Marie Slaughter (2004) shows how political officials, especially regulators and judges, weave a web of global governance and "world order" through international ties formed by these organizations.

In the cultural field, the major world religions, media conglomerates, multinational corporations, and international tourism transmit and translate meaning (embedded in faith traditions, ideas, products, and practices) and symbols across international boundaries. The development of the international communication infrastructure (radio, satellites, intercontinental telecommunication cables) and the rapid expansion of communication technologies (Internet, cell phones, television) foster this process. Closely related is social globalization, or transnational connections formed by mobile individuals as

they create social relationships. For instance, the density of international ties across countries grows as migrants maintain connections to their origin countries (e.g., through remitting money back home) while building new relationships in their destination countries (e.g., through work, community, and family).

Many identify the environment as a fifth dimension of globalization. If nations are the nodes in international networks, then environmental problems create connections by crossing borders: global warming, ozone depletion, and acid rain have all been defined by social movement activists and scientists as international problems that require international solutions. Indeed, environmental problems illustrate how the various dimensions of globalization sometimes reinforce one another: social movement activists bind together through international social movement organizations (social globalization) to spread awareness of environmental problems (cultural globalization) caused in part by multinational corporations (economic globalization), and urge the adoption of international agreements like the 1997 Kyoto Protocol on greenhouse gas emissions (political globalization).

WHEN AND WHERE IS GLOBALIZATION?

While the example of the Kyoto Protocol illustrates how the dimensions of globalization can cohere, intense international debate over the protocol raises questions about the pace and periodization of globalization, and, more fundamentally, about how "global" globalization is. Indeed, debate over the timing and extent of globalization animates much research. For instance, world-systems theorists such as Immanuel Wallerstein and Christopher Chase-Dunn trace the millennia-long evolution of international economic and political systems, and world-society theorists such as John Meyer and John Boli view social and cultural globalization through a long historical lens that looks back over a century. Social scientists have not reached consensus on when globalization in its various forms began, but there is an emerging consensus that the world has experienced a renewed and possibly distinct economic globalization since the mid-1970s (i.e., after the oil crises and the collapse of the Bretton Woods system of fixed exchange rates in 1973). Only during this period did the level of international trade surpass its previous peak in the early twentieth century. Thus, economic globalization may follow waves, with crests of integration followed by troughs of separation.

In the political dimension, there is also evidence that globalization substantially intensified in the latter half of the twentieth century. With the establishment of the United Nations and related IGOs (including the International Monetary Fund, World Bank Group, International Labour Organization, and World Health Organization), a global governance framework emerged. It has fostered the creation of thousands of intergovernmental and nongovernmental organizations that generate a network of international association (Boli and Thomas 1999). Key nodes in this network include regional organizations like the European Union Page 334 | (EU) that liberalize trade and create common policies among nations within negotiated geographical boundaries. The EU has progressed furthest toward the creation of a regional market and government, as it has allowed the free movement of people across borders, eliminated barriers to trade, created a supranational court, and established supranational policies. The EU, established as the European Economic Community in 1957, may have inspired regional integration efforts in other parts of the world, including Southeast Asia—the Association of Southeast Asian Nations (ASEAN, 1967); South America—Mercado Común del Sur (Southern Common

Market or Mercosur, 1991); North America—the North American Free Trade Agreement (NAFTA, 1994); Central America—the Central American Common Market (CACM, 1960); and Africa—the Organization of African Unity (OAU, 1963). These organizations may transform world politics by changing how states interact and by generating new layers of policy and politics.

The accelerating economic liberalization and polity construction within geographical regions fuels the debate over where globalization actually happens (indeed, a large literature addresses whether regional integration creates "stepping-stones" or "stumbling blocks" to a fully integrated global system). Here again, the network heuristic helps. Some images of globalization depict a world where national nodes worldwide are increasingly interconnected without regard to place, while others allow for a more fragmented and uneven network where some nodes are linked much more densely than others. These contrasting images manifest in research that has shown, for instance, that Western Europe is much more densely intertwined in both the economic and political dimensions than nations in other world regions.

WHAT DOES GLOBALIZATION DO?

Setting aside controversies of period and place, social scientists blame or credit globalization for a panoply of social ills and goods, from economic inequality to economic growth, from political domination to democratization, from the decline of national sovereignty to the renaissance of the state, from social engagement to xenophobia, and from cultural homogenization to ethnic conflict. Meanwhile, others see a feeble globalization. Here, this entry reviews some of the key arguments for what globalization does.

Globalization, advanced partly by IGOs like the World Trade Organization and the International Monetary Fund that compel economic liberalization, has been the subject of vigorous debate about growing income gaps between rich and poor. The argument is that, in the name of international competitiveness, government revenue and expenditures are cut, and industries are deregulated and privatized. Globalization is also blamed for lowering the wages of less-skilled workers by shifting manufacturing jobs to lower-wage countries, and by enlarging the pool of low-wage labor through immigration. In turn, in low-wage countries of the "Global South," globalization is blamed for proliferating sweatshops owned by multinational corporations, producing an underclass of nonunionized labor, and generating an exploitive transnational capitalist and entrepreneurial class. Moving from individuals to countries, globalization arguably benefits rich countries at the expense of poor countries, by further concentrating wealth in rich countries as profits are repatriated from the Global South to the Global North. On the other hand, much of the literature has been skeptical of the criticisms that have been leveled at globalization. Just to take one example of the potentially salutary effects of globalization, it has been argued that globalization actually reduces disparities among rich and poor countries in their overall levels of economic development, by spreading industrialization to poor countries.

Social scientists also disagree intensely over whether globalization brings about political convergence among states. There is evidence that states adopt increasingly similar policies in areas such as education, welfare, the environment, human rights, and population as they interact more with international organizations. International organizations, it is argued, create and diffuse policy models

(or “scripts”) to states, and states adopt these models, in part, to appear as legitimate members of a world society. This process may reflect the spread of modern, Western culture (e.g., individualism, universalism, rationalism, science, and progress) around the globe. These claims remain controversial, and some argue that international organizations serve national interests and as such have strictly limited independent influence. It is a major challenge to contemporary social science to bring some resolution to the varied, contradictory, and multivalent picture of globalization that has emerged.

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Doing Business in 2006

Creating Jobs



A copublication of the World Bank and the International Finance Corporation

Creating jobs: an overview

Who reformed most?
Where is doing business easy?
Less costly does not mean less protection
More reform is needed in Africa
Success requires new jobs in the formal economy

If you were opening a new business in Lao PDR, the start-up procedures would take 198 days. If you were opening one in Syria, you would have to put up $61,000 in minimum capital—51 times average annual income. If you were building a warehouse in Bosnia and Herzegovina, the fees for utility hook-up and compliance with building regulations would amount to 87 times average income. And if you ran a business in Guatemala, it would take you 1,459 days to resolve a simple dispute in the courts. If you were paying all business taxes in Sierra Leone, they would take 164% of your company's gross profit.[1]

Starting a business is a leap of faith even in the best of circumstances. Governments should encourage the daring. And many do. In 2004, 99 countries—two-thirds of the *Doing Business* sample—introduced 185 reforms to make it easier to do business. They simplified some aspect of business regulations, strengthened property rights, reduced exporting and importing costs, eased tax burdens and increased access to credit.

Such reforms allow firms to grow faster and create more jobs. An increasing number of those jobs will be in the formal economy because the benefits of being formal (such as easier access to credit and better utility services) often outweigh the costs (such as taxes). And more formal jobs will mean that more workers are protected by pensions, safety regulations and health benefits.

Women, who now make up three-quarters of workers in the informal sector, will be big beneficiaries. So will young and inexperienced workers looking for their first job.

Jobs are a priority for countries emerging from conflict, to absorb former soldiers into the workforce and quickly enable families to rebuild their lives. Without jobs there is a high risk that these countries will return to conflict. And jobs in the formal economy are a priority for countries in Africa—which have the most obstacles to doing business and are reforming more slowly than anywhere else.

Who reformed most?

In 2004 Serbia and Montenegro led in making the kinds of reforms that can spur growth in firms and jobs, improving in 8 of the 10 areas studied by *Doing Business* (table 1.1). The capital requirement for starting a new business was cut from 5,000 euros to 500. The time to start a new business was reduced from 51 days to 15. A new labor law made it easier to hire workers by allowing firms to offer term contracts rather than having to hire under indefinite contracts even when addressing temporary needs. The time to resolve commercial disputes fell from 1,028 days to 635, thanks to a new code of civil procedure. Payroll and sales tax were replaced by a value added tax, which is easier to collect. The number of new registered (formal) firms in 2004 jumped by 42% over the previous year.

Georgia was the runner-up reformer. A new licensing law cut from 909 to 159 the number of licensed activities. A one-stop shop was created for license applications, so that now businesses can submit all documents there, with no verification by other agencies required. A simplified tax code eliminated 12 of 21 taxes. And the time

to register property fell by 75%, and the cost by 70%.

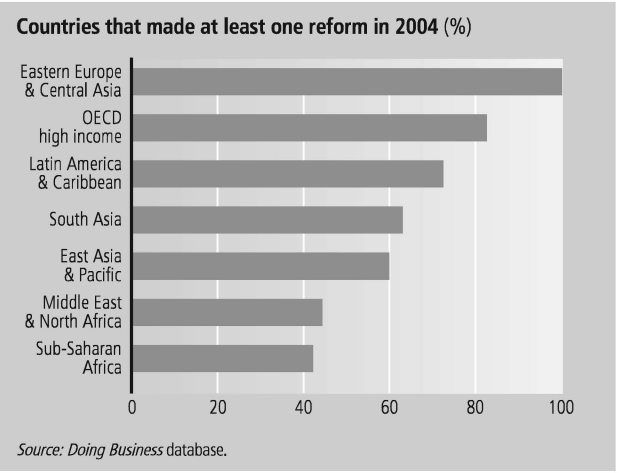
Regionally, the most reform took place in Eastern Europe and Central Asia, where every country took at least one step to make things easier for business (figure 1.1). Many of these reforms were driven by integration with the European Union. Three Eastern European countries—Slovakia, Romania and Latvia—were among the top 12 reformers in 2004 (see table 1.1), and Slovakia was the leading reformer in 2003. All 3 have made it easier for new businesses to open. These efforts appear to be paying off: in 2004 the number of new start-ups jumped by 8% in Latvia, 13% in Slovakia and 22% in Romania. The most common reforms in the region, occurring in half the countries, involved simplifying tax administration and reducing tax burdens. Earlier reforms in Estonia, Russia and Slovakia led the way.

Some of the boldest reforms, driving the biggest improvements in the *Doing Business* indicators, were:

- Serbia and Montenegro's simplification of business start-up.
- Egypt's streamlining of customs procedures and trade documents.
- Brazil's improvements to bankruptcy law.

Serbia and Montenegro moved start-up registrations from its courts to a new administrative registry. Entrepreneurs can register online, and a "silence is consent" rule ensures rapid approval. In addition, a new unified electronic database links the commercial courts, statistics bureau, customs office, national bank and municipalities. With these reforms, a company can start operating in 15 days rather than 51 (figure 1.2).

FIGURE 1.1
Every country in Eastern Europe and Central Asia reformed



Source: Doing Business database.

Egypt established a single window for trade documentation and merged 26 approvals into 5. A time limit of 2 days for passing through customs now applies. Improvements at customs were part of a broader reform to cut the number of tariff bands from 27 to 6 and simplify inspection procedures at the border.

Brazil's new bankruptcy law gives insolvent companies the option of remaining open while undergoing restructuring. Creditors have more power to direct reorganization proceedings by establishing creditors' committees that vote on restructuring plans. Secured creditors now get preference over tax claims when assets are sold.

TABLE 1.1
The top reformers in 2004

Country	Starting a business	Dealing with licenses	Hiring and firing	Registering property	Getting credit	Protecting investors	Paying taxes	Trading across borders	Enforcing contracts	Closing a business
Serbia and Montenegro	✓	✓	✓	✓	✓		✓		✓	✓
Georgia	✓	✓	✓	✓			✓			
Vietnam	✓			✓		✓			✓	✓
Slovakia	✓		✓	✓	✓					
Germany	✓		✓					✓	✓	
Egypt	✓			✓	✓			✓		
Finland		✓	✓				✓			✓
Romania	✓				✓		✓		✓	
Latvia	✓			✓			✓		✓	
Pakistan	✓			✓		✓		✓		
Rwanda					✓			✓	✓	
Netherlands		✓		✓			✓			

Note: Countries are ranked on the number of reforms. When countries have the same number of reforms, they are ranked on the impact of the reforms on the *Doing Business* indicators. The larger the improvement in ranking on each set of indicators, the higher the country ranks as a reformer.

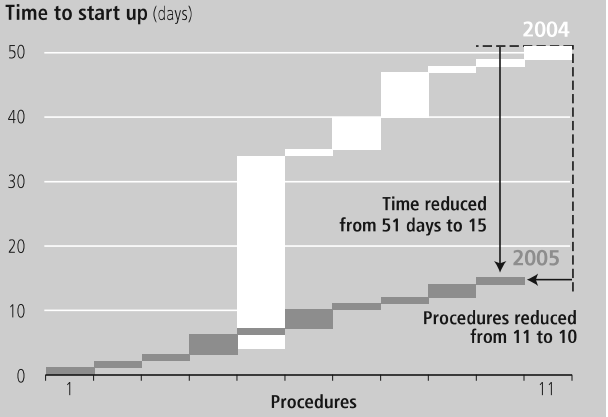
Source: Doing Business database.

The new law halved the average time for going through bankruptcy from 10 years to 5 and is expected to raise the recovery rate from 0% of company assets to 7.5%.

But not all changes in *Doing Business* indicators were for the better. In 2004, 20 countries—18 of them poor—made it harder to do business. Among them:

- Madagascar raised its minimum capital requirement for starting a business to $6,500—22 times annual income per capita.
- Chad raised transfer taxes and notary fees for registering property. Taxes and fees to buy land or buildings equal 21% of their value—among the highest levels in the world.
- Mauritania raised its corporate income tax rate from 20% to 25%—the only country to increase this tax in 2004.

FIGURE 1.2
Making entry easier in Serbia and Montenegro



Source: Doing Business database.

Where is doing business easy?

New Zealand has the most business-friendly regulation in the world, as measured by the *Doing Business* indicators (table 1.2). Singapore is the runner-up. The United States is third. Five other East Asian countries—Hong Kong (China), Japan, Thailand, Malaysia and Korea—are among the top 30. So are the Baltic countries—Lithuania, Estonia and Latvia. Their ranking is a remarkable achievement, as only a decade has passed since they first began reforms.

But the rankings on the ease of doing business also show that many reformers still have a long way to go. Although Eastern Europe was the top reforming region, some of its countries still rank poorly on the ease of doing business. For example, Serbia and Montenegro's rank is 92, Croatia's is 118 and Ukraine's 124. Egypt, another top reformer in 2004, ranks 141. And India, though making big gains on collateral recovery and ease of registering property, ranks 116—25 places behind China.

Rankings on the ease of doing business do not tell the whole story. The indicator is limited in scope. It does not account for a country's proximity to large markets, quality of infrastructure services (other than services related to trading across borders), the security of property from theft and looting, macroeconomic conditions or the underlying strength of institutions. Thus while Jamaica ranks close (at 43) on the ease of doing business to France (at 44), this does not mean that businesses are better off operating in Kingston rather than in Paris. Crime and macroeconomic imbalances—2 issues not directly studied in *Doing Business*—make Jamaica a less attractive destination for investment.

But a high ranking on the ease of doing business does mean that the government has created a regulatory environment conducive to the operation of business. Often, improvements on the *Doing Business* indicators proxy for broader reforms to laws and institutions, which affect more than the administrative procedures and the time and cost to comply with business regulation.

TABLE 1.2
Top 30 economies on the ease of doing business

1	New Zealand	16	Estonia
2	Singapore	17	Switzerland
3	United States	18	Belgium
4	Canada	19	Germany
5	Norway	20	Thailand
6	Australia	21	Malaysia
7	Hong Kong, China	22	Puerto Rico
8	Denmark	23	Mauritius
9	United Kingdom	24	Netherlands
10	Japan	25	Chile
11	Ireland	26	Latvia
12	Iceland	27	Korea
13	Finland	28	South Africa
14	Sweden	29	Israel
15	Lithuania	30	Spain

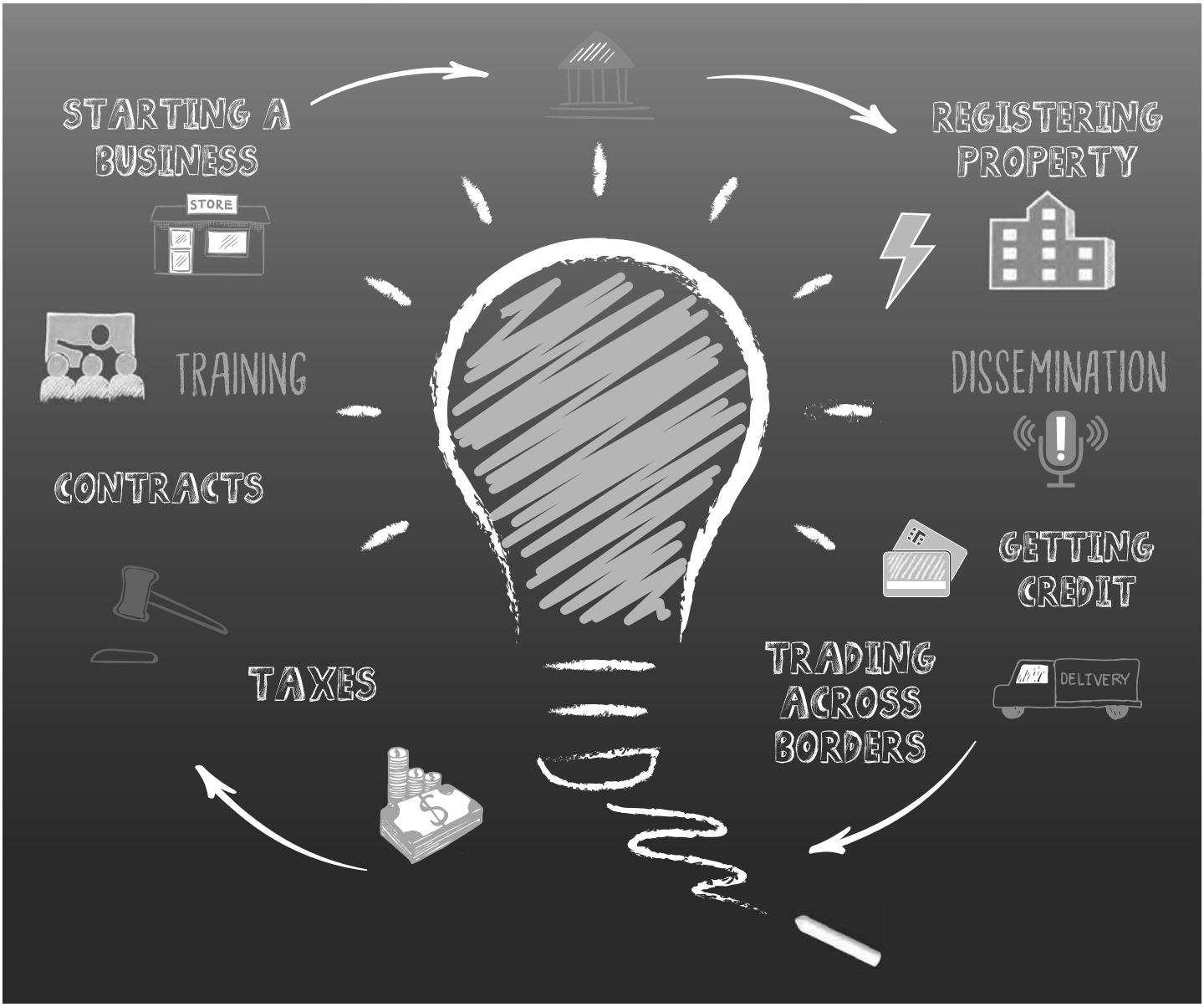
Note: The rankings for all economies are benchmarked to January 2005 and reported in the Country tables. The ease of doing business averages country rankings across the 10 topics covered in *Doing Business in 2006*. This year's rankings are not comparable to last year's as three new sets of indicators—on dealing with licenses, paying taxes and trading across borders—have been included. See the Data notes for details.

Source: Doing Business database.

16TH EDITION

DOING BUSINESS 2019

Training for Reform



*COMPARING BUSINESS REGULATION FOR DOMESTIC FIRMS IN **190** ECONOMIES*

A World Bank Group Flagship Report

Overview

An economy cannot thrive without a healthy private sector. When local businesses flourish, they create jobs and generate income that can be spent and invested domestically. Any rational government that cares about the economic well-being and advancement of its constituency pays special attention to laws and regulations affecting local small and medium-size enterprises (SMEs). Effective business regulation affords micro and small firms the opportunity to grow, innovate and, when applicable, move from the informal to the formal sector of an economy. Like its 15 predecessors, *Doing Business 2019* continues to enable regulators to assess and benchmark their domestic business regulatory environments.

Doing Business advocates for both regulatory quality and efficiency. It is important to have effective rules in place that are easy to follow and understand. To realize economic gains, reduce corruption and encourage SMEs to flourish, unnecessary red tape should be eliminated. However, specific safeguards must be put in place to ensure high-quality business regulatory processes; efficiency alone is not enough for regulation to function well. What use is it when one can transfer property in just a few days and at a low cost, but the property registry contains unreliable information with incomplete geographic coverage? *Doing Business* exposes cases with evident discrepancies between regulatory quality and efficiency, signaling to regulators what needs to be reformed.

Doing Business 2019 measures the processes for business incorporation, getting a building permit, obtaining an electricity connection, transferring property, getting access to credit, protecting minority investors, paying taxes, engaging in international trade, enforcing contracts and resolving insolvency. *Doing Business* collects and publishes data on labor market regulation with a focus on the flexibility of employment regulation as well as several aspects of job quality. However, this regulatory area does not constitute part of the ease of doing business ranking (figure 1.1). For more details on the *Doing Business* indicators, see the data notes at http://www.doingbusiness.org.

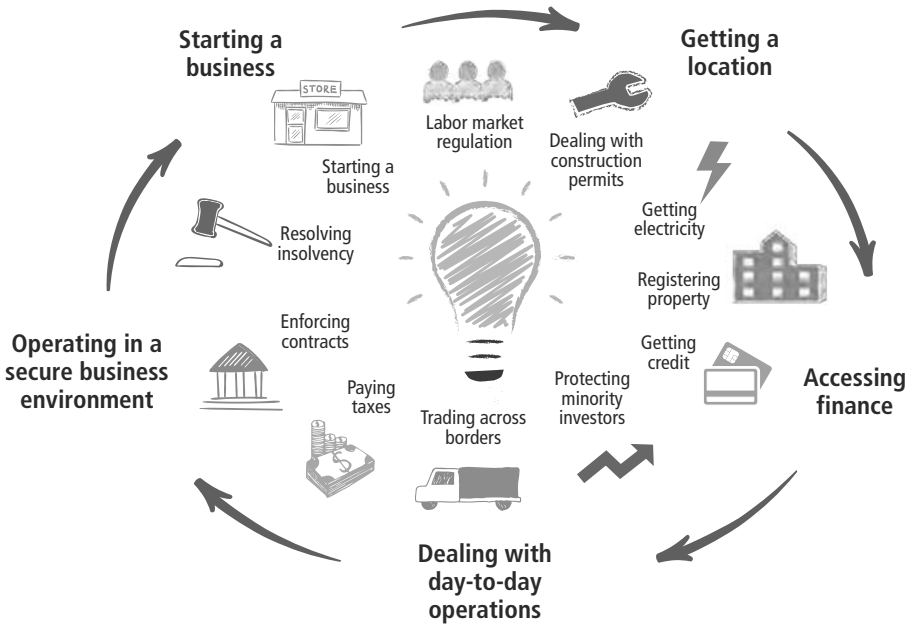
Each of the measured business regulatory areas is important to nascent and existing entrepreneurs. However, as *Doing Business* data show, SME owners face drastically different realities across economies as they set up and operate their businesses. An entrepreneur in Uganda, for example, will spend nearly a month and undertake 13 procedures to set up a new company. The entrepreneur will then be required to manage another 18 interactions with different



- *Doing Business* captured a record 314 regulatory reforms between June 2, 2017, and May 1, 2018. Worldwide, 128 economies introduced substantial regulatory improvements making it easier to do business in all areas measured by *Doing Business*.
- The economies with the most notable improvement in *Doing Business 2019* are Afghanistan, Djibouti, China, Azerbaijan, India, Togo, Kenya, Côte d'Ivoire, Turkey and Rwanda.
- One-third of all business regulatory reforms recorded by *Doing Business 2019* were in the economies of Sub-Saharan Africa. With a total of 107 reforms, Sub-Saharan Africa once again has a record number this year.
- The BRIC economies—Brazil, the Russian Federation, India and China—introduced a total of 21 reforms, with getting electricity and trading across borders the most common areas of improvement.
- The 10 top economies in the ease of doing business ranking share common features of regulatory efficiency and quality, including mandatory inspections during construction, automated tools used by distribution utilities to restore service during power outages, strong safeguards available to creditors in insolvency proceedings and automated specialized commercial courts.
- Training opportunities for service providers and users are positively associated with the ease of doing business score. Similarly, increased public-private communication on legislative changes and processes affecting SMEs are associated with more reforms and better performance on the *Doing Business* indicators.



FIGURE 1.1 What is measured in *Doing Business*?



Source: Doing Business database.
Note: Labor market regulation is not included in the ease of doing business ranking.

agencies and wait an additional four months to obtain a building permit. Once the construction of the warehouse is completed, the entrepreneur will need to wait another two months and cash out 7,513.6% of income per capita to obtain a connection to the electrical grid. In contrast, a Danish entrepreneur can expect to be able to register a new business in just 3.5 days, complete all required legal procedures to build a warehouse through seven steps in slightly over two months and secure a reliable electricity connection for about 100% of local income per capita. Differences in regulatory and institutional quality can affect how many new businesses are created and the dynamism of the private sector, which generates jobs and economic opportunities. In Denmark the average number of newly registered companies is eight per 1,000 workers per year, whereas in Uganda this figure is less than one new company per 1,000 workers per year.[1] Many factors explain this difference, including the level of business regulation.[2]

Doing Business does not claim to cover all the areas pertinent to private sector development and growth. The report has a set of clear limitations; *Doing Business* data alone are not sufficient to assess the overall competitiveness or foreign investment prospects of an economy. *Doing Business* does not assess market size, the soundness and depth of financial markets, macroeconomic conditions, foreign investment, security or political stability. However, the *Doing Business* indicators do offer insights for policy makers to identify areas for reform and improve the local business environment. For more information on what is measured and what is not, see the chapter About *Doing Business*.

WHAT ARE THE BENEFITS OF IMPROVED BUSINESS REGULATION?

Doing Business includes 11 indicator sets that measure aspects of business regulation which are important to domestic small and medium-size companies and national competitiveness. Evidence from economic literature corroborates the economic relevance and importance of the areas measured by *Doing Business*. In the case of the starting a business indicator set alone, more than 300 research articles have been published in the top 100 academic journals since 2003 assessing how the regulatory environment for entry affects a wide range of economic outcomes such as productivity, growth, employment and informality. Recent research shows the positive effects of improved business regulation. Fewer procedures and lower levels of minimum capital, for example, are positively and significantly associated with the process of starting a business. Where procedures are more complex or unclear, the likelihood of corruption is higher.[3] Another study discusses the benefits to companies of formal registration, such as greater access to new equipment and a larger scale of operations, which can lead to increased competitiveness and productivity.[4]

In the context of construction permitting, simplicity and transparency are key in allowing businesses to expand and build new and safe infrastructure. Research shows that regulatory burdens often pose substantial obstacles for investors. Discrepancies among existing laws, for example, can lead to unnecessary and even contradictory compliance requirements.[5] Furthermore, lengthy processing times for required approvals—as is the case in Ghana—can drive up costs and spur the development of an informal construction sector, where falsified construction permits result in unsafe infrastructure.[6]

Electricity is a necessity for any business to function properly and expand. It is also an important element in the competitiveness and strengthening of human capital in an economy. Research data indicate that higher electricity costs tend to have an adverse impact on businesses. As prices rise, firms shift their focus to less electricity-intensive production processes, resulting in reduced output and productivity.[7] Equally important is the reliability of a power connection. Recent research finds that power outages and deficient power infrastructure in Sub-Saharan Africa had a measurable negative impact on economic growth over the period 1995–2007.[8]

Similarly, clearly defined regulation and equal access to property rights are essential for enabling businesses to expand their operations. If governments do not put in place adequate land ownership protections and leave investors open to land disputes or property seizures, stakeholders would be disinclined to put money into land and property development projects. A recent study exploring whether political institutions have an impact on the effectiveness of economic reforms in promoting growth finds that financial and trade reforms are more effective in developing economies with sound property rights. This evidence suggests that sufficiently developed property rights may be a precondition for reaping the growth benefits of reform.[9] Ample literature on the importance of property rights finds a strong association between investment, access to finance, productivity and economic growth.[10]

Another area measured by *Doing Business* is the protection of minority investors. Greater protection helps foster trust and confidence and, in turn, spurs greater access to finance for entrepreneurs.[11] The indicator set focuses on how policy makers mitigate the risk that corporate executives, directors and majority shareholders will use their position to advance their own interests at the expense of the company and other shareholders. Clear rules, robust rights and increased transparency are some of the regulatory instruments at their disposal. Corporate governance is a key determinant of investment efficiency,[12] while shareholders' ability to sue and hold directors accountable are essential checks and balances.[13]

Finally, the regulation of labor markets is critical as policy makers work to create more and better jobs for their citizens. Labor regulation is also an area of interest to researchers as they strive to assess the optimal balance between adequate worker protections and labor market efficiency. In India, for example, research shows that when faced with restrictive labor laws, firms choose to circumvent such legislation by hiring workers indirectly through contractors, especially in times of economic uncertainty.[14] Another study on foreign investment and the organization of global firms suggests that firms consider the strength of worker bargaining power when making sourcing decisions.[15]

Doing Business 2014 presented a synthesis of the fast-growing literature published in top-ranking economic journals using *Doing Business* data for analysis or motivation.[16] The chapter reviews the different estimation methods used in economic analysis and summarizes the recent research by area of study and methodology, including firm entry and labor market regulation, trade regulations and cost and tax regulations. *Doing Business 2016* also presented an extended review of the literature published in 70 top academic law journals focusing on four sets of indicators: enforcing contracts, getting credit (legal rights), protecting minority investors and resolving insolvency.[17] For further research insights, updated annually, see the chapter About *Doing Business* and the *Doing Business* website at http://www.doingbusiness.org/research.

WHERE IS BUSINESS REGULATION BETTER?

Doing Business benchmarks aspects of business regulation and practice using specific case studies with standardized assumptions. Based on an economy's performance in each of the 11 measured areas, the report scores the efficiency and quality of the business environment. This approach facilitates the comparison of regulation and practice across economies and allows for changes to be tracked over time. The ease of doing business score (box 1.1) serves as the basis for ranking economies on their business environment: to obtain the ranking, economies are sorted by their scores. The ease of doing business score shows an economy's absolute position to the best regulatory practice, while the ease of doing business ranking is an indication of an economy's position relative to that of other economies.

The economies that rank highest in the ease of doing business (table 1.1) are those that have consistently well-designed business regulation or whose regulatory environments have thrived thanks to comprehensive reform over the years. The top three economies this year—New Zealand, Singapore and Denmark—exemplify a business-friendly environment. Meanwhile, Mauritius, which joins the group of

BOX 1.1 What is the ease of doing business score?

This year the name of the *Doing Business* distance to frontier score has been changed to "ease of doing business score" to better reflect the main idea of the measure—a score indicating an economy's position to the best regulatory practice. Nevertheless, the process for calculating the score remains the same. The score combines measures with different units such as time to start a company or procedures to transfer a property. The score captures the gap between an economy's current performance and a measure of best regulatory practice set in *Doing Business 2015* across the entire sample of the same 41 indicators for 10 *Doing Business* indicator sets used in previous years. For example, according to the *Doing Business* database, across all economies and over time, the least time needed to start a business is 0.5 days, while in the worst 5% of cases it takes more than 100 days. Half a day is, therefore, considered the best performance, while 100 days is the worst. Higher scores show absolute better ease of doing business (the best score is set at 100), while lower scores show absolute poorer ease of doing business (the worst performance is set at 0). The percentage point scores of an economy on different indicators can be averaged together to obtain an aggregate score. For more details, see the chapter on the ease of doing business score and ease of doing business ranking available at http://www.doingbusiness.org.

top 20 economies this year (the only Sub-Saharan African economy to do so), has reformed its business environment methodically over time. Indeed, over the past decade Mauritius has reformed more than once in almost all areas measured by *Doing Business*.[18] Following seven reforms in the area of property registration captured by *Doing Business* since 2005, for example, the time needed to register property has decreased more than 12 times; the time needed for business incorporation has decreased almost 10 times as a result of four reforms in starting a business.[19]

A continuous and focused reform agenda keeps an economy competitive and vigilant, as others also keep improving. Two economies that enter the top 20 this year—the United Arab Emirates and Malaysia—have maintained such a reform momentum. The United Arab Emirates is the highest-ranking economy in the Middle East and North Africa region, with reforms captured in four areas. Six reforms in Malaysia were measured by *Doing Business*, resulting in the second highest regional improvement in the ease of doing business score.

Twelve of the top 20 economies are from the OECD high-income group; four are from East Asia and the Pacific, two are from Europe and Central Asia and one each is from Sub-Saharan Africa and the Middle East and North Africa. Except for low-income economies, all income groups are represented. The regional diversity and varying income levels among the top 20 economies underscore the point that any economy can make it to the top, as long as it has few bureaucratic hurdles and strong laws and regulation. The efficiency and quality of regulation are what matter most for a good performance in the ease of doing business ranking.

The top 20 economies share a number of international good practices. In the area of starting a business, 13 of these economies have at least one procedure that can be completed online in 0.5 days. The electricity distribution utilities in all but one of the top 20 economies use automated tools, allowing for faster, more efficient and more secure restoration of service during power outages. In the areas of construction and land administration, in all top 20 economies mandatory inspections are always done in practice during the construction of a warehouse, and the majority have comprehensive geographic coverage. The quality of legal infrastructure and the strength of legal institutions is also robust. In all top 20 economies, for example, the insolvency framework stipulates that a creditor has the right to object to decisions accepting or rejecting creditors' claims, providing strong safeguards to creditors in insolvency proceedings. Court automation is prevalent, and judgments are enforced twice as fast on average (95.6 days) than in the remaining economies (200 days). These economies also have strong disclosure requirements in place to prevent the misuse of corporate assets by directors for personal gain. Most mandate that a shareholder must immediately disclose transactions—as well as any conflicts of interest—to other shareholders. To date, no economy has reached the best regulatory performance on all indicators; every economy can progress further by learning from the experience of others.

More trends emerge from the list of the top 50 economies. Regionally, almost 60% of the top 50 economies are from the OECD high-income group, followed by Europe and Central Asia (24%) and East Asia and the Pacific (12%). South Asia and Latin America and the Caribbean are the two regions absent from the top 50 ranking. Upper-middle-income economies represent almost 26% of the top 50 economies. Georgia, Kosovo and Moldova are the three lower-middle-income economies on the list and Rwanda is the only low-income economy. There is, however, a large variation between regions' regulatory efficiency and regulatory quality (figure 1.2). While four of the 10 top improvers in *Doing Business 2019* are Sub-Saharan African economies, the

TABLE 1.1 Ease of doing business ranking

Rank	Economy	EODB score	EODB score change	Rank	Economy	EODB score	EODB score change	Rank	Economy	EODB score	EODB score change
1	New Zealand	86.59	0.00	65	Colombia	69.24	+0.20	129	Barbados	56.78	0.00
2	Singapore	85.24	+0.27	66	Luxembourg	69.01	0.00	130	St. Vincent and the Grenadines	56.35	+0.01
3	Denmark	84.64	+0.59	67	Costa Rica	68.89	-0.47	131	Cabo Verde	55.95	+0.02
4	Hong Kong SAR, China	84.22	+0.04	68	Peru	68.83	+0.56	132	Nicaragua	55.64	+0.37
5	Korea, Rep.	84.14	-0.01	69	Vietnam	68.36	+1.59	133	Palau	55.59	+0.01
6	Georgia	83.28	+0.48	70	Kyrgyz Republic	68.33	+2.57	134	Guyana	55.57	-1.21
7	Norway	82.95	+0.25	71	Ukraine	68.25	+0.94	135	Mozambique	55.53	+1.78
8	United States	82.75	-0.01	72	Greece	68.08	-0.12	136	Pakistan	55.31	+2.53
9	United Kingdom	82.65	+0.33	73	Indonesia	67.96	+1.42	137	Togo	55.20	+6.32
10	Macedonia, FYR	81.55	+0.32	74	Mongolia	67.74	+0.27	138	Cambodia	54.80	+0.41
11	United Arab Emirates	81.28	+2.37	75	Jamaica	67.47	+0.55	139	Maldives	54.43	+0.10
12	Sweden	81.27	0.00	76	Uzbekistan	67.40	+1.08	140	St. Kitts and Nevis	54.36	+0.01
13	Taiwan, China	80.90	+0.24	77	India	67.23	+6.63	141	Senegal	54.15	+0.37
14	Lithuania	80.83	+0.29	78	Oman	67.19	-0.02	142	Lebanon	54.04	+0.07
15	Malaysia	80.60	+2.57	79	Panama	66.12	+0.41	143	Niger	53.72	+1.24
16	Estonia	80.50	+0.01	80	Tunisia	66.11	+1.51	144	Tanzania	53.63	+0.34
17	Finland	80.35	+0.05	81	Bhutan	66.08	+0.20	145	Mali	53.50	+0.23
18	Australia	80.13	-0.01	82	South Africa	66.03	+1.37	146	Nigeria	52.89	+1.37
19	Latvia	79.59	+0.33	83	Qatar	65.89	+0.64	147	Grenada	52.71	+0.07
20	Mauritius	79.58	+1.29	84	Malta	65.43	+0.28	148	Mauritania	51.99	+0.92
21	Iceland	79.35	+0.05	85	El Salvador	65.41	+0.21	149	Gambia, The	51.72	+0.23
22	Canada	79.26	+0.38	86	Botswana	65.40	+0.46	150	Marshall Islands	51.62	+0.01
23	Ireland	78.91	-0.51	87	Zambia	65.08	+1.48	151	Burkina Faso	51.57	+0.12
24	Germany	78.90	0.00	88	San Marino	64.74	+2.27	152	Guinea	51.51	+2.02
25	Azerbaijan	78.64	+7.10	89	Bosnia and Herzegovina	63.82	+0.27	153	Benin	51.42	+0.13
26	Austria	78.57	+0.03	90	Samoa	63.77	+0.01	154	Lao PDR	51.26	+0.11
27	Thailand	78.45	+1.06	91	Tonga	63.59	+0.03	155	Zimbabwe	50.44	+1.92
28	Kazakhstan	77.89	+0.73	92	Saudi Arabia	63.50	+1.62	156	Bolivia	50.32	+0.15
29	Rwanda	77.88	+4.15	93	St. Lucia	63.02	+0.06	157	Algeria	49.65	+2.06
30	Spain	77.68	+0.07	94	Vanuatu	62.87	-0.21	158	Kiribati	49.07	+0.33
31	Russian Federation	77.37	+0.61	95	Uruguay	62.60	+0.34	159	Ethiopia	49.06	+0.91
32	France	77.29	+0.99	96	Seychelles	62.41	-0.01	160	Micronesia, Fed. Sts.	48.99	0.00
33	Poland	76.95	-0.36	97	Kuwait	62.20	+0.75	161	Madagascar	48.89	+0.71
34	Portugal	76.55	-0.07	98	Guatemala	62.17	+1.01	162	Sudan	48.84	+3.75
35	Czech Republic	76.10	+0.05	99	Djibouti	62.02	+8.87	163	Sierra Leone	48.74	+0.15
36	Netherlands	76.04	+0.01	100	Sri Lanka	61.22	+1.80	164	Comoros	48.66	+0.14
37	Belarus	75.77	+0.72	101	Fiji	61.15	+0.04	165	Suriname	48.05	-0.05
38	Switzerland	75.69	+0.01	102	Dominican Republic	61.12	+0.55	166	Cameroon	47.78	+0.83
39	Japan	75.65	+0.05	103	Dominica	61.07	+0.04	167	Afghanistan	47.77	+10.64
40	Slovenia	75.61	+0.02	104	Jordan	60.98	+1.42	168	Burundi	47.41	+0.73
41	Armenia	75.37	+2.06	105	Trinidad and Tobago	60.81	-0.12	169	Gabon	45.58	-0.23
42	Slovak Republic	75.17	+0.29	106	Lesotho	60.60	+0.19	170	São Tomé and Príncipe	45.14	+0.30
43	Turkey	74.33	+4.34	107	Namibia	60.53	+0.24	171	Iraq	44.72	+0.04
44	Kosovo	74.15	+0.44	108	Papua New Guinea	60.12	+1.19	171	Myanmar	44.72	+0.51
45	Belgium	73.95	+2.24	109	Brazil	60.01	+2.96	173	Angola	43.86	+2.16
46	China	73.64	+8.64	110	Nepal	59.63	-0.32	174	Liberia	43.51	-0.04
47	Moldova	73.54	+0.38	111	Malawi	59.59	+0.84	175	Guinea-Bissau	42.85	+0.27
48	Serbia	73.49	+0.17	112	Antigua and Barbuda	59.48	+0.06	176	Bangladesh	41.97	+0.91
49	Israel	73.23	+0.64	113	Paraguay	59.40	+0.41	177	Equatorial Guinea	41.94	+0.28
50	Montenegro	72.73	+0.20	114	Ghana	59.22	+2.06	178	Timor-Leste	41.60	+1.71
51	Italy	72.56	-0.15	115	Solomon Islands	59.17	+0.33	179	Syrian Arab Republic	41.57	+0.02
52	Romania	72.30	-0.53	116	West Bank and Gaza	59.11	+0.39	180	Congo, Rep.	39.83	+0.36
53	Hungary	72.28	+0.34	117	Eswatini	58.95	+0.13	181	Chad	39.36	+1.15
54	Mexico	72.09	-0.18	118	Bahamas, The	58.90	+0.77	182	Haiti	38.52	+0.11
55	Brunei Darussalam	72.03	+1.85	119	Argentina	58.80	+0.87	183	Central African Republic	36.90	+2.67
56	Chile	71.81	+0.37	120	Egypt, Arab Rep.	58.56	+2.74	184	Congo, Dem. Rep.	36.85	+0.67
57	Cyprus	71.71	+0.44	121	Honduras	58.22	+0.09	185	South Sudan	35.34	+2.04
58	Croatia	71.40	+0.34	122	Côte d'Ivoire	58.00	+4.94	186	Libya	33.44	+0.23
59	Bulgaria	71.24	+0.11	123	Ecuador	57.94	+0.12	187	Yemen, Rep.	32.41	-0.59
60	Morocco	71.02	+2.46	124	Philippines	57.68	+1.36	188	Venezuela, RB	30.61	-0.24
61	Kenya	70.31	+5.25	125	Belize	57.13	+0.02	189	Eritrea	23.07	+0.13
62	Bahrain	69.85	+1.82	126	Tajikistan	57.11	+0.08	190	Somalia	20.04	+0.06
63	Albania	69.51	+0.50	127	Uganda	57.06	+0.65				
64	Puerto Rico (U.S.)	69.46	+0.20	128	Iran, Islamic Rep.	56.98	+2.34				

Source: Doing Business database.

Note: The ease of doing business rankings are benchmarked to May 1, 2018, and based on the average of each economy's ease of doing business scores for the 10 topics included in the aggregate ranking. For the economies for which the data cover two cities, scores are a population-weighted average for the two cities. A positive change indicates an improvement in the score between 2016/17 and 2017/18 (and therefore an improvement in the overall business environment as measured by *Doing Business*), while a negative change indicates a deterioration and a 0.00 indicates no change in the score.

World Bank set to launch more robust, transparent business climate rankings

economictimes.indiatimes.com/news/international/business/world-bank-set-to-launch-more-robust-transparent-business-climate-rankings/articleshow/99906987.cms

ReutersLast Updated: May 01, 2023, 11:51:55 PM IST
Synopsis

The World bank said a pilot edition of the new replacement annual series called "Business Ready" would be published in the spring of 2024, covering an initial group of 54 economies in Asia, Latin America, Europe, the Middle East and Sub-Saharan Africa. The bank scrapped Doing Business in September 2021, citing internal audits and an independent probe that found senior World Bank leaders had pressured staff to alter data to favor China.

The World Bank will announce on Monday a new methodology for assessing the business climate in up to 180 countries after embarrassing revelations of data irregularities and favoritism toward China forced it to cancel the "Doing Business" rankings two years ago.

The bank said a pilot edition of the new replacement annual series called "Business Ready" would be published in the spring of 2024, covering an initial group of 54 economies in Asia, Latin America, Europe, the Middle East and Sub-Saharan Africa.

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Subsequent reports adding more countries will follow in the next two years as the bank refines its methodology and ramps up the new flagship project, which aims to help countries attract investment and boost jobs and productivity to accelerate development.

The bank scrapped Doing Business in September 2021, citing internal audits and an independent probe that found senior World Bank leaders had pressured staff to alter data to favor China, and cited data irregularities that also boosted rankings of other countries, including Saudi Arabia, the United Arab Emirates and Azerbaijan.

"Business Ready improves upon and replaces the World Bank Group's earlier Doing Business project. It reflects a more balanced and transparent approach toward evaluating a country's business and investment climate," the bank said in a statement.

World Bank Chief Economist Indermit Gill said the new approach enabled "a fuller and sharper measure of the investment climate of countries - something that is badly needed in a global economy in the midst of a generalized slowdown."

"Business Ready" was shaped by recommendations from World Bank experts, governments, the private sector, and civil society groups, and includes for the first time worker rights, as defined by the International Labor Organization, while acknowledging that regulation can also have positive aspects.

"The main thing that went wrong was the data integrity of Doing Business was compromised," Norman Loayza, director of the World Bank's Indicators Group, which leads the project, told Reuters. "The main point for us is that we need to ensure data integrity and we have a very comprehensive approach to do that."

Loayza said the bank would publish all data collected for the project - raw data, scores and calculations to obtain the scores - from private sector contributors, as well as surveys of entrepreneurs, company owners and managers to ensure full data transparency, unlike the predecessor report.

The bank will also make available the tools needed by outsiders to replicate the results of the data assessments.

But World Bank officials were still debating whether to revive the business climate rankings that were at the heart of the "Doing Business" controversy or produce an overall index, Loayza said, with a decision expected prior to the first report.

He said the rankings were criticized for encouraging political pressure to try to lift country scores, but also helped spur nearly 4,000 regulatory reforms in developing and developed economies over the past two decades.

Loayza said the new project focuses on 10 topics covering the lifecycle of a firm, including business entry, utility services, labor, dispute resolution, market competition, taxation and insolvency - another move aimed at addressing criticism of the earlier product.

"We take into account not only the perspective of the private entrepreneur, but also the perspective of workers, consumers and other market participants," he said. "So for instance, we will look for worker safety, environmental sustainability and market competition."

CHAPTER 28

COMPARATIVE CONTRACT LAW

E. ALLAN FARNSWORTH

New York†

I. The Prominence of Contracts in Comparative Law 900

II. Approaches to Comparative Contract Law 902

III. International Commercial Contracts 905

IV. Basis for Enforcement 907
1. Historical Background in Roman Law 907
2. Common-Law and Civilian Solutions 908
3. Bases for Refusing Enforcement 910
4. Formalities Required for Enforceability 914

V. Requirement of Agreement 915
1. Offer and Acceptance; Definitiveness of the Contract 915
2. Precontractual Liability 917

VI. The Content of the Contract 918
1. Introduction 918
2. Integrity of the Writing 920

† This is the last contribution of one of the leading contract lawyers in the world. Allan Farnsworth died on 31 January 2005 while he was working on this chapter. Professor Larry T. Garvin of the Michael E. Moritz College of Law, Ohio State University, and the editors revised the essay for publication. They would like to thank Professor Muriel Fabre-Magnan of the University of Nantes and Professor Bernhard Schloh of the Free University of Brussels for their helpful comments. Sections I, II, and XI were added by the editors and Section X by Professor Garvin. The tentative conclusion under XI appears to be justified particularly in view of the fact that Allan Farnsworth was a key member of the UNIDROIT Working Group that prepared the Principles of International Commercial Contracts.

and in terms of the realities of international negotiation and litigation. Since international trade, and economic relations more generally, depend mainly on private contracts, understanding the similarities and differences among the various national legal systems is a matter of immediate practical relevance. Thus, law and policy makers, the bench and the bar, and the international business co - munity have a strong interest in understanding contract law in a transboundary context and are often avid consumers of its comparative study. This, in turn, provides incentives (and promises rewards) for comparatists addressing contract law issues.

II. Approaches to Comparative Contract Law

Aside from occasional works on the historical background of modern contract law,[9] comparative studies in this area can be assigned to four main groups. Three are more specifically defined with regard to their approaches and agendas while a fourth may be considered a residual category.

One specific approach is the search for commonalities among the contract l ws of various legal systems. The original project of this type had a global scope: in the 1960s, Rudolf Schlesinger at the Cornell Law School organized a large-scale study purporting to identify a 'common core' of rules on contract formation shared by most developed legal systems in the world. While its actual results, eventually published in two massive volumes,[10] are considered scarcely relevant today the approach was pioneering. Its major successor is an initiative limited to the laws of Europe: in 1994, scholars at the University of Trento, Italy, launched the search for a 'Common Core of European Private Law'. While this so-called Trento Project encompasses other areas of private law as well, it has generated several vo umes focusing particularly on (European) contract law. Each work is gauging the existence of a 'common core' in a specific context.[11] A related, though quite different, undertaking is the first treatise on European contract law: Hein Kötz's

[9] See eg Reinhard Zimmermann, *The Law of Obligations: Roman Foundations of the Civilian Tradition* (1990; paperback edn 1996), 34–833; Gordley, *Philosophical Origins* (n 7).

[10] Rudolf Schlesinger, *Formation of Contracts: A Study of the Common Core of Legal Systems* (2 vols, 1968).

[11] Reinhard Zimmermann and Simon Whittaker (eds), *Good Faith in European Contract Law* (2000); James Gordley (ed), *The Enforceability of Promises in European Contract Law* (2001); Ruth Sefton-Green (ed), *Mistake, Fraud and Duties to Inform in European Contract Law* (2005).

ground-breaking *Europäisches Vertragsrecht* describes and analyzes the subject along the lines of common problems and themes.[12]

It is only a small step from the search for a 'common core' to agendas of contract law harmonization and unification. Thus, this second branch of comparative contract law often builds on the search for commonalities. Yet, it also goes much further and seeks actively to establish compromises bridging the gap between the various systems' concepts and rules. Efforts to harmonize or even unify contract law are driven less by academic interest than by the practical (real or perceived) needs of the business community for internationally uniform contract rules. These efforts have a fairly long and chequered history, especially with regard to the law of sales. They go back at least to the work of Ernst Rabel in the first half of the twentieth century. Rabel pioneered the establishment of an internationally uniform sales law in his two-volume survey *Das Recht des Warenkaufs* (The Law of the Sale of Goods), published in 1936 and 1958 respectively.[13] In subsequent decades, various attempts to unify sales law through international conventions drafted by the Hague Conference of Private International Law engendered little success. Yet, Rabel's belated triumph came with the adoption of the United Nations Convention on the International Sale of Goods (CISG) in Vienna in 1980. The Convention has been ratified by more than sixty countries throughout the world and is undoubtedly the greatest success of international contract law unification to date.[14] Most other efforts in this area have resulted in so-called soft-law, that is, restatement-like 'principles'. On a worldwide scale, the UNIDROIT Principles of International Commercial Contracts (1994, amended 2004),[15] drafted at the International Institute for the Unification of Private Law in Rome, lack legislative force but are used increasingly in international commercial arbitration. In the European context, the most noteworthy success is the publication of the Principles of European Contract Law, drafted by a Commission on European Contract Law led by Ole Lando.[16] The Principles of this so-called Lando Commission have generated enormous scholarly interest and may serve as the blueprint for future legislation on European contract law. In addition, several other unification projects are currently under way.[17]

[12] Hein Kötz, *Europäisches Vertragsrecht* (vol I, 1996; English trans under the title *European Contract Law* by Tony Weir, vol I, 1997).

[13] Ernst Rabel, *Das Recht des Warenkaufs* (vol I, 1936; vol II, 1958).

[14] For details, see Chapter 29 in this *Handbook*.

[15] UNIDROIT (ed), *Unidroit Principles of International Commercial Contracts 2004* (2004); for comment, see Michael Joachim Bonell, 'Unidroit Principles 2004—The New Edition of the Principles of International Commercial Contracts adopted by the International Institute for the Unification of Private Law', (2004) *Uniform LR* 5 ff; Reinhard Zimmermann, 'Die Unidroit-Grundregeln der internationalen Handelsverträge 2004 in vergleichender Perspektive', (2005) 13 *Zeitschrift für Europäisches Privatrecht* 264 ff.

[16] Ole Lando and Hugh Beale (eds), *Principles of European Contract Law* (parts I and II, 1999); Ole Lando, Eric Clive, André Prüm, and Reinhard Zimmermann (eds), *Principles of European Contract Law* (part III, 2003).

[17] For details, see Chapters 16 and 29 in this *Handbook*.

A third major branch of comparative contract law is the study of the influence exercised by one country's (or tradition's) contract law on other legal systems. This approach is part of the comparative law genre focusing on legal transplants which is addressed in a separate chapter of this *Handbook*. Like comparative contract law generally, the tracing of transboundary influence has occurred mainly in the civil versus common-law context. It is widely known among comparatists today that civilian contract doctrine exercised considerable influence on the common law world. This is true not only for earlier English borrowings from Roman law but, as especially Brian Simpson has shown,[18] it is even more remarkable in the late nineteenth century when French and German doctrine had a significant impact on English contract law. In a similar vein, Stefan Riesenfeld has described the migration of certain German ideas to the United States in the early twentieth century.[19] Around the middle of the last century, several German and Austrian émigré scholars, notably Friedrich Kessler, exercised considerable influence on American contract law as well.[20] From a more current perspective, there is also the (still largely unexplored) question of the reverse influence of common-law contract types (such as leasing or factoring) and, more visibly, prolix drafting styles, on a worldwide level.

Beyond these three, fairly specific, approaches comparative contract law has traditionally consisted mainly in the general study of doctrinal similarities and differences between various legal systems, again largely with regard to the civil and the common law. In this, quasi-residual, category, some scholars have focused on individual topics,[21] others have sought to cut across a broader spectrum.[22] Their goal has been mainly to show how similar problems can be handled in different ways; how different approaches often lead to similar outcomes (or vice versa); and, occasionally, how comparing contract law leads to a better understanding of one's own regime and provides ideas for law reform.

The present chapter follows essentially the fourth, more general, approach and provides an overview of major issues in the civil versus common-law context. t focuses on general contract law, as opposed to specific contracts, and thus reflects the current state of international debate. Apart, of course, from the contract of sale which also always serves as the paradigm for debates on issues of general

[18] Simpson, (1975) 91 *LQR* 247 ff; see also above, n 7.

[19] Stefan Riesenfeld, 'The Impact of German Legal Ideas and Institutions on Legal Thought and Institutions in the United States', in Mathias Reimann (ed), *The Reception of Continental Ideas in the Common Law World 1820–1920* (1993), especially at 92 ff.

[20] Jutta Klapisch, *Der Einfluß der deutschen und österreichischen Emigranten auf contracts of adhesion und bargaining in good faith im US-amerikanischen Recht* (1991).

[21] A well-known example is Basil Markesinis, 'Cause and Consideration: A Study in Parallel', (1978) 37 *Cambridge LJ* 53 ff.

[22] See eg Donald Harris and Dennis Tallon, *Contract Law Today: Anglo-French Comparisons* (1989); P. D. V. Marsh, *Comparative Contract Law: England, France, Germany* (1994); a broader range of issues is covered in the Symposium, 'Contract Law in a Changing World', (1992) 40 *AJCL* 541 ff.

contract law, comparative discussion of specific types of contracts has remained very limited.[23]

III. International Commercial Contracts

Exchange is the mainspring of any economic system that relies on free enterprise. Such a system allocates resources largely by exchanges arranged by bargaining between private parties. In these exchanges each party gives something to the other party and receives something in return in order to maximize its own economic advantage on terms tolerable to the other. Because of differences in value judgments and because of the division of labour, it is usually possible for each to gain.[24]

Many of the most important of these exchanges are between commercial parties. Others, however, involve consumers, friends, or family members. Although contract law governs the enforceability of their promises, that law is not unitary. When major efforts have been mounted to provide uniform rules for international contracts, they have tended to limit their reach to commercial contracts. Thus the widely adopted United Nations Convention on Contracts for the International Sale of Goods does not apply to consumer contracts, nor do the UNIDROIT Principles for International Commercial Contracts.[25] The discussion that follows will also emphasize commercial contracts.

Sophisticated systems governing such commercial contracts are found in a wide variety of legal systems around the world. Because of space constraints, this chapter will focus on the one hand on civilian systems, notably the Romanistic systems epitomized by France, together with the Germanic systems typified by Germany, and on the other hand common law systems, particularly those of England and the United States. Many civilian systems, including those just mentioned, recognize a distinction between 'commercial' contracts on the one hand and 'civil', or non-commercial, contracts on the other. In those systems, important practical

[23] But see eg Werner Lorenz, 'Contracts for Work on Goods and Building Contracts', in *International Encyclopedia of Comparative Law* (vol VIII, ch 8, 1980) and William B. Fisch, 'Professional Services', in *International Encyclopedia of Comparative Law* (vol VIII, ch 9, 1999).

[24] cf also Arthur von Mehren, 'A General View of Contract', in *International Encyclopedia of Comparative Law* (vol VII, ch 1, 1982); James Gordley, 'Contract in Pre-Commercial Societies and in Western History', in *International Encyclopedia of Comparative Law* (vol VII, ch 2, 1997).

[25] See Art 2(a) CISG; on which see Peter Schlechtriem, in Peter Schlechtriem and Ingeborg Schwenzer (eds), *Commentary on the UN Convention on the International Sale of Goods (CISG)* (2nd edn, 2005), Art 2, nn 5 ff; Preamble to PICC and comment 2 in UNIDROIT (n 15), 2 f.

consequences turn on whether a transaction is classified as commercial or civil. Rules for civil contracts are found in a civil code while special rules for commercial contracts are often found in a commercial code. In Germanic systems, the criterion for classification is subjective and depends on the quality of the parties as 'merchants' or 'mercantile enterprises'. In systems influenced by the French, the criterion for classification is objective and depends on whether the transaction involves a 'mercantile act'. No formal distinction between commercial and civil law exists in common-law systems. In the United States, the Uniform Commercial Code is not limited to commercial transactions, although it contains some special rules for contracts for the sale of goods involving parties designated as 'merchants' and for consumer leases of goods.[26] Even within the civilian systems the distinction between 'commercial' and 'civil' contracts has been criticized for some time. Much more important in modern discussions about contract law, and its integrity, is the related issue of consumer protection. Particularly in Europe, a great number of statutes in the area of consumer contract law, often based on EC Directives, have been passed in piecemeal fashion and the question has thus arisen how to resolve this unsatisfactory state of affairs. Some countries (among them France and Austria) have enacted consumer codes whereas others (among them the Netherlands and Germany) have attempted to integrate their consumer legislation into the general civil code. The question is hotly debated on both a national and European level, the answer depending largely on whether general contract law and consumer contract law are seen as serving the same, or different, aims.[27] This issue cannot be pursued here.

The discussion that follows concentrates on aspects of contracts relevant to international transactions. These are, for the most part, transactions in which promises are exchanged for other promises. From the standpoint of contract law, the decision to enforce such exchanges of promises, even before any performance by either party, opened a Pandora's box of problems. The questions that will be explored here are these: First, what basis or bases are recognized as justifying the enforceability of a promise and what are the conditions of enforceability? Second, how is it to be determined whether the parties have reached agreement? Third, how is the scope of a party's obligations under a contract determined? Fourth, how does the law ensure that the exchange of promises will be followed by performance of those promises? Fifth, when will changed circumstances be taken into account in determining the parties' obligations? Sixth, in the event of one party's non-performance, what remedies are available to the other party? And seventh, how do these promises affect the rights of third parties?

[26] For a detailed discussion, see Denis Tallon, 'Civil Law and Commercial Law', in *International Encyclopedia of Comparative Law* (vol VIII, ch 2, 1983); and see Francesco Galgano, 'Diritto civile e diritto commerciale', in *idem* (ed), *Atalante di diritto privato comparato* (1992), 35 ff.

[27] For a discussion, see, most recently, Reinhard Zimmermann, 'Consumer Contract Law and General Contract Law: The German Experience', (2005) 58 *Current Legal Problems* 415 ff.

IV. Bases for Enforcement

1. Historical Background in Roman Law

No legal system has ever been reckless enough to make all promises enforceable. One can, however, approach the question of enforceability from two opposite extremes—by assuming that promises are generally enforceable, subject to certain exceptions, or by assuming that promises are generally unenforceable, similarly subject to certain exceptions. Both civil-law and common-law courts have made this latter assumption.

With the development of competitive markets and the specialization of labour, it became essential to provide a general basis for the enforcement of promises, even before any performance by either party. Such transactions were a far cry from the simple credit transaction such as loan of money or sale of goods, for the primitive mind saw the resulting debt as recoverable not because of the debtor's promise to pay but because the debtor would otherwise be unjustly enriched.

The notion that a promise itself may give rise to an enforceable duty was an achievement of Roman law. But since the human mind is slow to generalize, it is not surprising that the history of contract law in Roman times is the account of the development of a number of discrete categories of promises that would be enforced, rather than the story of the creation of a general basis for enforcing promises.

'Consensual' contracts afforded a legal basis for enforcing purely exchanges of promises, even before any performance by either party, but in keeping with the pattern of evolution through the growth of exceptions, they were limited to four important types of contracts—sale, hire, partnership, and mandate.[28] In addition, unilateral promises were enforceable, provided a strict form of words was used.[29] Even as late as the time of Justinian in the sixth century, the most important expansion beyond the categories of classical Roman law was to recognize yet another category known as 'innominate' contracts.[30] Unlike consensual contracts, they were not confined to specified classes of transactions. But they were severely limited because they did not cover exchanges of promises even before any performance by either party, for they were binding only when one of the parties had completed performance. The development of a general basis for enforcing

[28] For details, see Zimmermann (n 9), 230 ff.

[29] On the Roman *stipulatio*, see Zimmermann (n 9), 68 ff. Apart from that four types of 'real' contracts were recognized (loan for use, loan for consumption, pledge, and deposit); in these cases, obligations only arose with the handing over of whatever object the contract was about; see Zimmermann (n 9), 153 ff.

[30] For details of the development, see Zimmermann (n 9), 532 ff; cf also 511 ff.

promises—the foundation of a general theory of contract—was therefore left to the great modern legal systems that arose in Europe during the Middle Ages: the common-law system that grew up in England and the civil-law systems that emerged on the European continent.

2. Common-Law and Civilian Solutions

Because the influence of Roman law in England had faded with the breakup of the Roman political system, the common law began at a less advanced stage than that attained by Roman law. English courts therefore painfully constructed such a basis beginning in the Middle Ages. That they succeeded in doing so was all the more remarkable in view of the fact that, when they began, the English law of contracts was little more advanced than that of many primitive societies. Like Roman law, they created categories of actionable promises.[31] One of the most important of these, the action of debt, was no better suited than were the innominate contracts of Roman law to exchanges before any performance by either party, because the action of debt also required that the promisee had actually performed. It was only at the end of the sixteenth century that, goaded by competition from the ecclesiastical courts, the common-law courts were prepared to enforce exchanges of unexecuted promises.[32]

The basis of enforcement developed by common-law courts came to be known as the 'doctrine of consideration'. At first, the word *consideration* had been used without technical significance, but during the sixteenth century it came to be a word of art that expressed the sum of the conditions necessary for an action for breach of contract. The word thus came to be used to identify those promises that in the eyes of the common law were important enough to society to justify legal sanctions for their enforcement. It was, not surprisingly, neither a simple nor a logical test.[33]

Conventional learning is that a promisor's mere promise to do something is not enforceable unless supported by consideration. The essence of consideration came to be an exchange in which a promise was made in order to obtain something—often called a *quid pro quo*—in return. What the promisee could give might be either a promise or a performance. It was often said that the consideration could be either a benefit to the promisor or a detriment to the promisee, which remains

[31] For details, see Simpson (n 6), 1 ff; David Ibbetson, *A Historical Introduction to the Law of Obligations* (1999), 24 ff; Gerhard Kegel, *Vertrag und Delikt* (2002), 35 ff.

[32] On the rise of the action of assumpsit, see Simpson (n 6), 199 ff; Ibbetson (n 31), 126 ff; Kegel (n 31), 51 ff.

[33] On the history of the doctrine of consideration, see Simpson (n 6), 316 ff, 375 ff; Ibbetson (n 31), 141 ff; Kegel (n 31), 66 ff; Jörg Benedict, 'Consideration: Formalismus und Realismus im Common Law of Contract', (2005) 69 *RabelsZ* 1 ff.

the general approach in England.[34] The Restatement of Contracts abandoned the historical requirement of a benefit or a detriment and in its place formulated a 'bargain' test, now widely accepted in the United States. Under this test, consideration must be something, either a promise or a performance, that is bargained for, that is, sought by the promisor in exchange for the promise and given by the promisee in exchange for the promise.[35]

The requirement of consideration took care of the bulk of economically vital commercial agreements, and found easy acceptance in a society entering a commercial age. In view of the difficulty that other societies have had in developing a general basis for enforcing promises, it is perhaps less remarkable that the basis developed by the common law is logically flawed than that the common law succeeded in developing any basis at all.

The doctrine of consideration is not a device for policing contracts to assure that they are fair to both parties. Consideration does not have to be 'adequate' or 'sufficient', though those adjectives are sometimes added by courts.[36] Nor does the consideration have to be substantial in value, though marked disparity in value may signal the absence of bargain—of merely 'nominal' consideration. Furthermore, the requirement of an actual bargain is not taken so seriously as to exclude routine transactions concluded on the basis of standardized agreements to which one party simply adheres without any real negotiation of terms.

One commercially significant area affected by consideration is contract modification. Under the pre-existing duty rule, a modification to a contract must itself be supported by consideration to be binding. The rule persists in common-law nations, though it has been limited by statute and by various judicial incursions, particularly in the United States.[37]

In the United States, spurred by the Restatement of Contracts, the doctrine of 'promissory estoppel' developed during the twentieth century as an alternative to the doctrine of consideration as a basis for enforcing promises. Under the doctrine of consideration, the promisee's unsolicited reliance is not consideration because it is not bargained for. Under the doctrine of promissory estoppel, however, the promisee's unsolicited reliance on a promise may preclude the promisor from asserting the absence of consideration for the promise if the promisor should have reasonably expected such reliance. The doctrine has been applied not only to

[34] See eg *Midland Bank Trust Co Ltd v Green* [1981] AC 513; G. H. Treitel, *The Law of Contract* (11th edn, 2003), 67 ff.

[35] Restatement (Second) of Contracts § 71.

[36] Restatement (Second) of Contracts § 79; E. Allan Farnsworth, *Farnsworth on Contracts* (vol I, 3rd edn, 2004), 124 ff. For a comparative evaluation, see Ferdinand Fromholzer, *Consideration* (1997); for an analytical evaluation, see Stephen A. Smith, *Contract Theory* (2004), 215 ff.

[37] Perhaps the most significant incursion is § 2–209(1) UCC, which abolished the pre-existing duty rule for goods contracts. On the pre-existing duty rule, see Farnsworth (n 36, vol I) 520 ff; Fromholzer (n 36), 131 ff.

donative promises but also to other unremunerated promises. It has not yet been generalized in England as it has in the United States.[38]

In many civil-law systems, including the Germanic, there is no requirement comparable to consideration and it is enough if a promise is made with an intention to be bound.[39] In French law and some related systems it is often said that for an obligation in a synallagmatic contract (a bilateral contract with reciprocal promises) to be enforceable it must have an underlying *causa* or *cause*.[40] Under such a contract, the *cause* is the reason that led a party to engage in the transaction. French courts do not engage in a subjective inquiry into the motivations of the parties, but if the performance to be rendered in return for an obligation is worthless, of no genuine importance, a court may decline to enforce the obligation on the ground that there is an absence of *cause*. This necessarily vague concept is not usually invoked by courts as a basis for insisting on equivalence in exchanges, though some recent cases suggest its potential use.[41] Today, *cause* is important largely in providing a basis for enabling a court to refuse to enforce a contract if it is legally or morally offensive.[42] In addition, donative promises in civil-law systems are enforceable, but typically require notarization as an authenticating formality.[43]

3. Bases for Refusing Enforcement

All legal systems impose threshold conditions for the making of enforceable contracts. Thus some classes of persons, often because of youthfulness or diminished or impaired mental ability, are denied the capacity to make contracts.[44]

[38] Restatement (Second) of Contracts § 90. For comment, see Farnsworth (n 36, vol I), 167 ff; English law does not recognize a cause of action based on promissory estoppel, instead limiting it to a purely defensive role: *Combe v Combe* [1951] 2 KB 215.

[39] For the historical development of the principle of *pacta sunt servanda* under the *ius commune*, see Klaus-Peter Nanz, 'Die Entstehung des allgemeinen Vertragsbegriffs im 16. bis 18. Jahrhundert' (1985); Zimmermann (n 9), 537 ff; John Barton (ed), *Towards a General Law of Contract* (1990); Kegel (n 31), 3 ff.

[40] For the historical development, see Zimmermann (n 9), 549 ff.

[41] See eg Cass com, 22 October 1996, D 1997, 121. For comment, see François Terré, Philippe Simler, and Yves Lequette, *Droit Civil: Les Obligations* (9th edn, 2005), no. 342.

[42] For a comparative evaluation of cause and consideration as 'indicia of seriousness' of a promise, see Zweigert and Kötz (n 2), 388 ff; Kötz (n 12), 52 ff; P. G. Monateri, Francesco Galgano, and Guido Alpa, in Galgano (n 26), 89 ff; and see the case studies and comparative comment in James Gordley (ed), *The Enforceability of Promises in European Contract Law* (2001). Neither PECL nor PICC recognize cause or consideration; see Art 2:201 (1) PECL and Art 3.2 PICC ('. . . without any further requirement').

[43] Melvin A. Eisenberg, 'Donative Promises', (1979) 47 *University of Chicago LR* 1; John P. Dawson, *Gifts and Promises: Continental and American Law Compared* (1980); Zimmermann (n 9), 477 ff; James Gordley, *The Foundations of Private Law: Property, Tort, Contract, Unjust Enrichment* (2006), 352 ff.

[44] Zweigert and Kötz (n 2), 348 ff; Kötz (n 12), 97 ff; for the United States, see Farnsworth (n 36, vol I), 442 ff.

Furthermore, even assuming competent parties, abuse of the bargaining process by one of them may impair the enforceability of the resulting agreement. The two most common kinds of abuse are those arising from conduct that is misleading and from conduct that is coercive. Protection against these two kinds of abuse is commonly afforded by allowing the abused party to undo the transaction by avoiding it, restoring both parties to their positions before their agreement.[45]

With the standardization of contract terms, courts and legislatures were faced with more subtle inroads on the integrity of the bargaining process. The typical agreement in a routine transaction came to consist of a standard form containing terms prepared by one party and assented to by the other with little or no opportunity for negotiation. Traditional contract law, designed for a paradigmatic agreement that had been reached by two parties of equal bargaining power by a process of free negotiation, was ill-equipped to meet the challenge posed by standard terms.

Standardizing terms has obvious advantages. It renders individual negotiations unnecessary, lowering transaction costs and thereby serving the interest of both parties. Furthermore, because a judicial interpretation of one standard form serves as an interpretation of similar forms, standardization facilitates the accumulation of experience and helps to make risks calculable. Dangers are inherent in standardization, however, for it affords a means by which one party may impose terms on another unwitting or even unwilling party. The standard form is typically proffered as a take-it-or-leave-it proposition, often called a *contract of adhesion*, under which the only alternative to complete adherence is outright rejection.

The traditional concern of courts in policing contracts has been with abuse of the bargaining process rather than with the fairness of the resulting bargain. Neither consideration in common-law systems nor *cause* in French systems polices the substance of a bargain. And the doctrine of *laesio enormis*, which at one time permitted avoidance of unequal contracts in civil-law countries, has been rejected save at most for a few vestiges.[46]

Courts steeped in traditional contract doctrine were therefore not receptive to the argument that a party should be relieved of an agreement on the grounds of imposition of standard terms. Nevertheless, in hard cases, courts strained to afford relief to the weaker party and, in doing so, developed several techniques. Sometimes they held that the standard terms did not become part of the contract at all, as where the terms were in small print, located on the back of a form, or

[45] Zimmermann (n 9), 651 ff; Zweigert and Kötz (n 2), 424 ff; Kötz (n 12), 196 ff; Thomas Probst, 'Defects in the Contracting Process', in *International Encyclopedia of Comparative Law* (vol XI, ch 11, III and IV, 2001); Thomas Schindler, *Rechtsgeschäftliche Entscheidungsfreiheit und Drohung* (2005); Smith (n 36), 315 ff; Arts 4:107 f PECL; Arts 3.8 f PICC.

[46] On the doctrine of *laesio enormis*, see Zimmermann (n 9), 259 ff; F. Willem Grosheide, 'Iustum Pretium Redivivum?', in: F. Willem Grosheide and Ewoud Hondius (eds), *International Contract Law 2003* (2004), 69 ff; Gordley, *Foundations* (n 43), 364 ff.

incorporated by an obscure reference. Sometimes they applied rules of str construction, finding the terms unclear or ambiguous and then interpreting the *contra proferentem* ('against the profferer'). However, none of these traditior judicial techniques was adequate, at least in theory, to protect an unfortuna person who had actual knowledge and understanding of the terms.[47]

In the years following World War II, it was increasingly recognized that suc judicial techniques were inadequate and that abusive clauses must be subjected t tighter legislative and judicial control. Much of the concern with standardize terms was everywhere directed at the protection of consumers, on the rationale that the consumer, presumably the weaker party, must be protected against term favoring firms that abused their economic superiority. The result has been a plethora of legislative measures proscribing specific types of abuse or requiring clearer or earlier disclosure of especially important terms.[48]

German legislation automatically invalidates standard terms of business if, contrary to the precepts of good faith, they place the other party at an unreasonable disadvantage.[49] More generally, it provides that 'surprise' clauses do not become part of the contract if they are so 'unusual that the other party could not be expected to suppose that they would be there'.[50] This legislation applies even though both parties are merchants. In addition, consumers may invoke lists of standard terms that are either proscribed or that are proscribed if they prove disproportionately harmful.[51]

French legislation dating from 1978 empowered the government to issue decrees prohibiting specified clauses in contracts between merchants and consumers in so far as they gave the former an unfair advantage and seemed to have been imposed on the consumer by an abuse of economic power.[52] The commission set up to do this was inactive and in 1991 the Cour de Cassation held that it was open to the courts to do this.[53] *Clauses abusives* may also be invalidated under the general law of contract.

In England, following World War II, there grew up a judge-made rule that an exculpatory clause is no defense to a claim based on a 'fundamental breach of contract', for the reason that in case of such a breach the contract as a whole is at

[47] For a historical account of standard terms of business, and how to police them, see Sibylle Hofer, Phillip Hellwege, and Stefan Vogenauer, in Mathias Schmoeckel, Joachim Rückert, and Reinhard Zimmermann, *Historisch-kritischer Kommentar zum BGB* (vol II, in preparation), §§ 305–10; see also Farnsworth (n 36, vol I), 556 ff.

[48] For comparative accounts, see Zweigert and Kötz (n 2), 333 ff; Kötz (n 12), 137 ff; Karl-Heinz Neumayer, 'Contracting Subject to Standard Terms and Conditions', in *International Encyclopedia of Comparative Law* (vol VII, ch XII, 1999).

[49] § 9 AGBG (Standard Terms of Business Act) of 1976; now § 307 BGB.

[50] § 3 AGBG; now § 305 c I BGB. [51] §§ 10 f AGBG; now §§ 308 f BGB.

[52] Art L 132–1 *Code de la consommation.*

[53] Cass 1e civ, 14 May 1991, D 1991, 449. The pertinent statute has been revised greatly in light of the EC Directive on unfair terms in consumer contracts of 1993.

an end and the clause disappears. However, the House of Lords closed the door on this rule in 1980.[54] In 1977, the Unfair Contract Terms Act gave judges wide power of control over unfair clauses that exclude or limit liability, particularly where consumers are involved.[55]

In 1993 an additional layer of European law was added by an European Community Directive requiring member states to introduce provisions applicable to a contract that, rather than being individually negotiated, has been drafted in advance so that the consumer has had no ability to influence its substance. Courts are to be permitted to hold a clause in such a contract invalid if, contrary to the requirements of good faith, the clause causes a significant imbalance under the contract.[56] The implementing legislation varied widely.[57] German law largely remained intact, as for the most part it already regulated standard terms as strictly, or more strictly, than did the Directive. French law changed materially, now incorporating the 'black list' of unfair terms contained in the EC Directive. England, in contrast, enacted the Unfair Terms in Consumer Contracts Regulations in 1999, which run alongside the 1977 Act. As in France, the English approach largely incorporates the Directive with no amendment.[58]

In the United States, the problem of abusive clauses is dealt with by the doctrine of unconscionability, which allows a court to refuse to enforce part or all of a contract should all or part of the contract be unconscionable. This doctrine is rooted in the practice of courts of Equity, which withheld equitable relief if a contract is so unfair as to shock the conscience of the court. It gained currency through its adoption in the Uniform Commercial Code, and since has become established in the common law.[59] The concept is largely undefined in the Code, but cases and commentators have filled that gap. Courts have characterized the presence of unreasonably favourable terms as substantive unconscionability and the absence of meaningful choice in determining those terms as procedural unconscionability. They weigh all elements of both substantive and procedural unconscionability and may conclude that the contract is unconscionable because

[54] *Photo Production Ltd v Securicor Transport Ltd* [1980] AC 827.

[55] For details, see Treitel (n 34), 246 ff.

[56] Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts, [1993] OJ L 95/93.

[57] See Jürgen Basedow, in *Münchener Kommentar zum Bürgerlichen Gesetzbuch* (vol IIa, 4th edn, 2003), Vor § 305, nn 18 ff.

[58] The Principles of European Contract Law (which do not contain provisions specifically dealing with consumer contracts) have a general provision, but no 'black list': Art 4:110 PECL. There is no equivalent in the UNIDROIT Principles of International Commercial Contracts.

[59] § 2–302 UCC; Restatement (Second) of Contracts § 208. See further Farnsworth (n 36, vol I), 577 ff.

of the overall imbalance. They have resisted applying the doctrine when the only substantive and no procedural unconscionability.[60]

In addition to refusing enforcement in order to protect the interests of on the parties, courts sometimes refuse enforcement in order to protect the inter of the public as a whole. In all legal systems, courts reserve this power to th selves. French law brings into play the concept of *cause* on the rationale th contract cannot be based on a *cause illicite*. A court will examine not only reason that led a party to engage in the transaction, for example, the expectation acquiring land in return for a price, but also the party's ulterior motive, such operating a casino or a bordello, and determine whether this motive is offensive law or morals.[61]

4. Formalities Required for Enforceability

All legal systems make some use of formalities as conditions of enforceability. Their functions may include facilitating proof and confirming seriousness o intention. Many civil-law systems, however, have no general requirement of formality as a condition of enforcement, though a writing or other formality ma be required for specific types of contracts. Thus German law requires a writing fo suretyship provisions in contracts, and contracts for the sale of land must be in notarial form.[63] Such requirements as exist may not affect commercial transactions, as in the case of the French *Code civil*'s requirement of a writing for every non-commercial contract involving more than a trifling sum.[64] Furthermore, in systems following the French, when a formality is required the effect may be merely to limit the means of *proof*, as by witnesses, rather than to affect the *validity* of the agreement.

In contrast, a fear of false testimony regarding oral contracts prompted Britain to enact the Statute of Frauds in 1677. It provided that designated classes of

[60] For other devices policing contracts which are procedurally as well as substantively unfair (such as undue influence, or § 138 II BGB, ie the rule on 'usury'), see, against the general background of freedom of contract, Zweigert and Kötz (n 2), 323 ff; Kötz (n 12), 130 ff; Arthur von Mehren, 'The Formation of Contracts', in *International Encyclopedia of Comparative Law* (vol VII, ch 9, 1992), nn 62 ff; Jacques du Plessis and Reinhard Zimmermann, 'The Relevance of Reverence: Undue Influence Civilian Style', (2004) 10 *Maastricht Journal of European and Comparative Law* 345 ff; Art 4:109 PECL; Art 3.10 PICC.

[61] For historical and comparative discussion of illegality and immorality, see Zimmermann (n 9), 697 ff; Zweigert and Kötz (n 2), 380 ff; Kötz (n 12), 154 ff; Arts 15:101 ff PECL; this subject is not yet covered by the PICC; Farnsworth (n 36, vol II), 1 ff.

[62] Generally, see Zimmermann (n 9), 82 ff; Zweigert and Kötz (n 2), 365 ff; Kötz (n 12), 78 ff; Arthur von Mehren, 'Formal Requirements', in *International Encyclopedia of Comparative Law* (vol VII, ch 10, 1998); Paul Brasseur, 'Le formalisme dans la formation des contrats: Approches de droit comparé', in Michel Fontaine (ed), *Le processus de formation du contrat* (2002), 605 ff.

[63] §§ 311 b I and 766 BGB. [64] Art 1341 *Code civil*.

contracts were not enforceable unless evidenced by a signed writing. The most important of these classes were contracts of suretyship, contracts for the sale of an interest in land, contracts not to be performed within a year from the time of their making, and contracts for the sale of goods. Most American states adopted similar statutes covering these classes.

In 1954, after 277 years, Parliament repealed most of the Statute of Frauds, retaining only the provisions for contracts of suretyship and contracts for the sale of an interest in land.[65] There has been no widespread movement of this kind in the United States, where the Statute of Frauds retains much of its vigour and has been retained in the Uniform Commercial Code, with some amelioration, for contracts for the sale of goods. Indeed, there is a tendency to require the formality of a writing as a means of protecting unsophisticated parties such as consumers. Many American courts have shown hostility to the one-year provision, however, and have limited it radically.[66]

V. Requirement of Agreement

1. Offer and Acceptance; Definitiveness of the Contract

Agreement is the basis of contract, and all legal systems impose two requirements in determining whether there has been legally binding agreement. First, the parties must have manifested their *assent* to be bound, a requirement that follows from the premise that contractual liability is consensual. Second, the agreement to which they manifested their assent must be *definite* enough to be enforceable, a requirement that is implicit in the premise that contract law protects the promisee's expectation. The focus here will be on the first of these requirements, where the differences among legal systems are sharpest.

Contract law characteristically envisions the process of agreement in terms of a discrete offer by one party and an acceptance by the other.[67] Once the offer is accepted, both parties are bound by the resulting contract. A major difference among legal systems goes to the revocability of the offer before a contract has resulted from its acceptance. Revocation by the offeror after the acceptance has

[65] The Statute of Frauds for real property was revised again in 1989, this time to strengthen the formal requirements: Hugh G. Beale (general ed), *Chitty on Contracts* (29th edn, 2004, vol I), 334 ff.

[66] § 2–201 UCC. On judicial hostility to the one-year provision, see Farnsworth (n 36, vol II), 129 ff. On the Statute of Frauds in general, see Farnsworth (n 36, vol II), 101 ff.

[67] For the history of the doctrine of offer and acceptance, see Zimmermann (n 9), 559 ff; Gordley, *Origins* (n 7), 45 ff, 79 ff, 81 f, 139 f, 175 ff.

reached the offeree is to be distinguished from withdrawal by the offeror before th acceptance has reached the offeree, as to which the offeror is free.[68]

In the common law an offer has no binding force and can be revoked at any tim before acceptance. The hardship on the offeree is traditionally mitigated somewha by the common law's 'mailbox' rule,[69] under which an offer received by mail i accepted as soon as the offeree has dispatched an acceptance. The offeree risks revocation only during the time between the arrival of offer and the dispatch of acceptance. Perhaps surprisingly, an offer is revocable even if it provides that i cannot be revoked for a stated period. This is a consequence of the doctrine of consideration, the provision for irrevocability being regarded as a promise not to revoke that is not binding if not supported by consideration. A common practice is for the offeree to pay a nominal sum as consideration, converting the offer into an irrevocable option. It is also possible that revocation of an offer may be precluded under the doctrine of promisory estoppel. Furthermore, in the United States an offeror can make an irrevocable 'firm offer' for the sale of goods under the Uniform Commercial Code.[70]

In French law, too, the offeror is generally free to revoke the offer at any time, although in some circumstances revocation may be regarded as a *faute* and therefore illegitimate if it is abusive and frustrates the offeree's legitimate expectations. In such a case revocation is sanctionable in damages. This is the case where the offer fixes a period of irrevocability or where the circumstances indicate a reasonable time for irrevocability. French law is unclear as to whether an acceptance is effective on dispatch or on receipt.[71]

German law takes a different position, under which, absent a provision to the contrary, every offer is irrevocable during a reasonable period, even if no period has been fixed. During that period revocation is impossible and a purported revocation has no legal effect. If the offer fixes a period of irrevocability, it cannot be revoked during that period. In any case, an acceptance is effective, not when it is dispatched, but when it reaches the offeree.[72]

[68] For comparative discussions, see Zweigert and Kötz (n 2), 356 ff; Kötz (n 12), 16 ff; Arthur von Mehren (n 60), nn 134 ff; Franco Ferrari, 'La Formazione del contratto', in Galgano (n 26), 67 ff; Catherine Delforge, 'La formation des contrats sous un angle dynamique: Reflexions comparatives', in Fontaine (n 62), 137 ff; Arts 14 ff CISG; Arts 2:201 ff PECL; Arts 2.1.1 PICC; for discussion of these international instruments, see Eva Luig, *Der internationale Vertragsschluss* (2002).

[69] Established in *Adams v Lindsell* (1818) 1 B & Ald 681, 106 ER 250; confirmed by the House of Lords in *Dunlop v Higgins* (1848) 1 HLC 381, 9 ER 805 and adopted generally in the United States, see Restatement (Second) of Contracts § 63.

[70] § 2–205 UCC; for other approaches to converting offers into option contracts, see Restatement (Second) of Contracts § 87. English law is less accommodating; see *Chitty on Contracts* (n 65, vol I), 321 ff.

[71] Terré *et al* (n 41), nos. 168 ff.

[72] §§ 145 ff BGB. Other civil law systems differ, with a few requiring actual notice. CISG and the UNIDROIT Principles separate acceptance from revocation; an acceptance is effective only upon receipt, as in Germany, but the offer may not be revoked after the acceptance has been dispatched.

Whether an agreement is sufficiently definite to display the requisite intent to be bound likewise varies among legal systems. Certainly an agreement can prove too indefinite to enforce. Romanistic systems generally require that a contract have an *objet*, a requirement absent elsewhere.[73] As will be discussed, missing terms can be supplied by the courts, or are supplied legislatively.

2. Precontractual Liability

If negotiating parties sign the documents at the closing they clearly have assented to the terms contained therein. But problems arise if the negotiations fail and the documents are not signed. The resolution of disputes arising out of the failure of negotiations has assumed increasing importance. Common-law and civil-law systems have arrived at different solutions.[74]

Common-law courts have traditionally accorded parties the freedom to negotiate without risk of precontractual liability. Before an offer is accepted, neither party is bound. This broad freedom of negotiation is subject to occasional exceptions if, for example, the aggrieved party has a claim in restitution for a benefit to the other party during the negotiations, has been harmed by a misrepresentation or, at least in the United States, has relied on a specific promise made by the other party during the negotiations.[75]

German courts have adapted the concept of *culpa in contrahendo* (fault in contracting) developed by Rudolf von Jhering after the middle of the nineteenth century[76] and now codified in § 311 II BGB, to hold that a party that fails to observe the 'necessary *diligentia*' in negotiations commits a breach of its contractual obligations and is accountable for the other party's reliance losses. Although the mere breaking off of negotiations does not constitute such a failure, a party may be liable if it refuses without an appropriate ground to conclude a contract after conducting itself in such a way that the other party justifiably counted on a contract coming into existence.

[73] Arts 1108, 1129, 1591 *Code civil*; but see now the developments sketched by Bertrand Fages, 'Einige neuere Entwicklungen des französischen allgemeinen Vertragsrechts im Lichte der Grundregeln der Lando-Kommission', (2003) 11 *Zeitschrift für Europäisches Vertragsrecht* 514 ff. For a comparative discussion, see Kötz (n 12), 42 ff; cf also Art 2:103 PECL.

[74] See Arthur von Mehren (n 60), nn 112 ff; Kötz (n 12), 34 ff; Gordley, *Foundations* (n 43), 297 ff; Zimmermann and Whittaker (n 11), 171 ff; Bertrand de Coninck, 'Le droit commun de la rupture des négotiacions précontractuelles', in Fontaine (n 62), 15 ff; Ewoud Hondius, 'Pre-Contractual Liability', in F. Willem Grosheide and Ewoud Hondius (n 46), 5 ff; Arts 2:301 f PECL; Arts 2.1.15 PICC.

[75] Farnsworth (n 36, vol I), 391 ff.

[76] Rudolf von Jhering, 'Culpa in contrahendo, oder Schadensersatz bei nichtigen oder nicht zur Perfektion gelangten Verträgen', (1861) 4 *Jherings Jahrbücher für die Dogmatik des bürgerlichen Rechts* 16 ff.

Early in the twentieth century, a French scholar, Raymond Saleilles, advanced the view that after parties have entered into negotiations both must act in good faith and neither can break off the negotiations 'arbitrarily' without compensating the other for its reliance.[77] French courts have imposed liability on a theory of tort, the wrong being viewed as an *abus de droit* for which bad faith even without malice will suffice. Bad faith may be found where a party has negotiated with no serious intention to contract or where a party breaks off negotiations abruptly and without justification.

Legal systems also differ as to the enforceability of an explicit agreement by the parties to negotiate in good faith. Such agreements are clearly enforceable in civil-law systems. However, English courts have been adamant in refusing to enforce such agreements[78] on two grounds: first, that the scope of such an obligation is too indefinite to be enforceable; and, second, that there is no way to calculate expectation damages for breach of such an obligation because there is no way to determine the terms of the contract that might have been reached. Many courts in the United States have rejected these arguments and have enforced agreements to negotiate, at least where they have been concluded after some significant terms have been agreed upon. In answer to the second argument, these courts have calculated damages not on the basis of lost expectation but on the basis of reliance, sometimes including lost opportunities to conclude other contracts. In answer to the argument of indefiniteness, the same courts have concluded that at the very least it is a breach of the obligation to negotiate in good faith if a party simply refuses to abide by a term on which agreement has been reached unless the other party makes a concession on some matter yet to be negotiated.[79]

VI. The Content of the Contract

1. Introduction

Most of what we usually think of as 'contract law' consists of a legal framework within which parties may create their own rights and duties by agreement. Developed societies confer upon contracting parties wide power to shape their

[77] Raymond Saleilles, 'De la responsabilité précontractuelle', (1907) 6 *Revue Trimestrielle de Droit Civil* 697, 717 ff.

[78] See the references in Treitel (n 34), 59 ff.

[79] Farnsworth (n 36, vol I), 391 ff; *idem*, 'Precontractual Liability and Preliminary Agreements: F ir Dealing and Failed Negotiations', (1987) 87 *Columbia LR* 217, 264 ff.

relationships under the principle of party autonomy or 'freedom of contract', and many contract disputes relate not to this legal framework but rather to the rights and duties that the parties themselves have created. Such controversies over the 'interpretation' or 'construction' of the contract[80] represent a substantial fraction of all contract disputes.

Before a party can be charged with a breach, the scope of that party's obligation must be determined. To begin with, a court will look at the language of the contract itself. In addition a court will look to terms implied in law, terms that are read into contract—sometimes on the basis of statute and sometimes as a matter of judicial discretion—in order to fill gaps in the language of the contract.[81] With rare exceptions for fields such as insurance law and consumer protection law, these rules are not mandatory, that is, not impervious to the parties' attempts to change them; instead, the parties are free to contract out of them. In the United States, such rules are commonly known as *default* rules, in Germany as *dispositives Recht*, and in France as *lois supplétives*.

Most civil-law systems know a default rule of great importance and widespread impact that requires a contracting party to behave according to good faith, or what is in German *Treu und Glauben* and in French *bonne foi*.[82] The common law traditionally knows no such default rule. English courts have been adamant in refusing to accept such a vague restraint on the behaviour of a contracting party, though they sometimes achieve the same ends by fashioning more specific rules.[83] In the United States, a remarkable exception in the common-law world, courts generally recognize a default rule that requires a contracting party to behave according to *good faith and fair dealing*, a vague standard that may, nevertheless, be less broad than its civil-law counterpart.[84] Yet, many American courts do not allow an independent cause of action for lack of good faith, except in cases of bad faith denial of an insurance claim which may be actionable in tort.

[80] On which see Zimmermann (n 9), 621 ff; Zweigert and Kötz (n 2), 400 ff; Kötz (n 12), 106 ff; Arts 5:101 PECL; Arts 4.1 ff PICC.

[81] For example, in England many default terms are supplied by the Sale of Goods Act of 1979 and the Supply of Goods and Services Act of 1982, though the courts readily fill in remaining gaps. On implied terms in English law in comparative perspective, see Martin Schmidt-Kessel, 'Implied Terms—Auf der Suche nach dem Funktionsäquivalent', (1997) 96 *Zeitschrift für Vergleichende Rechtswissenschaft* 101 ff; Wolfgang Grobecker, *Implied Terms und Treu und Glauben* (1998); and see Smith (n 36), 280 ff.

[82] For comparative analysis, see Jack Beatson and Daniel Friedmann (eds), *Good Faith and Fault in Contract Law* (1995); Hein Kötz, 'Towards a European Civil Code: The Duty of Good Faith', in *The Law of Obligations: Essays in Celebration of John Fleming* (1998), 243 ff; Martijn Hesselink, *De redelijkheid en billijkheid in het Europese privaatrecht—Good Faith in European Private Law* (1999); Zimmermann and Whittaker (n 11), 7 ff.

[83] *Interfoto Picture Library Ltd v Stilletto Visual Programmes Ltd* [1989] 1 QB 433.

[84] See Robert S. Summers, 'The Conceptualisation of Good Faith in American Contract Law: A General Account', in Zimmermann and Whittaker (n 11), 118 ff; Steven J. Burton and Eric G. Andersen, *Contractual Good Faith* (1995); cf also the explicit reference to good faith in § 1–203 UCC and Restatement (Second) of Contracts § 205.

A vexing related problem is how to determine the terms of a contract when the offer and acceptance differ. The classic answer makes a non-conforming acceptance a rejection and counter-offer.[85] Especially for contracts created by the exchange of standard forms, this proves impracticable. French and German case law has tended to place the terms of the parties at parity, allowing formation and replacing terms in conflict with default terms.[86] English law normally treats the differing forms as creating no contract until one party expressly assents or until performance. In the latter case the final document provides the terms of the contract.[87] American law depends upon the context. At common law, the answer is very much along English lines. For the sale of goods, the Uniform Commercial Code provides a somewhat muddy answer that variously yields something like French and German law or something like a first-shot rule, subject to a materiality test.[88]

2. Integrity of the Writing

Common-law systems show great respect for the integrity of written contracts. After lengthy negotiations, contracting parties often reduce part or all of their agreement to writing in order to provide trustworthy evidence of the agreement and avoid reliance on uncertain memory. If litigation ensues, however, one party may seek to introduce evidence of the earlier negotiations in an effort to show that the terms of the agreement are different than those shown in the writing. Faced with such a possibility, the parties may prefer to facilitate the resolution of disputes by excluding from the scope of their agreement those matters not reflected in the writing.

In common-law systems, the integrity of the writing is assured by the 'parol evidence rule', a rule with little counterpart in civil-law systems.[89] This rule may bar the use of extrinsic evidence—evidence outside the writing—to contradict and perhaps even to supplement the writing. The name of the rule is misleading, for it is not limited to oral (or 'parol') negotiations and may exclude such writings as letters, telegrams, memoranda, and preliminary drafts. Nor is it a rule of 'evidence' but one of substantive law.

[85] See eg § 150 II BGB. This 'mirror-image' rule has been softened somewhat in many legal systems to allow for contract formation where the offer and acceptance differ immaterially.

[86] For comparative accounts, see Kötz (n 12), 32 f; von Mehren (n 60), nn 157 ff; Catherine Delforge, 'Le conflit né de la confrontation de conditions générales contradictoires et son incidence sur la formation des contrats', in Fontaine (n 62), 479 ff; Ernst A. Kramer, ' "Battle of the Forms": Eine rechtsvergleichende Skizze mit Blick auf das schweizerische Recht', in *Gauchs Welt: Recht, Vertragsrecht und Baurecht. Festschrift für Peter Gauch* (2004), 493 ff; and see Art 2:209 PECL; Art 2.1.22 PICC.

[87] *Butler Machine Tool Co Ltd v Ex-Cell-O Corp (England) Ltd* [1979] 1 WLR 401.

[88] § 2–207 UCC.

[89] Though French law, in Art 1341 *Code civil*, provides that parol may not vary or contradict certain writings. This provision has been relaxed judicially.

The rule is intended to give legal effect to the parties' intention to make their writing at least a final and perhaps also a complete expression of their agreement. If the parties had such an intention, the agreement is said to be *integrated* and the rule applies. If they intended the writing to be a final expression of the terms it contains, but not a complete expression of all the terms agreed upon—some terms remaining unwritten—the agreement is said to be *partially* integrated and evidence of prior agreements or negotiations is admissible to supplement the writing though not to contradict it. If the parties intended the writing to be a complete expression of all the terms agreed upon, as well as a final expression of the terms it contains, the agreement is *completely* integrated and not even evidence of 'a consistent additional term' is admissible to supplement the writing. These preclusions, however, generally do not extend to usage or course of dealing.[90]

In order to make it clear that a contract is completely integrated, agreements in common-law countries often contain what is commonly known as a 'merger clause', which merges prior negotiations into the writing by reciting that the writing contains the entire agreement. Courts have generally given effect to such clauses.[91]

When the interpretation of the language of a writing is in issue, an adjunct to the parol evidence rule known as the 'plain meaning rule' may protect the integrity of the writing. In determining the meaning of contract, courts in all legal systems generally consider themselves free to look to all the relevant circumstances, including evidence of prior negotiations, even if it shows that both parties attached to the contract language a meaning different from the one that would ordinarily be given to it. Under the plain meaning rule, however, a court may refuse to consider evidence of prior negotiations to interpret contract language in a completely integrated writing that the court considers unambiguous on its face. The essence of this rule is that there are some instances in which the meaning of language, when taken in context, is so clear that evidence of prior negotiations ought not to be used in its interpretation. Civil-law jurisdictions are less wedded to plain meaning.[92]

[90] Restatement (Second) of Contracts § 213; Farnsworth (n 36, vol II), 219 ff; *Chitty on Contracts* (n 65, vol I), 752 ff.

[91] cf also Art 2:105 PECL; Art 2.1.17 PICC.

[92] See Art 1156 *Code civil*; § 133 BGB; and see Stefan Vogenauer, in Mathias Schmoeckel, Joachim Rückert, and Reinhard Zimmermann, *Historisch-kritischer Kommentar zum BGB* (vol I, 2003), §§ 133, 157.

VII. Performance and Breach

Legal systems show a wide variety of approaches with respect to the rights of a party that claims that the other party is in breach of contract. Two distinct questions may be posed. First, how is a court to determine whether there has been a breach of contract? Second, if there has been a breach, how is a court to determine whether that breach is serious enough to justify the aggrieved party in ending the contractual relationship?

1. Determining Whether There Has Been a Breach

As to the first question, there is an important difference between common-law and civil-law systems.[93] In common-law systems, the norm is that of strict performance. A party is expected to perform in accordance with the letter of the contract, and a failure to do so is actionable, without regard to the fault of the non-performing party. Furthermore, a failure to render strict performance is of itself actionable, with no requirement that the aggrieved party give any notice or make any protest.

Here civil-law systems often differ in two significant respects from their common-law counterparts. First, in some civil-law systems, notably those based on German law, fault helps determine whether there has been breach. In principle, a party can avoid liability for breach by proving that it used reasonable care under the circumstances; thus under German law, delay is not a breach unless the delay is due to some fact or behaviour on the part of the obligor for which the obligor is 'responsible'.[94] Second, unlike the common law, many civil-law systems are not unitary. The German system, for example, divides breaches into the categories of impossibility and delay, with a residual category of 'positive breach of contract'.[95]

[93] For comparative discussions, see Zweigert and Kötz (n 2), 486 ff; G. H. Treitel, *Remedies for Breach of Contract: A Comparative Account* (1988); Gareth H. Jones and Peter Schlechtriem, 'Breach of Contract (Deficiencies in a Party's Performance)', in *International Encyclopedia of Comparative Law* (vol VII, ch 15, 1999); for an analytical discussion of the common law approach, see Smith (n 36), 376 ff.

[94] For comparative discussion of the relevance of fault, see Treitel, *Remedies* (n 93), 7 ff; Jones and Schlechtriem (n 93), nn 203 ff. International instruments such as CISC, PECL, and PICC do not base liability for breach of contract on fault. German law, however, has retained the fault criterion (even if only for the claim for damages) also under the new regime introduced as a result of the Modernization of the Law of Obligations Act in 2002: cf § 280 I 2 BGB.

[95] For the law before 2002, see the overview in Zweigert and Kötz (n 2), 488 ff; Zimmermann (n 9), 806 ff. The different types of breach survive as significant elements for determining the debtor's liability details even under the new law, albeit under a uniform umbrella concept of breach of duty (*Pflichtverletzung*). For details, see Reinhard Zimmermann, *The New German Law of Obligations: Historical and Comparative Perspectives* (2005), 39 ff. The international instruments adopt a unitary approach; see Arts 45 ff, 61 ff (breach of contract); Chs 8 and 9 PECL (non-performance); Ch 7 PICC (non-performance).

Impossibility of performance will also be treated differently depending on whether it is original or subsequent.[96] German law treats delayed performance as a special instance of default, and may not afford the aggrieved party the remedies for default by reason of the mere fact that the obligor failed to perform at the maturity date. The aggrieved party must make a protest (*Mahnung*) to put the other party in default and start a default period running, unless a time for performance has been fixed with reference to the calendar, or thirty days have passed after invoicing.[97]

French law distinguishes between an obligation to achieve a specific result (*obligation de résultat*) and an obligation to use reasonable efforts to achieve a result (*obligation de moyens*), as would commonly be undertaken by a doctor or lawyer or a person agreeing to manage another's business. For the former the obligee need only prove non-performance, leaving the obligee to prove excuse (*cause étrangère*); for the latter the obligee must prove both non-performance and fault. In principle no claim for damages, whether for delay or non-performance, can ordinarily be brought until the other party has been put in default by a formal protest (*mise en demeure*), though this is unnecessary if, for example, there is a fixed period for performance.[98]

2. Determining Whether Breach Justifies Ending Relationship

A mere breach or other failure of performance does not necessarily entitle the aggrieved party to end the contractual relationship, at least in the absence of a specific cancellation provision. A serious failure of performance, however, generally allows the aggrieved party at its election to end that relationship. Legal systems differ with respect to how serious a default is required to justify ending the contractual relationship, with respect to the extent to which the aggrieved party is entitled to use self-help in ending that relationship, and with respect to the nature of the aggrieved party's rights when the relationship is ended.[99]

English courts often focus on the significance of the relevant term, holding that the term must be 'essential' in order to justify ending the contractual relationship. In dealing with contracts for the sale of goods, they distinguish between conditions

[96] §§ 283, 311 a BGB; see Zimmermann, *New German Law of Obligations* (n 95), 52 f, 62 ff.

[97] § 286 BGB. For comparative discussion, see Treitel, *Remedies* (n 93), 136 ff. CISG, PECL, and PICC do not recognize a requirement of notice.

[98] For an overview of the French system, see Zweigert and Kötz (n 2), 496 ff.

[99] For comparative discussion, see Treitel, *Remedies* (n 93), 318 ff; Axel Flessner, 'Befreiung vom Vertrag wegen Nichterfüllung', (1997) 5 *Zeitschrift für Europäisches Privatrecht* 255 ff; for the international development, see Peter Schlechtriem, 'Abstandnahme vom Vertrag', in Jürgen Basedow (ed), *Europäische Vertragsrechtsvereinheitlichung und deutsches Recht* (2000), 159 ff; Ingeborg Schwenzer, 'Rechtsbehelfe und Rückabwicklungsmodelle im CISG, in den European und UNIDROIT Principles, im Gandolfi-Entwurf und im deutschen Schuldrechtsmodernisierungsgesetz', in Peter Schlechtriem (ed), *Wandlungen des Schuldrechts* (2002), 37 ff.

and warranties. A condition is an important term, a breach of which may give a right to end the contractual relationship, while a warranty is a subsidiary term, a breach of which gives right to damages only.[100]

This distinction is unknown in the United States where the focus is generally on the magnitude of the breach and not on the significance of the term. When the parties have exchanged promises, courts generally regard substantial performance by each party as a 'constructive' (or implied) condition of the other party's obligation to perform. If a party's non-performance is significant enough to be characterized as 'material', the non-performance at least justifies the aggrieved party in invoking the constructive condition and suspending its own performance, giving the other party a chance to cure the non-performance. If the non-performance continues without cure for a significant time, the aggrieved party is entitled to end the relationship.[101]

In common-law systems, an aggrieved party that is justified in ending the contractual relationship is entitled to declare the contract cancelled by giving notice to the other party. Of course, an aggrieved party runs the risk of overstepping the bounds of the law, for ending the contractual relationship and refusing to perform without justification is itself a material breach.

Under German law, the other party's failure to perform does not, as a rule, itself entitle an aggrieved party to end the contractual relationship. If the debtor does not perform, or does not perform properly, at the time when he has to effect performance, the creditor must generally allow the debtor a grace period. If the debtor does not perform within that period, the creditor may terminate the contract, whether or not the debtor was at fault.[102] However, he is automatically released from his obligation in cases where the debtor becomes free as a result of the fact that performance has become impossible.[103]

Under French law, the right to end the contractual relationship follows from the

[100] For details, see Treitel, *Contract* (n 34), 788 ff; for the historical background, see Reinhard Zimmermann, ' "Heard Melodies are Sweet, but those Unheard are Sweeter . . .": Conditio Tacita, Implied Condition und die Fortbildung des europäischen Vertragsrechts', (1993) 193 *Archiv für die civilistische Praxis* 153 ff.

[101] Farnsworth (n 36, vol II), 470 ff. For the sale of goods, any departure from 'perfect tender' allows the buyer to declare total breach. This apparently harsh rule is mitigated by a broad cure right and by exceptions for installment contracts: §§ 2–508, 2–601, 2–612 UCC.

[102] § 323 BGB; for details, see Zimmermann, *New German Law of Obligations* (n 95), 66 ff. If it is kept in mind that there are exceptions to the requirement of fixing a grace period for certain cases of serious breach, the practical result will often be the same as under Arts 9:301 (1) PECL and 7.3.1 PICC. Here, termination is available in cases of fundamental breach of contract, but the creditor may elevate a non-fundamental delay of performance to a fundamental one by means of granting a grace period: Arts 8:106 (3), 9:301 (2) PECL, 7.1.5 (3) PICC; cf also Arts 47, 49, 63, 64 CISG. The notion of essential breach is defined in Arts 25 CISG and 8:103 PECL; cf also Art 7.3.1 (2) PICC and Gerhard Lubbe, 'Fundamental Breach under the CISG: A Source of Fundamentally Divergent Results', (2004) 68 *RabelsZ* 444 ff.

[103] § 326 BGB; for a comparable rule in the international instruments, see Art 9:303 (4) PECL.

view that every synallagmatic contract is regarded as concluded under a resolutive condition of proper performance of the reciprocal duties. As under German law, some obligations are characterized as 'ancillary' or 'secondary' and are sanctioned only by damages. The contract is not, however, 'resolved' as a matter of law by the other party's failure to perform its undertaking, and the aggrieved party can either claim performance or put an end to the relationship.[104] If the aggrieved party claims the latter, self-help is severely limited, for *résolution* can be sought only in legal proceedings.[105] It is for the judge, who has broad discretion, to determine the gravity of the breach and order *résolution*, grant a period of grace (*délai de grâce*) during which the other party must render performance, uphold the contract, or, in the case of a contract for the sale of goods, order price reduction for defects that are not serious. There are some exceptions, and legal proceedings are not required, for example, if the contract contains an express provision for termination on occurrence of a stated event. Furthermore, if a fixed time is provided for a buyer to take delivery of goods, the seller can regard the contract as terminated if the buyer does not take delivery within that time.[106]

Various terms are used for the aggrieved party's ending the contractual relationship: termination, cancellation, rescission, avoidance. Ending the relationship necessarily liberates the parties from their remaining obligations of performance. Like full performance, it results in the discharge of the aggrieved party.

The doctrine of anticipatory repudiation, which enables an aggrieved party to claim damages even before performance becomes due, is often regarded as an important common-law peculiarity.[107] If, before the time for performance of a party's obligations has arrived, that party repudiates by stating that it will not or cannot perform those obligations, the aggrieved party need not wait until the time for performance has arrived but can immediately terminate the contract and claim damages for total breach. Indeed, in the United States even insecurity as to performance allows the insecure party to demand adequate assurances of performance from the other party, suspend its own performance if it is com-mercially reasonable to do so, and, should the assurances not issue, declare the contract repudiated.[108] Anticipatory repudiation is also, however, known outside the common-law world. Thus, German law recognizes the possibility that an anticipatory repudiation may justify termination of the contract and/or may allow the aggrieved party to claim damages. 109

IX. Remedies

1. Damages

When one party breaches a contract, the central purpose of most legal systems is to put the aggrieved party in the position in which it would have been had the contract been performed. Often this is attempted by an award of money damages that, in effect, imposes a new obligation—one to pay money—for the breach of the old. The objective of money damages is to redress loss by compensating the promisee and not to deter breach by punishing the party in breach.[119] For this reason, punitive damages are generally not available for breach of contract. An aggrieved party will often be content with an award of monetary damages, as may be the case if that party can use the money to purchase substitute goods or services elsewhere. This does not, to be sure, take account of the costs of litigating the dispute which may be necessary to get an award of damages.

2. Stipulated Damages

In some cases, the parties will want to include in their contract a provision stipulating the sums payable as damages in the event of various possible breaches. Such a provision is commonly regarded as both a ceiling and a floor for recovery. The enforceability of such stipulated damage provisions varies among legal systems.[120]

Civil-law systems are generally receptive to such provisions. French law starts from a principle of literal enforcement of provisions stipulating damages. Some years ago, however, the *Code civil* was amended to allow the judge to reduce or increase stipulated damages if the clause is manifestly excessive or derisory, in order to deal with abuses in certain types of transactions.[121] In German law, stipulated damage clauses are generally enforceable, but if the amount is unreasonably high the court can reduce it to a reasonable sum.[122]

The common law takes a more restrictive approach. The most important restriction is the one denying the parties the power to stipulate in their contract a

[119] These damages include only foreseeable losses, though French law makes an exception in cases of fraud, for which causation is the only limit: Arts 1150 f *Code civil*. See further Zimmermann (n 9), 829 ff; Treitel, *Contract* (n 34), 965 ff; Gordley, *Foundations* (n 43), 395 ff; Smith (n 36), 409 ff; Art 74 CISG; Art 9:503 PECL; Art 7.4.4 PICC; Florian Faust, *Die Vorhersehbarkeit des Schadens gemäß Art. 74 S. 2 UN-Kaufrecht (CISG)* (1996).

[120] Zimmermann (n 9), 95 ff; Ralf-Peter Sossna, *Die Geschichte der Begrenzung von Vertragsstrafen* (1993); Treitel, *Remedies* (n 93), 208 ff; Harriet Schelhaas, *Het boetebeding in het Europese contractenrecht* (2004); Art 9:509 PECL; Art 7.4.13 PICC.

[121] Art 1152 al 2 *Code civil*. [122] § 343 BGB.

sum of money payable as damages that is so large as to be characterized as a 'penalty'. If the stipulated sum is significantly larger than the amount required for compensation, the stipulation may have an *in terrorem* effect on the promisor that will deter breach, perhaps inefficiently, by compelling performance. Common-law courts therefore exercise a power to condemn stipulated damage provisions that depart from the compensation principle, that is, contractual clauses providing for what are called penalties rather than for what are called liquidated damages.

If a stipulated damage provision is condemned as a penalty, the remainder of the agreement stands, and the aggrieved party is remitted to conventional damages for breach of that agreement. Drawing a line between liquidated damages and penalties has proved no simple matter for common-law courts. Several factors may be relevant. The most important is that the stipulated sum must be a reasonable forecast of the presumed loss, viewed as of the time when the contract is made. A second factor is that the damages to be anticipated as resulting from the breach must be uncertain in amount or difficult to prove.[123]

3. Specific Relief

Sometimes the aggrieved party will not find monetary damages satisfactory and will prefer specific relief. Of course if the promise of the party in breach was simply to pay a sum of money, the effect of a judgment for monetary damages is to give the aggrieved party specific relief. But it is not always easy for a court to place a monetary value on the loss occasioned by a breach. The broken promise may be one to deliver goods that have special 'sentimental' value to the aggrieved party, or it may be one that requires performance over a long period of time so that it will be difficult to forecast damages.

It is everywhere agreed that a buyer of goods must not resort to self-help to seize goods from a seller or use similar private means to coerce performance. An aggrieved party must go to court to get specific relief. Civil-law courts start with the principle that specific relief for breach of contract is generally available. Common-law courts, on the other hand, start with the principle that specific relief for breach of contract is an equitable remedy that will only be ordered when damages or other common-law remedies afford inadequate protection to the aggrieved party.[124]

[123] For details, see Treitel, *Contract* (n 34), 999 ff; *idem, Remedies* (n 93), 228 ff; Farnsworth (n 36, vol III), 300 ff.

[124] For historical and comparative analyses, see Zimmermann (n 9), 770 ff; Zweigert and Kötz (n 2), 470 ff; Treitel, *Remedies* (n 93), 43 ff; Gordley, *Foundations* (n 43), 388 ff; Shael Herman, 'Specific Performance: A Comparative Analysis', (2003) 7 *Edinburgh LR* 5 ff, 194 ff; and see Smith (n 36), 398 ff; Melvin A. Eisenberg, 'Actual and Virtual Specific Performance, the Theory of Efficient Breach, and the Indifference Principle in Contract Law', (2005) 23 *California LR* 975 ff.

In German law, a contracting party is entitled to demand specific relief. The law subjects this to exceptions, as where specific relief is impossible. If the obligation is to deliver movable property, enforcement involves the aid of an official who takes the property from the party in breach and gives it to the aggrieved party. If the obligation is to do an act that can be performed by another person, as in the case of a contract to build or to deliver generic goods, the aggrieved party can ask the court for authorization to have the act done at the expense of the party in breach, who may be required to pay in advance. But personal constraint is not excluded, and if an act cannot be performed by another person, or where performance consists of forbearance, failing to comply with the court's judgment may be punished by fine and imprisonment.[125]

The French and related systems also recognize in principle the availability of *exécution en nature* or what is called 'direct' execution. French law, however, proceeds in a very grudging manner in enforcing judgments of specific relief and the general availability of such relief is subject to an important exception. The *Code civil* distinguishes between obligations to transfer property (*obligations de donner*) on the one hand and obligations to do or not to do (*obligations de faire ou de ne pas faire*) on the other hand. Obligations of the former kind may be specifically enforced by having an officer of the court put the aggrieved party into possession, though otherwise state actors will not use force in support of *exécution en nature*.[126] If the obligation is to deliver generic goods, the court may authorize the purchaser to buy replacement goods at the seller's expense.[127] Under the *Code civil*, however, obligations to do or not to do are sanctioned only by damages and cannot be directly enforced, at least in the realm of personal services.[128] To help enforce promises, whether those giving rise to specific performance or merely to damages, the courts also developed the *astreinte*.[129] It usually takes the form of a judgment for performance or damages, coupled with a condemnation by which the party in breach must pay a fixed sum for each day or other period that that party remains in default. If, at the end of the period, the party in breach has still not performed, the aggrieved party may apply for a liquidation of the *astreinte* and for the issue of a further *astreinte*. The *astreinte* is not available to compel the performance of personal services, though it may be used to enforce negative injunctions. In contrast to German law, the fine is payable to the breached-against party, not to the state.[130]

[125] §§ 883, 887, 888, 890 German Civil Procedure Act; and see Zweigert and Kötz (n 2), 472 ff; Treitel, *Remedies* (n 93), 51 ff.

[126] Art 826 *Code de procédure civile.*

[127] Art 1144 *Code civil.*

[128] Art 1142 *Code civil* (based on the maxim of 'nemo potest praecise cogi ad factum' of the *ius commune*).

[129] It has since been codified in Law No. 91–650 of 9 July 1991, Arts 33–7.

[130] For details of the French system, see Zweigert and Kötz (n 2), 475 ff; Treitel, *Remedies* (n 93), 55 ff; Oliver Remien, *Rechtsverwirklichung durch Zwangsgeld* (1992), 33 ff.

The common law takes a very different approach to specific relief, one shaped by history.[131] Save for exceptional actions like replevin for goods, the law courts granted only substitutional relief, and the typical judgment declared that the plaintiff recover from the defendant a sum of money. Aside from the law courts stood a separate and parallel system of courts of Equity, presided over by a chancellor, and claimants could proceed in either law or Equity. Courts of Equity, in contrast to courts of law, granted direct relief for breach of contract in the form of an order of specific performance. In addition, they might, instead of ordering specific performance, direct a party by means of an injunction to refrain from doing a specified act. Where the performance due under the contract consists simply of forbearance, the effect of an injunction is to order specific performance. Often, however, a negative injunction is used as an indirect means of enforcing a duty to act. Decrees in Equity came to take the form of a chancellor's personal command to the defendant to do or not to do something, on pain of being held in contempt—either criminal contempt, at the instance of the judge, or civil contempt, at the instance of the plaintiff. Either could subject the defendant to imprisonment or fine—drastic remedies, which yielded significant limitations on their employ.

The most important historical limitation grew up out of the circumstance that the chancellor had originally granted equitable relief in order to remedy the deficiencies of the common law. Equitable remedies were therefore readily characterized as 'extraordinary'. When, during a long jurisdictional struggle in England between the two systems of courts, some means of accommodation was needed, an 'adequacy' test was developed to prevent the chancellor from encroaching on the powers of the common-law judges. Equity would stay its hand if the remedy at law of an award of damages at law was 'adequate' to protect the injured party.

To the 'adequacy' test was added the gloss that damages were ordinarily adequate—a gloss encouraged by a confidence that a market economy ought to enable the injured party to arrange a substitute transaction. English courts came to regard money damages as the norm and specific relief as the deviation. Only for land, which English courts regarded with particular esteem, was a general exception made. Each parcel, however ordinary, was considered 'unique', and its value was regarded as to some extent speculative. American courts act similarly, though they are more willing to consider routine transactions in land fungible and susceptible to damages, rather than specific performance.[132] In addition, damages will not be adequate to protect the injured party's expectation if the loss caused by the breach cannot be estimated with sufficient certainty, as with contracts involving matters of taste or sentiment.[133] It may also be the case even concerning contracts

[131] For what follows, see Rheinstein (n 6), 138 ff; Zweigert and Kötz (n 2), 479 ff; Treitel, *Remedies* (n 93), 63 ff; *idem*, *Contract* (n 34), 1019 ff; Gareth Jones and William Goodhart, *Specific Performance* 2nd edn, 1996); Farnsworth (n 36, vol III), 161 ff.

[132] See eg *Van Wagner Advertising Corp v S & M Enters*, 492 NE2d 756 (New York, 1986).

[133] See eg *Falcke v Gray*, 4 Drew 651 (Ch 1859); Restatement (Second) of Contracts § 360.

of a more commercial character, where an extended period for performanc renders impossible the accurate forecast of damages at trial.

A second historical limitation, or group of limitations, is based on the conce that equitable relief is discretionary, allowing the chancellor to withhold reli if considerations of fairness or morality dictated. Relief is sometimes refused o the ground that it would impose on the court burdens of supervision that ar disproportionate to the advantages to be gained. Because the restraints on th availability of equitable relief have traditionally been viewed as limitations on th court's jurisdiction, it has been generally supposed that the parties cannot enlarg the availability of specific performance or injunction by contract.[134]

In practice, the difference between the availability of specific relief in common law systems and in civil-law systems may not be as great as at first appears.[13] The contemporary approach in common-law nations is to compare remedies to determine which is more effective in affording suitable protection to the injured party. The concept of adequacy has thus tended to become relative, and the com-parison more often leads to granting equitable relief than was historically the case. In civil-law countries, the theoretical availability of specific relief may have limited practical importance because of a preference for money damages. The buyer that fails to receive promised goods may well find it preferable to purchase substitute goods on the market and claim money damages from the seller rather than seek to compel the seller to provide the goods or ask for some other form of specific relief. Nevertheless the attitudes of civil-law and common-law systems toward specific relief remain fundamentally different.

XI. A TENTATIVE CONCLUSION

The overview provided in this chapter has revealed a number of differences between civilian legal systems and the law, and also between French and German law as two main exponents of the civil-law tradition and, to some extent, even between English and US-American law. The same is true of other major issues in the field of general contract law that have not been touched upon: contractual capacity,[143] mistake, [144] agency, [145] or assignment.[146] But the overview has also shown that there is a gradual convergence.[147] It is due to developments in all of the four legal systems covered in this chapter: English, US-American, French, and German law. And it has enabled scholars from around the world to elaborate an inter-national restatement of contract law (the UNIDROIT Principles of International Commercial Contracts) and scholars from all the member states of the European Union to formulate a restatement of European contract law (the Principles of European Contract Law). These documents, in turn, may provide guidance for the future development of the national contract laws. They are discussed in some detail in Chapters 16 and 29 in this Handbook.

JOHN LEONARD, Plaintiff, -against- PESICO, INC., Defenant.

88 F. Supp. 2d 116 (S.D.N.Y.1999)

WOOD, U.S.D.J.:

Plaintiff brought this action seeking, among other things, specific performance of an alleged offer of a Harrier Jet, featured in a television advertisement for defendant's "Pepsi Stuff" promotion. Defendant has moved for summary judgment pursuant to *Federal Rule of Civil Procedure 56*. For the reasons stated below, defendant's motion is granted.

I. Background

This case arises out of a promotional campaign conducted by defendant, the producer and distributor of the soft drinks Pepsi and Diet Pepsi. The promotion, entitled "Pepsi Stuff," encouraged consumers to collect "Pepsi Points" from specially marked packages of Pepsi or Diet Pepsi and redeem these points for merchandise featuring the Pepsi logo. Before introducing the promotion nationally, defendant conducted a test of the promotion in the Pacific Northwest from October 1995 to March 1996. A Pepsi Stuff catalog was distributed to consumers in the test market, including Washington State. Plaintiff is a resident of Seattle, Washington. While living in Seattle, plaintiff saw the Pepsi Stuff commercial that he contends constituted an offer of a Harrier Jet.

A. *The Alleged Offer*

Because whether the television commercial constituted an offer is the central question in this case, the Court will describe the commercial in detail. The commercial opens upon an idyllic, suburban morning, where the chirping of birds in sun-dappled trees welcomes a paperboy on his morning route. As the newspaper hits the stoop of a conventional two-story house, the tattoo of a military drum introduces the subtitle, "MONDAY 7:58 AM." The stirring strains of a martial air mark the appearance of a well-coiffed teenager preparing to leave for school, dressed in a shirt emblazoned with the Pepsi logo, a red-white-and-blue ball. While the teenager confidently preens, the military drumroll again sounds as the subtitle "T-SHIRT 75 PEPSI POINTS" scrolls across the screen. Bursting from his room, the teenager strides down the hallway wearing a leather jacket. The drumroll sounds again, as the subtitle "LEATHER JACKET 1450 PEPSI POINTS" appears. The teenager opens the door of his house and, unfazed by the glare of the early morning sunshine, puts on a pair of sunglasses. The drumroll then accompanies the subtitle "SHADES 175 PEPSI POINTS." A voiceover then intones, "Introducing the new Pepsi Stuff catalog," as the camera focuses on the cover of the catalog.[2]

FN2 At this point, the following message appears at the bottom of the screen: "Offer not available in all areas. See details on specially marked packages."

The scene then shifts to three young boys sitting in front of a high school building. The boy in the middle is intent on his Pepsi Stuff Catalog, while the boys on either side are each drinking Pepsi. The three boys gaze in awe at an object rushing overhead, as the military march builds to a crescendo. The Harrier Jet is not yet visible, but the observer senses the presence of a mighty plane as the extreme winds generated by its flight create a paper maelstrom in a classroom devoted to an otherwise dull physics lesson. Finally, the Harrier Jet swings into view and lands by the side of the school building, next to a bicycle rack. Several students run for cover, and the velocity of the wind strips one hapless faculty member down to his underwear.

While the faculty member is being deprived of his dignity, the voiceover announces: “Now the more Pepsi you drink, the more great stuff you’re gonna get.”

The teenager opens the cockpit of the fighter and can be seen, helmetless, holding a Pepsi. “Looking very pleased with himself,” the teenager exclaims, “Sure beats the bus,” and chortles. The military drumroll sounds a final time, as the following words appear: “HARRIER FIGHTER 7,000,000 PEPSI POINTS.” A few seconds later, the following appears in more stylized script: “Drink Pepsi -- Get Stuff.” With that message, the music and the commercial end with a triumphant flourish.

Inspired by this commercial, plaintiff set out to obtain a Harrier Jet. Plaintiff explains that he is “typical of the ‘Pepsi Generation’ . . . he is young, has an adventurous spirit, and the notion of obtaining a Harrier Jet appealed to him enormously.” Plaintiff consulted the Pepsi Stuff Catalog. The Catalog features youths dressed in Pepsi Stuff regalia or enjoying Pepsi Stuff accessories, such as “Blue Shades” (“As if you need another reason to look forward to sunny days.”), “Pepsi Tees” (“Live in ‘em. Laugh in ‘em. Get in ‘em.”), “Bag of Balls” (“Three balls. One bag. No rules.”), and “Pepsi Phone Card” (“Call your mom!”). The Catalog specifies the number of Pepsi Points required to obtain promotional merchandise. The Catalog includes an Order Form which lists, on one side, fifty-three items of Pepsi Stuff merchandise redeemable for Pepsi Points. Conspicuously absent from the Order Form is any entry or description of a Harrier Jet. The amount of Pepsi Points required to obtain the listed merchandise ranges from 15 (for a “Jacket Tattoo” (“Sew ‘em on your jacket, not your arm.”)) to 3300 (for a “Fila Mountain Bike” (“Rugged. All-terrain. Exclusively for Pepsi.”)). It should be noted that plaintiff objects to the implication that because an item was not shown in the Catalog, it was unavailable.

The rear foldout pages of the Catalog contain directions for redeeming Pepsi Points for merchandise. (*See* Catalog, at rear foldout pages.) These directions note that merchandise may be ordered “only” with the original Order Form. The Catalog notes that in the event that a consumer lacks enough Pepsi Points to obtain a desired item, additional Pepsi Points may be purchased for ten cents each; however, at least fifteen original Pepsi Points must accompany each order.

Although plaintiff initially set out to collect 7,000,000 Pepsi Points by consuming Pepsi products, it soon became clear to him that he “would not be able to buy (let alone drink) enough Pepsi to collect the necessary Pepsi Points fast enough.” Reevaluating his strategy, plaintiff “focused for the first time on the packaging materials in the Pepsi Stuff promotion,” and realized that buying Pepsi Points would be a more promising option. Through acquaintances, plaintiff ultimately raised about $ 700,000.

B. *Plaintiff’s Efforts to Redeem the Alleged Offer*

On or about March 27, 1996, plaintiff submitted an Order Form, fifteen original Pepsi Points, and a check for $ 700,008.50. Plaintiff appears to have been represented by counsel at the time he mailed his check; the check is drawn on an account of plaintiff’s first set of attorneys. At the bottom of the Order Form, plaintiff wrote in “1 Harrier Jet” in the “Item” column and “7,000,000” in the “Total Points” column. In a letter accompanying his submission, plaintiff stated that the check was to purchase additional Pepsi Points “expressly for obtaining a new Harrier jet as advertised in your Pepsi Stuff commercial.”

On or about May 7, 1996, defendant’s fulfillment house rejected plaintiff’s submission and returned the check, explaining that:

> The item that you have requested is not part of the Pepsi Stuff collection. It is not included in the catalogue or on the order form, and only catalogue merchandise can be redeemed under this program.
>
> The Harrier jet in the Pepsi commercial is fanciful and is simply included to create a humorous and entertaining ad. We apologize for any misunderstanding or confusion that you may have experienced and are enclosing some free product coupons for your use.

Plaintiff's previous counsel responded on or about May 14, 1996, as follows:

> Your letter of May 7, 1996 is totally unacceptable. We have reviewed the video tape of the Pepsi Stuff commercial . . . and it clearly offers the new Harrier jet for 7,000,000 Pepsi Points. Our client followed your rules explicitly. . . .
>
> This is a formal demand that you honor your commitment and make immediate arrangements to transfer the new Harrier jet to our client. If we do not receive transfer instructions within ten (10) business days of the date of this letter you will leave us no choice but to file an appropriate action against Pepsi . . . .

This letter was apparently sent onward to the advertising company responsible for the actual commercial, BBDO New York ("BBDO"). In a letter dated May 30, 1996, BBDO Vice President Raymond E. McGovern, Jr., explained to plaintiff that:

> I find it hard to believe that you are of the opinion that the Pepsi Stuff commercial ("Commercial") really offers a new Harrier Jet. The use of the Jet was clearly a joke that was meant to make the Commercial more humorous and entertaining. In my opinion, no reasonable person would agree with your analysis of the Commercial.

On or about June 17, 1996, plaintiff mailed a similar demand letter to defendant.

Litigation of this case initially involved two lawsuits, the first a declaratory judgment action brought by PepsiCo in this district, and the second an action brought by Leonard in Florida state court. PepsiCo brought suit in this Court on July 18, 1996, seeking a declaratory judgment stating that it had no obligation to furnish plaintiff with a Harrier Jet. In response to PepsiCo's suit in New York, Leonard brought suit in Florida state court on August 6, 1996, although this case had nothing to do with Florida. That suit was removed to the Southern District of Florida in September 1996.

Once the Florida action had been transferred, Leonard moved to dismiss the declaratory judgment action for lack of personal jurisdiction. In an Order dated November 24, 1997, the Court granted the motion to dismiss for lack of personal jurisdiction in case 96 Civ. 5320, from which PepsiCo appealed. Leonard also moved to voluntarily dismiss the Florida action. While the Court indicated that the motion was proper, it noted that PepsiCo was entitled to some compensation for the costs of litigating this case in Florida, a forum that had no meaningful relationship to the case. In an Order dated December 15, 1997, the Court granted Leonard's motion to voluntarily dismiss this case without prejudice, but did so on condition that Leonard pay certain attorneys' fees.

In an Order dated October 1, 1998, the Court ordered Leonard to pay $ 88,162 in attorneys' fees within thirty days. Leonard failed to do so, yet sought nonetheless to appeal from his voluntary dismissal and the

imposition of fees…Rather than pay the attorneys' fees, Leonard elected to proceed with litigation, and shortly thereafter retained present counsel.

On February 22, 1999, the Second Circuit endorsed the parties' stipulations to the dismissal of any appeals taken thus far in this case. Those stipulations noted that Leonard had consented to the jurisdiction of this Court and that PepsiCo agreed not to seek enforcement of the attorneys' fees award. With these issues having been waived, PepsiCo moved for summary judgment pursuant to *Federal Rule of Civil Procedure 56*. The present motion thus follows three years of jurisdictional and procedural wrangling.

II. Discussion

A. *The Legal Framework*…

B. *Defendant's Advertisement Was Not an Offer*

1. *Advertisements as Offers*

The general rule is that an advertisement does not constitute an offer. The *Restatement (Second) of Contracts* explains that:

> Advertisements of goods by display, sign, handbill, newspaper, radio or television are not ordinarily intended or understood as offers to sell. The same is true of catalogues, price lists and circulars, even though the terms of suggested bargains may be stated in some detail. It is of course possible to make an offer by an advertisement directed to the general public (see § 29), but there must ordinarily be some language of commitment or some invitation to take action without further communication.

Restatement (Second) of Contracts § 26 cmt. b (1979). Similarly, a leading treatise notes that:

> It is quite possible to make a definite and operative offer to buy or sell goods by advertisement, in a newspaper, by a handbill, a catalog or circular or on a placard in a store window. *It is not customary to do this, however; and the presumption is the other way*. . . . Such advertisements are understood to be mere requests to consider and examine and negotiate; and no one can reasonably regard them as otherwise unless the circumstances are exceptional and the words used are very plain and clear.

An advertisement is not transformed into an enforceable offer merely by a potential offeree's expression of willingness to accept the offer through, among other means, completion of an order form. In *Mesaros v. United States, 845 F.2d 1576 (Fed. Cir. 1988)*, for example, the plaintiffs sued the United States Mint for failure to deliver a number of Statue of Liberty commemorative coins that they had ordered. When demand for the coins proved unexpectedly robust, a number of individuals who had sent in their orders in a timely fashion were left empty-handed. *See id. at 1578-80*. The court began by noting the "well-established" rule that advertisements and order forms are "mere notices and solicitations for offers which create no power of acceptance in the recipient." The spurned coin collectors could not maintain a breach of contract action because no contract would be formed until the advertiser accepted the order form and processed payment. Under these principles, plaintiff's letter of March 27, 1996, with the Order Form and the appropriate number of Pepsi Points, constituted the offer. There would be no enforceable contract until defendant accepted the Order Form and cashed the check.

The exception to the rule that advertisements do not create any power of acceptance in potential offerees is where the advertisement is "clear, definite, and explicit, and leaves nothing open for negotiation," in that circumstance, "it constitutes an offer, acceptance of which will complete the contract." *Lefkowitz v. Great Minneapolis Surplus Store, 251 Minn. 188, 86 N.W.2d 689, 691 (Minn. 1957)*. In *Lefkowitz*, defendant had published a newspaper announcement stating: "Saturday 9 AM Sharp, 3 Brand New Fur Coats, Worth to $ 100.00, First Come First Served $ 1 Each." *86 N.W.2d at 690*. Mr. Morris Lefkowitz arrived at the store, dollar in hand, but was informed that under defendant's "house rules," the offer was open to ladies, but not gentlemen. *See id.* The court ruled that because plaintiff had fulfilled all of the terms of the advertisement and the advertisement was specific and left nothing open for negotiation, a contract had been formed. *See id.; see also Johnson v. Capital City Ford Co., 85 So. 2d 75, 79 (La. Ct. App. 1955)* (finding that newspaper advertisement was sufficiently certain and definite to constitute an offer).

The present case is distinguishable from *Lefkowitz*. First, the commercial cannot be regarded in itself as sufficiently definite, because it specifically reserved the details of the offer to a separate writing, the Catalog. [6] The commercial itself made no mention of the steps a potential offeree would be required to take to accept the alleged offer of a Harrier Jet. The advertisement in *Lefkowitz*, in contrast, "identified the person who could accept."[7] Second, even if the Catalog had included a Harrier Jet among the items that could be obtained by redemption of Pepsi Points, the advertisement of a Harrier Jet by both television commercial and catalog would still not constitute an offer. As the *Mesaros* court explained, the absence of any words of limitation such as "first come, first served," renders the alleged offer sufficiently indefinite that no contract could be formed. *See Mesaros, 845 F.2d at 1581*. "A customer would not usually have reason to believe that the shopkeeper intended exposure to the risk of a multitude of acceptances resulting in a number of contracts exceeding the shopkeeper's inventory." Farnsworth, *supra*, at 242. There was no such danger in *Lefkowitz*, owing to the limitation "first come, first served."

FN6 It also communicated additional words of reservation: "Offer not available in all areas. See details on specially marked packages."

FN7 The reservation of the details of the offer in this case distinguishes it from *Payne v. Lautz Bros. & Co., 166 N.Y.S. 844 (City Ct. Buffalo 1916)*. In *Payne*, a stamp and coupon broker purchased massive quantities of coupons produced by defendant, a soap company, and tried to redeem them for 4,000 round-trip tickets to a local beach. The court ruled for plaintiff, noting that the advertisements were "absolutely unrestricted. It contained no reference whatever to any of its previous advertising of any form." *Id. at 848*. In the present case, by contrast, the commercial explicitly reserved the details of the offer to the Catalog.

The Court finds, in sum, that the Harrier Jet commercial was merely an advertisement. The Court now turns to the line of cases upon which plaintiff rests much of his argument….

C. *An Objective, Reasonable Person Would Not Have Considered the Commercial an Offer*

Plaintiff's understanding of the commercial as an offer must also be rejected because the Court finds that no objective person could reasonably have concluded that the commercial actually offered consumers a Harrier Jet.

1. *Objective Reasonable Person Standard*

In evaluating the commercial, the Court must not consider defendant's subjective intent in making the commercial, or plaintiff's subjective view of what the commercial offered, but what an objective, reasona-

ble person would have understood the commercial to convey. *See Kay-R Elec. Corp. v. Stone & Weber Constr. Co., 23 F.3d 55, 57 (2d Cir. 1994)* ("We are not concerned with what was going through the heads of the parties at the time [of the alleged contract]. Rather, we are talking about the objective principles of contract law."); *Mesaros, 845 F.2d at 1581* ("A basic rule of contracts holds that whether an offer has been made depends on the objective reasonableness of the alleged offeree's belief that the advertisement or solicitation was intended as an offer."); Farnsworth, *supra*, § 3.10, at 237; Williston, *supra*, § 4:7 at 296-97.

If it is clear that an offer was not serious, then no offer has been made:

> What kind of act creates a power of acceptance and is therefore an offer? It must be an expression of will or intention. It must be an act that leads the offeree reasonably to conclude that a power to create a contract is conferred. This applies to the content of the power as well as to the fact of its existence. *It is on this ground that we must exclude* invitations to deal or acts of mere preliminary negotiation, and *acts evidently done in jest* or without intent to create legal relations.

Corbin on Contracts, § 1.11 at 30 (emphasis added). An obvious joke, of course, would not give rise to a contract. *See, e.g., Graves v. Northern N.Y. Pub. Co., 260 A.D. 900, 22 N.Y.S.2d 537 (App. Div. 4th Dept. 1940)* (dismissing claim to offer of $ 1000, which appeared in the "joke column" of the newspaper, to any person who could provide a commonly available phone number). On the other hand, if there is no indication that the offer is "evidently in jest," and that an objective, reasonable person would find that the offer was serious, then there may be a valid offer. *See Barnes, 549 P.2d at 1155* ("If the jest is not apparent and a reasonable hearer would believe that an offer was being made, then the speaker risks the formation of a contract which was not intended."); *see also Lucy v. Zehmer, 196 Va. 493, 84 S.E.2d 516, 518, 520 (Va. 1954)* (ordering specific performance of a contract to purchase a farm despite defendant's protestation that the transaction was done in jest as "'just a bunch of two doggoned drunks bluffing'").

2. *Necessity of a Jury Determination*

Plaintiff also contends that summary judgment is improper because the question of whether the commercial conveyed a sincere offer can be answered only by a jury. Relying on dictum from *Gallagher v. Delaney, 139 F.3d 338 (2d Cir. 1998)*, plaintiff argues that a federal judge comes from a "narrow segment of the enormously broad American socio-economic spectrum," *id. at 342*, and, thus, that the question whether the commercial constituted a serious offer must be decided by a jury composed of, *inter alia*, members of the "Pepsi Generation," who are, as plaintiff puts it, "young, open to adventure, willing to do the unconventional." (*See* Leonard Aff. P 2.) Plaintiff essentially argues that a federal judge would view his claim differently than fellow members of the "Pepsi Generation."

Plaintiff's argument that his claim must be put to a jury is without merit. *Gallagher* involved a claim of sexual harassment in which the defendant allegedly invited plaintiff to sit on his lap, gave her inappropriate Valentine's Day gifts, told her that "she brought out feelings that he had not had since he was sixteen," and "invited her to help him feed the ducks in the pond, since he was 'a bachelor for the evening.'" *Gallagher, 139 F.3d at 344*. The court concluded that a jury determination was particularly appropriate because a federal judge lacked "the current real-life experience required in interpreting subtle sexual dynamics of the workplace based on nuances, subtle perceptions, and implicit communications." *Id. at 342*. This case, in contrast, presents a question of whether there was an offer to enter into a contract, requiring the Court to determine how a reasonable, objective person would have understood defendant's commercial. Such an

inquiry is commonly performed by courts on a motion for summary judgment. *See Krumme, 143 F.3d at 83*; *Bourque, 42 F.3d at 708*; *Wards Co., 761 F.2d at 120*.

3. *Whether the Commercial Was "Evidently Done In Jest"*

Plaintiff's insistence that the commercial appears to be a serious offer requires the Court to explain why the commercial is funny. Explaining why a joke is funny is a daunting task; as the essayist E.B. White has remarked, "Humor can be dissected, as a frog can, but the thing dies in the process . . . ." [11] The commercial is the embodiment of what defendant appropriately characterizes as "zany humor."

11 *Quoted in* Gerald R. Ford, *Humor and the Presidency* 23 (1987).

First, the commercial suggests, as commercials often do, that use of the advertised product will transform what, for most youth, can be a fairly routine and ordinary experience. The military tattoo and stirring martial music, as well as the use of subtitles in a Courier font that scroll terse messages across the screen, such as "MONDAY 7:58 AM," evoke military and espionage thrillers. The implication of the commercial is that Pepsi Stuff merchandise will inject drama and moment into hitherto unexceptional lives. The commercial in this case thus makes the exaggerated claims similar to those of many television advertisements: that by consuming the featured clothing, car, beer, or potato chips, one will become attractive, stylish, desirable, and admired by all. A reasonable viewer would understand such advertisements as mere puffery, not as statements of fact, *see, e.g., Hubbard v. General Motors Corp., 1996 U.S. Dist. LEXIS 6974, 95* Civ. 4362 (AGS), 1996 WL 274018, at *6 (S.D.N.Y. May 22, 1996) (advertisement describing automobile as "Like a Rock," was mere puffery, not a warranty of quality); *Lovett, 207 N.Y.S. at 756*; and refrain from interpreting the promises of the commercial as being literally true.

Second, the callow youth featured in the commercial is a highly improbable pilot, one who could barely be trusted with the keys to his parents' car, much less the prize aircraft of the United States Marine Corps. Rather than checking the fuel gauges on his aircraft, the teenager spends his precious preflight minutes preening. The youth's concern for his coiffure appears to extend to his flying without a helmet. Finally, the teenager's comment that flying a Harrier Jet to school "sure beats the bus" evinces an improbably insouciant attitude toward the relative difficulty and danger of piloting a fighter plane in a residential area, as opposed to taking public transportation.

Third, the notion of traveling to school in a Harrier Jet is an exaggerated adolescent fantasy. In this commercial, the fantasy is underscored by how the teenager's schoolmates gape in admiration, ignoring their physics lesson. The force of the wind generated by the Harrier Jet blows off one teacher's clothes, literally defrocking an authority figure. As if to emphasize the fantastic quality of having a Harrier Jet arrive at school, the Jet lands next to a plebeian bike rack. This fantasy is, of course, extremely unrealistic. No school would provide landing space for a student's fighter jet, or condone the disruption the jet's use would cause.

Fourth, the primary mission of a Harrier Jet, according to the United States Marine Corps, is to "attack and destroy surface targets under day and night visual conditions." United States Marine Corps, Factfile: AV-8B Harrier II (last modified Dec. 5, 1995) <http://www.hqmc.usmc.mil/factfile.nsf>. Manufactured by McDonnell Douglas, the Harrier Jet played a significant role in the air offensive of Operation Desert Storm in 1991. *See id.* The jet is designed to carry a considerable armament load, including Sidewinder and Maverick missiles. *See id.* As one news report has noted, "Fully loaded, the Harrier can float like a butterfly and sting like a bee -- albeit a roaring 14-ton butterfly and a bee with 9,200 pounds of bombs and missiles." Jer-

ry Allegood, *Marines Rely on Harrier Jet, Despite Critics*, News & Observer (Raleigh), Nov. 4, 1990, at C1. In light of the Harrier Jet's well-documented function in attacking and destroying surface and air targets, armed reconnaissance and air interdiction, and offensive and defensive anti-aircraft warfare, depiction of such a jet as a way to get to school in the morning is clearly not serious even if, as plaintiff contends, the jet is capable of being acquired "in a form that eliminates [its] potential for military use."

Fifth, the number of Pepsi Points the commercial mentions as required to "purchase" the jet is 7,000,000. To amass that number of points, one would have to drink 7,000,000 Pepsis (or roughly 190 Pepsis a day for the next hundred years -- an unlikely possibility), or one would have to purchase approximately $ 700,000 worth of Pepsi Points. The cost of a Harrier Jet is roughly $ 23 million dollars, a fact of which plaintiff was aware when he set out to gather the amount he believed necessary to accept the alleged offer. Even if an objective, reasonable person were not aware of this fact, he would conclude that purchasing a fighter plane for $ 700,000 is a deal too good to be true.

Plaintiff argues that a reasonable, objective person would have understood the commercial to make a serious offer of a Harrier Jet because there was "absolutely no distinction in the manner" (Pl. Mem. at 13,) in which the items in the commercial were presented. Plaintiff also relies upon a press release highlighting the promotional campaign, issued by defendant, in which "no mention is made by [defendant] of humor, or anything of the sort." (*Id. at 5*.) These arguments suggest merely that the humor of the promotional campaign was tongue in cheek. Humor is not limited to what Justice Cardozo called "the rough and boisterous joke . . . [that] evokes its own guffaws." *Murphy v. Steeplechase Amusement Co., 250 N.Y. 479, 483, 166 N.E. 173, 174 (1929)*. In light of the obvious absurdity of the commercial, the Court rejects plaintiff's argument that the commercial was not clearly in jest…

III. Conclusion

In sum, there are three reasons why plaintiff's demand cannot prevail as a matter of law. First, the commercial was merely an advertisement, not a unilateral offer. Second, the tongue-in-cheek attitude of the commercial would not cause a reasonable person to conclude that a soft drink company would be giving away fighter planes as part of a promotion. Third, there is no writing between the parties sufficient to satisfy the Statute of Frauds.

For the reasons stated above, the Court grants defendant's motion for summary judgment. The Clerk of Court is instructed to close these cases. Any pending motions are moot.

SO ORDERED.

Campbell Soup Co. v. Wentz

United States Court of Appeals for the Third Circuit

November 16, 1948, Argued ; December 23, 1948, Decided

172 F.2d 80; 1948 U.S. App. LEXIS 2000

These are appeals from judgments of the District Court denying equitable relief to the buyer under a contract for the sale of carrots. The defendants in No. 9648 are the contract sellers. The defendant in No. 9649 is the second purchaser of part of the carrots which are the subject matter of the contract.

The transactions which raise the issues may be briefly summarized. On June 21, 1947, Campbell Soup Company (Campbell), a New Jersey corporation, entered into a written contract with George B. Wentz and Harry T. Wentz, who are Pennsylvania farmers, for delivery by the Wentzes to Campbell of all the Chantenay red cored carrots to be grown on fifteen acres of the Wentz farm during the 1947 season. Where the contract was entered into does not appear. The contract provides, however, for delivery of the carrots at the Campbell plant in Camden, New Jersey. The prices specified in the contract ranged from $ 23 to $ 30 per ton according to the time of delivery. The contract price for January, 1948 was $ 30 a ton.

The Wentzes harvested approximately 100 tons of carrots from the fifteen acres covered by the contract. Early in January, 1948, they told a Campbell representative that they would not deliver their carrots at the contract price. The market price at that time was at least $ 90 per ton, and Chantenay red cored carrots were virtually unobtainable. The Wentzes then sold approximately 62 tons of their carrots to the defendant Lojeski, a neighboring farmer. Lojeski resold about 58 tons on the open market, approximately half to Campbell and the balance to other purchasers.

On January 9, 1948, Campbell, suspecting that Lojeski was selling it 'contract carrots,' refused to purchase any more, and instituted these suits against the Wentz brothers and Lojeski to enjoin further sale of the contract carrots to others, and to compel specific performance of the contract.

The trial court denied equitable relief.[1] We agree with the result reached, but on a different ground from that relied upon by the District Court.

The case has been presented by both sides as though Erie Railroad v. Tompkins, 1938, 304 U.S. 64, 58 S.Ct. 817, 82 L.Ed. 1188, 114 A.L.R. 1487, and Klaxon Company v. Stentor Electric Manufacturing Co., Inc., 1941, 313 U.S. 487, 61 S.Ct. 1020, 85 L.Ed. 1477, had never been decided. We are not advised as to the place of the contract, although as we have pointed out in other cases, the Pennsylvania conflict of laws rule, which binds us here, refers matters concerning the validity and extent of obligation of the contract to the place of making.[2] In this instance, however, the absence of data on which to base a rule of reference does not preclude the decision of the case.[3] We have said several

[1] The issue is preserved on appeal by an arrangement under which Campbell received all the carrots held by the Wentzes and Lojeski, paying a stipulated market price of $ 90 per ton, $ 30 to the defendants, and the balance into the registry of the District Court pending the outcome of these appeals.

[2] A. M. Webb & Co. v. Robert P. Miller Co., 3 Cir., 1946, 157 F.2d 865; Griffin v. Metal Products Co., 1919, 264 Pa. 254, 107 A. 713; Restatement, Conflict of Laws § 332 (1934). Cf. Texas Motorcoaches v. A.C.F. Motors Co., 3 Cir., 1946, 154 F.2d 91; Restatement, Conflict of Laws § 358 (1934).

[3] Gray v. Premier Investment Co., D.C.W.D. La., 1943, 51 F.Supp. 944; Texas Co. v. Central Fuel Oil Co., 8 Cir., 1912, 194 Fed. 1.

times in this Circuit that the question of the form of relief is a matter for a federal court to decide.[4] But neither federal decisions nor the law of New Jersey or Pennsylvania as expressed in the Uniform Sales Act[5] differ upon this point. A party may have specific performance of a contract for the sale of chattels if the legal remedy is inadequate. Inadequacy of the legal remedy is necessarily a matter to be determined by an examination of the facts in each particular instance.

We think that on the question of adequacy of the legal remedy the case is one appropriate for specific performance. It was expressly found that at the time of the trial it was 'virtually impossible to obtain Chantenay carrots in the open market.' This Chantenay carrot is one which the plaintiff uses in large quantities, furnishing the seed to the growers with whom it makes contracts. It was not claimed that in nutritive value it is any better than other types of carrots. Its blunt shape makes it easier to handle in processing. And its color and texture differ from other varieties. The color is brighter than other carrots. The trial court found that the plaintiff failed to establish what proportion of its carrots is used for the production of soup stock and what proportion is used as identifiable physical ingredients in its soups. We do not think lack of proof on that point is material. It did appear that the plaintiff uses carrots in fifteen of its twenty-one soups. It also appeared that it uses these Chantenay carrots diced in some of them and that the appearance is uniform. The preservation of uniformity in appearance in a food article marketed throughout the country and sold under the manufacturer's name is a matter of considerable commercial significance and one which is properly considered in determining whether a substitute ingredient is just as good as the original.

The trial court concluded that the plaintiff had failed to establish that the carrots, 'judged by objective standards,' are unique goods. This we think is not a pure fact conclusion like a finding that Chantenay carrots are of uniform color. It is either a conclusion of law or of mixed fact and law and we are bound to exercise our independent judgment upon it. That the test for specific performance is not necessarily 'objective' is shown by the many cases in which equity has given it to enforce contracts for articles- family heirlooms and the like- the value of which was personal to the plaintiff.[6]

Judged by the general standards applicable to determining the adequacy of the legal remedy[7] we think that on this point the case is a proper one for equitable relief. There is considerable authority, old and new, showing liberality in the granting of an equitable remedy.[8] We see no reason why a court should be reluctant to grant specific relief when it can be given without supervision of the court or other time-consuming processes against one who has deliberately broken his agreement. Here the goods of the special type contracted for were unavailable on the open market, the plaintiff had contracted for them long ahead in anticipation of its needs, and had built up a general reputation for its products as part of which reputation uniform appearance was important. We think if this were all that was involved in the case specific performance should have been granted.

The reason that we shall affirm instead of reversing with an order for specific performance is found in the contract itself. We think it is too hard a bargain and too one-sided an agreement to entitle

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[4] Orth v. Transit Investment Corp., 3 Cir., 1942, 132 F.2d 938; Black & Yates v. Mahogany Assn., 3 Cir., 1941, 129 F.2d 227, 148 A.L.R. 841, certiorari denied, 1942, 317 U.S. 672, 63 S.Ct. 76, 87 L.Ed. 539. Cf. Note, 55 Yale L.J. 401 (1946).

[5] Uniform Sales Act, § 68, N.J.S.A. 46:30-74; 69 P.S. § 313.

[6] 5 Williston, Contracts § 1419 n. 6 (Rev. ed. 1937).

[7] Restatement, Contracts § 361 (1932); 5 Williston, Contracts § 1419 (Rev. ed. 1937); 1 Pomeroy, Equity Jurisprudence § 221b (5th ed. 1941).

[8] Note, 152 A.L.R. 4 (1944). Professor Williston has consistently advocated a more liberal use of equitable remedies, especially under the specific performance provision of the Uniform Sales Act. 3 Williston, Sales § 601 (Rev. ed. 1948); 5 Williston, Contracts § 1419 (Rev. ed. 1937).

the plaintiff to relief in a court of conscience. For each individual grower the agreement is made by filling in names and quantity and price on a printed form furnished by the buyer. This form has quite obviously been drawn by skilful draftsmen with the buyer's interests in mind.

Paragraph 2 provides for the manner of delivery. Carrots are to have their stalks cut off and be in clean sanitary bags or other containers approved by Campbell. This paragraph concludes with a statement that Campbell's determination of conformance with specifications shall be conclusive.

The defendants attack this provision as unconscionable. We do not think that it is, standing by itself. We think that the provision is comparable to the promise to perform to the satisfaction of another[9] and that Campbell would be held liable if it refused carrots which did in fact conform to the specifications.[10]

The next paragraph allows Campbell to refuse carrots in excess of twelve tons to the acre. The next contains a covenant by the grower that he will not sell carrots to anyone else except the carrots rejected by Campbell nor will he permit anyone else to grow carrots on his land. Paragraph 10 provides liquidated damages to the extent of $ 50 per acre for any breach by the grower. There is no provision for liquidated or any other damages for breach of contract by Campbell.

The provision of the contract which we think is the hardest is paragraph 9, set out in the margin.[11] It will be noted that Campbell is excused from accepting carrots under certain circumstances. But even under such circumstances the grower, while he cannot say Campbell is liable for failure to take the carrots, is not permitted to sell them elsewhere unless Campbell agrees. This is the kind of provision which the late Francis H. Bohlen would call 'carrying a good joke too far.' What the grower may do with his product under the circumstances set out is not clear. He has covenanted not to store it anywhere except on his own farm and also not to sell to anybody else.

We are not suggesting that the contract is illegal. Nor are we suggesting any excuse for the grower in this case who has deliberately broken an agreement entered into with Campbell. We do think, however, that a party who has offered and succeeded in getting an agreement as tough as this one is, should not come to a chancellor and ask court help in the enforcement of its terms. That equity does not enforce unconscionable bargains is too well established to require elaborate citation.[12]

The plaintiff argues that the provisions of the contract are separable. We agree that they are, but do not think that decisions separating out certain provisions from illegal contracts [**9] are in point here. As already said, we do not suggest that this contract is illegal. All we say is that the sum total of its provisions drives too hard a bargain for a court of conscience to assist.

This disposition of the problem makes unnecessary further discussion of the separate liability of Lojeski, who was not a party to the contract, but who purchased some of the carrots from the Wentzes. The judgments will be affirmed.

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[9] Restatement, Contracts § 265 (1932); 3 Williston, Contracts § 675A (Rev. ed. 1937).

[10] 3 Williston, Contracts § 675A, n. 11 (Rev. ed. 1937).

[11] 'Grower shall not be obligated to deliver any Carrots which he is unable to harvest or deliver, nor shall Campbell be obligated to receive or pay for any Carrots which it is unable to inspect, grade, receive, handle, use or pack at or ship in processed form from its plants in Camden (1) because of any circumstance beyond the control of Grower or Campbell, as the case may be, or (2) because of any labor disturbance, work stoppage, slow-down, or strike involving any of Campbell's employees. Campbell shall not be liable for any delay in receiving Carrots due to any of the above contingencies. During periods when Campbell is unable to receive Grower's Carrots, Grower may with Campbell's written consent, dispose of his Carrots elsewhere. Grower may not, however, sell or otherwise dispose of any Carrots which he is unable to deliver to Campbell.'

[12] 4 Pomeroy, Equity Jurisprudence § 1405a (5th ed. 1941); 5 Williston, Contracts § 1425 (Rev. ed. 1937).

Rich HILL and Enza Hill, on behalf of a class of persons similarly situated, Plaintiffs-Appellees, v.
GATEWAY 2000, INC., Defendant-Appellant.
105 F.3d 1147 (7th Cir. 1997).

EASTERBROOK, Circuit Judge.

A customer picks up the phone, orders a computer, and gives a credit card number. Presently a box arrives, containing the computer and a list of terms, said to govern unless the customer returns the computer within 30 days. Are these terms effective as the parties' contract, or is the contract term-free because the order-taker did not read any terms over the phone and elicit the customer's assent?

One of the terms in the box containing a Gateway 2000 system was an arbitration clause. Rich and Enza Hill, the customers, kept the computer more than 30 days before complaining about its components and performance. They filed suit in federal court arguing, among other things, that the product's shortcomings make Gateway a racketeer (mail and wire fraud are said to be the predicate offenses), leading to treble damages under RICO for the Hills and a class of all other purchasers. Gateway asked the district court to enforce the arbitration clause; the judge refused, writing that " [t]he present record is insufficient to support a finding of a valid arbitration agreement between the parties or that the plaintiffs were given adequate notice of the arbitration clause." Gateway took an immediate appeal, as is its right. 9 U.S.C. § 16(a)(1)(A).

The Hills say that the arbitration clause did not stand out: they concede noticing the statement of terms but deny reading it closely enough to discover the agreement to arbitrate, and they ask us to conclude that they therefore may go to court. Yet an agreement to arbitrate must be enforced " save upon such grounds as exist at law or in equity for the revocation of any contract." 9 U.S.C. § 2. *Doctor's Associates, Inc. v. Casarotto,* 517U.S. 681, 116 S.Ct. 1652, 134 L.Ed.2d 902 (1996), holds that this provision of the Federal Arbitration Act is inconsistent with any requirement that an arbitration clause be prominent. A contract need not be read to be effective; people who accept take the risk that the unread terms may in retrospect prove unwelcome…Terms inside Gateway's box stand or fall together. If they constitute the parties' contract because the Hills had an opportunity to return the computer after reading them, then all must be enforced.

ProCD, Inc. v. Zeidenberg, 86 F.3d 1447 (7th Cir.1996), holds that terms inside a box of software bind consumers who use the software after an opportunity to read the terms and to reject them by returning the product. Likewise, *Carnival Cruise Lines, Inc. v. Shute,* 499 U.S. 585, 111 S.Ct. 1522, 113 L.Ed.2d 622 (1991), enforces a forum-selection clause that was included among three pages of terms attached to a cruise ship ticket. *ProCD* and *Carnival Cruise Lines* exemplify the many commercial transactions in which people pay for products with terms to follow; *ProCD* discusses others. 86 F.3d at 1451-52. The district court concluded in *ProCD* that the contract is formed when the consumer pays for the software; as a result, the court held, only terms known to the consumer at that moment are part of the contract, and provisos inside the box do not count. Although this is one way a contract could be formed, it is not the only way: " A vendor, as master of the offer, may invite acceptance by conduct, and may propose limitations on the kind of conduct that constitutes acceptance. A buyer may accept by performing the acts the vendor proposes to treat as acceptance." *Id.* at 1452. Gateway shipped computers with the same sort of accept-or-return offer ProCD made to users of its software. *ProCD* relied on the Uniform Commercial Code rather than any peculiarities of Wisconsin law; both Illinois and South Dakota, the two states whose law might govern relations between Gateway and the Hills, have adopted the UCC; neither side has pointed us to any atypical doctrines in those states that might be pertinent; *ProCD* therefore applies to this dispute.

Plaintiffs ask us to limit *ProCD* to software, but where's the sense in that? *ProCD* is about the law of contract, not the law of software. Payment preceding the revelation of full terms is common for air transportation, insurance, and many other endeavors. Practical considerations support allowing vendors to enclose the full legal terms with their products. Cashiers cannot be expected to read legal documents to customers before ringing up sales. If the staff at

the other end of the phone for direct-sales operations such as Gateway's had to read the four-page statement of terms before taking the buyer's credit card number, the droning voice would anesthetize rather than enlighten many potential buyers. Others would hang up in a rage over the waste of their time. And oral recitation would not avoid customers' assertions (whether true or feigned) that the clerk did not read term X to them, or that they did not remember or understand it. Writing provides benefits for both sides of commercial transactions. Customers as a group are better off when vendors skip costly and ineffectual steps such as telephonic recitation, and use instead a simple approve-or-return device. Competent adults are bound by such documents, read or unread. For what little it is worth, we add that the box from Gateway was crammed with software. The computer came with an operating system, without which it was useful only as a boat anchor. See *Digital Equipment Corp. v. Uniq Digital Technologies, Inc.*, 73 F.3d 756, 761 (7th Cir.1996). Gateway also included many application programs. So the Hills' effort to limit *ProCD* to software would not avail them factually, even if it were sound legally-which it is not.

For their second sally, the Hills contend that ProCD should be limited to executory contracts (to licenses in particular), and therefore does not apply because both parties' performance of this contract was complete when the box arrived at their home…

Next the Hills insist that *ProCD* is irrelevant because Zeidenberg was a "merchant" and they are not…

At oral argument the Hills propounded still another distinction: the box containing ProCD's software displayed a notice that additional terms were within, while the box containing Gateway's computer did not. The difference is functional, not legal. Consumers browsing the aisles of a store can look at the box, and if they are unwilling to deal with the prospect of additional terms can leave the box alone, avoiding the transactions costs of returning the package after reviewing its contents. Gateway's box, by contrast, is just a shipping carton; it is not on display anywhere. Its function is to protect the product during transit, and the information on its sides is for the use of handlers rather than would-be purchasers.

Perhaps the Hills would have had a better argument if they were first alerted to the bundling of hardware and legal-ware after opening the box and wanted to return the computer in order to avoid disagreeable terms, but were dissuaded by the expense of shipping. What the remedy would be in such a case-could it exceed the shipping charges?-is an interesting question, but one that need not detain us because the Hills knew before they ordered the computer that the carton would include *some* important terms, and they did not seek to discover these in advance. Gateway's ads state that their products come with limited warranties and lifetime support. How limited was the warranty-30 days, with service contingent on shipping the computer back, or five years, with free onsite service? What sort of support was offered? Shoppers have three principal ways to discover these things. First, they can ask the vendor to send a copy before deciding whether to buy. The Magnuson-Moss Warranty Act requires firms to distribute their warranty terms on request, 15 U.S.C. § 2302(b)(1)(A); the Hills do not contend that Gateway would have refused to enclose the remaining terms too. Concealment would be bad for business, scaring some customers away and leading to excess returns from others. Second, shoppers can consult public sources (computer magazines, the Web sites of vendors) that may contain this information. Third, they may inspect the documents after the product's delivery. Like Zeidenberg, the Hills took the third option. By keeping the computer beyond 30 days, the Hills accepted Gateway's offer, including the arbitration clause.

The Hills' remaining arguments, including a contention that the arbitration clause is unenforceable as part of a scheme to defraud, do not require more than a citation to *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 87 S.Ct. 1801, 18 L.Ed.2d 1270 (1967). Whatever may be said pro and con about the cost and efficacy of arbitration (which the Hills disparage) is for Congress and the contracting parties to consider. Claims based on RICO are no less arbitrable than those founded on the contract or the law of torts. ..The decision of the district court is vacated, and this case is remanded with instructions to compel the Hills to submit their dispute to arbitration.

MARC BRAGG v. LINDEN RESEARCH, INC. and PHILIP ROSEDALE[*]

487 F. Supp. 2d 593 (D.C.E.Penn.2007)

EDUARDO C. ROBRENO, J.

This case is about virtual property maintained on a virtual world on the Internet. Plaintiff, March Bragg, Esq., claims an ownership interest in such virtual property. Bragg contends that Defendants, the operators of the virtual world, unlawfully confiscated his virtual property and denied him access to their virtual world. Ultimately at issue in this case are the novel questions of what rights and obligations grow out of the relationship between the owner and creator of a virtual world and its resident-customers. While the property and the world where it is found are "virtual," the dispute is real.

Presently before the Court are Defendants' Motion to Dismiss for Lack of Personal Jurisdiction (doc. no. 2) and Motion to Compel Arbitration (doc. no. 3). For the reasons set forth below, the motions will be denied.

I. BACKGROUND

A. *Second Life*

The defendants in this case, Linden Research Inc. ("Linden") and its Chief Executive Officer, Philip Rosedale, operate a multiplayer role-playing game set in the virtual world known as "Second Life." Participants create avatars to represent themselves, and Second Life is populated by hundreds of thousands of avatars, whose interactions with one another are limited only by the human imagination. According to Plaintiff, many people "are now living large portions of their lives, forming friendships with others, building and acquiring virtual property, forming contracts, substantial business relationships and forming social organizations" in virtual worlds such as Second Life.. Owning property in and having access to this virtual world is, moreover, apparently important to the plaintiff in this case.

B. *Recognition of Property Rights*

In November 2003, Linden announced that it would recognize participants' full intellectual property protection for the digital content they created or otherwise owned in Second Life. As a result, Second Life avatars may now buy, own, and sell virtual goods ranging "from cars to homes to slot machines." Most significantly for this case, avatars may purchase "virtual land," make improvements to that land, exclude other avatars from entering onto the land, rent the land, or sell the land to other avatars for a profit. Assertedly, by recognizing virtual property rights, Linden would distinguish itself from other virtual worlds available on the Internet and thus increase participation in Second Life.

Defendant Rosedale personally joined in efforts to publicize Linden's recognition of rights to virtual property. For example, in 2003, Rosedale stated in a press release made available on Second Life's website that:

> Until now, any content created by users for persistent state worlds, such as Everquest(R) or Star Wars Galaxies TM, has essentially become the property of the company developing and hosting the world. . . . We believe our new policy recognizes the fact that persistent world users are making significant contributions to building these worlds and should be able to both own the content they create and share in the value that is created. The preservation of users' property rights is a necessary step toward the emergence of genuinely real online worlds.

Press Release, Linden Lab, *Linden Lab Preserves Real World Intellectual Property Rights of Users of its Second Life Online Services* (Nov. 14, 2003). After this initial announcement, Rosedale continued to personally hype the ownership of virtual property on Second Life. In an interview in 2004, for example, Rosedale stated: "The idea of land ownership and the ease with which you can own land and do something with it . . . is intoxicating. . . . Land ownership feels important and tangible. It's a real piece of the future." Michael Learmonth, *Virtual Real Estate Boom Draws Real Dollars*, USA Today, June 3, 2004. Rosedale recently gave an extended interview for Inc. magazine, where he appeared on the cover stating, "What you have in Second Life is real and it is yours. It doesn't belong to us. You can make money." Michael Fitzgerald, *How Philip Rosedale Created Second Life*, Inc., Feb. 2007. [6]

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[*] Some citations and footnotes omitted.

Rosedale even created his own avatar and held virtual town hall meetings on Second Life where he made representations about the purchase of virtual land. Bragg "attended" such meetings and relied on the representations that Rosedale made therein.

C. *Plaintiffs' Participation in Second Life*

In 2005, Plaintiff Marc Bragg, Esq., signed up and paid Linden to participate in Second Life. Bragg claims that he was induced into "investing" in virtual land by representations made by Linden and Rosedale in press releases, interviews, and through the Second Life website.. Bragg also paid Linden real money as "tax" on his land. By April 2006, Bragg had not only purchased numerous parcels of land in his Second Life, he had also digitally crafted "fireworks" that he was able to sell to other avatars for a profit. Bragg also acquired other virtual items from other avatars.

The dispute ultimately at issue in this case arose on April 30, 2006, when Bragg acquired a parcel of virtual land named "Taessot" for $ 300. Linden sent Bragg an email advising him that Taessot had been improperly purchased through an "exploit." Linden took Taesot away. It then froze Bragg's account, effectively confiscating all of the virtual property and currency that he maintained on his account with Second Life.

Bragg brought suit against Linden and Rosedale in the Court of Common Pleas of Chester County, Pennsylvania, on October 3, 2006. Linden and Rosedale removed the case to this Court (doc. no. 1) and then, within a week, moved to compel arbitration (doc. no. 3)…

III. MOTION TO COMPEL ARBITRATION

Defendants have also filed a motion to compel arbitration that seeks to dismiss this action and compel Bragg to submit his claims to arbitration according to the Rules of the International Chamber of Commerce ("ICC") in San Francisco.

A. *Relevant Facts*

Before a person is permitted to participate in Second Life, she must accept the Terms of Service of Second Life (the "TOS") by clicking a button indicating acceptance of the TOS. Bragg concedes that he clicked the "accept" button before accessing Second Life. Compl. P 126. Included in the TOS are a California choice of law provision, an arbitration provision, and forum selection clause. Specifically, located in the fourteenth line of the thirteenth paragraph under the heading "GENERAL PROVISIONS," and following provisions regarding the applicability of export and import laws to Second Life, the following language appears:

> Any dispute or claim arising out of or in connection with this Agreement or the performance, breach or termination thereof, shall be finally settled by binding arbitration in San Francisco, California under the Rules of Arbitration of the International Chamber of Commerce by three arbitrators appointed in accordance with said rules. . . . Notwithstanding the foregoing, either party may apply to any court of competent jurisdiction for injunctive relief or enforcement of this arbitration provision without breach of this arbitration provision.

B. *Legal Standards*

1. *Federal law applies*

The Federal Arbitration Act ("FAA") requires that the Court apply federal substantive law here because the arbitration agreement is connected to a transaction involving interstate commerce…

Whether the arbitration agreement is connected to a transaction involving interstate commerce is a factual determination that must be made by the Court. *State Farm, 233 F.3d at 713 n.1*. Here, Bragg is a Pennsylvania resident. Linden is a Delaware corporation headquartered in California. Rosedale is a California resident. Bragg entered into the TOS and purchased virtual land through the Internet on Second Life as a result of representations made on the national media. The arbitration agreement is clearly connected to interstate commerce, and the Court will apply the federal substantive law that has emerged from interpretation of the FAA.

2. *The Legal Standard Under the FAA*

Under the FAA, on the motion of a party, a court must stay proceedings and order the parties to arbitrate the dispute if the court finds that the parties have agreed in writing to do so. *9 U.S.C. §§ 3*, *4*, *6*. A party seeking to compel arbitration must show (1) that a valid agreement to arbitrate exists between the parties and (2) that the specific dispute falls within the scope of the agreement.

In determining whether a valid agreement to arbitrate exists between the parties, the Third Circuit has instructed district courts to give the party opposing arbitration "the benefit of all reasonable doubts and inferences that may arise," …While there is a presumption that a particular dispute is within the *scope* of an arbitration agreement, there is no such "presumption" or "policy" that favors the *existence* of a valid agreement to arbitrate.

C. *Application*

1. *Unconscionabilty of the Arbitration Agreement*

Bragg resists enforcement of the TOS's arbitration provision on the basis that it is "both procedurally and substantively unconscionable and is itself evidence of defendants' scheme to deprive Plaintiff (and others) of both their money and their day in court."

Section 2 of the FAA provides that written arbitration agreements "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract." *9 U.S.C. § 2*. Thus, "generally applicable contract defenses, such as fraud, duress, or unconscionability, may be applied to invalidate arbitration agreements without contravening *§ 2*." When determining whether such defenses might apply to any purported agreement to arbitrate the dispute in question, "courts generally . . . should apply ordinary state-law principles that govern the formation of contracts." Thus, the Court will apply California state law to determine whether the arbitration provision is unconscionable.

Under California law, unconscionability has both procedural and substantive components. The procedural component can be satisfied by showing (1) oppression through the existence of unequal bargaining positions or (2) surprise through hidden terms common in the context of adhesion contracts. The substantive component can be satisfied by showing overly harsh or one-sided results that "shock the conscience." The two elements operate on a sliding scale such that the more significant one is, the less significant the other need be. However, a claim of unconscionability cannot be determined merely by examining the face of the contract; there must be an inquiry into the circumstances under which the contract was executed, and the contract's purpose, and effect.

(a) *Procedural Unconscionability*

A contract or clause is procedurally unconscionable if it is a contract of adhesion. A contract of adhesion, in turn, is a "standardized contract, which, imposed and drafted by the party of superior bargaining strength, relegates to the subscribing party only the opportunity to adhere to the contract or reject it." Under California law, "the critical factor in procedural unconscionability analysis is the manner in which the contract or the disputed clause was presented and negotiated."…

The TOS are a contract of adhesion. Linden presents the TOS on a take-it-or-leave-it basis. A potential participant can either click "assent" to the TOS, and then gain entrance to Second Life's virtual world, or refuse assent and be denied access. Linden also clearly has superior bargaining strength over Bragg. Although Bragg is an experienced attorney, who believes he is expert enough to comment on numerous industry standards and the "rights" or participants in virtual worlds, he was never presented with an opportunity to use his experience and lawyering skills to negotiate terms different from the TOS that Linden offered.

Moreover, there was no "reasonably available market alternatives [to defeat] a claim of adhesiveness." Although it is not the only virtual world on the Internet, Second Life was the first and only virtual world to specifically grant its participants property rights in virtual land.

The procedural element of unconscionability also "focuses on . . . surprise." In determining whether surprise exists, California courts focus not on the plaintiff's subjective reading of the contract, but rather, more objectively, on "the extent to which the supposedly agreed-upon terms of the bargain are hidden in the prolix printed form drafted by the party seeking to enforce the disputed terms." In *Gutierrez*, the court found such surprise where an arbitration clause was "particularly inconspicuous, printed in eight-point typeface on the opposite side of the signature page of the lease." *Id.*

Here, although the TOS are ubiquitous throughout Second Life, Linden buried the TOS's arbitration provision in a lengthy paragraph under the benign heading "GENERAL PROVISIONS."…Linden also failed to make available the costs and rules of arbitration in the ICC by either setting them forth in the TOS or by providing a hyper-link to another page or website where they are available. Bragg Decl. P 20.

Comb is most instructive.[1] In that case, the plaintiffs challenged an arbitration provision that was part of an agreement to which they had assented, in circumstances similar to this case, by clicking their assent on an online application page. The defendant, PayPal, was a large company with millions of individual online customers. The plaintiffs, with one exception, were all individual customers of PayPal. Given the small amount of the average transaction with PayPal, the fact that most PayPal customers were private individuals, and that there was a "dispute as to whether PayPal's competitors offer their services without requiring customers to enter into arbitration agreements," the court concluded that the user agreement at issue "satisfie[d] the criteria for procedural unconscionability under California law." Here, as in *Comb*, procedural unconscionability is satisfied.

(b) *Substantive Unconscionability*

Even if an agreement is procedurally unconscionable, "it may nonetheless be enforceable if the substantive terms are reasonable." Here, a number of the TOS's elements lead the Court to conclude that Bragg has demonstrated that the TOS are substantively unconscionable.

(i) *Mutuality*

Under California law, substantive unconscionability has been found where an arbitration provision forces the weaker party to arbitrate claims but permits a choice of forums for the stronger party. In other words, the arbitration remedy must contain a "modicum of bilaterality." This principle has been extended to arbitration provisions that allow the stronger party a range of remedies before arbitrating a dispute, such as self-help, while relegating to the weaker party the sole remedy of arbitration.

In *Comb*, for example, the court found a lack of mutuality where the user agreement allowed PayPal "at its sole discretion" to restrict accounts, withhold funds, undertake its own investigation of a customer's financial records, close accounts, and procure ownership of all funds in dispute unless and until the customer is "later determined to be entitled to the funds in dispute." Also significant was the fact that the user agreement was "subject to change by PayPal without prior notice (unless prior notice is required by law), by posting of the revised Agreement on the PayPal website." *Id.*

Here, the TOS contain many of the same elements that made the PayPal user agreement substantively unconscionable for lack of mutuality. The TOS proclaim that "Linden has the right at any time for any reason or no reason to suspend or terminate your Account, terminate this Agreement, and/or refuse any and all current or future use of the Service without notice or liability to you." Whether or not a customer has breached the Agreement is "determined in Linden's sole discretion." Linden also reserves the right to return no money at all based on mere "suspicions of fraud" or other violations of law. Finally, the TOS state that "Linden may amend this Agreement . . . at any time in its sole discretion by posting the amended Agreement [on its website]."

In effect, the TOS provide Linden with a variety of one-sided remedies to resolve disputes, while forcing its customers to arbitrate any disputes with Linden. This is precisely what occurred here. When a dispute arose, Linden exercised its option to use self-help by freezing Bragg's account, retaining funds that Linden alone determined were subject to dispute, and then telling Bragg that he could resolve the dispute by initiating a costly arbitration process. The TOS expressly authorized Linden to engage in such unilateral conduct. As in *Comb*, "[f]or all practical purposes, a customer may resolve disputes only after [Linden] has had control of the disputed funds for an indefinite period of time," and may only resolve those disputes by initiating arbitration..

Linden's right to modify the arbitration clause is also significant. "The effect of [Linden's] unilateral right to modify the arbitration clause is that it could . . . craft precisely the sort of asymmetrical arbitration agreement that is prohibited under California law as unconscionable. This lack of mutuality supports a finding of substantive unconscionability.

(ii) *Costs of Arbitration and Fee-Sharing*

Bragg claims that the cost of an individual arbitration under the TOS is likely to exceed $ 13,540, with an estimated initiation cost of at least $ 10,000. Pl.'s Reply at 5-6. He has also submitted a Declaration of Personal Financial Infor-

[1] Comb v. Paypal, Inc., 218 F. Supp. 2d 1165 (N.D. Cal. 2002).

mation stating that such arbitration would be cost-prohibitive for him (doc. no. 41). Linden disputes Bragg's calculations, estimating that the costs associated with arbitration would total $ 7,500, with Bragg advancing $ 3,750 at the outset of arbitration.

At oral argument, the parties were unable to resolve this dispute, even after referencing numerous provisions and charts contained within the ICC Rules. The Court's own calculations, however, indicate that the costs of arbitration, excluding arbitration, would total $ 17,250. With a recovery of $ 75,000,[2] the ICC's administrative expenses would be $ 2,625 (3.5% of $ 75,000). *See* ICC Rules at 28. In addition, arbitrator's fees could be set between 2.0% ($ 1,500) and 11.0% ($ 8,250) of the amount at issue per arbitrator. If the ICC set the arbitrator's fees at the mid-point of this range, the arbitrator's fees would be $ 4,875 per arbitrator. Here, however, the TOS requires that three arbitrators be used to resolve a dispute. TOS P 13. Thus, the Court estimates the costs of arbitration with the ICC to be $ 17,250 ($ 2,625 + (3 x $ 4,875)), although they could reach as high as $ 27,375 ($ 2,625 + (3 x $ 8,250)).[3]

These costs might not, on their own, support a finding of substantive unconscionability. However, the ICC Rules also provide that the costs and fees must be shared among the parties, and an estimate of those costs and fees must be advanced at the initiation of arbitration. California law has often been applied to declare arbitration fee-sharing schemes unenforceable. *See Ting v. AT&T, 319 F.3d 1126, 1151 (9th Cir. 2003)*. Such schemes are unconscionable where they "impose[] on some consumers costs greater than those a complainant would bear if he or she would file the same complaint in court." In *Ting*, for example, the Ninth Circuit held that a scheme requiring AT&T customers to split arbitration costs with AT&T rendered an arbitration provision unconscionable.

Here, even taking Defendants characterization of the fees to be accurate, the total estimate of costs and fees would be $ 7,500, which would result in Bragg having to advance $ 3,750 at the outset of arbitration. *See* Dfts.' Reply at 11. The court's own estimates place the amount that Bragg would likely have to advance at $ 8,625, but they could reach as high as $ 13,687.50. Any of these figures are significantly greater than the costs that Bragg bears by filing his action in a state or federal court. Accordingly, the arbitration costs and fee-splitting scheme together also support a finding of unconscionability.

(iii) *Venue*

The TOS also require that any arbitration take place in San Francisco, California. TOS P 13. In *Comb*, the Court found that a similar forum selection clause supported a finding of substantive unconscionability, because the place in which arbitration was to occur was unreasonable, taking into account "the respective circumstances of the parties." As in *Comb*, the record in this case shows that Linden serves millions of customers across the United States and that the average transaction through or with Second Life involves a relatively small amount. In such circumstances, California law dictates that it is not "reasonable for individual consumers from throughout the country to travel to one locale to arbitrate claims involving such minimal sums." Indeed, "[l]imiting venue to [Linden's] backyard appears to be yet one more means by which the arbitration clause serves to shield [Linden] from liability instead of providing a neutral forum in which to arbitrate disputes."

(iv) *Confidentiality Provision*

Arbitration before the ICC, pursuant to the TOS, must be kept confidential pursuant to the ICC rules. Applying California law to an arbitration provision, the Ninth Circuit held that such confidentiality supports a finding that an arbitration clause was substantively unconscionable. The Ninth Circuit reasoned that if the company succeeds in imposing a gag order on arbitration proceedings, it places itself in a far superior legal posture by ensuring that none of its potential opponents have access to precedent while, at the same time, the company accumulates a wealth of knowledge on how to negotiate the terms of its own unilaterally crafted contract. The unavailability of arbitral decisions could also prevent potential plaintiffs from obtaining the information needed to build a case of intentional misconduct against a company. *See id.*

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[2] The Court's calculations are based on its finding that $ 75,000 is at issue, the minimum necessary to satisfy the requirements of diversity jurisdiction in this case. After a hearing on Bragg's motion to remand this case back to state court, the Court found that this jurisdictional threshold had been met.

[3] At oral argument, Bragg asserted repeatedly that the schedule of arbitrator's fees in the ICC Rules represents the fee "per arbitrator," which would have to be tripled in this case as the TOS provides for three arbitrators. *See* Tran. of 2/5/07 Hrg. at pp. 68, 74. Defendants never refuted this point.

This does not mean that confidentiality provisions in an arbitration scheme or agreement are, in every instance, per se unconscionable under California law. Here, however, taken together with other provisions of the TOS, the confidentiality provision gives rise for concern of the conscionability of the arbitration clause.

Thus, the confidentiality of the arbitration scheme that Linden imposed also supports a finding that the arbitration clause is unconscionable.

(v) *Legitimate Business Realities*

Under California law, a contract may provide a "margin of safety" that provides the party with superior bargaining strength protection for which it has a legitimate commercial need. "However, unless the 'business realities' that create the special need for such an advantage are explained in the contract itself, . . . it must be factually established." When a contract is alleged to be unconscionable, "the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose, and effect to aid the court in making the determination." The statutory scheme reflects "legislative recognition that a claim of unconscionability often cannot be determined merely by examining the face of the contract, but will require inquiry into its setting, purpose, and effect."

Here, neither in its briefing nor at oral argument did Linden even attempt to offer evidence that "business realities" justify the one-sidedness of the dispute resolution scheme that the TOS constructs in Linden's favor.

(c) *Conclusion*

When a dispute arises in Second Life, Linden is not obligated to initiate arbitration. Rather, the TOS expressly allow Linden, at its "sole discretion" and based on mere "suspicion," to unilaterally freeze a participant's account, refuse access to the virtual and real currency contained within that account, and then confiscate the participant's virtual property and real estate. A participant wishing to resolve any dispute, on the other hand, after having forfeited its interest in Second Life, must then initiate arbitration in Linden's place of business. To initiate arbitration involves advancing fees to pay for no less than three arbitrators at a cost far greater than would be involved in litigating in the state or federal court system. Moreover, under these circumstances, the confidentiality of the proceedings helps ensure that arbitration itself is fought on an uneven field by ensuring that, through the accumulation of experience, Linden becomes an expert in litigating the terms of the TOS, while plaintiffs remain novices without the benefit of learning from past precedent.

Taken together, the lack of mutuality, the costs of arbitration, the forum selection clause, and the confidentiality provision that Linden unilaterally imposes through the TOS demonstrate that the arbitration clause is not designed to provide Second Life participants an effective means of resolving disputes with Linden. Rather, it is a one-sided means which tilts unfairly, in almost all situations, in Linden's favor. As in *Comb*, through the use of an arbitration clause, Linden "appears to be attempting to insulate itself contractually from any meaningful challenge to its alleged practices."

The Court notes that the concerns with procedural unconscionability are somewhat mitigated by Bragg's being an experienced attorney. However, "because the unilateral modification clause renders the arbitration provision severely one-sided in the substantive dimension, even moderate procedural unconscionability renders the arbitration agreement unenforceable."

Finding that the arbitration clause is procedurally and substantively unconscionable, the Court will refuse to enforce it.

2. *"Blueliningˮ the Arbitration Agreement*

Alternatively, Linden has offered to ameliorate the one-sidedness of the TOS's arbitration provision by suggesting that Linden could waive the requirements for three arbitrators, post the initial fees of arbitration, and agree to arbitrate in Philadelphia instead of San Francisco.

California law allows a court to "blueline" an arbitration agreement to remove an element that renders it substantively unconscionable. However, a court is not obligated to blueline when an "arbitration provision is so permeated by substantive unconscionability that it cannot be cured by severance or any other action short of rewriting the contract." Where an arbitration provision has "multiple defects that indicate a systematic effort to impose arbitration on [the plaintiff], not simply as an alternative to litigation, but as an inferior forum that works to [the defendant's] advantage," and there simply is "no single provision [the court] can strike or restrict in order to remove the unconscionable taint from the agreement," the court can simply refuse to enforce the arbitration provision. .

The arbitration clause before the Court is simply not one where a single term may be stricken to render the agreement conscionable. "The unilateral modification 'pervade[s]' and 'taint[s] with illegality' the entire agreement to arbitrate, [and] severance of terms within the arbitration clause would not cure the problem. Bluelining in this case will require the redrafting of the agreement.

The Court declines to rewrite the agreement, at Linden's request, to save an unconscionable arbitration provision which Linden itself drafted and now seeks to enforce. Rather than provide a reasonable alternative for dispute resolution, this agreement compels a one-sided resolution of disputes between the parties.

IV. CONCLUSION

For the reasons set forth above, the Court will deny Rosedale's motion to dismiss for lack of jurisdiction. The Court will also deny Defendants' motion to compel arbitration. An appropriate order follows.

Otis F. Wood, Appellant, v. Lucy, Lady Duff-Gordon, Respondent

Court of Appeals of New York, 222 N.Y. 88; 118 N.E. 214

November 14, 1917, Argued, December 4, 1917, Decided

Wood v. Duff-Gordon, 177 App. Div. 624, reversed.

Cardozo, J. Cuddeback, McLaughlin and Andrews, JJ., concur; Hiscock, Ch. J., Chase and Crane, JJ., dissent.

The defendant styles herself "a creator of fashions." Her favor helps a sale. Manufacturers of dresses, millinery and like articles are glad to pay for a certificate of her approval. The things which she designs, fabrics, parasols and what not, have a new value in the public mind when issued in her name. She employed the plaintiff to help her to turn this vogue into money. He was to have the exclusive right, subject always to her approval, to place her indorsements on the designs of others. He was also to have the exclusive right to place her own designs on sale, or to license others to market them. In return, she was to have one-half of "all profits and revenues" derived from any contracts he might make. The exclusive right was to last at least one year from April 1, 1915, and thereafter from year to year unless terminated by notice of ninety days. The plaintiff says that he kept the contract on his part, and that the defendant broke it. She placed her indorsement on fabrics, dresses and millinery without his knowledge, and withheld the profits. He sues her for the damages, and the case comes here on demurrer.

The agreement of employment is signed by both parties. It has a wealth of recitals. The defendant insists, however, that it lacks the elements of a contract. She says that the plaintiff does not bind himself to anything. It is true that he does not promise in so many words that he will use reasonable efforts to place the defendant's indorsements and market her designs. We think, however, that such a promise is fairly to be implied. The law has outgrown its primitive stage of formalism when the precise word was the sovereign talisman, and every slip was fatal. It takes a broader view to-day. A promise may be lacking, and yet the whole writing may be "instinct with an obligation," imperfectly expressed (Scott, J., in McCall Co. v. Wright, 133 App. Div. 62; Moran v. Standard Oil Co., 211 N. Y. 187, 198). If that is so, there is a contract.

The implication of a promise here finds support in many circumstances. The defendant gave an exclusive privilege. She was to have no right for at least a year to place her own indorsements or market her own designs except through the agency of the plaintiff. The acceptance of the exclusive agency was an assumption of its duties (Phoenix Hermetic Co. v. Filtrine Mfg. Co., 164 App. Div. 424; W. G. Taylor Co. v. Bannerman, 120 Wis. 189; Mueller v. Bethesda Mineral Spring Co., 88 Mich. 390). We are not to suppose that one party was to be placed at the mercy of the other (Hearn v. Stevens & Bro., 111 App. Div. 101, 106; Russell v. Allerton, 108 N. Y. 288). Many other terms of the agreement point the same way. We are told at the outset by way of recital that "the said Otis F. Wood possesses a business organization

adapted to the placing of such indorsements as the said Lucy, Lady Duff-Gordon has approved." The implication is that the plaintiff's business organization will be used for the purpose for which it is adapted. But the terms of the defendant's compensation are even more significant. Her sole compensation for the grant of an exclusive agency is to be one-half of all the profits resulting from the plaintiff's efforts. Unless he gave his efforts, she could never get anything. Without an implied promise, the transaction cannot have such business "efficacy as both parties must have intended that at all events it should have" (Bowen, L. J., in The Moorcock, 14 P. D. 64, 68). But the contract does not stop there. The plaintiff goes on to promise that he will account monthly for all moneys received by him, and that he will take out all such patents and copyrights and trademarks as may in his judgment be necessary to protect the rights and articles affected by the agreement. It is true, of course, as the Appellate Division has said, that if he was under no duty to try to market designs or to place certificates of indorsement, his promise to account for profits or take out copyrights would be valueless. But in determining the intention of the parties, the promise has a value. It helps to enforce the conclusion that the plaintiff had some duties. His promise to pay the defendant one-half of the profits and revenues resulting from the exclusive agency and to render accounts monthly, was a promise to use reasonable efforts to bring profits and revenues into existence. For this conclusion, the authorities are ample…

The judgment of the Appellate Division should be reversed, and the order of the Special Term affirmed, with costs in the Appellate Division and in this court.

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CAUSA AND CONSIDERATION IN THE LAW OF CONTRACTS

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Although the common law is the general basis of the law of this country and of the law of the British Empire, and has therefore a claim to the principal interest and attention of the Anglo-American lawyer, he cannot afford wholly to neglect the study of the civil law. Not only are the commercial relations with foreign countries increasing from year to year, but a considerable portion of the territory of the United States and its possessions and of the British Empire are governed wholly or in part by the doctrines of the civil law. One of the most fundamental differences between the common law and the civil law which is of special importance from the standpoint of business is presented by the question of *causa* and consideration in the law of contracts.

In Louisiana,[1] in the Canal Zone,[2] in Porto Rico,[3] in the Philippine Islands[4] and in certain parts of the British Empire a contract is valid if it has a sufficient *causa*. The meaning of the term *causa* and its relation to the Anglo-American doctrine of consideration has thus been mooted a great deal in the courts—particularly in those of South Africa. Through the influence of Chief Justice de Villiers of the Supreme Court of the colony of the Cape of Good Hope the doctrine became finally established in that colony that the two requirements were in

[1] Civil Code, Arts. 1899-1900.
[2] Civil Code, Art. 1524.
[3] Civil Code, secs. 1228, 1241.
[4] Civil Code, Arts. 1261, 1274.

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doctrine of "presupposition" (*causa*), which was applicable to all juristic acts. According to him any declaration of will could be avoided in Roman law by means of an *exceptio* and *actio* if the presupposition (*causa*) under which such declaration was apparently made, did not exist. In order to be legally effective, the presupposition of a declaration of will must, however, as regards transactions *inter vivos,* be recognizable by the other party.[46] Most of the writers are satisfied, however, that such a general doctrine is not supported by the Roman law texts.[47] Referring to this doctrine Regelsberger adds the following criticism:[48]

"It must be rejected all the more readily because it contains a danger for the security of legal transactions. The supporters of the doctrine have not succeeded in assigning definite limits to the notion of presupposition so far as it is of legal consequence. Under the wide mantle of presupposition it is possible to introduce as causes for annulment all the motives which may produce the intention to enter into a legal transaction . . . It will be found upon closer examination that the desired object can be attained in some other way—frequently in proving the existence of an implied condition, and in case of testamentary dispositions also in proving a mistake in motive."

From what precedes it is apparent that the word *causa* in its application to the law of contracts had in Roman law proper a number of different meanings. No general theory can be deduced from the Roman texts. The following words from Bry summarize as accurately as is possible the Roman law of *causa.* He says:

"The Romans had no theory of *causa,* nor did they consider it an essential condition for the validity of contracts, but they have often applied the principles of *causa.*"[49]

II

Let us turn our attention now to the development of the modern notion of *causa.*

The abandonment of the Roman theory concerning nude pacts came only through a slow process of development. Seuffert[50] has traced the story of this development. From his account it appears that the new doctrine did not become the prevailing view until the seventeenth century,[51] although it was recognized before that time by eminent writers. It was finally established in the eighteenth century.[52] The change came

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[46] Windscheid, *Pendekten,* sec. 98.
[47] For the literature see *ibid.,* sec. 98, note; 1 Regelsberger, *Pandekten,* 606, note.
[48] Regelsberger, *op. cit.,* 607.
[49] Bry, *Principes de droit romain* (5th ed.) 502.
[50] Seuffert, *Zur Geschichte der obligatorischen Verträge,* 1881.
[51] *Ibid.,* 130.
[52] *Ibid.,* 138.

HeinOnline -- 28 Yale L.J. 630 1918-1919

about in part through the influence of the canon law,[53] which regarded the breach of a promise as a lie and therefore as a sin, the penalty for which was excommunication. The natural law jurists also contributed largely to the establishment of the new doctrine.[54] They taught that the enforceable quality of all agreements was demanded by natural law and that the non-enforceability of pacts was a specific Roman doctrine which was opposed to natural law. The idea arose in the seventeenth century[55] that the enforceability of all formal contracts was connected with the old Germanic law because of the high regard in which they held the duty of keeping faith, but it has been shown since[56] that the Germanic law recognized only formal and *real,* and not consensual contracts.

Notwithstanding the change of view just outlined the jurists continued to use the phraseology of the Roman law. This fact makes it particularly difficult to trace the origin and development of the modern doctrine of *causa.* For example: Ulrich Zasius,[57] the greatest German jurist of the sixteenth century, still subscribed to the rule that nude pacts are unenforceable by action, but he attached a new meaning to the term, connecting it with the *condictio sine causa* of the Roman law. Jurists in other countries appear to have done the same thing.[58] It is interesting to note that just as the formalistic requirements of the Roman law were giving way to more liberal doctrines, the existence of a *causa* was being insisted upon as a condition precedent to the creation of obligations. In Grotius[59] we find the following language:

"It was the rule and practice (amongst the Germans) that all promises made for any *reasonable cause* (*redelyke oorzaak*) gave a right both of action and of exception." "By reasonable cause is meant whenever the promise (*toezegging of belofte*) is made by way of gift, or is auxiliary to any other transaction, whether it be made at the same time as such transaction or afterwards."

And Huber[60] states laconically in 1699:

"All promises must have a cause (*oorzaak*), and without it can have no effect."

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[53] *Liber Extra,* I, 35, 143; Seuffert, *op. cit.,* 4.

[54] Seuffert, *op. cit.,* 130–131, 137.

[55] *Ibid.,* 130.

[56] Sohm, *Das Recht der Eheschliessung,* 1875, 226 ff.; Stobbe, *Reurecht und Vertragsschluss nach älterem deutschen Recht,* 13 *Zeitschrift für Rechtsgeschichte,* 209 ff.

[57] Zasius, *Digestum Vetus,* XII, 1, 41; cited by Seuffert, *op. cit.,* 97.

[58] Seuffert, *op. cit.,* 97.

[59] Grotius, *Inleiding tot de hollandsche Rechtsgeleerdheid,* Bk. III, part 1, sec. 52. (Maasdorp, *op. cit.,* 39.)

[60] Huber, *Hedensdaegse Rechtsgeleertheyt,* Bk. III, ch. 21, secs. 6, 7, cited by Maasdorp, *op. cit.,* 40.

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III

The statement is sometimes made that *causa* is perhaps the germ of the English doctrine of consideration.[86] Salmond[87] has attempted to show that our doctrine of consideration was a modification of the Roman *causa* which was adopted by equity and was then borrowed by the common law courts. It is now established,[88] however, that the doctrine is of common law growth and remained uninfluenced by the principles of Roman or continental law. All that was borrowed from the Roman law was the phrase *"ex nudo pacto non oritur actio,"* which came to denote in English law something quite different from what it did at Rome.[89] It was applied originally to those agreements on which an action of debt could not be brought for want of a *quid pro quo,* and later when the action of assumpsit was developed it designated those agreements which were unenforceable because they lacked consideration.

The characteristic features of the modern doctrine of consideration are the following: 1. An agreement which is not contained in a sealed instrument is inoperative unless it is supported by a consideration. 2. According to the traditional statement consideration may consist either in some benefit to the promisor or in some detriment to the promisee.[90] A moral obligation is not sufficient. 3. Consideration is a fact which operates as one of the conventional causes or inducements of a promise. This statement does not cover acts in subsequent reliance upon a promise unless they were requested as the expected and agreed return. 4. Adequacy of consideration is not required. The value of the act or forbearance may be entirely out of proportion to the value of the promise of the other party.

Although the term "consideration" came in the course of time to mean something quite distinct from *causa,* they were used interchangeably over a considerable period of time in the English law. In *Calthorpe's Case*[91] consideration is still defined as a "cause or meritorious occasion, requiring a mutual recompense, in fact or in law."

That agreements in order to be enforceable in the English law must be either under seal or be supported by a valuable consideration was not definitely settled until the end of the eighteenth century. In *Pillans*

[86] Morice, *op. cit.,* 78.

[87] Salmond (1887) 3 L. QUART. REV. 166, 178; *Essays on Jurisprudence and Legal History,* no. 4.

[88] Ames, *Lectures on Legal History,* 129, 147-148; Wald's Pollock, *Contracts* (ed. Williston) 191. See also Hare, *Contracts,* chs. 7 and 8; Holmes, *Common Law,* 253, 254; 3 Holdsworth, *History of English Law,* 319.

[89] Wald's Pollock, *Contracts* (ed. Williston) 192, note. *Causa* in the sense of "clothing" or "vesture" of the agreement was adopted by the early English writers. Maitland, *Bracton & Azo,* 143; Bracton, 99a; Britton, 1, 156.

[90] *Currie v. Misa* (1875) L. R. 10 Exch. 163.

[91] (1574, K. B.) 3 Dyer, 336b.

HeinOnline -- 28 Yale L.J. 636 1918-1919

v. Van Mierop,[92] decided in 1765, Lord Mansfield and the other judges held that a bill of exchange was valid without a consideration according to the law merchant. Lord Mansfield added, however:

"I take it, that the ancient notion about the want of consideration was for the sake of *evidence* only; for when it is reduced into writing, as in covenants, specialties, bonds, etc., there was no objection to the want of consideration. And the statute of frauds proceeded upon the same principle."

In Lord Mansfield's opinion, therefore, any agreement required by law to be in writing could be valid without a consideration if it satisfied that requirement. The House of Lords did not accept this view, however, but in *Rann v. Hughes,*[93] a case involving the statute of frauds, held that the writing was not a substitute for consideration in English law.

"It is undoubtedly true," says the learned court, "that every man is by the law of nature bound to fulfil his engagements. It is equally true that the law of this country supplies no means, nor affords any remedy, to compel the performance of an agreement made without sufficient consideration; such agreement is *nudum pactum ex quo non oritur actio;* and whatsoever may be the sense of this maxim in the civil law, it is in the last-mentioned sense only that it is to be understood in our law. . . . All contracts are by the law of England distinguished into agreements by specialty, and agreements by parol; nor is there any such third class as some of the counsel have endeavored to maintain, as contracts in writing. If they be merely written and not specialties, they are parol, and a consideration must be proved."[94]

From what precedes it is apparent that the distinction in English law between agreements based upon consideration and contracts without a consideration does not correspond to the Roman division of contracts and enforceable pacts on the one hand and nude pacts on the other. Not all agreements based upon a sufficient consideration within the meaning of the English law would fall within the recognized classes of contracts or vested pacts in Roman law.[95] An agreement without consideration in the English sense, on the other hand, would be enforceable in Roman law if it was a wholly gratuitous commission (*mandatum*)[96] or a *constitutum*[97] or an agreement to make a gift (*donatio*) within the limits fixed.[98]

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[92] (1765, K. B.) 3 Burr. 1663.

[93] (1778, K. B.) 7 T. R. 350, note. According to the theory of the early French law a writing dispensed with the need of a *causa.* Brissaud, *History of French Private Law,* 516, note.

[94] (1778, K. B.) 7 T. R. 350, note.

[95] See, *supra,* pp. 623–4.

[96] Sohm, *op. cit.,* 407.

[97] *Ibid.,* 416.

[98] *Ibid.,* 212.

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Civil Law Contracts

Jul 01, 2012 QuickCounsel

By Christopher Meldrum, ACC

Overview

In the wake of globalization and the growth of the international marketplace, in-house lawyers increasingly find themselves advising their clients on contracts governed by foreign law. Often these legal systems will differ not only on the substance of their legislation, but in their approaches to the formation, execution, breach, and compensation of contracts. A misunderstanding of the basic contract principles of these systems or an assumption that contract methods and forms can just be exported from jurisdiction to jurisdiction can result in costly consequences for corporations. Accordingly, it has become increasingly important for corporate counsel to have at least a tangential familiarity with the approach to contracts used by the foreign jurisdictions in which his client wishes to operate. This QuickCounsel highlights some of the key differences in contract law between civil law and common law legal systems.

Back to top

Classification of Contracts

The common law approach to contracts is primarily concerned with predicting the impact and potential binding legal consequences of a party's promises. Essentially, it is not so important what the contract is for or how it structured, but whether the promise of performance that it is based upon is enforceable. This is not the case with civil law, which places a much higher importance upon the classification of its legal principles. Under civil law, every concept must fit into distinct legal categories that define the principle's relationship to other legal precepts. This classification system makes these principles easy to identify and record in the respective nation's contract law. Accordingly, civil law contracts are divided in to several different categories. The four most important classifications for common law lawyers to understand are the bilateral, unilateral, onerous, and gratuitous contracts.

Bilateral and Unilateral Contracts

Although the names are similar to those most common law lawyers encounter in a first year contracts course, civil law unilateral and bilateral contracts are very different. Where the common law focuses on the irrevocable *promises* of the contracting parties, the civil law instead focuses on the parties' *obligations* to each other. For example, under a civil law bilateral contract, such as a lease, one party is obliged to provide rent while the other party is obliged to provide the use and enjoyment of the property for a period of time. Similarly, under a civil law unilateral contract, such as a donation or *inter vivos* gift, only one party is obliged to provide the money or service, without a corresponding expectation of performance. This distinction between the systems may create required contractual obligations for a party under the civil law system (e.g. such as paying donative gift) that would not otherwise exist under the common law.

Onerous and Gratuitous Promises

Another civil law classification relates to the advantage each party expects to receive from the agreement. A contract, such as a sale of goods, in which both parties expect to receive an advantage in exchange for the service or item they provide, is considered onerous. A contract where one party provides an advantage without receiving anything in return, such as a donation, is a gratuitous contract. This is an important distinction. Under the common law only onerous promises are enforceable, since gratuitous promises lack consideration. However, under the civil law, where a gratuitous promise can be enforced, it would be entirely possible for a party to be obligated to deliver on the promise of gift or action.

Back to top

Creation of a Contractual Agreement

One of the principle divergences between the common law and civil law is in their approach to contract formation. The common law seeks to establish at what point in time a promise was made and when that promise begins to have legal implications. In order to conduct this analysis, the common law focuses on three basic principles: Offer, Acceptance, and Consideration. In addition to the common law elements, civil law focuses on several elements necessary to demonstrate that the agreement was the result of an exercise of the parties' free will.

The first of these elements that a court will examine is consent. Like a common law jurisdiction, civil law courts will look for evidence of mistake, adhesion, duress, or fraud to determine whether the parties freely consented to the agreement. In conducting this examination, they will analyze the respective offer and acceptance of the parties. This method has certain similarities to the common law approach, such as the requirement that the offer have the real intent to contract and that acceptance conform to the contract terms. However, civil law contains many nuances that substantially affect contract formation. For instance, many civil law jurisdictions (e.g. Germany) only recognize acceptance when the offeror knows or can reasonably learn of it. In the common law countries, like the U.S., it is usually effective upon the offeree's dispatch of the acceptance.

The second element that must be present in civil law contracts is capacity. Like common law, civil law recognizes classes of individuals incapable of entering into a valid contract. These individuals, however, cannot under pretext of incapacity impeach their own contracts, except in the cases provided for by the law.

In addition to capacity, civil law contracts also require the presence of subject matter or purpose of the contract. This subject matter or purpose is usually the agreed upon good or service for which the parties are contracting. For example, the "purpose" of a contract for a sale of goods is the purchase of the respective goods. Likewise, the purpose of a rental agreement is for the use of the premises. This subject matter is based off of the set classification that the civil law assigns to different contractual forms. The classification may in turn further define additional structural requirements that the parties must comply with in order to give the contract full legal force.

Finally the contract must have a legal cause, i.e. the determinative reason of the parties entering into the agreement must be legal. However this reason should not be confused with the party's individual motive for entering into the contract or the legality of the contract. Legal cause is instead more akin to the common law principle of consideration. It is the objective and standard motive that any party entering into an agreement would have for that type of legal contract. For example, the legal cause of the sale of goods would be to exchange the good in exchange for a set price. Furthermore, in the civil law, just as with the common law, this reason for entering into the contract must both be serious and find a corresponding obligation made by the other party. However, unlike the common law, in which a party may still claim reliance when consideration is not present, a lack of legal cause renders a civil law contract unenforceable.

Back to top

Performance Damages

Another principle difference between the common and civil law systems is in their approach to performance damages and remedies. For most common law lawyers, "specific performance" is an equitable remedy reserved for only the most extraordinary circumstances, such as the transfer of unique property. Because of the common law courts' cautious approach to its use, specific performance is usually backed by the full enforcement power of the judiciary when invoked. Noncompliance includes fines, penalties, and even possible contempt charges. Instead of making use of such an extreme remedy, common law courts will instead award monetary damages calculated based on either the inured party's reasonable expectation of reward or restitution of their loss. Simultaneously, the common law system will also require the injured party to mitigate damages, thereby encouraging economic efficiency through the completion of the envisioned transaction rather than delaying and seeking a windfall judgment. Under this approach, it is very common for contractual parties, with the full blessing of the court, to more efficiently allocate their resources by breaching an agreement and settling for less than the contract amount.

The civil law system takes the opposite approach to specific performance and monetary damages. Because of the civil law's desire to enforce the parties voluntarily enacted obligations, specific performance is a statutory remedy that the civil law courts are expected to turn to first. It may be replaced by monetary damages only in those cases where specific performance is either unfeasible or inadmissible. Although it is frequently awarded, however, specific performance is less likely to be enforced in civil law countries because of the relative weakness of the remedial measures available to their courts. For example, under the French System, where contempt charges are usually limited to criminal proceedings and are therefore unavailable in civil actions, French courts must make use of *astreinte*, where the courts seek to end a party's resistance to its decision through a fee payable to the state for each day of delay. In many civil law jurisdictions, only after a claim for specific performance has been issued may the defendant, through a complicated process, convert it into a claim for monetary damages.

Back to top

Conclusion

The civil law and common law approaches to contracts are similar in many respects. There are, however, certain nuances between the two systems that international practitioners should be aware of in order to ensure that they properly advance and protect their client's needs and interests. These differences affect not only the types of contracts that are enforceable under each system, but also the steps of creating a contractual agreement and the damage available upon its breach. A basic understanding of these nuisances will allow counsel to spot potential issues and efficiently advance the client's business objectives.

Back to top

Additional Resources

Web Resources

- World Fact Book (U.S. Central Intelligence Agency) (providing a list of countries and a description of the respective legal systems)
- Guide to Law Online (Law Library of Congress)
- International Resources (Washburn School of Law)
- Contract Law (The Canadian Encyclopedia)

Book and Article Resources

- Alain A. Levasseur, Comparative Law of Contracts: Cases And Materials (2008)
- Julian Hermida, Convergence of Civil Law and Common Law Contracts in the Space Field, (2004)
- Giuditta Cordero Moss, International Contracts Between Common Law and Civil Law (2007)
- Henrik Lando, The Myth of Specific Performance in Civil Law Countries (2003)

Back to top

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Export 3.10.1.1 Unilateral vs. Bilateral Contracts – Manufactured Difficulties Introduction

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The common law, as the Sixth Interim Report of the English Law Revision Committee 23 (1937) informs us,

> traditionally divides parol contracts into two classes, the bilateral contract of a promise for a promise, and the unilateral contract of a promise for an act. In the case of bilateral contracts one promise is held to be consideration for the other, the agreement, therefore, becoming effective at the moment when the promises are exchanged. In the case of a unilateral contract, however, the promise does not become binding until the act has been completely performed. A promisor may therefore withdraw his promise at any time before completion of the act, even though he knows that the promisee has already entered upon the performance and has nearly completed it.

Not so long ago, the practical wisdom of "the great dichotomy," ingeniously elaborated and defended by Langdell in his Summary of the Law of Contracts 248 (2d ed. 1880) and by Williston, 1 Williston §13, was accepted as if grounded in the nature of things, and its application was not regarded as difficult, at least in theory. Its implications, however harsh in an individual case, were treated as just, since the division purported to be in keeping with the intentions of the offeror, "the master of the bargain." In terms of this analysis, the doing of the act constitutes acceptance, the bargained-for consideration, and the offeree's performance

The case material that follows serves to show the powerful influence of the famous distinction and its gradual erosion. Some courts have not hesitated to apply the distinction literally even where performance of the requested act would require considerable time and effort, and have permitted the offeror to revoke his offer as long as he had not received the whole consideration. These courts regarded the offeree as adequately protected by a recovery in quantum meruit. Other courts, however, have found the rigid application of the division, when applied to actual life situations and not to the hypothetical case of the climbing of a flag-pole, difficult to reconcile with their sense of justice. Small wonder that they did not regret the discovery that the line of demarcation between the two institutions is often blurred; nor did they hesitate to tamper with the whole doctrine, even at the risk of an over-correction. The Restatement of Contracts, reflecting modern case law, has narrowed the gap between unilateral and bilateral contracts. See §§31, 45, 56, 63.

The reform movement received a powerful impetus by the attack on the famous distinction in Llewellyn's article, On Our Case-Law of Contract: Offer and Acceptance, 48 Yale L.J. 1, 779 (1938-1939), which makes the argument that "the great dichotomy," based

on the erroneous assumption that businessmen always bargain in terms of acts or of promises, fails to correspond to the notions of businessmen as to when "a deal is on." His observations are worth quoting.

> . . . The great dichotomy in the orthodox doctrine of Offer and Acceptance is that between bilateral and unilateral contract.[131] But there have been signs over thirty years or more of difficulty with it and its implications. Perhaps it is time to recanvass the life-situation with which it has to deal. And so to recanvass the cases which its office is to reflect and to guide.
>
> This will not be easy doing. The rules of Offer and Acceptance have been worked over; they have been written over; they have been shaped and rubbed smooth with pumice, they wear the deep rich polish of a thousand class rooms; they have a grip on the vision and indeed on the affections held by no other rules "of law," real or pseudo. For it was Offer and Acceptance which first led each of us out of laydom into The Law. Puzzled, befogged, adrift in the strange words and technique of cases, with only our sane feeling of what was decent for a compass, we felt the warm sun suddenly, we knew that we were arriving, we knew we too could "think like a lawyer." That was when we learned to down seasickness as A revoked when B was almost up the flag-pole. Within the first October, we had achieved a technical glee in justifying judgment then for A; and succulent memory lingers, of the way our dumber brethren were pilloried as Laymen still. This is therefore no area of "rules" to be disturbed. It is an area where we want no disturbance, and will brook none. It is the Rabbit-Hole down which we fell into the Law, and to him who has gone down it, no queer phenomenon is strange; he has been magicked; the logic of Wonderland we then entered makes mere discrepant decision negligible. And it is not only hard, it is obnoxious, for any of us who have gone through that experience to even conceive of Offer and Acceptance as perhaps in need of re-examination.

(Id. at 32)

The impact of this criticism is reflected in the Uniform Commercial Code and the Restatement of Contracts. U.C.C. §2-206, "Offer and Acceptance in Formation of Contract," reads as follows:

> (1) Unless otherwise unambiguously indicated by the language or circumstances
>
> (a) an offer to make a contract shall be construed as inviting acceptance in any manner and by any medium reasonable in circumstances;
>
> (b) an order or other offer to buy goods for prompt or current shipment shall be construed as inviting acceptance either by a prompt promise to ship or by the prompt or current shipment of conforming or non-conforming goods, but such a shipment of non-conforming goods does not constitute an acceptance if the seller seasonably notifies the buyer that the shipment is offered only as an accommodation to the buyer.
>
> (2) Where the beginning of a requested performance is a reasonable mode of acceptance an offeror who is not notified of acceptance within a reasonable time may treat the offer as having lapsed before acceptance.

The Restatement Second has followed this trend by deleting §12 of the original Restatement which defined unilateral and bilateral contracts. These terms are no longer used because of doubts as to the utility of the distinction (Reporter's note to §12).[132] While §31 of the original Restatement laid down a presumption that an offer invites a bilateral contract, §32 of the Restatement Second favors a different interpretation. It reads:

> Invitation of Promise or Performance
> In case of doubt an offer is interpreted as inviting the offeree to accept either by promising to perform what the offer requests or by rendering the performance, as the offeree chooses.[133]

This does not mean, however, that the Restatement Second has ignored the fact that a promise is often binding on the promisor even though the promisee is not bound by any corresponding obligation. This is strikingly illustrated by the rule laid down in §45.[134] Consult Braucher, Offer and Acceptance in The Second Restatement, 74 Yale L.J. 302 (1964).

[131] The argument is that the classical bilateral-unilateral distinction dies as it approaches fact either of life or of case decision. I put forward as a major piece of evidence the prominence which that distinction has in the table of contents of 1 Williston and Thompson, [Contracts (1936)], and the lack of correspondence of the text, and much more of the notes, to the suggestions in the table of contents. The Restatement shows the distinction only in the background, coloring much, but not explicitly, as a fundamental cleavage.

[132] Restatement Second §12, Reporter's Note (Tent. Draft No. 1, 1964):

> As defined in the original Restatement, "unilateral contract" included three quite different types of transaction: (1) the promise which does not contemplate a bargain, such as the promise under seal to make a gift, (2) certain option contracts, such as the option under seal (see §§24A, 45), and (3) the bargain completed on one side, such as the loan which is to be repaid. This grouping of unlike transactions was productive of confusion.

[133] See also §30. It reads:

> Form of Acceptance Invited
>
> (1) An offer may invite or require acceptance to he made by an affirmative answer in words, or by performing or refraining from performing a specified act, or may empower the offeree to make a selection of terms in this acceptance.
>
> (2) Unless otherwise indicated by the language or the circumstances, an offer invites acceptance in any manner and by any medium reasonable in the circumstances.
>
> [See also §55].

[134] It reads:

> Option Contract Created by Part Performance or Tender
>
> (1) Where an offer invites an offeree to accept by rendering a performance and does not invite a promissory acceptance, an option contract is created when the offeree begins the invited performance or tenders part of it.
>
> (2) The offeror's duty of performance under any option contract so created is conditional on completion or tender of the invited performance in accordance with the terms of the offer.

Consult also, §25; §87, *supra* p. 315.

Antoine Tézenas du Montcel, Paul Jourdan-Nayac, Etienne Chesneau and Abel Colomb, Executing Contracts in France, Thomson Reuters Practical Law, 19 February 2021

When is a written contract required? 1
Contracts required to be in writing to be valid 1
Contracts that must be proved in writing 2
Why use a written contract in commercial matters? 2
Types of written contract 2
Private deed 2
Authentic instrument 3
Notarial deed: a type of authentic instrument 3
When is a notary required? 3
Formalities for notarisation 4

An overview of the law and practice relating to the form execution of contracts under French law. The note includes a summary of the different forms that contracts can take and when a private deed or a notarial deed may be necessary. It also covers virtual closings and the use of electronic signatures.

When is a written contract required?

The basic position in French law is that contractual parties have freedom of contract (article 1102, Civil Code (Code civil)). They are free to agree the content and form of their contract, within the limits set by law (article 1102, Civil Code). French law also provides for a mutual consent principle, whereby a contract is legally binding whether concluded orally or in writing, unless the law requires a particular form (article 1172, Civil Code). Therefore, it is possible to conclude some agreements verbally or by an exchange of correspondence (see Counterparts).

In some cases, the party's intent at the time of the contract can be determined by the courts by reference to the parties' subsequent behaviour (French Supreme Court (Cour de Cassation), Civil Chamber 1, 13 December 1988, 86-19.068, published in the Bulletin). However, this will not apply if the terms of the contract are clear and precise (article 1192, Civil Code).

In certain cases, the Civil Code requires a contract, and other legal documents, to be in writing to make them valid (see Contracts required to be in writing to be valid). Some contracts also require a specific type of written document, an authentic instrument (acte authentique), as a condition of validity (see Authentic instrument).

In addition, written form may be necessary to prove the existence and contents of a contract, or questions arising as to its performance, in court. See Contracts that must be proved in writing.

Even if written form is not legally required, it is generally advisable to put a contract in writing for evidentiary reasons.

Contracts required to be in writing to be valid

Contracts that must be in writing to be valid include:

- Contracts transferring partnership interests (actes de cession des parts sociales) in a private limited company (société à responsabilité limitée) or in a general partnership (société en nom collectif) (articles L.221-14 and L.223-17, Commercial Code (Code de commerce), respectively).
- The assignment of contracts (article 1216, Civil Code).
- The assignment of receivables (article 1322, Civil Code).
- Retention of title clauses (article L.624-16, Commercial Code).

- Fixed-term employment contracts (article L.1251-42,
- Labour Code (Code du travail)).
- Land transfers (articles 1589-2, Civil Code and L.526-9, Commercial Code).
- Guarantees (cautionnements). An individual who enters into a private agreement as a guarantor with a professional creditor has to include a specific handwritten statement (mention) as a requirement for the validity of the guarantee (article L.331-1, Consumer Code (Code de la consommation)).
- The articles of association (statuts) of a company (article 1835, Civil Code).
- Pledges (nantissements) (article L.142-3, Commercial Code).

Included in this list are contracts that are specifically required to be made in the form of a private or notarial deed (see Private deed and Notarial deed: a type of authentic instrument).

Contracts that must be proved in writing

Even if written form is not required for legal validity, if a dispute arises as to the existence, contents or performance of an agreement, a written contract may be necessary for evidentiary purposes (for example, to adduce it as evidence of a contract in court or for tax purposes) (article 1364, Civil Code).

A contract relating to a sum or value exceeding EUR1,500 must generally be proved in writing in the form of a private or notarial deed (article 1359, Civil Code). This general rule is subject to the following exceptions:

- Commercial acts involving traders may be proved by any means, unless otherwise provided by law (article L.110-3, Commercial Code). The requirement for written agreement is relaxed for commercial transactions,
- in recognition of the fact that traders generally require less contractual protection than, for example,
- consumers and they need the flexibility to conclude agreements expediently.
- A written contract is not required for the purposes of proof:
    - if there is material or moral impossibility of obtaining proof in writing;
    - if it is customary not to have a written contract; or
    - for cases where the written contract has been lost following a force majeure. (Article 1360, Civil Code.)
- Article 1360 gives discretion to a judge to allow a contract to be proved by other means. For example, there may be moral impossibility of obtaining written proof in the case of an agreement made between family members.
- A written contract may be replaced for the purposes of proof by a judicial confession (aveu judiciaire), a decisive oath (serment décisoire) or a commencement of proof in writing corroborated by another means of proof (article 1361, Civil Code).

Any written evidence constitutes a “beginning of proof in writing” (commencement de preuve par écrit), if it originates from the person who is challenging the act, or a person they represent, and renders the allegation likely to be true (articles 1361 and 1362, Civil Code). This exception gives a judge a wide discretion to allow a document to be adduced in court as evidence, if it makes it plausible that a contract was entered into by a party who disputes this fact. A reference to a notarial deed or private deed on a public register is deemed as the beginning of proof in writing.

Why use a written contract in commercial matters?

Despite the exception for commercial acts in article L.110-3 of the Commercial Code, most corporate and commercial contracts are documented in writing for probative and enforceability purposes. Accordingly, a contract will be entered into in writing either because the law requires it or because the parties have agreed to it for probative and enforceability purposes.

Types of written contract

Written contracts typically take one of the following legal forms, which may be prescribed by law:

- A private deed. See Private deed.
- An authentic instrument. See Authentic instrument.

In addition, the parties may choose to execute an attorney’s deed (acte d’avocat), which is a type of private deed. Adopting this form can assist in the enforceability of a contract. See Use of an attorney’s deed for enforceability purposes.

Private deed

A private deed is a signed contract (or other legal act) that is drawn up and agreed privately between its parties. A private deed is binding on its parties (and their heirs and successors in title), if one of the following conditions is met:

- The signatories in question recognise the private deed, including their signature.
- The private deed is legally considered as recognised. This would include where the private deed has been countersigned by the attorneys (avocats) of each party or a by an attorney acting on behalf of both parties (see Use of an attorney's deed for enforceability purposes).

(Articles 1372 and 1374, Civil Code.)

A party, or their heirs or successors in title, may contest the authenticity of a private deed, if they do not recognise its contents or their signature. If they do so, the judge must follow a signature verification procedure to ascertain whether the document has been drafted and signed by the person to whom it is attributed (article 1373, Civil Code).

Authentic instrument

An authentic instrument is a legal document that has been drawn up and executed with the required formalities by a public official, who has the requisite competence and capacity to act (article 1369, Civil Code). Most commonly, agreements entered in authentic form are drawn up by notaries who are public officers (see Notarial deed: a type of authentic instrument), provided that such agreements are made in France and subject to French law.

Other public officials, such judges and official keepers of public registries, are also able to issue authentic instruments, such as judgments and certificates of vital record (for example, birth certificates). In addition, bailiff deeds (actes d'huissier) that are executed under a delegation of the law (for example, a court summons) are classified as authentic instruments. However, these types of documents are beyond the scope of this note, which focuses on the main forms for executing a contract, namely private and notarial deeds.

Notarial deed: a type of authentic instrument

A notarial deed is document that is classified under French law as a type of authentic instrument. Notaries are public officials who can authenticate contracts and other documents, certify the date of execution, preserve deposited deeds, and deliver official or certified copies (article 1, Ordinance No 45-2590 of 2 November 1945 (on the status of the notary)).

A notarial deed is deemed to be authentic and its validity can only be challenged by a plea of forgery (inscription de faux) (article 1371, Civil Code).

If any of the required formalities for a public deed are not observed (or the notary was not competent or capable of acting), but the document has been signed by the parties, the document takes effect as a private deed (article 1370, Civil Code).

When is a notary required?

For certain types of contract and other legal acts, French law requires the use of a notarial deed, or an authentic instrument in general. For corporate law matters, the use of notarial deeds is less common and most transactions may be executed by private deed. However, a notary is required, and benefits from a monopoly under French law, if real estate assets are transferred as part of a deal (although this may not be the case for the purposes of a deal relating to shares of a company owning a real estate property).

Notarial deeds have executory force (force exécutoire). This means they can be enforced directly by a bailiff (huissier de justice) without the need to obtain a court judgment (article 19, Notaries Act 1803 (Loi contenant organisation du notariat (loi 25 ventôse an XI)) and article 3, Law No 91-650 of 9 July 1991 (reforming the civil procedure of execution)).

Notarial deeds (or authentic instruments in general) are prescribed for the following types of contract:

- Certain types of donation, notably those relating to real estate (article 931, Civil Code).
- Conventional mortgages (hypothèques conventionnelles) (article 2416, Civil Code).
- Transfers of land that must be registered and the creation or registration of limited rights in land in general (article 4, Decree no 55-22 of 4 January 1955 (Land register reforms)).
- Certain types of fiducie, relating to jointly owned property, rights or security interests (article 2012, Civil Code). A fiducie is a French legal concept that has similar characteristics to a common law trust.

- Marriage contracts and wills, if their authors want these documents to be made as authentic instruments with a certain date and to be kept and registered by the notary. In the case of inheritances, if at least one real estate asset is included in the legacy, a meeting before a notary will also be necessary to handle the property transfer.

Formalities for notarisation

A notarial deed is a legally binding document, such as a contract, that is drafted by a notary. The parties (or their authorised representatives) must sign the notarial deed in the presence of the notary, who also signs it (article 10, Decree No 71-941 of 26 November 1971 (Notarial Deeds). The notary must, in principle, authenticate the instrument in person and read the deed to the parties to ensure they understand its content, or else the authentic instrument is invalid. However, if these formalities have not been complied with, the document may still qualify as a private deed, if it has been dated and executed by all parties. In such a case, specific rules may apply to prevent one party from avoiding its obligations purely on the basis of the formal invalidity of the concerned instrument.

For some types of notarial deed (for example, a revocation of a will), the presence and signature of more than one notary or witnesses is also required, to provide certainty over its date of execution (article 9, Notaries Act).

Before executing the deed, the notary checks and records the identity, nationality, capacity and domicile of each party (article 5, Decree No 71-941). In exceptional cases, information about the parties may be attested to by two witnesses. See also Capacity and authority.

The notary advises the parties as to the scope and effect of the deed, as well as other relevant information.

In terms of its contents, a notarial deed must:

- State the name and place of establishment of the notary, the name and domicile of the witnesses, the place where the deed is made and the date on which each signature is affixed. The notaries' national regulation (règlement national du notariat) expressly limits the locations where a notarial deed can be executed (that is, in the notary's offices, in the offices of another notary, at the residence of one of the parties to the notarial deed, in administrative premises, in a court of law or in a hospital).
- Contain the names, surnames and domiciles of the parties and of all the signatories of the deed.
- State that the deed has been read by the parties or that it has been read to them.
- Have its appendices signed by the notary, for such appendices to be part of the notarial deed.

(Article 6, Decree on Notarial Deeds No 71-941.)

There are also requirements as to the format of the deed. For example, numbers must be stated in letters the first time they are cited (unless they are the result of a calculation), as must the date of execution.

Abbreviations must be cited in full at least once in the document (article 8, Decree on Notarial Deeds No 71-941). The document must be legible and not contain unnecessary blank spaces, other than those that have been identified and recorded by the notary at the end of the deed (article 9, Decree on Notarial Deeds No 71-941). There are also compulsory statements, which are not a condition of validity of the notarial deed, but which are required to file such deed with the land registry (service de la publicité foncière) and to ensure its enforceability against third parties.

In addition to signing the execution block at the end of the deed, the parties and the notary must in principle initial each page. This is because any pages that have not been initialled do not form part of the notarial deed (article 14 al.4, Decree on Notarial Deeds No 71-941).

However, in practice, a patented binding system (for example, "Assemblact") is often used, which avoids the need for the parties and the notary to initial each page. Instead, only a few pages must be signed for the deed to be validly executed.

Once the notarial deed has been executed, the notary must keep the original document, referred to as the "minute", in their office. If the parties require a copy, the notary can issue authenticated copies of the minute.

The notary must also keep a record of the deeds they hold. If a notarial deed is required to be filed with a public registry (such as the land registry or companies and commercial register), this will be carried out by the notary (article 26, Decree No 71-941 on Notarial Deeds).

As public officials, notaries are also in charge of collecting taxes, duties, rates and charges triggered by the operation resulting from the notarial deed (for instance, any transfer capital gains tax in case of disposal of a real estate property, if applicable) and to transfer them to the public treasury.

Jane K. Winn
UJM-Lyon3 2019

Unilateral Contract in French and American Contract Law

French Civil Code, Obligations, Title IIII Of Contracts and of Conventional Obligations in General

Art. 1101 A contract is an agreement by which one or several persons bind themselves, towards one or several others, to transfer, to do or not to do something.

Art. 1102 A contract is synallagmatic or bilateral where the contracting parties bind themselves mutually towards each other.

Art. 1103 It is unilateral where one or more persons are bound towards one or several others, without there being any obligation on the part of the latter.

Art. 1104 It is commutative where each party binds himself to transfer or do a thing which is considered as the equivalent of what is transferred to him or of what is done for him. Where the equivalent consists in a chance of gain or of loss for each party, depending upon an uncertain event, a contract is aleatory.

Art. 1105 A contract of benevolence is one by which one of the parties procures a purely gratuitous advantage to the other.

Art. 1106 A contract for value is one which obliges each party to transfer or do something.

Art. 1107 Contracts, whether they have a specific denomination or not, are subject to general rules, which are the subject matter of this Title.

US First Restatement of Contracts (1932)

§ 12. Unilateral and Bilateral Contracts.

A unilateral contract is one in which no promisor receives a promise as consideration for his promise A bilateral contract is one in which there are mutual promises between two parties to the contract; each party being both a promisor and a promisee.

Comment:

a. In a unilateral contract the exchange for the promise is something other than a promise; in a bilateral contract promises are exchanged for one another.

b. There must always be at least two parties to a contract, whether unilateral or bilateral, and there must usually be an expression of assent by each. In many cases, however, a promise becomes a contract even though no return promise is made by the promisee. In such cases, the legal duty is unilateral, resting on the promisor alone. The correlative legal right is also unilateral, being possessed by the promisee alone. The statement often made that unless both parties are bound neither is bound is quite erroneous, as a universal statement.

C. A unilateral contract is in a very real sense, as its name implies, a one-sided contract. There are two parties to the contract, it is true, and a manifestation of assent on the part of each is usually necessary to its formation; but one of the requisites for making the contract should not be confused with the contract itself. The contract is merely the promise, not the mutual manifestation of assent or the consideration paid for the promise. In a bilateral contract, on the other hand, as there are contractual promises on both sides, the contract is properly called bilateral.

§ 31 Presumption That Offer Invites a Bilateral Contract.

In case of doubt it is presumed that an offer invites the formation of a bilateral contract by an acceptance amounting in effect to a promise by the offeree to perform what the offer requests, rather than the formation of one or more unilateral contracts by actual performance on the part of the offeree.

US Second Restatement of Contracts (1982)

§ 25. Option Contracts

An option contract is a promise which meets the requirements for the formation of a contract and limits the promisor's power to revoke an offer.

§ 32. Invitation of Promise or Performance

In case of doubt an offer is interpreted as inviting the offeree to accept either by promising to perform what the offer requests or by rendering the performance, as the offeree chooses.

Illustrations:

1. A writes B, "If you will mow my lawn next week, I will pay you $10." B can accept A's offer either by promptly promising to mow the lawn or by mowing it as requested.

2. A says to B: "If you finish that table you are making and deliver it to my house today, I will give you $100 for it." B replies, "I'll do it." There is a contract. B could also accept by delivering the table as requested.

b. Offer limited to acceptance by performance only. Language or circumstances sometimes make it clear that the offeree is not to bind himself in advance of performance. His promise may be worthless to the offeror, or the circumstances may make it unreasonable for the offeror to expect a firm commitment from the offeree. In such cases, the offer does not invite a promissory acceptance, and a promise is ineffective as an acceptance. Examples are found in offers of reward or of prizes in a contest, made to a large number of people but to be accepted by only one. Non-commercial arrangements among relatives and friends and offers which leave important terms to be fixed by the offeree in the course of performance provide other examples.

§90. PROMISE REASONABLY INDUCING ACTION OR FORBEARANCE

(1) A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise. The remedy granted for breach may be limited as justice requires.

Comments:

a. Relation to other rules.... This Section is often referred to in terms of "promissory estoppel," a phrase suggesting an extension of the doctrine of estoppel. Estoppel prevents a person from showing the truth contrary to a representation of fact made by him after another has relied on the representation....

Certainly reliance is one of the main bases for enforcement of the half-completed exchange, and the probability of reliance lends support to the enforcement of the executory exchange. See Comments to §§72, 75. This Section thus states a basic principle which often renders inquiry unnecessary as to the precise scope of the policy of enforcing bargains. Sections 87-89 state particular applications of the same principle to promises ancillary to bargains, and it also applies in a wide variety of non-commercial situations.

b. Character of reliance protected. The principle of this Section is flexible. The promisor is affected only by reliance which he does or should foresee, and enforcement must be necessary to avoid injustice. Satisfaction of the latter requirement may depend on the reasonableness of the promisee's reliance, on its definite and substantial character in relation to the remedy sought, on the formality with which the promise is made, on the extent to which the evidentiary, cautionary, deterrent and channeling functions of form are met by the commercial setting or otherwise, and on the extent to which such other policies as the enforcement of bargains and the prevention of unjust enrichment are relevant....The force of particular factors varies in different types of cases....

Illustrations:

> 2. A promises B not to foreclose, for a specified time, a mortgage which A holds on B's land. B thereafter makes improvements on the land. A's promise is binding and may be enforced by denial of foreclosure before the time has elapsed.
>
> 3. A sues B in a municipal court for damages for personal injuries caused by B's negligence. After the one year statute of limitations has run,B requests A to discontinue the action and start again in the superior court where the action can be consolidated with other actions against B arising out of the same accident. A does so. B's implied promise that no harm to A will result bars B from asserting the statute of limitations as a defense.
>
> 4. A has been employed by B for 40 years. B promises to pay A a pension of $200 per month when A retires. A retires and forbears to work elsewhere for several years while B pays the pension. B's promise is binding.

c. Reliance by third persons. If a promise is made to one party for the benefit of another, it is often foreseeable that the beneficiary will rely on the promise. Enforcement of the promise in such cases rests on the same basis and depends on the same factors as in cases of reliance by the promisee. Justifiable

reliance by third persons who are not beneficiaries is less likely, but may sometimes reinforce the claim of the promisee or beneficiary.

d. Partial enforcement. A promise binding under this section is a contract, and full-scale enforcement by normal remedies is often appropriate. But the same factors which bear on whether any relief should be granted also bear on the character and extent of the remedy. In particular, relief may sometimes be limited to restitution or to damages or specific relief measured by the extent of the promisee's reliance rather than by the terms of the promise.... Unless there is unjust enrichment of the promisor, damages should not put the promisee in a better position than performance of the promise would have put him. See §§344, 349.

Illustrations:

> 8. A applies to B, a distributor of radios manufactured by C, for a "dealer franchise" to sell C's products. Such franchises are revocable at will. B erroneously informs A that C has accepted the application and will soon award the franchise, that A can proceed to employ salesmen and solicit orders, and that A will receive an initial delivery of at least 30 radios. A expends $1,150 in preparing to do business, but does not receive the franchise or any radios. B is liable to A for the $1,150 but not for the lost profit on 30 radios....
>
> 9. The facts being otherwise as stated in Illustration 8, B gives A the erroneous information deliberately and with C's approval and requires A to buy the assets of a deceased former dealer and thus discharge C's "moral obligation " to the widow. C is liable to A not only for A's expenses but also for the lost profit on 30 radios.

526 N.W.2d 369 (1995)

Kevin RUUD, et al., Respondents,

v.

GREAT PLAINS SUPPLY, INC., et al., Petitioners, Appellants.

No. C5-93-527.

Supreme Court of Minnesota.

January 20, 1995.

370 *370 John A. Warchol, Warchol, Berndt & Hajek, P.A., Minneapolis, for appellant.

Zenas Baer, Wefald and Baer, Hawley, for respondent.

Heard, considered and decided by the court en banc.

OPINION

GARDEBRING, Justice.

This case involves issues of employment law arising out of a relationship between respondent Kevin Ruud and appellant Great Plains Supply, Inc. (GPS). After he was terminated as the manager of GPS's Sioux City, Iowa store, Kevin Ruud and his wife Diane Ruud sued GPS and certain GPS officials, alleging breach of express contract, breach of implied contract by promissory estoppel and fraud and misrepresentation. Included in the suit was Diane Ruud's claim that, in reliance upon promises of GPS as to the security of Kevin Ruud's employment, she quit her job, sold the family home in Twin Valley, Minnesota and moved to Sioux City.

The trial court dismissed the claims against the individual defendants and granted GPS's motion for summary judgment on all claims. The court of appeals reversed the summary judgment as to breach of contract and promissory estoppel, but affirmed on the fraud and misrepresentation claim.[1] We reverse and reinstate the decision of the trial court.

Kevin Ruud was employed by GPS from July 1978 until October 1991 in a variety of positions. In early 1988 he became the manager of GPS's Twin Valley, Minnesota store. Diane Ruud was employed as Vice President of the Twin Valley State Bank, the family owned a home in Twin Valley, and the Ruuds' three children attended school in the community.

In March of 1990, Ruud began talks with Michael Wigley, owner of GPS, about a transfer to a GPS store in Sioux City, Iowa. Kevin Ruud knew that the Sioux City store was unprofitable and might have to be closed. He asked Wigley what would happen to him if he accepted the job offer, and the job did not work out as planned. In response, Ruud alleged that Wigley stated, "Good employees are taken care of" and "You are considered a good employee."

Several days later, Kevin Ruud met with Ronald Nelson, vice-president of GPS and manager of the district in which Sioux City was located. They discussed the transfer to Sioux City and again Kevin Ruud asked about job security. Nelson stated, "Good employees [are taken] care of." Kevin Ruud alleged that Nelson additionally told him that if the job in Sioux City did not work out, he would be offered a "similar" position elsewhere in the organization. Nelson offered Ruud the Sioux City managerial position, and Kevin Ruud declined.

371 *371 On March 30, 1990, during a telephone conversation between Kevin Ruud and Wigley, a second job offer was made. In a memo dated April 2, 1990, Wigley confirmed what he believed to be the content of the oral offer which he had made to Kevin Ruud on March 30, 1990. The memo referenced various terms of employment, including salary, living allowance, bonus structure, moving and related expenses, and time off; it contained no provisions on job security. Ruud

accepted the second job offer and began employment for GPS in Sioux City in April 1990.

Kevin Ruud moved to Sioux City first with the plan that his family would follow in the spring of 1991, when their oldest child graduated from high school. Kevin Ruud asserted this plan changed because GPS "demanded" that he move his family to Sioux City sooner. The "demand" was made in a conversation between Nelson and Kevin Ruud about a month after he was transferred to Sioux City. Nelson asked him how he was doing in the new location. Kevin Ruud answered that there were some difficulties in adjusting to bachelor life. Kevin Ruud alleged that Nelson responded, "Well, you better get your family down here then." Kevin Ruud claims that the "demand" was made again in June. In November 1990, Diane Ruud terminated her employment as Vice President of the Twin Valley State Bank, sold the family home, and moved the Ruud family to Sioux City, with one child staying in Twin Valley to finish high school. Diane Ruud did not talk to GPS about this issue nor did she believe that her husband's job was threatened if the family did not move.

The Sioux City store continued to operate at a loss under Kevin Ruud's management. In May 1991, Ruud asked Nelson what would happen to him in the event the Sioux City store closed down. Ruud alleged that Nelson again replied, "Good employees are taken care of." On July 22, 1991, Nelson told Ruud that he would be terminated as manager of the Sioux City store and offered him three other employment opportunities within GPS. Two of the job offers required another relocation and none was at a managerial level. Each of the offered positions would have resulted in decreased compensation to Kevin Ruud. He rejected all of the offered positions. The Ruud family moved back to Twin Valley, Minnesota.

Kevin and Diane Ruud filed suit against Wigley, Nelson and GPS claiming breach of an express employment contract for permanent employment, breach of an implied contract created by promissory estoppel, and fraud and misrepresentation. The trial court granted summary judgment in favor of GPS and dismissed the claims against Wigley and Nelson. Ruud appealed the decision. The court of appeals reversed the trial court as to the issues of modification of contract, promissory estoppel, and the wife's claim of promissory estoppel, holding that there were genuine issues of material fact. As to the issue of misrepresentation and fraud, the court of appeals affirmed the trial court's holding.

Summary judgment is proper when no issues of material fact exist and one party is entitled to judgment as a matter of law. Minn.R.Civ.P. 56.03. On appeal, this court is to determine whether any issues of material fact exist and whether the trial court erred in its application of the law. *Offerdahl v. University of Minn. Hosps. & Clinics*, 426 **N.W.2d** 425, 427 (Minn.1988). The evidence is viewed in the light most favorable to the nonmoving party. *State v. City of Mounds View*, 518 **N.W.2d** 567, 571 (Minn.1994).

The usual employer-employee relationship is terminable at the will of either party. *Cederstrand v. Lutheran Brotherhood*, 263 Minn. 520, 532, 117 **N.W.2d** 213, 221 (1962). A promise of employment on particular terms, if in the form of an offer and if accepted by the employee for valuable consideration, may create a binding unilateral contract which will alter an at-will contract. *Pine River State Bank v. Mettille*, 333 **N.W.2d** 622, 626 (Minn.1983).

The offer, though required to be definite in form and communicated to the offeree, *id.* at 626, may be inferred from words spoken or from the conduct of the parties, viewed objectively. *Cederstrand*, 263 Minn. at 533, 117 **N.W.2d** at 221. An employer's general statements of policy are no more than that and do not meet the contractual requirements for an offer.
372 *Pine River State* *372 *Bank*, 333 **N.W.2d** at 627. For example, in *Degen v. Investors Diversified Services, Inc.*, 260 Minn. 424, 110 **N.W.2d** 863 (1961), we found no offer for lifetime employment where the employer told the employee that he had a great future with the company and that he could consider his job a "career situation." *Id.* 260 Minn. at 428, 110 **N.W.2d** at 866. Further, in *Cederstrand* we identified the issue as one of determining whether there was an "intention to make such a promise as an offer and to be bound by it." *Cederstrand*, 263 Minn. at 533, 117 **N.W.2d** at 221.

It is conceded that, absent the comments of Wigley and Nelson, Kevin Ruud was an at-will employee.[2] Therefore, we must determine whether these comments constitute a definite offer so as to modify the terms of his existing at-will employment, that is, whether they manifest an intent to promise "permanent" employment.[3] In determining that the statements created an issue of material fact on the issue of contract modification, the court of appeals focused on the context and surrounding circumstances, noting that Kevin Ruud was aware of the financial difficulties of the Sioux City

store and that he inquired specifically as to his future. We do not find this reasoning persuasive.

The statements by Nelson and Wigley are similar to those at issue in *Cederstrand,* where the president of a large insurance company told employees "there would be no dismissals as long as people showed willingness to work and the ability and wanting to learn," *Cederstrand*, 117 **N.W.2d** at 216, and in *Degen,* where the employer discussed a "career situation." 260 Minn. at 428, 110 **N.W.2d** at 866. We conclude that Wigley and Nelson did not intend that GPS offer Kevin Ruud a "permanent" job, but rather were simply making policy statements as to the general goodwill of the company toward Kevin Ruud and its other employees. Furthermore, even if there was an intention to modify the contract, the statements of Wigley and Nelson are so vague as to leave undeterminable the nature of that modification. Therefore, we conclude that as a matter of law, the statements of Nelson and Wigley are not sufficiently definite to create an offer of permanent employment.

Next we turn to Kevin Ruud's claim that the statements of Wigley and Nelson support a claim under a theory of promissory estoppel. Promissory estoppel is a creature of equity which implies "a contract in law where none exist in fact." *Grouse v. Group Health Plan, Inc.*, 306 **N.W.2d** 114, 116 (Minn.1981). The application of promissory estoppel requires the analysis of three elements:

1. Was there a clear and definite promise?

2. Did the promisor intend to induce reliance, and did such reliance occur?

3. Must the promise be enforced to prevent an injustice?

Cohen v. Cowles Media Co., 479 **N.W.2d** 387, 391 (Minn.1992). We need not go beyond the first requirement, that the promise be clear and definite. Our analysis as to the modification of the employment contract is dispositive here, as well: as a matter of law, the statements of Wigley and Nelson are simply not "clear and definite" enough to support a claim for
373 promissory estoppel.[4] *373 Accordingly, the decision of the court of appeals is reversed and the summary judgment is reinstated.

[1] The court of appeal's affirmance of the summary judgment on the fraud and misrepresentation claims was not appealed to this court.

[2] The terms of Ruud's employment were governed by corporate policies contained in a handbook. The handbook states that GPS is an at-will employer and reserves the right to terminate any employee at any time for any reason. Ruud was hired after the policy became effective, thus, the policy applied to him. *Pine River State Bank*, 333 **N.W.2d** at 627. Ruud acknowledged receiving and reading the handbook.

[3] For purposes of the summary judgment motion, GPS conceded the truth of the Ruuds' allegations.

[4] Because we hold that at least one of the basic requirements for application of the doctrine of promissory estoppel is not met, we need not consider the reach of promissory estoppel to third parties. However, we note that the court of appeals relied upon its own case, *Dallum v. Farmers Union Cent. Exch., Inc.*, 462 **N.W.2d** 608, 613 (Minn.App.1990), *pet. for rev. denied* (Minn. Jan. 14, 1991), which in turn relied upon the Wisconsin case, *Hoffman v. Red Owl Stores, Inc.*, 26 Wis.2d 683, 133 **N.W.2d** 267 (1965). In *Hoffman,* however, the promisor specifically requested that the third party act in reliance on the promise. *Id.,* 133 **N.W.2d** at 275. Here, Diane Ruud had not been informed by her husband (or GPS) that GPS was requiring the family to move to Sioux City, nor had she been told that Kevin's job would be in jeopardy if she did not move.

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Name /thl_tbl621_3058006/winn/Mp_1 12/12/2006 04:42PM Plate # 0 pg 1 # 1

The Impact of EU Unfair Contract Terms Law on U.S. Business-to-Consumer Internet Merchants

*By Jane K. Winn and Mark Webber**

It is in acquiring, using and exchanging things that individuals come to have social lives.[1]

1. Introduction

When the Court of Appeals for Versailles issued its decision in *AOL France v. UFC Que Choisir*[2] in September 2005, it sent the message to U.S. Internet businesses that even contractual boilerplate localized for European markets may be invalid in European consumer transactions. In that case, a French consumer advocacy group challenged the terms AOL offered its French customers after AOL had made extensive revisions to its standard form contracts to respond to the concerns regarding those terms expressed in an advisory opinion by a French consumer protection agency. In 2004, a trial court invalidated nearly every term in the revised agreement; the appeals court affirmed on all counts. Subsequently, in July 2006 following concerns raised by the Office of Fair Trading ("OFT"), a United Kingdom government agency charged with "making sure markets work well for consumers,"[3] Dell Corporation Limited changed its online terms and conditions to make them fairer to consumers.[4] European consumer contract law had an impact in both cases. At issue for AOL France and Dell Corporation Limited was the application of France's and the UK's consumer contract law which is based on the Unfair Contract Terms Directive of 1994[5] and calls into question the validity of many of the terms that U.S. courts routinely enforce in transactions involving American consumers and merchants.

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1. Celia Lury, Consumer Culture 12 (1996).

2. AOL France v. UFC Que Choisir, R.G. N° 04/05564, Cour d'appel [CA] [regional court of appeal] Versailles, 1e ch., Sept. 15, 2005, J.C.P. IV 150905, *available at* http://www.clauses-abusives.fr/juris/cav150905.pdf; see *infra* Part 4 for a detailed discussion of the case.

3. *See* OFT—About the Office of Fair Trading, *available at* http://www.oft.gov.uk/About/default.htm.

4. *See* Press Release, Office of Fair Trading, *Dell to improve terms and conditions for consumers* (July 6, 2006) (U.K.), *available at* http://www.oft.gov.uk/News/Press+releases/2006/111-06.htm.

5. Council Directive 93/13, 1993 O.J. (L 95) 29 (EEC) [hereinafter "UCT Directive"], *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:31993L0013:EN:NOT.

Name /thl_tbl621_3058006/winn/Mp_2 12/12/2006 04:42PM Plate # 0 pg 2 # 2

In 2005, the OFT published a guide for UK merchants regarding the application of the UK's unfair contract terms law to Internet transactions.[6] That Guidance, *IT Consumer Contracts Made at a Distance*, may also be valuable to U.S. Internet merchants doing business with European consumers who are trying to understand the broad scope of EU unfair contract terms law and its application to their businesses. Since the mid-1990s, the OFT has published hundreds of "case reports" explaining its interpretations of individual contract terms in light of UK contract law.[7] The 2005 Guidance provides a helpful summary of the OFT's decisions in the area of Internet transactions. The OFT specifically references the 2005 Guidance in its press release on Dell Corporation Limited. The OFT reinforces its message that the Guidance is "to help distance sales businesses ensure their terms and conditions comply with the relevant regulations."[8]

This article focuses on the application of EU unfair contract terms law to retail Internet transactions that U.S. businesses might engage in with European consumers. It compares attitudes toward consumer protection regulation in the U.S. and the EU to provide some context within which the specific provisions of unfair contract terms law can be understood. While many lawyers and legal academics in the U.S. who study the development of online markets are aware of the profound differences in U.S. and EU information privacy laws,[9] the magnitude of the divergence in consumer electronic contracting law is not as widely recognized. The development of contract law on unfair terms in Europe over the last 25 years is an important change in EU contract law that has no direct counterpart in U.S. contract law. The application of contract law on unfair terms to online transactions is not at all surprising to lawyers in the EU, but may come as quite a surprise to U.S. businesses and the lawyers who advise them if they have mistakenly assumed that cross-border variations in consumer contract law are not great.[10] As some have learned to their detriment, it is not sufficient for businesses to simply deploy U.S. versions of their online terms and conditions in their European operations.

2. Diverging Perspectives on the Aims of Consumer Protection

Although there is some debate about the conventional wisdom that regulators in Europe adopt a more "precautionary" approach while U.S. regulators are pre-

6. *See* Office of Fair Trading, Publ'n No. 672, IT Consumer Contracts Made at a Distance—Guidance on Compliance with the Distance Selling and Unfair Terms in Consumer Contracts Regulations (2005) (U.K.) [hereinafter "the Guidance"], *available at* http://www.oft.gov.uk/NR/rdonlyres/F0F8ED8F-CEF0-4C06-A500-F7C915DEEBD7/0/oft672.pdf.

7. Most copies of the Unfair Contract Terms Bulletin can be downloaded from the OFT Publications Web page at http://www.oft.gov.uk/News/Publications/Leaflet+Ordering.htm. Reports of undertakings by firms to settle charges brought by the OFT under the UK unfair contract terms legislation can be found at http://www.crw.gov.uk/Undertakings+and+court+action.

8. *See* Press Release, Office of Fair Trading, *supra* note 4.

9. *See, e.g.*, Dorothee Heisenberg, Negotiating Privacy: The European Union, The United States, and Personal Data Protection (2005).

10. On differences between U.S. and EU approaches to consumer protection law, see generally A. Brooke Overby, *An Institutional Analysis of Consumer Law*, 34 Vand. J. Transnat'l L. 1219 (2001); Jane K. Winn & Brian H. Bix, *Diverging Perspectives on Electronic Contracting in the U.S. and EU*, 54 Clev. St. L. Rev. 175 (2006).

Name /thl_tbl621_3058006/winn/Mp_3 12/12/2006 04:42PM Plate # 0 pg 3 # 3

pared to tolerate more risk,[11] the wisdom appears to reflect the trends in recent years in the area of consumer protection law. Through the development of unfair contract terms law, EU regulators have been expanding their oversight of consumer markets and expanding the role of administrative agencies in enforcement, at precisely the time that U.S. contract law has turned away from public regulatory models. The growing gap in contract law doctrine with regard to unfair contract terms appears to be yet another example of diverging long-term trends in political culture and economic regulation on either side of the Atlantic.[12] The U.S. was very active in enacting consumer protection laws during the 1960s and 1970s while there was relatively little activity in this area in Europe. The trends reversed during the 1980s, when the U.S. embraced more market-oriented approaches that required individuals to bear more risk in consumer transactions, while the EU embarked on a sweeping program of legislation to protect consumers from many of those risks.[13]

Political scientists and economists distinguish between "economic regulation" aimed at supporting competition in markets and "social regulation" aimed at protecting health and safety.[14] Consumer protection laws are now treated as a form of economic regulation in the U.S.; government intervention is appropriate only when it is clear that competition is not doing an adequate job of meeting consumer needs.[15] EU lawmakers appear to be skeptical that mere economic regulation provides enough support for online consumer markets in Europe.[16] In the "eEurope 2002 Action Plan,"[17] the European Commission noted that "[c]onsumer confidence needs to be enhanced if e-commerce is to achieve its full potential," acknowledging that consumers in the EU have been slower to embrace online commerce than their counterparts in the U.S. The Commission was already implementing legislation that tackled the consumer confidence problem on several fronts, including enacting strong data protection legislation, which is a form of social regulation in the EU,[18] and regulating consumer markets to make them safe for less sophisticated consumers, which has turned consumer contract law into

11. *See, e.g.*, Jonathan B. Wiener, *Whose Precaution After All? A Comment on the Comparison and Evolution of Risk Regulatory Systems*, 13 DUKE J. COMP. & INT'L L. 207 (2003) (suggesting that comparisons are often based on stereotypes and a limited number of examples of regulation that may not be representative of a more complex reality).

12. *See, e.g.*, Ragnar E. Löfstedt & David Vogel, *The Changing Character of Regulation: A Comparison of Europe and the United States*, 21 RISK ANALYSIS 399 (2001).

13. *Id.*

14. *See, e.g.*, Peter J. May, *Social Regulation*, *in* THE TOOLS OF GOVERNMENT: A GUIDE TO THE NEW GOVERNANCE (Lester M. Salamon ed., 2002).

15. *See, e.g.*, Richard A. Epstein, *Contract, not Regulation: UCITA [Uniform Computer Information Transactions Act] and High-Tech Consumers Meet Their Consumer Protection Critics*, *in* CONSUMER PROTECTION IN THE AGE OF THE 'INFORMATION ECONOMY' (Jane K. Winn ed., forthcoming 2006).

16. A complete description of recent consumer protection legislation passed in the EU can be found on the Directorate General for Health and Consumer Affairs Web site for Consumer Affairs issues at http://www.europa.eu.int/comm/consumers/index_en.htm (last visited July 20, 2006).

17. Now succeeded by *eEurope 2005: An Information Society for All, see* COM (2002) 263 final (May 28, 2002), *available at* http://europa.eu.int/eur-lex/en/com/cnc/2002/com2002_0263en01.pdf (last visited November 14, 2006).

18. *See generally* CHRISTOPHER KUNER, EUROPEAN DATA PRIVACY LAW AND ONLINE BUSINESS (2003).

Name /thl_tbl621_3058006/winn/Mp_4 12/12/2006 04:42PM Plate # 0 pg 4 # 4

another form of social regulation.[19] The EU social regulation approach to consumer markets is closer to the approaches taken in Canada,[20] Australia,[21] New Zealand,[22] Japan,[23] and other developed economies[24] than the U.S. competition-oriented approach.[25]

Many elements of EU consumer protection policy appear to be motivated by a desire to level the playing field among consumers to ensure that social rather than economic policy objectives are met.[26] By mandating a high minimum level of protection, EU online consumer contract law forces all merchants to internalize high compliance costs and constrains the range of possible innovation[27] in marketing channels.[28] By contrast, U.S. online consumer contract law sets a much lower mandatory minimum level of protection,[29] which appears to have opened the door to more rapid growth and greater innovation in online retail marketing.[30] If the U.S. approach has allowed more of the costs associated with innovation to be borne by individual consumers than the EU approach, then it would not be the first time that changes in the interpretation of American contract law have had the effect of subsidizing the growth of new markets.[31]

19. For example, within the Commission, consumer protection matters are handled by the Health and Consumer Protection Directorate General, which also oversees health and food safety regulations. *See* http://ec.europa.eu/dgs/health_consumer/index_en.htm.

20. *See, e.g.*, INDUSTRY CANADA, INTERNET SALES CONTRACT HARMONIZATION TEMPLATE (2001), *available at* http://strategis.ic.gc.ca/epic/internet/inoca-bc.nsf/vwapj/Sales_Template.pdf/$FILE/Sales_Template.pdf.

21. *See, e.g.*, Trade Practices Act, 1974 (Austl.), *available at* http://www.austlii.edu.au/au/legis/cth/consol_act/tpa1974149/.

22. *See, e.g.*, NEW ZEALAND MODEL CODE FOR CONSUMER PROTECTION IN ELECTRONIC COMMERCE (2000), *available at* http://www.consumeraffairs.govt.nz/policylawresearch/pdfpapers/model_code.pdf.

23. *See, e.g.*, Shōhisha keiyakuhō [Consumer Contract Act], Law No. 61 of 2000, *available at* http://www.cas.go.jp/jp/seisaku/hourei/data/CCA.pdf

24. *See, e.g.*, Unfair Contract Terms Act, Cap. 396 (1994) (Sing.), *available at* http://statutes.agc.gov.sg/.

25. The two different approaches need not necessarily be opposed to each other. Since it came to power in the UK in 1997, the Labour government has tried to find a "third way" that uses strong consumer protection laws as a mechanism to push UK industries to become more responsive to customer demands and thus more globally competitive. *See* DEPARTMENT OF TRADE AND INDUSTRY, MODERN MARKETS: CONFIDENT CONSUMERS, 1999, CM. 4410 (U.K.); DEPARTMENT OF TRADE AND INDUSTRY, EXTENDING COMPETITIVE MARKETS: EMPOWERED CONSUMERS, SUCCESSFUL BUSINESS (2005) (U.K.), *available at* http://www.dti.gov.uk/files/file23787.pdf.

26. GERAINT HOWELLS & STEPHEN WEATHERILL, CONSUMER PROTECTION LAW 3 (2d ed. 2005).

27. The UK government's official policy tries to embrace both protection and innovation: "[The government] want[s] a consumer regime that is fit for purpose for the 21st Century. A regime that will empower and protect consumers, support open, competitive and innovative markets, that is as fair to business as it is to consumers and that has the minimum regulation necessary to achieve these goals." *See* http://www.dti.gov.uk/consumers/policy/index.html.

28. This result can be thought of as "taxation by regulation." *See generally* Richard A. Posner, *Taxation by Regulation*, 2 BELL J. ECON. & MGMT. SCI. 22, 50 (1971).

29. For a summary of recent judicial decisions involving consumer complaints against online merchants, see Jane K. Winn, *Contracting Spyware by Contract*, 20 BERKELEY TECH. L.J. 1345 (2005).

30. Of course, many of these innovations ultimately fail. *See, e.g.*, Kent German, *Top 10 Dot-com Flops*, CNET.com, *available at* http://www.cnet.com/4520-11136_1-6278387-1.html.

31. *See generally* MORTON J. HORWITZ, THE TRANSFORMATION OF AMERICAN LAW, 1760–1860 (1977).

Name /thl_tbl621_3058006/winn/Mp_5 12/12/2006 04:42PM Plate # 0 pg 5 # 5

U.S. and EU protections for online consumers diverge not only in substance but also in how they are interpreted and enforced. The U.S. approach relies heavily on litigation as an enforcement mechanism, and the most frequently litigated issue has been whether the merchant has the right to reduce its own dispute resolution costs by limiting the consumer's access to the courts.[32] U.S. merchants engaged in Internet commerce with consumers routinely include an arbitration[33] or a choice-of-forum term in their standard form contracts to limit their exposure to litigation in remote forums, class action lawsuits, and punitive damage awards. Judicial decisions analyzing the effectiveness of various online contract formation mechanisms and the enforceability of various terms contained in standard form contracts often focus on these procedural provisions, and provide fragmentary or contradictory guidance with regard to other contract terms.[34] In Europe, consumers face fewer obstacles to bringing a lawsuit in a local forum against a remote vendor because standard form contract terms that impede consumers' rights of redress are invalidated as unfair.[35] However, litigation between individual consumers and merchants has become a less significant source of law even in a common law jurisdiction such as England because regulatory agencies play a greater role than courts in providing authoritative guidance regarding the application of consumer protection laws to online transactions.[36] Regulatory agencies also play a greater role in enforcing online consumer contract law protections, and in publicizing their efforts, than do their counterparts in the U.S.[37]

32. *See infra* text at notes 113–18.

33. Contrast the U.S. approach to the UK position where under Section 91 of the Arbitration Act of 1996, *available at* http://www.opsi.gov.uk/ACTS/acts1996/1996023.htm, a compulsory arbitration clause is automatically unfair if it relates to claims of GBP£5,000 or less. Unfair Arbitration Agreements (Specified Amount) Order 1999, *available at* http://www.opsi.gov.uk/si/si1999/uksi_19992167_en.pdf. Inclusion of such a term is always "unfair."

34. For recent attempts to make sense of the case law developing in this area, *see generally* Christina L. Kunz, Maureen F. Del Duca, Heather Thayer & Jennifer C. Debrow, *Click-Through Agreements: Strategies for Avoiding Disputes on Validity of Assent*, 57 BUS. LAW. 401 (2001); Christina L. Kunz, John E. Ottaviani, Elaine D. Ziff, Juliet M. Moringiello, Kathleen M. Porter & Jennifer C. Debrow, *Browse-Wrap Agreements: Validity of Implied Assent in Electronic Form Agreements*, 59 BUS. LAW. 279 (2003).

35. *See, e.g.*, Card No. IT001105 of the European Database on Case Law Concerning Unfair Contract Terms, *available at* https://adns.cec.eu.int/CLAB/SilverStream/Pages/pgHomeCLAB.html, discussed *infra* text at note 98; *see generally* Christopher R. Drahozal & Raymond J. Friel, *Consumer Arbitration in the European Union and the United States*, 28 N.C. J. INT'L L. & COM. REG. 357 (2002).

36. For example, the UK's Office of Fair Trading ("OFT") publishes case reports in Unfair Contract Terms Bulletins detailing cases where the OFT has obtained significant changes in consumer contract terms. *See., e.g.*, OFFICE OF FAIR TRADING, PUBL'N NO. 768, UNFAIR CONTRACT TERMS BULLETIN 29 (2005) (U.K.), *available at* http://www.oft.gov.uk/NR/rdonlyres/7E28C309-9E11-45C5-A3A7-07630B9876AD/0/oft768.pdf and published at http://www.crw.gov.uk.

37. *See infra* text accompanying notes 75–76 for discussion of UK OFT enforcement authority. While the U.S. Federal Trade Commission ("FTC") may have the authority to regulate overreaching by merchants in business to consumer contracts because contract terms are unfair, it is unlikely to do so in light of the current FTC Policy Statement on Unfairness (Letter from the Federal Trade Commission to Hon. Wendell Ford and Hon. John Danforth, Committee on Commerce, Science, and Transportation, United States Senate (Dec. 17, 1980), *reprinted in In re Int'l Harvester Co.*, 104 F.T.C. 949, 1073 (1984), *available at* http://www.ftc.gov/bcp/policystmt/ad-unfair.htm). *See* J. Howard Beales, III, The FTC's Use of Unfairness Authority: Its Rise, Fall and Resurrection, *available at* http://www.ftc.gov/speeches/beales/unfair0603.htm.

Name /thl_tbl621_3058006/winn/Mp_6 12/12/2006 04:42PM Plate # 0 pg 6 # 6

Some of the most significant differences between EU and U.S. consumer contract law are attributable to the Unfair Contract Terms Directive,[38] which regulates form contracts offered by merchants to consumers whether online or offline. In addition, the Distance Selling Directive,[39] which regulates transactions between remote merchants and consumers, whether by means of television, telemarketing, the Internet, or other electronic communications media, and the Electronic Commerce Directive,[40] which promotes transparency and accountability in online commerce, have had a significant impact on business to consumer transactions. This article provides an overview of the provisions of these relevant directives and principles of EU law drawn from other sources, supplemented by examples of how national laws implementing them work in particular member states such as the UK and France.[41]

3. EU Consumer Protection Law and Policy

EU consumer protection law has expanded in recent years as part of the ongoing effort to overcome barriers to the integration of European markets and to promote fair and vigorous competition in national consumer markets. In addition, as well as citing the goal of harmonization of the laws across Europe, EU consumer protection law also strives to provide legal certainty to help drive forward the development of ecommerce.[42] The Single European Act of 1986[43] and the push to complete the internal European market by 1992 were strongly oriented toward the liberalization and strengthening of market mechanisms. The European commitment to strengthening consumer protection laws as an integral part of strengthening the internal European market was made explicit in the Treaty of Maastricht,[44] and strengthened in the Treaty of Amsterdam.[45] In addition, in 1997, the European Commission announced its intention to create a coherent legal frame-

38. UCT Directive, *supra* note 5.

39. Council Directive 97/7, 1997 O.J. (L 144) 19 (EC) [hereinafter "DS Directive"], *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:31997L0007:EN:HTML.

40. Council Directive 00/31, 2000 O.J. (L 178) 1 (EC) [hereinafter "EC Directive"], *available at* http://europa.eu/eur-lex/pri/en/oj/dat/2000/l_178/l_17820000717en00010016.pdf.

41. As a general rule, EU Directives do not affect the rights and obligations of individuals until the directive has been transformed into national law, so it is necessary to consider legislation transforming the terms of directives into national law to get a full and accurate impression of the relevant law. There are limited exceptions. *See, e.g.*, Case 41/74, Van Duyn v. Home Office, 1974 E.C.R. 1337 (ECJ held that only directives that establish clear and unconditional legal norms and do not leave normative discretion to the member states have direct effect; however direct effects are normally effective against governments, not private parties); Case C-106/89, Marleasing SA v. La Commercial Internacional de Alimentacion SA, 1990 E.C.R. I-4135 (national law must be interpreted in light of directives even if they have not yet been transformed into national law).

42. *See* Recital to EC Directive, *supra* note 40.

43. Single European Act, O.J. L 169/1 (1987), [1987] 2 C.M.L.R. 741.

44. Treaty on European Union, Feb. 7, 1992, 1992 O.J. (C 191) 1, *available at* http://eur-lex.europa.eu/en/treaties/dat/11992M/htm/11992M.html.

45. Treaty of Amsterdam Amending the Treaty on European Union, the Treaties Establishing the European Communities and Related Acts, Oct. 2, 1997, 1997 O.J. (C 340) 1, *available at* http://eur-lex.europa.eu/en/treaties/dat/11997D/htm/11997D.html; Comprehensive Guide to the Treaty of Amsterdam, *available at* http://europa.eu/scadplus/leg/en/s50000.htm.

Name /thl_tbl621_3058006/winn/Mp_7 12/12/2006 04:42PM Plate # 0 pg 7 # 7

work within Europe for electronic commerce by the year 2000.[46] In recent years, the volume of new EU consumer protection legislation has slowed, but new legislation has not altogether stopped.[47]

The definition of consumer differs under EU and U.S. law. Under U.S. law, a consumer transaction is commonly defined as one undertaken by a natural person for goods or services for personal, family, or household use.[48] By contrast, most European countries define a consumer as someone acting outside her trade or profession.[49] Consequently, even merchants and professionals acting outside their professions may be protected by European law.[50] The European Court of Justice ("ECJ") has set limits on the ability of merchants in some countries to use the technicalities of consumer protection law to invalidate contracts with other merchants. For example, the ECJ held that a merchant who contacted other merchants to offer advertising for the sale of their businesses was not to required to give notice of a right to rescind the contracts within a certain number of days, even though the French government, the European Commission, and the Advocate General of the ECJ all argued that those protections should apply.[51] The ECJ similarly held that a son who had provided a personal guarantee on the business debts of his father was not entitled to challenge the validity of the guarantee on the ground that he had not been given any notice of a right to rescind.[52] The focus of the court was on the fact that the debts secured by the guarantee were incurred in the operation of a business, even though the guarantor was acting in an individual capacity.

Greater harmonization in Europe might be helpful in preventing some countries, notably Germany, from establishing too low a standard of competence for consumers and, as a result, significantly raising the compliance burdens on merchants. When trade associations representing established merchants allege unfair competition law violations by upstart competitors, a common ploy has been to ask courts to require all merchants to treat consumers as simpletons. The German Supreme Court upheld a German agency's ban on Lands' End advertising in Germany that included an "unconditional guarantee" on the ground that adver-

46. *A European Initiative in Electronic Commerce*, COM (1997) 157 final (June 16, 1997), *available at* http://cordis.europa.eu/esprit/src/ecomcom.htm.

47. For example, in 2005, the EU passed the Unfair Commercial Practices Directive, harmonizing and updating the law of unfair and deceptive trade practices in member states. *See* Giuseppe Abbamonte, *The Unfair Commercial Practices Directive: an example of the new European consumer protection approach*, COLUM. J. EUR. L. (forthcoming 2006) (on file with *The Business Lawyer*).

48. *See* 15 U.S.C. § 1602(h) (2000).

49. Brussels Convention 13(1) states that a consumer contract is one engaged in by a person outside his or her trade or profession, Case 150/77, Société Bertrand v. Paul Ott KG, 1978 E.C.R. 1431; Article 2(b) of the Unfair Contract Terms Directive defines a consumer as "any natural person who . . . is acting for purposes which are outside his trade, business or profession," UCT Directive, *supra* note 5, at art. 2(b).

50. HOWELLS & WEATHERILL, *supra* note 26, at 270.

51. Case C-361/89, Criminal Proceedings against Patrice Di Pinto, 1991 E.C.R. I-1189.

52. Case C-45/96, Bayerische Hypotheken-und Wechselbank AG v. Edgar Dietzinger, 1998 E.C.R. I-1199.

Name /thl_tbl621_3058006/winn/Mp_8 12/12/2006 04:42PM Plate # 0 pg 8 # 8

tising such a term violated German trade practices law.[53] An agency that monitors unfair advertising successfully sued the Lands' End catalog merchant for its unconditional money back guarantee, arguing that its offer amounted to "unfair competition."[54] The court outlawed the advertisements, which had met no resistance in Japan or England.[55] Other U.S. merchants in Germany have suffered similar indignities: Tupperware and Zippo have been banned from offering lifetime guarantees in Germany, while, also in Germany, Wal-Mart was not allowed to compensate customers who found better prices on the same products in competitors' stores.[56]

The ECJ has held that merchants are entitled to assume that they are dealing with a "reasonably well-informed, reasonably observant, and circumspect" consumer.[57] In other words, the ECJ expects that consumers take some responsibility to protect their own interests. The ECJ consequently has been skeptical regarding claims that advertisements are deceptive. In a case involving advertisements for Nissan cars, the ECJ held that an advertisement is misleading only if it is shown that a significant number of consumers to whom the advertisement is addressed are actually misled by it, or that if an additional fact had been made known to them, they would not have entered into a transaction with the advertiser.[58] The German Trade Protection Society Against Bad Commercial Practices tried to stop a French cosmetics company from distributing a brochure stating that consumers could "save up to 50 percent and more on 99 of your favorite Yves Rocher products" with the old price crossed out and a new lower price printed alongside in large red characters.[59] The Society argued that the brochure violated a German trade practices law prohibiting price comparisons that were "eye-catching," and the EJC struck down the German law. It held that German law unduly restricted free movement of goods in the common European market because the law was not proportionate to goals pursued—to protect consumers from the special lure of advertisements containing price comparisons.

53. Peggy Hollinger & Jeremy Grant, *Land's End to contest German ban in EU court*, FINANCIAL TIMES (LONDON), Sept. 6, 1999, at 2.

54. The argument was based on the premise that consumers are induced to pay higher prices when offered a "money back guarantee." Michael S. Greve, *New Insights from the Old Continent,* FEDERALIST OUTLOOK, Jan. 1, 2002, *available at* http://www.aei.org/publications/pubID.13528/pub_detail.asp.

55. John Schmid, *Germans Feel Tough New Climate of Competition*, THE TOCQUEVILLE CONNECTION (Nov. 5, 1999), *available at* http://www.adetocqueville.com/cgi-binloc/searchTTC.cgi?displayZop+2542.

56. Doris Hajewski, *Lands' End learns that, in Germany, good service is guaranteed trouble*, MILWAUKEE J. SENTINEL (WIS.), Sept. 8, 1999, at 1.

57. REINER SCHULZE, HANS SCHULTE-NOLKE & JACKIE JONES, A CASEBOOK ON EUROPEAN CONSUMER LAW 226 (2002); Case C-210/96, Gut Springenheide, 1998 E.C.R. I-4657, ¶ 31.

58. Case C-373/90, Criminal Proceedings against X (Nissan), 1992 E.C.R. I -131, ¶¶ 15, 16, *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:61990J0373:EN:HTML; *see also* Case C-470/93, Verein gegen Unwesen in Handel und Gewerbe Köln e.V. (association for combating unfair competition) v. Mars GmbH, 1995 E.C.R. I-1923, ¶ 24, *available at* http://europa.eu.int/eur-lex/lex/LexUriServ/LexUriServ.do?uri=CELEX:61993J0470:EN:HTML (challenged Mars ice cream bar promotion indicating "+10%" in colored part of wrapping, but colored part describing the promotion occupied more than 10% of wrapper; held not misleading to reasonably circumspect consumer).

59. Case C-126/91, Schutzverband gegen Unwesen in der Wirtschaft e.V. v. Yves Rocher GmbH, 1993 E.C.R. I-2396, ¶¶ 12, 14, *available at* http://europa.eu.int/eur-lex/lex/LexUriServ/LexUriServ.do?uri=CELEX:61991J0126:EN:HTML.

Name /thl_tbl621_3058006/winn/Mp_9 12/12/2006 04:42PM Plate # 0 pg 9 # 9

4. Unfair Contract Terms Law

Several European countries have enacted laws regulating "unfair" terms in standard form contracts used in consumer transactions. For example, in 1977 the UK had enacted the Unfair Contract Terms Act ("UCTA"), which limits the extent to which breach of contract, negligence, or other breaches of duty can be excluded by contract.[60] The UCTA therefore limits the enforcement of "exclusion clauses" (which are generally equivalent to "disclaimers" under U.S. law) in some instances altogether and in others to the extent they are not "fair and reasonable."[61] The UCTA applies not only to consumer transactions but also to certain business transactions.[62] However, not all EU member states enacted similar laws, so the Directorate General (DG) for Health and Consumer Affairs developed a directive, enacted in 1993, to harmonize consumer unfair contract terms laws in Europe.[63] The Directive goes far beyond the scope of the UCTA as it regulates terms which are generally seen as "unfair." The fundamental premise of the Directive is that general contract law is not adequate to protect consumers from overreaching by merchants, and that member states should adopt laws reflecting the consensus embodied in the Directive with regard to what constitutes "unfairness" in such situations where there is an inherent inequality of bargaining power.[64] This proposed regulation of unfair contract terms establishes a much lower threshold for intervention by courts and regulators than unconscionability under U.S. contract law or federal and state regulation of unfair and deceptive trade practices.[65] The Directive provides that contract terms not individually negotiated are unfair if they create a significant imbalance, to the consumer's detriment, between the rights and obligations of the contracting parties.[66] If a contract term is drafted in advance and the consumer has no influence over the substance of the term, then it is not individually negotiated, and hence subject to review based on substantive fairness.[67] Annex 1 to the Directive contains a non-exclusive list of terms that may be deemed unfair.[68]

60. *See* http://statutes.agc.gov.sg/non_version/cgi-bin/cgi_retrieve.pl?&actno=Reved-396&date=latest&method=part.

61. This test is referred to as the "reasonableness test," which is defined in Section 11 of UCTA.

62. *Id.* UCTA sections 2–7 apply to transactions carried out in the "course of business" so they do not apply to private contracts between individuals.

63. UCT Directive, *supra* note 5. Member States were expected to pass laws implementing its provisions by the end of 1994.

64. This focus on overreaching by merchants is in direct conflict with the general English law concept of "freedom of contract." *See generally* Howells & Weatherill, *supra* note 26, at 261.

65. Unconscionability generally requires a showing of both serious procedural misconduct and substantive overreaching. Restatement (Second) of Contracts § 208 (1981); U.C.C. § 2-302 (2002); *see generally* E. Alan Farnsworth, Contracts § 4.28 (4th ed. 2004).

66. UCT Directive, *supra* note 5, at art. 3.

67. *Id.* at art. 2.

68. The Annex provides examples of unfair terms, including limiting liability for death or personal injury resulting from an act or omission by the seller; disclaiming liability for total or partial non-performance or inadequate performance by the seller; binding the consumer while making the obligations of the seller conditional or optional; providing for excessive liquidated damages to be paid by the consumer in the event of breach; allowing the seller to terminate its obligations without giving the consumer the same right; allowing the seller to terminate a contract of indefinite term without

Name /thl_tbl621_3058006/winn/Mp_10 12/12/2006 04:42PM Plate # 0 pg 10 # 10

Under the Directive, the nature of the goods or services covered by the contract, the circumstances surrounding the formation of the contract, and the other terms in the contract or in another contract to which it relates are taken into account in assessing the unfairness of a term.[69] Contract terms offered to consumers in writing must always be drafted in plain language and where there is doubt as to the meaning of a term, the interpretation most favorable to the consumer prevails.[70] On their face, the plain language rules appear to have little substantive effect; however, the extent of their practical application is significant. Terms that may mislead or not be understood by consumers are open to challenge as unfair. In the UK, the OFT has made clear that consumers must be capable of understanding terms without resort to legal advice.[71] The OFT confirms that consumer contracts should use "ordinary words" to the extent possible and with their "normal meaning." Further, sentences should be short, and the text broken up with easily understandable subheadings "covering recognizably similar issues."[72] In France the Directive is built upon further by domestic legislation which stipulates that the use of the French language is mandatory.[73] In the event terms in a consumer contract are found to be unfair, those terms are not binding on consumers, although the remainder of the contract is enforceable.[74]

Under the UK's implementation of the Directive,[75] a consumer is not bound by a standard term in a contract with a seller or supplier if that term is unfair. As such, an unfair term does not form a part of the contract and the contract is potentially voidable. If a business refuses to accept that a term is unfair and unenforceable, then the consumer can seek an injunction from a court or other recognized body to not be bound by the term or to void the contract. In the UK, the Office of Fair Trading ("OFT") and other regulatory bodies such as the Trading Standards Services are granted the authority to enjoin in the courts businesses

reasonable notice or adequate grounds; requiring an action by the consumer to avoid liability; irrevocably binding the consumer to terms he or she had no real opportunity to review before the contract was formed; allowing the seller to alter the terms of the contract unilaterally without reference to conditions specified in the contract; allowing the seller to change delivery or price terms without giving the consumer the right to opt out of the modified contract; allowing the seller the exclusive right to interpret the contract; requiring the consumer to fulfill all of his or her obligations even if the seller has not fulfilled its obligations; and limiting the consumer's access to legal process by, for example, requiring arbitration.

69. UCT Directive, *supra* note 5, at art. 4.

70. *Id.*, at art. 5.

71. In the Guidance, the OFT confirms that "[i]t is our view that technical jargon such as references to 'indemnity' can have onerous implications of which consumers are not likely to be aware without such [legal] advice." *See* the Guidance, *supra* note 6, § C.10, at 68–69.

72. *Id.*, § C.8, at 68.

73. Law No. 94-665 of August 4, 1994, Journal Officiel de la République Française [J.O.] [Official Gazette of France], August 4, 1994 (known as Loi Toubon for the Minister of Culture at the time it was enacted), *available at* http://www.culture.gouv.fr/culture/dglf/lois/loi-fr.htm.

74. *Id.*, at art 6.

75. Unfair Terms in Consumer Contracts Regulations 1994, S.I. 1994/3159 (U.K.), *available at* http://www.opsi.gov.uk/si/si1994/Uksi_19943159_en_1.htm, as subsequently amended by the 1999 Regulations of the same name (S.I. 1999/2083) [hereinafter "the Regulations"], *available at* http://www.opsi.gov.uk/si/si1999/19992083.htm.

Name /thl_tbl621_3058006/winn/Mp_11 12/12/2006 04:42PM Plate # 0 pg 11 # 11

that continue to use terms that are unfair. That is coupled with an obligation on the OFT to give reasons as to its decision regarding the fairness of the term.[76]

In the UK, the test of unfairness is not whether the contractual term is deceitful. A standard term is unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract.[77] Recent case law has confirmed that the "requirement of good faith . . . is one of fair and open dealing."[78]

Unfair Terms in Consumer Contracts Regulations 1999 illustrates the test of unfairness and lists some types of terms that can be unfair.[79] The Regulations contain 17 categories of terms that can be unfair. This is a "grey" list. The OFT Guidance states that "terms are under suspicion of unfairness if they have the same purpose or can produce the same result as terms on the 'grey' list. They do not have to have the same form or mechanism."[80] Terms that may be unfair are summarized by the OFT in its guidance for consumers[81] along the following lines:

- Consumers being misled about a contract or their legal rights;
- Consumers being denied full redress if the contract is breached;
- Consumers being bound by a contract unfairly;
- The business not having to perform obligations;
- Consumers unfairly losing pre-payments if the contract is cancelled;
- The business varying the terms after contract formation; and
- Consumers being subject to unfair penalties.

English legal commentators have criticized the implementation of the Directive because the UCTA was not repealed when the Regulations were enacted, which has had the effect of leaving in place two somewhat incompatible sets of laws governing unfair contract terms.[82] At some point in the future, a single unified regime in the UK is likely, although in 2006 nothing specific has of yet been proposed by Parliament.

76. *Id.*, Regulations 12(1), 10(2).
77. *Id.*, Regulation 5(1).
78. Director General of Fair Trading v. First National Bank Plc [2002] 1 A.C. 481, 494 (Eng.).
79. *See* Schedule 2 to the Regulations, *supra* note 75.
80. *See* the Guidance, *supra* note 6, § C.5.
81. *See generally* Guidance for Consumer Advisers on the Unfair Terms in Consumer Contracts Regulations 1999, Sept. 8, 2000, *available at* http://www.oft.gov.uk/NR/rdonlyres/720A136C-9435-40C4-8549-7BDFCCF85B70/0/oft143.pdf.
82. *See, e.g.*, RICHARD CHRISTOU, BOILERPLATE PRACTICAL CLAUSES 151 (4th ed. 2005), on the differences in scope between the 1977 Act (UCTA) and the 1999 Regulations. At the request of the UK's Department of Trade and Industry, the Law Commission for England and Wales and the Scottish Law Commission (the "Law Commissions") recently examined the two regimes to consider harmonization in regard to their application in relation to consumers. The Law Commissions have published a report that concludes that although UCTA and the 1999 Regulations have similar effects, they are not consistent and some provisions overlap, making their combined application unnecessarily complex and contradictory. LAW COMMISSION, UNFAIR TERMS IN CONTRACT, 2005, Cm. 6464 (U.K.) (jointly with SCOTTISH LAW COMMISSION), *available at* http://www.lawcom.gov.uk/docs/lc292(1).pdf.

Name /thl_tbl621_3058006/winn/Mp_12 12/12/2006 04:42PM Plate # 0 pg 12 # 12

After the Directive was enacted in 1993, the Health and Consumer Affairs Directorate of the Commission created the European Database on Case Law Concerning Unfair Contract Terms ("CLAB database"), which is accessible to the public on the Internet.[83] The CLAB database was launched to assist the Commission in monitoring national case law developments based on the Directive and to provide information on judicial and administrative proceedings, including settlements and arbitration awards. Many of the cases in the database were brought by consumer protection advocacy groups in "group litigation" or "representative proceedings," which EU standing rules generally authorize for the redress of consumer grievances rather than U.S.-style class action litigation.[84] Cases in the database dealing with claims against Internet merchants include:

- On the ground of unfairness generally, an Austrian consumer protection group blocked the use by an Internet service provider of a contract term that required the consumer to agree to be bound by the terms of software licenses when he or she had not yet been given access to those terms,[85] and by a term that treated the contract as formed at the moment the online access started, while reserving the service provider's right to withdraw from the contract within 14 days for any reason;[86]
- On the ground of unfairness of the type described in Annex 1(q) of the Directive,[87] an Austrian consumer protection group blocked the use by an Internet service provider of a term making a consumer liable for 20% of the amount due under the contract for early termination even with cause;[88]
- On the ground of unfairness of the type described in Annex 1(b),[89] an

83. European Database on Case Law Concerning Unfair Contract Terms, *available at* https://adns.cec.eu.int/CLAB/SilverStream/Pages/pgHomeCLAB.html [hereinafter "CLAB database"].

84. *See generally* Edward F. Sherman, *American Class Actions: Significant Features and Developing Alternatives in Foreign Legal Systems*, 215 F.R.D. 130 (2003).

85. Card No. AT000794, CLAB database, *supra* note 83. The clause was also held to be unenforceable because it was grossly disadvantageous to the consumer under section 879, paragraph 3 of the Austrian Civil Code (ABGB); non-transparent under section 6, paragraph 3 of the Consumer Protection Law (KSchG); and so surprising that a consumer would not expect it to be in the contract under section 864a of the ABGB.

86. Card No. AT001387, CLAB database, *supra* note 83. The clause was also held to violate section 6, paragraph 2, subparagraph 1 of the Consumer Protection Act (KSchG) because it purported to give the internet service provider authority to terminate the contract without justification. Such a clause would only be enforceable if it had been individually negotiated by the merchant and the consumer, not contained in a standard form contract.

87. UCT Directive, *supra* note 5. Annex (q) prohibits "excluding or hindering the consumer's right to take legal action or exercise any other legal remedy, particularly by requiring the consumer to take disputes exclusively to arbitration not covered by legal provisions, unduly restricting the evidence available to him or imposing on him a burden of proof which, according to the applicable law, should lie with another party to the contract." *Id.*

88. Card No. AT001396, CLAB database, *supra* note 83. The clause was also held to be unenforceable because it was grossly disadvantageous under section 1336 of the ABGB because it purported to limit the authority of a court to modify the amount of liquidated damages.

89. Annex 1(b) prohibits "inappropriately excluding or limiting the legal rights of the consumer vis-à-vis the seller or supplier or another party in the event of total or partial non-performance or inadequate performance by the seller or supplier of any of the contractual obligations, including the option of offsetting a debt owed to the seller or supplier against any claim which the consumer may have against him." UCT Directive, *supra* note 5.

Name /thl_tbl621_3058006/winn/Mp_13 12/12/2006 04:42PM Plate # 0 pg 13 # 13

Austrian consumer protection group stopped an Internet service provider from disclaiming warranty liability for its services;[90]

- On the ground of unfairness of the type described in Annex 1(o),[91] an Austrian consumer protection group prevented an Internet service provider from denying consumers the right to withhold payments for its failure to provide services or for breach of warranty claims;[92]
- On the ground of unfairness of the type described in Annex 1(j),[93] a French consumer protection group prevented an Internet merchant from using a term that purported to allow it to change its general sales terms at any time;[94]
- On the ground of unfairness generally, a French consumer group caused an Internet merchant to accept returns of merchandise during the period of the consumer's right of return without regard to whether the goods had been used after the merchant had tried to limit returns during that period to unused merchandise only;[95]
- On the ground of unfairness of the type described in Annex 1(q), a French consumer group stopped an Internet merchant from requiring a consumer to note clearly on the delivery slip why the product was defective as a condition to the consumer's right to return the product for a refund;[96]
- On the ground of unfairness of the type described in Annex 1(b), a French consumer protection group prevented an Internet merchant from disclaiming liability for late delivery of goods;[97] and

90. Card No. AT001738, CLAB database, *supra* note 83. The clause was also held to violate Section 9 of the KSchG, which prohibits disclaimers of certain warranties implied in law; *see also* Card Nos. AT001740, AT002242, AT002243, AT002248, and AT002250, CLAB database, *supra* note 83 (finding contract terms unenforceable with reference to Annex 1(b) and Austrian warranty law).

91. UCT Directive, *supra* note 5. Annex 1(o) prohibits "obliging the consumer to fulfill all his obligations where the seller or supplier does not perform his." *Id.*

92. Card No. AT001738, CLAB database, *supra* note 83. The clause was also held to violate Section 6 of the KSchG, which preserves a consumer's right to withhold payments if a merchant fails to perform its duties under a contract.

93. UCT Directive, *supra* note 5. Annex 1(j) prohibits "enabling the seller or supplier to alter the terms of the contract unilaterally without a valid reason which is specified in the contract." *Id.*

94. Card No. FR001081, CLAB database, *supra* note 83. The clause was also held to violate section L 132-1 of the French Consumer Code, which prohibits a merchant from modifying the terms of a contract unilaterally without a valid justification. However, in Card No. FR1080, CLAB database, *supra* note 83, a French court held that a contract term used by the same Internet merchant informing consumers that they would be bound by its standard terms and providing an opportunity to review those terms was not unfair; and in Card No. FR1082, CLAB database, *supra* note 83, the same merchant was allowed to disclaim liability if goods sold had slight variations from the photographs of them provided on its Web site.

95. Card No. FR001084, CLAB database, *supra* note 83. The term was also invalid because it failed to recognize the consumer's seven-day right to return goods purchased from a distance seller. *See infra* text at notes 121–33 for a discussion of the DS Directive.

96. Card No. FR001085, CLAB database, *supra* note 83. The term was also invalid under article L 133-3 of the French Commercial Code and point 19 of summary recommendation n° 91-02 dated March 23, 1990, regarding contract terms that hinder the enforcement of legal rights by consumers.

97. Card No. FR001086, CLAB database, *supra* note 83; *see also* Card No. FR001088, CLAB database, *supra* note 83 (Internet travel service cannot shift liability for increases in fares to consumers).

Name /thl_tbl621_3058006/winn/Mp_14 12/12/2006 04:42PM Plate # 0 pg 14 # 14

- On the ground of unfairness of the type described in Annex 1(q), an Italian consumer successfully challenged a merchant's choice of forum clause specifying the forum as where the merchant's place of business was located.[98]

When U.S. Internet retail merchants decide to expand their services into European markets, U.S. managers may have a strong desire to use as many of the standard contract terms developed for U.S. markets as possible, and to limit the number of changes they make in their established business processes, especially if changes necessitate recoding and redesign of the merchant's Web site. This reluctance to localize contract terms and business processes may prove to be a costly error after European operations have been set up. The experience of AOL in France[99] shows the magnitude of changes that may be required to localize a U.S. business model and bring it into compliance with EU consumer protection law.

In 2002, the French Unfair Contract Terms Commission[100] held public hearings attended by both industry and consumer representatives. In 2003, it subsequently published a recommendation listing 28 types of clauses that were used by French Internet service providers in their standard form Internet access agreements with consumers which it deemed "unfair" under French law pursuant to French implementation of the Directive.[101] Although the French Unfair Contract Terms Commission's recommendations are not binding on French courts, in practice they are influential, and courts treat such recommendations with considerable deference when called upon to interpret French unfair contract terms law.[102] After these recommendations were issued, AOL revised and replaced the standard form consumer agreements it used in France. However, apparently relying on the fact that the Unfair Contract Terms Commission's recommendations were not binding, AOL elected not to act on all of them. Importantly, AOL also continued to apply the unrevised 2000 version of its standard form agreement to some of its existing customers. The Union Fédérale des Consommateurs-Que Choisir ("UFC")[103] brought suit against AOL, claiming that 36 terms found in the 2000 and the revised 2003 version of AOL's standard form agreement violated French law. As a national organization representing consumer interests, the UFC is authorized under French law to bring suit on behalf of French consumers collectively using

98. Card No. IT001105, *supra* note 35.

99. Although not a U.S. business, a similar case in France involving the internet service provider Tiscali illustrates how unfair contract principles were applied to online contracts. *See* R.G. N° 04/02911, Tribunal de grande instance [T.G.I.] [ordinary court of original jurisdiction] Paris, 1e ch., Apr. 5, 2005, tgip050405 (Fr.), *available at* http://www.clauses-abusives.fr/juris/tgip050405.pdf (24 out of 25 clauses challenged were deemed "unfair").

100. For more information about the La Commission des Clauses Abusives, *see* http://www.clauses-abusives.fr/.

101. Recommendation 03-01 (2003), *available at* http://www.clauses-abusives.fr/recom/03r01.htm.

102. Franklin Attorneys at Law, Court Rules Internet Access Agreement Terms Invalid, International Law Office.com, Mar. 10, 2005, *available at* http://www.internationallawoffice.com (copy on file with *The Business Lawyer*).

103. More information about the UFC is available at its Web site, www.quechoisir.org.

Name /thl_tbl621_3058006/winn/Mp_15 12/12/2006 04:42PM Plate # 0 pg 15 # 15

the "representative action" process.[104] Although AOL was the first Internet service provider to be tested by a French consumer rights association in this way, UFC has subsequently successfully brought suit against several French ISPs whose contract terms similarly did not comply with the Commission's recommendations.[105]

In 2004, the Tribunal de Grande Instance in the Paris suburb of Nanterre found that 31 of the 36 terms in the AOL agreements were either unfair or illegal and therefore null and void under French law.[106] The trial court found that the following terms were unenforceable against the consumer because they were unfair:

- The subscriber continuously must update his or her personal information, and the failure to do so terminates the subscriber agreement automatically and without notice;
- Tacit acceptance by the subscriber of the general conditions on use of the AOL Web site constitutes acceptance;
- The subscriber's sole remedy in the event of breach by AOL is termination of the subscriber agreement;
- The assumption that e-mail notices have been accepted two days after delivery;
- AOL's right to share the subscriber's personal data with third parties without his or her prior consent;
- AOL's unilateral right to modify the agreement, payment terms, and the subscriber's user name at AOL's discretion;
- AOL's right to terminate the agreement without cause, or to suspend or terminate the agreement without prior notice for minor breaches by the subscriber;
- AOL's right to bill for the remaining term after early termination by the subscriber; finding this term unfair because there was no provision permitting the subscriber to terminate early for cause without paying for the remaining term;
- AOL's right to add 15 seconds to each invoiced connection as well as charging in full for each service minute used; and
- AOL's right to disclaim liability for service interruptions, errors, and other failures.[107]

In addition, and more seriously for AOL, the trial court held the following terms to be illegal and therefore null and void:

104. La loi du 18 Janvier 1992 sur l'action en représentation conjointe.

105. *See Les principales clauses abusives et illicites, available at* http://www.quechoisir.org/Enquete.jsp;jsessionid=BC9E752D11BBEFD25B34FC9DF214AECF.tomcat-1?id=Ressources:Articles:BA0028CF57BE4F24C12571D800652548&catcss=TEL000&categorie=NoeudPClassement:80ECC2565681E625C1256F0100348CB8.

106. R.G. N° 02/03156, Tribunal de grande instance [T.G.I.] [ordinary court of original jurisdiction] Nanterre, 1e ch., June 2, 2004, tgin020604 (Fr.), *available at* http://www.clauses-abusives.fr/juris/tgin020604.pdf; Bradley Joslove & Andréi Krylov, *Standard American Business to Consumer Terms and Conditions in the EU*, 18 MICH. INT'L LAW. 1 (2005), *available at* http://www.michbar.org/international/pdfs/Spring05.pdf.

107. Joslove & Krylov, *supra* note 106, at 2–3.

Name /thl_tbl621_3058006/winn/Mp_16 12/12/2006 04:42PM Plate # 0 pg 16 # 16

- AOL's unilateral right to modify the agreement, even though that right was qualified by a duty to provide 30 days prior notice and the subscriber's right to terminate the agreement within that period;
- Tacit acceptance by the subscriber of modifications in payment terms constitutes acceptance;
- Subscribers must contest an invoice within 90 days; otherwise the amount due becomes uncontestable;
- A non-exclusive assignment from the subscriber to AOL for all content put online by the subscriber;
- AOL's right to collect exceptional fees from subscribers in the event of late payment or termination of the agreement;
- AOL's right to terminate the agreement for risk of non-payment;
- AOL's cap on its liability equal to the last 6 months of fees; and
- AOL's right to reasonable attorneys' fees in the event of the subscriber's breach.[108]

The court confirmed that contract terms that provide no recourse against the merchant cause a significant imbalance to the detriment of the online consumer. The court required AOL to remove the unfair and illegal terms from its agreements, to post the judgment of the court on AOL's home page, and to e-mail it to all its subscribers.[109] On September 15, 2005, the Court of Appeals in Versailles affirmed in full the decision of the Nanterre trial court.[110]

It is interesting to note that because of the harmonizing effect of the Directive, should the AOL matter have been tested in the UK, many of the same conclusions as to the unfairness of the contract terms under consideration would likely have been reached. The recent experience of Dell Corporation Limited supports this conclusion. In the summer of 2006, it became clear that the online retailer had been cooperating with the OFT and, as a result of concerns raised by the OFT, agreed (according to the OFT's own press release) to "improve the transparency of its agreements with consumers."[111] Notably that included separating the terms applicable to consumers from those Dell was using with its business customers (something some advisors had been recommending for some time). With obvious parallels to the *UFC-Que Choisir* case in France, Dell agreed to amend terms that purported to: "limit[] liability for negligence to the price of the product"; "exclude[] liability for consequential loss arising out of breach of contract"; "ex-

108. *Id.* A German court recently held that in terms and conditions used by online merchants, terms that permit the substitution of goods, require original packing be returned with goods or the online terms and conditions to be amended at any time are illegal and without effect under Sec. 307 of German Civil Code. Landgericht Frankfurt am Main, August 23, 2006, case No. 2/2 O 404/05 (on file with *The Business Lawyer*).

109. *Id.*

110. AOL France v. UFC Que Choisir, R.G. N° 04/05564, Cour d'appel [CA][regional court of appeal] Versailles, 1e ch., Sept. 15, 2005, J.C.P. IV 150905, *available at* http://www.clauses-abusives.fr/juris/cav150905.pdf; *see also* Bradley Joslove, *French Appeals Court Upholds Decision Calling AOL's Contract Terms Unfair*, 10 ELECTRONIC COM. & L. REP. 1137 (Nov. 23, 2005).

111. *See* OFT Press Releases, July 6, 2006, *available at* http://www.oft.gov.uk/News/Press+releases/2006/111-06.htm.

Name /thl_tbl621_3058006/winn/Mp_17 12/12/2006 04:42PM Plate # 0 pg 17 # 17

clude[ ] liability for oral representations not confirmed in writing"; and "require[ ] the consumer to notify Dell of any errors in its confirmation of the consumer's order immediately."[112] The changes made by Dell in response to OFT pressure indicate that UK authorities are actively policing the Internet to ensure consumer contracts are both "fair" and compliant with consumer protection laws.

Many U,S. courts have reviewed service agreements less favorable to consumers than the service agreement reviewed in the *UFC-Que Choisir* case and have had no trouble enforcing them. The analysis in U.S. cases is generally more focused on the enforceability of a choice of forum or arbitration term, so the issues raised in the *UFC-Que Choisir* case are rarely analyzed in depth. In *Hill v. Gateway 2000, Inc.*,[113] Judge Easterbrook held that the preprinted form contract enclosed with a computer that the Hills had ordered by telephone from Gateway was enforceable because the purchaser had a right to return the computer within 30 days if the terms were not acceptable.[114] The following year, a court in New York reviewed substantially the same contract and held that, although the terms of the preprinted form contract were generally enforceable, the arbitration clause it contained was unconscionable and therefore unenforceable.[115] As a general rule, most U.S. courts reviewing disputes between online service providers and consumers find both that a contract has been formed and that the choice of forum or arbitration term is enforceable, even if enforcement of the contract and its terms prevents a consumer from initiating a class action or resorting to the courts, so long as the contract is not unconscionable.[116] While some U.S. courts have been sympathetic to consumer claims that service providers' terms should not be enforced because they are unfair,[117] such terms are unenforceable under the Directive.[118]

112. *Id.*

113. 105 F.3d 1147 (7th Cir.), *cert. denied,* 522 U.S. 808 (1997).

114. 105 F. 3d at 1150. *Accord* Filias v. Gateway 2000, Inc., No. 97 C 2523, 1998 U.S. Dist. LEXIS 20358 (N.D. Ill. Jan. 15, 1998) (not unconscionable to require arbitration, but substituted American Arbitration Association as arbitrator in lieu of the International Chamber of Commerce as specified in the contract); Edmond v. Gateway 2000, Inc., No. CV000275134S, 2001 WL 359176 (Conn. Super. Ct. Mar. 20, 2001); Westendorf v. Gateway 2000, Inc., No. 16913, 2000 WL 307369 (Del. Ch. Mar. 16, 2000) (unpublished); Falbe v. Dell, Inc., No. 04-C-1425, 2004 WL 1588243 (N.D. Ill. July 14, 2004).

115. Brower v. Gateway 2000, Inc., 676 N.Y.S.2d 569 (N.Y. App. Div. 1998).

116. For cases involving unsuccessful claims by consumers unhappy with wireless service providers, *see* Forrest v. Verizon Commc'ns, Inc., 805 A.2d 1007 (D.C. 2002); O'Quin v. Verizon Wireless, 256 F. Supp. 2d 512 (M.D. La. 2003); Net2Phone, Inc. v. Superior Court, 135 Cal. Rptr. 2d 149 (Cal. Ct. App. 2003). For cases involving unsuccessful claims by consumers unhappy with Internet service providers, *see* Groff v. America Online, Inc., No. PC 97-0331, 1998 WL 307001 (R.I. Super. May 27, 1998); Caspi v. Microsoft Network, L.L.C., 732 A.2d 528 (N.J. Super. Ct. App. Div.), *cert. denied*, 743 A.2d 851 (1999); Celmins v. America Online, 748 So. 2d 1041 (Fla. Dist. Ct. App. 1999); America Online, Inc. v. Booker, 781 So.2d 423 (Fla. Dist. Ct. App. 2001); Motise v. America Online, Inc., 346 F. Supp. 2d 563 (S.D.N.Y. 2004).

117. Williams v. America Online, No. 00-0962, 2001 WL 135825 (Mass. Super. Ct. Feb. 8, 2001); Licitra v. Gateway, Inc., 734 N.Y.S.2d 389 (N.Y. City Civ. Ct. 2001); Scarcella v. America Online, 798 N.Y.S.2d 348 (N.Y. City Civ. Ct. 2004) (unpublished); Lozano v. AT&T Wireless, No. CV02-00090-WJR(AJWx), 2003 U.S. Dist. LEXIS 21794, at *5 (C.D. Cal. Aug. 18, 2003) (an arbitration term contained in a "Welcome Guide" sent after a consumer had subscribed to a telephone service was not enforceable (citing Ting v. AT&T, 319 F.3d 1126, 1134 (9th Cir. 2003)).

118. UCT Directive, *supra* note 5, Annex 1(q); *see* Richard M. Alderman, *Pre-Dispute Mandatory Arbitration in Consumer Contracts: A Call for Reform*, 38 HOUS. L. REV. 1237, 1242–43 at n.18 (2001).

Name /thl_tbl621_3058006/winn/Mp_18 12/12/2006 04:42PM Plate # 0 pg 18 # 18

5. Other EU Online Consumer Protections

Recent European consumer protection legislation has concentrated on online selling. The legislation has created a complex matrix of rules of which an online merchant must be aware before it can create a compliant trading platform. In addition, there are many existing examples of other pieces of domestic consumer protection legislation which are applicable in the online context.[119] Given the uncertainty surrounding the application of older consumer laws to online markets, one objective behind recent European online consumer legislation has been to create a stable environment to inspire consumer confidence in ecommerce.[120] In 1997, the EU adopted the Distance Selling Directive ("DS Directive").[121] The DS Directive promotes online commerce by providing consumers with the guarantee that they are protected by their own national consumer protection regimes when they enter into distance-selling contracts. "Distance selling" is defined as a contract regarding goods or services whereby the contract between the consumer and the supplier is formed at a distance through communications technology.[122] The rights granted consumers through the enactment of the DS Directive's provisions into national law may not be waived by the consumer.[123] The DS Directive contains provisions similar to the U.S. FTC Mail Order Rule,[124] which requires that a transaction be completed within 30 days or notice of the delay be sent to the consumer and the consumer given the option to cancel the transaction.[125]

The DS Directive covers most forms of direct marketing, including catalog mail order, telephone sales, direct-response television sales, newspapers, magazines, and electronic communications such as e-mail. The DS Directive requires that a consumer be given certain minimum information both at the time of contract solicitation and at or before the time of delivery.[126] Written confirmation of information must be received by the consumer in some form of durable medium accessible to the consumer.[127] Consumers must, subject to certain exceptions, be given an unconditional "cooling-off" period of at least seven working days within which the consumer can cancel its order for most goods and receive a full refund.[128] The DS Directive takes a further step in that the seven-day cancellation period can be extended by up to three months if the online merchant fails to

119. For example, in the UK alone the Trade Descriptions Act 1968, the Consumer Credit Act 1974, the Sales of Goods Act 1974, the Supply of Goods and Services Act 1982, and the Consumer Protection Act 1987, to name but a few, all have a direct impact on online sales.

120. *See* Preamble of the EC Directive, *supra* note 40.

121. Directive 97/7/EC of the European Parliament and of the Council of 20 May 1997 on the protection of consumers in respect of distance contracts, Council Directive 97/7, 1997 O.J. (L 144) 19 (EC), *available at* http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:31997L0007:EN:HTML. The Member States had until May 20, 2000, to enact national laws embodying the terms of the DS Directive. DS Directive, *supra* note 39, at art. 15.

122. DS Directive, *supra* note 39, at art. 2.

123. *Id.*, at art. 12.

124. 16 C.F.R. § 435.1 (2006).

125. DS Directive, *supra* note 39, at art. 7.

126. *Id.*, at art. 4.

127. *Id.*, at art. 5.

128. *Id.*, at art. 6.

Name /thl_tbl621_3058006/winn/Mp_19 12/12/2006 04:42PM Plate # 0 pg 19 # 19

provide information (again in a durable medium) about the cancellation right.[129] This provision might be thought of as a "penalty default" rule, which puts pressure on one party to a contract to disclose information that the other party needs to avoid a particular negative consequence that follows from non-disclosure.[130] Where the consumer exercises his or her right of withdrawal from the contract, the supplier is obliged to reimburse the consumer for any sums paid.[131] Cold-calling of consumers by telephone, fax, or e-mail is not permitted unless the consumer has consented.[132]

In an effort to protect merchants from unreasonable burdens in consumer transactions, certain types of transactions are exempt from the coverage of some DS Directive protections.[133] For example, unless the parties have otherwise agreed, the consumer's seven-day right of withdrawal does not apply to contracts for the provision of services if performance has begun before the seven days are up; for the supply of goods or services whose price depends on fluctuations in the financial market that cannot be controlled by the supplier; for the supply of goods made to the consumer's specifications or personalized, or which are likely to deteriorate or expire rapidly; for audio or video recordings or computer software which are unsealed by the consumer; for the supply of newspapers, periodicals, or magazines; or for gaming or lottery services.

In May 2000, the European Parliament approved the Electronic Commerce Directive,[134] which governs any information society service provider[135] including Internet service providers (ISPs), and providers of electronic contracting, online advertising, and other commercial communications. While an information society service provider is given the right to operate throughout the EU subject to regulation only by the government of the country where it is established, in return it is now required to provide minimum information (*e.g.*, its name, place of establishment, e-mail address, and VAT registration) to consumers.[136] Again, this is another push toward ensuring online transparency and enhancing consumer confidence in online transactions. Building upon the same ethos, merchants wishing to enter into contracts online are required to explain clearly and unequivocally

129. *See* Regulation 11(3) of the Consumer Protection (Distance Selling) Regulations 2000 (the UK implementation of the DS Directive), *available at* http://www.oft.gov.uk/Business/Legal/DSR/default.htm; DS Directive, *supra* note 39, at art. 6. German courts have recently held that German consumers have one month to revoke a contract unless notice is given at the time the contract is formed and not merely posted on the merchant's Web site. Hanseatisches Oberlandesgericht, August 24, 2006, case No. 3 U 103/06 (on file with *The Business Lawyer*); Kammergericht Berlin, June 18, 2006, case No. 5 W 156/06 (on file with *The Business Lawyer*).

130. *See generally* Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87 (1989).

131. Regulation 14 of the Consumer Protection (Distance Selling) Regulations 2000, *available at* http://www.oft.gov.uk/Business/Legal/DSR/default.htm.

132. DS Directive, *supra* note 39, at art. 10.

133. *Id.*, at art. 6(3).

134. EC Directive, *supra* note 40. In the UK, the Directive was implemented as the Electronic Commerce (EC Directive) Regulations 2002 [hereinafter "EC Regulation"], *available at* http://www.opsi.gov.uk/si/si2002/20022013.htm.

135. EC Directive, *supra* note 40, at art. 1(2) as defined.

136. EC Directive, *supra* note 40, at art. 6; EC Regulation, *supra* note 134, at art. 6.

Name /thl_tbl621_3058006/winn/Mp_20 12/12/2006 04:42PM Plate # 0 pg 20 # 20

prior to the formation of the contract the steps of contract formation,[137] whether the contract is accessible after formation, and procedures for handling errors in contract formation. In addition, the Electronic Commerce Directive clarifies the moment of the conclusion of a contract in certain cases: when a contract is formed by an end user giving assent to an offer through a technological means, such as clicking on an icon or button, then the contract is concluded when the end user receives an acknowledgment of receipt of that manifestation of assent from the other party.[138] Service providers are required to provide end users of online contracting services with an effective means of identifying and correcting errors and accidental transactions.[139]

6. Conclusion

U.S. Internet businesses that target consumers in Europe need to be aware that standard form contracts that work well in the U.S. may be unenforceable in the EU. Managers of U.S. Internet businesses need to recognize the enormity of the changes that may be required in their business processes and technology before their sites have been fully "localized" for European market conditions. AOL's French subsidiary tried unsuccessfully to minimize the number of changes it made to localize its business model and found that its terms of service with French consumers were nearly all unenforceable because they were unfair. Subsequently Dell's subsidiary in the UK also fell afoul of the laws against unfair consumer contract terms. These and other cases dealing with EU unfair contract terms law show the lack of enthusiasm among some of the U.S.'s major trading partners for the U.S. market-oriented approach to consumer protection law. The EU approach to B2C transactions reflects a continued commitment to strong regulatory oversight of Internet consumer markets.

137. We are referring not to the formal legal rules for the contract formation, but the technical and procedural steps required by the consumer in order to conclude the contract.

138. EC Directive, *supra* note 40, at art. 11; EC Regulation, *supra* note 134, at art. 11.

139. *See* sources cited in note 138, *supra.*

Tony Brower Appellants v. Gateway 2000, Inc., Respondents.
SUPREME COURT OF NEW YORK, APPELLATE DIVISION,
246 A.D.2d 246*; *676 N.Y.S.2d 569 (1998)

Milonas, J. P.

Appellants are among the many consumers who purchased computers and software products from defendant Gateway 2000 through a direct-sales system, by mail or telephone order. As of July 3, 1995, it was Gateway's practice to include with the materials shipped to the purchaser along with the merchandise a copy of its "Standard Terms and Conditions Agreement" and any relevant warranties for the products in the shipment. The Agreement begins with a "Note to the Customer, " which provides, in slightly larger print than the remainder of the document, in a box that spans the width of the page: "This document contains Gateway 2000's Standard Terms and Conditions. By keeping your Gateway 2000 computer system beyond thirty (30) days after the date of delivery, you accept these Terms and Conditions." The document consists of 16 paragraphs, and, as is relevant to this appeal, paragraph 10 of the agreement, entitled "dispute resolution," reads as follows: "Any dispute or controversy arising out of or relating to this Agreement or its interpretation shall be settled exclusively and finally by arbitration. The arbitration shall be conducted in accordance with the Rules of Conciliation and Arbitration of the International Chamber of Commerce. The arbitration shall be conducted in Chicago, Illinois, U.S.A. before a sole arbitrator. Any award rendered in any such arbitration proceeding shall be final and binding on each of the parties, and judgment may be entered thereon in a court of competent jurisdiction."

Plaintiffs commenced this action on behalf of themselves and others similarly situated for compensatory and punitive damages, alleging deceptive sales practices in seven causes of action, including breach of warranty, breach of contract, fraud and unfair trade practices. In particular, the allegations focused on Gateway's representations and advertising that promised "service when you need it," including around-the-clock free technical support, free software technical support and certain on-site services. According to plaintiffs, not only were they unable to avail themselves of this offer because it was virtually impossible to get through to a technician, but also Gateway continued to advertise this claim notwithstanding numerous complaints and reports about the problem.

Insofar as is relevant to appellants, who purchased their computers after July 3, 1995, Gateway moved to dismiss the complaint based on the arbitration clause in the Agreement. Appellants argued that the arbitration clause is invalid under *UCC 2-207*, unconscionable under *UCC 2-302* and an unenforceable contract of adhesion. Specifically, they claimed that the provision was obscure; that a customer could not reasonably be expected to appreciate or investigate its meaning and effect; that the International Chamber of Commerce (ICC) was not a forum commonly used for consumer matters; and that because ICC headquarters were in France, it was particularly difficult to locate the organization and its rules. To illustrate just how inaccessible the forum was, appellants advised the court that the ICC was not registered with the Secretary of State, that efforts to locate and contact the ICC had been unsuccessful and that apparently the only way to attempt to contact the ICC was through the United States Council for International Business, with which the ICC maintained some sort of relationship.

In support of their arguments, appellants submitted a copy of the ICC's Rules of Conciliation and Arbitration and contended that the cost of ICC arbitration was prohibitive, particularly given the amount of the typical consumer claim involved. For example, a claim of less than $ 50,000 required advance fees of $ 4,000 (more than the cost of most Gateway products), of which the $ 2000 registration fee was nonre-

fundable even if the consumer prevailed at the arbitration. Consumers would also incur travel expenses disproportionate to the damages sought, which appellants' counsel estimated would not exceed $ 1,000 per customer in this action, as well as bear the cost of Gateway's legal fees if the consumer did not prevail at the arbitration; in this respect, the ICC Rules follow the "loser pays" rule used in England. Also, although Chicago was designated as the site of the actual arbitration, all correspondence must be sent to ICC headquarters in France.

The [lower] Court dismissed the complaint as to appellants based on the arbitration clause in the Agreements delivered with their computers. We agree with the court's decision and reasoning in all respects but for the issue of the unconscionability of the designation of the ICC as the arbitration body…

…the [lower] Court took note of the litigation in Federal courts on this very issue, and, indeed, on this very arbitration clause. In *Hill v Gateway 2000 (105 F3d 1147*), plaintiffs in a class action contested the identical Gateway contract in dispute before us, including the enforceability of the arbitration clause. As that court framed the issue, the "[t]erms inside Gateway's box stand or fall together. If they constitute the parties' contract because the Hills had an opportunity to return the computer after reading them, then all must be enforced". The court then concluded that the contract was not formed with the placement of a telephone order or with the delivery of the goods. Instead, an enforceable contract was formed only with the consumer's decision to retain the merchandise beyond the 30-day period specified in the agreement. Thus, the agreement as a whole, including the arbitration clause, was enforceable.

This conclusion was in keeping with the same court's decision in *ProCD, Inc. v Zeidenberg (86 F3d 1447*), where it found that detailed terms enclosed within the packaging of particular computer software purchased in a retail outlet constituted the contract between the vendor and the consumer who retained the product. In that case, the Seventh Circuit held that *UCC 2-207* did not apply and indeed was "irrelevant" to such transactions, noting that the section is generally invoked where multiple agreements have been exchanged between the parties in a classic "battle of the forms," whereas *ProCD* (as well as *Hill* and this case) involves but a single form.

The *Hill* decision, in its examination of the formation of the contract, takes note of the realities of conducting business in today's world. Transactions involving "cash now, terms later" have become commonplace, enabling the consumer to make purchases of sophisticated merchandise such as computers over the phone or by mail--and even by computer. Indeed, the concept of "[p]ayment preceding the revelation of full terms" is particularly common in certain industries, such as air transportation and insurance.

While *Hill* and *ProCD,* as the [lower] Court recognized, are not controlling (although they are decisions of the United States Court of Appeals for the circuit encompassing the forum State designated for arbitration), we agree with their rationale that, in such transactions, there is no agreement or contract upon the placement of the order or even upon the receipt of the goods. By the terms of the Agreement at issue, it is only after the consumer has affirmatively retained the merchandise for more than 30 days--within which the consumer has presumably examined and even used the product(s) and read the agreement--that the contract has been effectuated. In this respect, the case is distinguishable from *S&T Sportswear Corp. v Drake Fabrics (190 AD2d 598*), cited by appellants, where this Court found that an arbitration clause found on the reverse side of defendant's draft sales contract did constitute a "material alteration" where the parties did in fact have a pre-existing oral agreement.

While appellants argue that *Hill (supra*) is contrary to the law of New York in that it departs from the holding of cases such as *Matter of Marlene Indus. Corp. (Carnac Textiles) (45 NY2d 327*) and its progeny, we

disagree with their interpretation of both cases: *Hill* not only involves one form only, as distinguished from the "battle of the forms" scenario of the cases appellants cite, but these cases are simply inapplicable because, as explained, no contract was formed here or in *Hill* until the merchandise was retained beyond the 30-day period. The disputed arbitration clause is simply one provision of the sole contract "proposed" between the parties.

Second, with respect to appellants' claim that the arbitration clause is unenforceable as a contract of adhesion, in that it involved no choice or negotiation on the part of the consumer but was a "take it or leave it" proposition (*see, e.g., Matter of State of New York v Ford Motor Co., 74 NY2d 495, 503)*, we find that this argument, too, was properly rejected by the Court. Although the parties clearly do not possess equal bargaining power, this factor alone does not invalidate the contract as one of adhesion. As the [lower] Court observed, with the ability to make the purchase elsewhere and the express option to return the goods, the consumer is not in a "take it or leave it" position at all; if any term of the agreement is unacceptable to the consumer, he or she can easily buy a competitor's product instead--either from a retailer or directly from the manufacturer--and reject Gateway's agreement by returning the merchandise. The consumer has 30 days to make that decision. Within that time, the consumer can inspect the goods and examine and seek clarification of the terms of the agreement; until those 30 days have elapsed, the consumer has the unqualified right to return the merchandise, because the goods or terms are unsatisfactory or for no reason at all.

While returning the goods to avoid the formation of the contract entails affirmative action on the part of the consumer, and even some expense, this may be seen as a trade-off for the convenience and savings for which the consumer presumably opted when he or she chose to make a purchase of such consequence by phone or mail as an alternative to on-site retail shopping. That a consumer does not read the agreement or thereafter claims he or she failed to understand or appreciate some term therein does not invalidate the contract any more than such claim would undo a contract formed under other circumstances (*see, e.g., Morris v Snappy Car Rental, 84 NY2d 21, 30)*…

Finally, we turn to appellants' argument that the [lower] Court should have declared the contract unenforceable, pursuant to *UCC 2-302*, on the ground that the arbitration clause is unconscionable due to the unduly burdensome procedure and cost for the individual consumer. The [lower] Court found that while a class action lawsuit, such as the one herein, may be a less costly alternative to the arbitration (which is generally less costly than litigation), that does not alter the binding effect of the valid arbitration clause contained in the agreement.

As a general matter, under New York law, unconscionability requires a showing that a contract is "both procedurally and substantively unconscionable when made" (*Gillman v Chase Manhattan Bank, 73 NY2d 1, 10)*. That is, there must be "some showing of 'an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party'. The *Avco* Court took pains to note, however, that the purpose of this doctrine is not to redress the inequality between the parties but simply to ensure that the more powerful party cannot " 'surprise' " the other party with some overly oppressive term.

As to the procedural element, a court will look to the contract formation process to determine if in fact one party lacked any meaningful choice in entering into the contract, taking into consideration such factors as the setting of the transaction, the experience and education of the party claiming unconscionability, whether the contract contained "fine print," whether the seller used "high-pressured tactics" and any dis-

parity in the parties' bargaining power (*Gillman v Chase Manhattan Bank, supra, at 11*). None of these factors supports appellants' claim here. Any purchaser has 30 days within which to thoroughly examine the contents of their shipment, including the terms of the Agreement, and seek clarification of any term therein. The Agreement itself, which is entitled in large print "Standard Terms and Conditions Agreement," consists of only four pages and 16 paragraphs, all of which appear in the same size print. Moreover, despite appellants' claims to the contrary, the arbitration clause is in no way "hidden" or "tucked away" within a complex document of inordinate length, nor is the option of returning the merchandise, to avoid the contract, somehow a "precarious" one. We also reject appellants' insinuation that, by using the word "standard," Gateway deliberately meant to convey to the consumer that the terms were standard within the industry, when the document clearly purports to be no more than *Gateway's* "standard terms and conditions."

With respect to the substantive element, which entails an examination of the substance of the Agreement in order to determine whether the terms unreasonably favor one party, we do not find that the possible inconvenience of the chosen site (Chicago) alone rises to the level of unconscionability. We do find, however, that the excessive cost factor that is necessarily entailed in arbitrating before the ICC is unreasonable and surely serves to deter the individual consumer from invoking the process. Barred from resorting to the courts by the arbitration clause in the first instance, the designation of a financially prohibitive forum effectively bars consumers from this forum as well; consumers are thus left with no forum at all in which to resolve a dispute. In this regard, we note that this particular claim is not mentioned in the *Hill* decision, which upheld the clause as part of an enforceable contract.

While it is true that, under New York law, unconscionability is generally predicated on the presence of both the procedural and substantive elements, the substantive element alone may be sufficient to render the terms of the provision at issue unenforceable. Excessive fees, such as those incurred under the ICC procedure, have been grounds for finding an arbitration provision unenforceable or commercially unreasonable.

In the *Filias* case previously mentioned, the Federal District Court stated that it was "inclined to agree" with the argument that selection of the ICC rendered the clause unconscionable, but concluded that the issue was moot because Gateway had agreed to arbitrate before the American Arbitration Association (AAA) and sought court appointment of the AAA pursuant to Federal Arbitration Act (9 USC) *§ 5*. The court accordingly granted Gateway's motion to compel arbitration and appointed the AAA in lieu of the ICC. Plaintiffs in that action (who are represented by counsel for appellants before us) contend that costs associated with the AAA process are also excessive, given the amount of the individual consumer's damages, and their motion for reconsideration of the court's decision has not yet been decided. While the AAA rules and costs are not part of the record before us, the parties agree that there is a minimum, nonrefundable filing fee of $ 500, and appellants claim each consumer could spend in excess of $ 1,000 to arbitrate in this forum.

Gateway's agreement to the substitution of the AAA is not limited to the *Filias* plaintiffs. Gateway's brief includes the text of a new arbitration agreement that it claims has been extended to all customers, past, present and future (apparently through publication in a quarterly magazine sent to anyone who has ever purchased a Gateway product). The new arbitration agreement provides for the consumer's choice of the AAA or the ICC as the arbitral body and the designation of any location for the arbitration by agreement of the parties, which "shall not be unreasonably withheld." It also provides telephone numbers at which the AAA and the ICC may be reached for information regarding the "organizations and their procedures."

As noted, however, appellants complain that the AAA fees are also excessive and thus in no way have they accepted defendant's offer (*see, UCC 2-209*); because they make the same claim as to the AAA as they did with respect to the ICC, the issue of unconscionability is not rendered moot, as defendant suggests. We cannot determine on this record whether the AAA process and costs would be so "egregiously oppressive" that they, too, would be unconscionable. Thus, we modify the order on appeal to the extent of finding that portion of the arbitration provision requiring arbitration before the ICC to be unconscionable and remand to Supreme Court so that the parties have the opportunity to seek appropriate substitution of an arbitrator pursuant to the Federal Arbitration Act (*9 USC § 1 et seq.*), which provides for such court designation of an arbitrator upon application of either party, where, for whatever reason, one is not otherwise designated (*9 USC § 5*)…

Accordingly, the order of Supreme Court, New York County (Beatrice Shainswit, J.), entered October 21, 1997, which, to the extent appealed from, granted defendants' motion to dismiss the complaint as to appellants on the ground that there was a valid agreement to arbitrate between the parties, should be modified, on the law and the facts, to the extent of vacating that portion of the arbitration agreement as requires arbitration before the International Chamber of Commerce, with leave to the parties to seek appointment of an arbitrator pursuant to *9 USC § 5* and remanding the matter for that purpose, and otherwise affirmed, without costs.

Nardelli, Mazzarelli and Saxe, JJ., concur.

Arbitration Everywhere, Stacking the Deck of Justice

nytimes.com/2015/11/01/business/dealbook/arbitration-everywhere-stacking-the-deck-of-justice.html

By Jessica Silver-Greenberg and Robert Gebeloff October 30, 2015

On Page 5 of a credit card contract used by American Express, beneath an explainer on interest rates and late fees, past the details about annual membership, is a clause that most customers probably miss. If cardholders have a problem with their account, American Express explains, the company "may elect to resolve any claim by individual arbitration."

Those nine words are at the center of a far-reaching power play orchestrated by American corporations, an investigation by The New York Times has found.

By inserting individual arbitration clauses into a soaring number of consumer and employment contracts, companies like American Express devised a way to circumvent the courts and bar people from joining together in class-action lawsuits, realistically the only tool citizens have to fight illegal or deceitful business practices.

Over the last few years, it has become increasingly difficult to apply for a credit card, use a cellphone, get cable or Internet service, or shop online without agreeing to private arbitration. The same applies to getting a job, renting a car or placing a relative in a nursing home.

Among the class actions thrown out because of the clauses was one brought by Time Warner customers over charges they said mysteriously appeared on their bills and another against a travel booking website accused of conspiring to fix hotel prices. A top executive at Goldman Sachs who sued on behalf of bankers claiming sex discrimination was also blocked, as were African-American employees at Taco Bell restaurants who said they were denied promotions, forced to work the worst shifts and subjected to degrading comments.

Some state judges have called the class-action bans a "get out of jail free" card, because it is nearly impossible for one individual to take on a corporation with vast resources.

Patricia Rowe of Greenville, S.C., learned this firsthand when she initiated a class action against AT&T. Ms. Rowe, who was challenging a $600 fee for canceling her phone service, was among more than 900 AT&T customers in three states who complained about excessive charges, state records show. When the case was thrown out last year, she was forced to give up and pay the $600. Fighting AT&T on her own in arbitration, she said, would have cost far more.

By banning class actions, companies have essentially disabled consumer challenges to practices like predatory lending, wage theft and discrimination, court records show.

“This is among the most profound shifts in our legal history,” William G. Young, a federal judge in Boston who was appointed by President Ronald Reagan, said in an interview. “Ominously, business has a good chance of opting out of the legal system altogether and misbehaving without reproach.”

More than a decade in the making, the move to block class actions was engineered by a Wall Street-led coalition of credit card companies and retailers, according to interviews with coalition members and court records. Strategizing from law offices on Park Avenue and in Washington, members of the group came up with a plan to insulate themselves from the costly lawsuits. Their work culminated in two Supreme Court rulings, in 2011 and 2013, that enshrined the use of class-action bans in contracts. The decisions drew little attention outside legal circles, even though they upended decades of jurisprudence put in place to protect consumers and employees.

One of the players behind the scenes, The Times found, was John G. Roberts Jr., who as a private lawyer representing Discover Bank unsuccessfully petitioned the Supreme Court to hear a case involving class-action bans. By the time the Supreme Court handed down its favorable decisions, he was the chief justice.

Corporations said that class actions were not needed because arbitration enabled individuals to resolve their grievances easily. But court and arbitration records show the opposite has happened: Once blocked from going to court as a group, most people dropped their claims entirely.

The Times investigation was based on thousands of court records and interviews with hundreds of lawyers, corporate executives, judges, arbitrators and plaintiffs in 35 states.

Since no government agency tracks class actions, The Times examined federal cases filed between 2010 and 2014. Of 1,179 class actions that companies sought to push into arbitration, judges ruled in their favor in four out of every five cases.

In 2014 alone, judges upheld class-action bans in 134 out of 162 cases.

Some of the lawsuits involved small banking fees, including one brought by Citibank customers who said they were duped into buying insurance they were never eligible to use. Fees like this, multiplied over millions of customers, amount to billions of dollars in profits for companies.

Removing the Ability to Sue

A New York Times study of the increasing use of arbitration clauses in contracts, which has effectively forced millions of people to sign away their right to go to court.

The data provides only part of the picture, since it does not capture the people who were dissuaded from filing class actions.

A spokeswoman for American Express said that over the last few years, banking regulators have examined the company's business practices, largely obviating the need for class actions. The regulators "have required significant remediations and large fines to address issues they found, with very little loss in value to the consumer," said the spokeswoman, Marina H. Norville.

Law enforcement officials, though, say they have lost an essential tool for uncovering patterns of corporate abuse. In a letter last year to the Consumer Financial Protection Bureau, attorneys general in 16 states warned that "unlawful business practices" could flourish with the proliferation of class-action bans.

In October, the bureau outlined rules to prevent financial firms from banning class actions. Almost immediately, the U.S. Chamber of Commerce galvanized forces to stop the move.

Andrew J. Pincus, a law partner at Mayer Brown in Washington who has represented companies that use arbitration, said class actions yielded little relief for plaintiffs. "Arbitration provides a way for people to hold companies accountable without spending a lot of money," Mr. Pincus said. "It's a system that can work."

Support for that assertion has been anecdotal, since there is no central database of arbitrations. But by assembling records from arbitration firms across the country, The Times found that between 2010 and 2014, only 505 consumers went to arbitration over a dispute of $2,500 or less.

Verizon, which has more than 125 million subscribers, faced 65 consumer arbitrations in those five years, the data shows. Time Warner Cable, which has 15 million customers, faced seven.

One federal judge remarked in an opinion that "only a lunatic or a fanatic sues for $30."

Daniel Dempsey of Tucson admits he might be both. He has spent three years and $35,000 fighting Citibank in arbitration over a $125 late fee on his credit card. Mr. Dempsey, who previously worked in Citi's investment bank, said the erroneous charge ruined his credit score, and he vowed to continue until he was awarded damages.

The odds are not in his favor. Roughly two-thirds of consumers contesting credit card fraud, fees or costly loans received no monetary awards in arbitration, according to The Times's data.

The Supreme Court's rulings amounted to a legal coup for a group of corporate lawyers who figured out how to twin arbitration clauses with class-action bans. The lawyers represented clients that had paid billions of dollars to resolve class actions over the years. The lawsuits, companies said, were driven by plaintiffs' lawyers who stood to make millions of dollars. They said they had no choice but to settle even those cases that were without merit.

“These lawsuits were not about protecting consumers but about plaintiffs’ lawyers,” said Duncan E. MacDonald, a former general counsel for Citibank who was part of the group. “These were nuclear weapons aimed at companies.”

Consumer advocates disagreed. A class action, they argued, allowed people who lost small amounts of money to join together to seek relief. Others exposed wrongdoing, including a case against auto dealers who charged minority customers higher interest rates on car loans.

The consequences of arbitration clauses can be seen far beyond the financial sector. Even lawsuits that would not have been brought by a class have been forced out of the courts, according to the Times investigation. Taking Wall Street’s lead, businesses — including obstetrics practices, private schools and funeral homes — have employed arbitration clauses to shield themselves from liability, interviews and arbitration and court records show.

Thousands of cases brought by single plaintiffs over fraud, wrongful death and rape are now being decided behind closed doors. And the rules of arbitration largely favor companies, which can even steer cases to friendly arbitrators, interviews and records show.

The sharp shift away from the civil justice system has barely registered with Americans. F. Paul Bland Jr., the executive director of Public Justice, a national consumer advocacy group, attributed this to the tangle of bans placed inside clauses added to contracts that no one reads in the first place.

“Corporations are allowed to strip people of their constitutional right to go to court,” Mr. Bland said. “Imagine the reaction if you took away people’s Second Amendment right to own a gun.”

A Powerful Coalition Forms

At Italian Colors, a small restaurant tucked in an Oakland, Calif., strip mall, crayons and butcher paper adorn the tables, and a giant bottle of wine signed by the regulars sits in the entryway.

The laid-back vibe matches that of the restaurant’s owner and chef, Alan Carlson, who prides himself on running an establishment that not only serves great food — one crowd-pleaser is the spaghetti Bolognese — but also doesn’t take itself too seriously.

“I’ve been a ski bum, a line cook at a Greek diner and owned restaurants, and it’s all been about having fun,” Mr. Carlson said.

Somewhat of a libertarian, Mr. Carlson said he used to associate big lawsuits with “ambulance chasers.” But that was before he needed one.

In 2003, he sued American Express on behalf of small businesses over steep processing fees. The fees — 30 percent higher than Visa's or MasterCard's — were hurting profits, but the restaurants could not afford to turn away diners who used American Express corporate cards.

It was a classic antitrust case: A big company was accused of using its monopoly power to charge unfair prices. But as Italian Colors v. American Express wended its way through the courts over the next 10 years, it became something far more momentous.

When the case was filed, the alliance of corporate interests, including credit card companies, national retailers and carmakers, had already been strategizing on how to eliminate class actions.

The effort was led by a lawyer at Ballard Spahr, a Philadelphia firm that represented big banks. The only thing the lawyer, Alan S. Kaplinsky, had in common with Mr. Carlson was a first name. Laser-focused and admirably relentless, Mr. Kaplinsky preferred his polo shirts buttoned up and tucked in.

Among his clients were Alabama money lenders accused of duping customers into taking out credit cards. Settlements were costly; trying the cases in front of sympathetic juries was worse.

Mr. Kaplinsky was searching for solutions when he remembered helping, as a young lawyer, a mutual savings and loan association draft an arbitration clause, he said in an interview. Banks could take it a step further, he thought, by writing class-action bans into the clauses.

"Clients were telling me they were getting killed by frivolous lawsuits and asking me what on earth could be done about it," Mr. Kaplinsky said.

He soon joined forces with lawyers at WilmerHale, a firm that had represented big banks. The group invited corporate legal teams in July 1999 to the law firm's New York offices to strategize about arbitration.

Attendees included representatives from Bank of America, Chase, Citigroup, Discover, Sears, Toyota and General Electric. At a subsequent teleconference, participants dialed in remotely using an easy-to-remember code: a-r-b-i-t-r-a-t-i-o-n.

Details of the meetings, and of more than a dozen others over the next three years, were culled from court records filed in a federal lawsuit in Manhattan and corroborated in interviews with lawyers who attended.

The records and interviews show that lawyers for the companies talked about arbitration clauses as a means to an end. The goal was to kill class actions and send plaintiffs' lawyers to the "employment lines."

Of the companies participating, only American Express and First USA had adopted an arbitration clause banning class actions; months later, Discover Bank added its own. By the time the meetings concluded, many of the companies had followed suit.

To keep track of whether judges upheld or rejected the class-action bans, Mr. Kaplinsky set up a scorecard. In the positive column were courts in Pennsylvania and Georgia, which upheld a clause used by some companies that gave consumers a small window to opt out of arbitration.

On the negative side were courts in California and one in Massachusetts, which struck down a class-action waiver in a Comcast cable contract. The judge found that the ban would shield the company "even in cases where it has violated the law."

Many judges across the country did not object to companies' requiring consumers to use arbitration. But they bridled at preventing those consumers from banding together to bring a case.

State law guaranteed citizens a means to defend their rights, and contracts that tried to take that away were "unconscionable," many judges said. In other words, class-action bans were unfair.

Petitioning the Highest Court

The push by Mr. Kaplinsky's group coincided with the Chamber of Commerce's own campaign against class actions, which they called a scourge on companies.

In particular, the chamber pointed to an Illinois judge who had ordered Philip Morris to pay more than $10 billion for playing down risks associated with light cigarettes.

At the other end of the spectrum, the chamber also criticized so-called coupon lawsuits that generated big paydays for lawyers and little money for consumers. In one, against a television manufacturer accused of selling sets with fuzzy pictures, plaintiffs each received $25 or $50 coupons while their lawyers collected $22 million.

"It's not like the class-action system is a land of milk and honey," said Matthew Webb, a senior vice president at the Institute for Legal Reform, a chamber affiliate.

Once a state or federal judge certifies plaintiffs as a class, the suits are often unstoppable, the chamber has said — even if no one has been harmed. It has also said that plaintiffs' lawyers have brought cases in jurisdictions that were known to be friendly to class actions.

The chamber scored a victory when Congress passed the Class Action Fairness Act in 2005, which allowed companies to move cases into federal court and out of state courts considered hostile to corporate defendants.

Brian T. Fitzpatrick, a former clerk to Justice Antonin Scalia who teaches law at Vanderbilt University, said criticizing class actions for small awards was misleading. By their very nature, the lawsuits are intended to help large groups of people get back small individual amounts, Mr. Fitzpatrick said.

“Without a class action, if someone loses $500, they will not be able to do anything about it,” he said.

Walter Hackett, who worked as a banker until 2007, said the real threat was cases that force companies to abandon lucrative billing practices.

“When banks make mistakes or do bad things, they tend to do them many times and to many people,” said Mr. Hackett, who switched sides and became a consumer lawyer.

With state courts still blocking their efforts, Mr. Kaplinsky’s group focused on getting a case to the Supreme Court.

Success hinged on the justices’ applying the Federal Arbitration Act, a dusty 1925 law that formalized the use of arbitration for disagreements between businesses. Since the mid-1980s, the court had expanded the scope of the law to cover a range of disputes between companies and their employees and customers.

In fact, when Congress passed the act, lawmakers specifically emphasized that it was meant for businesses. Some raised concerns that companies would one day twist the law to impose arbitration on their workers, according to minutes from a congressional hearing.

The Supreme Court had never taken a case that centered on whether the Federal Arbitration Act allowed plaintiffs to form a class action.

A lawsuit in California’s courts looked promising. The defendant, Discover Bank, was accused of charging unfair fees. A lower court upheld the bank’s class-action ban, but the state’s Court of Appeals negated it, accusing Discover of trying to grant itself a “license to push the boundaries of good business practices to their furthest limits.”

Discover, one of the companies involved with Mr. Kaplinsky’s group, then petitioned the Supreme Court to intervene. Representing the company was John G. Roberts Jr., at the time a prominent corporate defense lawyer.

With much at stake, Mr. Kaplinsky said, he spoke with Mr. Roberts and offered input on the brief Mr. Roberts was drafting to the Supreme Court. “He was a really nice guy,” Mr. Kaplinsky said.

As a private lawyer, John G. Roberts Jr. unsuccessfully petitioned the Supreme Court to hear a case involving class-action bans. During his tenure as chief justice, the Supreme Court has ruled in favor of the bans.CreditChip Somodevilla/Getty Images

Image
As a private lawyer, John G. Roberts Jr. unsuccessfully petitioned the Supreme Court to hear a case involving class-action bans. During his tenure as chief justice, the Supreme Court has ruled in favor of the bans.CreditChip Somodevilla/Getty Images

In the subsequent petition, Mr. Roberts wrote that the California appeals court had overstepped its bounds in violation of the Federal Arbitration Act. Allowing consumers to bring a case as a class, he wrote, would violate the "core purpose of the Arbitration Act: to enforce arbitration agreements according to their terms."

In essence, companies were using the law to push disputes out of court, and then imposing conditions that made it impossible to pursue those disputes in arbitration.

The Supreme Court declined to take up the case.

A Victory for Corporations

Determined, businesses sweetened the terms of arbitration to try to tempt the Supreme Court to wade into the fray, according to interviews. A clause drafted for AT&T, for example, promised to award certain customers who prevailed in arbitration at least $7,500 and to pay them double their legal fees.

In 2010, the Supreme Court agreed to hear a case. In AT&T v. Concepcion, customers said the company had promised them a free phone if they signed up for service, and then charged them $30.22 anyway.

Once again, the ruling involved the California courts and their rejection of a class-action ban as "unconscionable." By then, Mr. Roberts was chief justice.

Lawyers for both sides focused on the power of state courts.

Mr. Pincus, the Mayer Brown partner, represented AT&T and said that the Federal Arbitration Act superseded state law. In his main argument, Mr. Pincus accused state courts of making up special rules to discriminate against arbitration.

Deepak Gupta, who at age 34 was already known as a skilled appellate lawyer, worked for the plaintiffs. Mr. Gupta countered that the state courts should be free to enforce their own laws.

"We thought we had a fighting chance if we argued the case was about the importance of states' rights," Mr. Gupta said in an interview.

Sitting in the gallery during opening arguments, Mr. Kaplinsky had a different take on the Roberts court, which seemed to favor arbitration. "We were pretty sure we had his vote," Mr. Kaplinsky said.

When the court ruled 5-4 in favor of AT&T, it largely skipped over Mr. Pincus's central argument.

"Requiring the availability of classwide arbitration," Justice Scalia wrote for the majority, "interferes with fundamental attributes of arbitration." The main purpose of the Federal Arbitration Act, he wrote, "is to ensure the enforcement of arbitration agreements according to their terms."

It was essentially the same argument Mr. Roberts had made as a lawyer in the Discover case.

With the Supreme Court marginalizing state law, the only option left for consumer advocates was to use a federal law to fight back.

Enter Mr. Carlson, the owner of Italian Colors, who was still fighting with American Express. After the company won the first round, Mr. Carlson's lawyers appealed, saying the class-action ban prevented merchants from exercising their federal rights to fight a monopoly.

"In a contest between just me — a restaurant in Oakland — and American Express, who do you think wins?" Mr. Carlson said.

Individually, none of the merchants could pay for a case that could cost more than $1 million in expert analysis alone.

The United States Court of Appeals for the Second Circuit, which included Sonia M. Sotomayor, ruled in the plaintiffs' favor in 2009.

American Express appealed again, and the case ultimately went to the Supreme Court. By the time the court heard it, in 2013, Ms. Sotomayor was a justice and recused herself.

The case centered on the Sherman Act, a muscular antitrust law that empowered citizens to take on monopolistic entities. Conservatives and liberals on previous Supreme Courts had consistently found that Americans should be guaranteed a way to exercise that right.

On June 20, 2013, the justices abandoned the precedent and ruled in favor of American Express.

Arbitration clauses could outlaw class actions, the court said, even if a class action was the only realistic way to bring a case. "The antitrust laws do not guarantee an affordable procedural path to the vindication of every claim," Justice Scalia wrote.

Within hours, critics from across the political spectrum registered their disbelief on legal blogs. "No one thinks they got it right," Judge Young of Boston wrote later in a decision.

The most withering criticism came from Justice Elena Kagan, who wrote the dissenting opinion. "The monopolist gets to use its monopoly power to insist on a contract effectively depriving its victims of all legal recourse," she wrote. She went on to say that

her colleagues in the majority were effectively telling those victims, “Too darn bad.”

Back in Oakland, Mr. Carlson got the news from his lawyer. The restaurateur said he had no choice but to continue accepting American Express. About a third of his customers use it, including many who run up bigger tabs because the cards are tied to expense accounts.

Mr. Carlson did make one change, though. He added a special bourbon cocktail to the menu. “I call it the Scalia,” he said. “It’s bitter and tough to swallow.”

A Clause for All Occasions

Signs posted in a theater in Los Angeles and a hamburger joint in East Texas informed guests that, simply by walking in, they had agreed to arbitration. Consumer contracts with Amazon, Netflix, Travelocity, eBay and DirecTV now contain arbitration clauses. Even Ashley Madison, the online site for adulterers, requires that clients agree to them.

It is virtually impossible to rent a car without signing an agreement like Budget’s, which reads, “Arbitration, No Class Actions.” The same goes for purchasing just about anything online, which makes adding the clauses even easier.

The “birth of a thousand clauses,” as one corporate lawyer put it, has caught millions of Americans by surprise.

James Pendergast had no idea he had agreed to arbitration until a class-action suit he filed on behalf of Sprint customers in Miami was thrown out of court. They had sued the company after noticing that their monthly bills contained roaming charges incurred in their homes.

The cost of arbitration was far more than the $20 charges Mr. Pendergast was contesting. And his lawyer, Douglas F. Eaton, advised him that winning would require high-tech experts at a six-figure bill.

If he lost, Mr. Pendergast might even have to pay for Sprint’s lawyers. “Why would anyone risk that?” Mr. Eaton said.

The data on consumer arbitration obtained by The Times shows that Sprint, a company with more than 57 million subscribers, faced only six arbitrations between 2010 and 2014.

“Just imagine how many customers Sprint can take money from because of arbitration,” Mr. Pendergast said.

Sprint declined to comment.

Few industries more keenly understood the potential of arbitration clauses than financial firms. A particularly bruising set of lawsuits starting in 2009 revealed an accounting device that more than a dozen banks employed on debit card transactions. Customers accused the banks of deducting big payments like monthly rent before taking out smaller charges like those for a pack of gum — even if the customer bought the gum first.

Changing the order of transactions, the lawsuits said, allowed the banks to increase the number of times they could charge overdraft fees, typically $35 a pop. Forced into court, the banks settled the cases for more than $1 billion.

At least seven of the banks in the overdraft cases have since added arbitration clauses, The Times found.

A lot is at stake. Since regulations prompted by the 2008 financial crisis crimped profits from trading and other risky activities, revenue from fees has become crucial to banks' profits.

Together, the three largest banks in the country — JPMorgan Chase, Bank of America and Wells Fargo — made more than $1 billion through overdraft fees in the first three months of 2015, according to the Federal Deposit Insurance Corporation.

In interviews, corporate executives and defense lawyers predicted that consumers would use arbitration once it became more familiar. They added that people could also get relief in small claims court, an option often not covered by arbitration clauses. But much like arbitration, few people go to small claims court, according to court data and interviews with judges.

While many companies also include an opt-out provision on arbitration — typically between 30 and 45 days — few consumers take advantage of it because they do not realize they have signed a clause to begin with, or do not understand its consequences, according to interviews with lawyers and plaintiffs.

Companies noted in interviews that arbitration incentivized them to resolve many customer disputes informally.

Matthew Kilgore, of Rohnert Park, Calif., had no such luck.

A bread truck driver, Mr. Kilgore had dreamed of being a helicopter pilot ever since his father, who was in the Navy, took him to an air show when he was a child.

At 28, after his first daughter was born, he enrolled at Silver State Helicopters, a for-profit school in Oakland, taking out a $55,950 loan from Key Bank to pay for the program.

Less than halfway into training, Mr. Kilgore got a call from his flight instructor, who said Silver State was bankrupt. In disbelief, he drove to Oakland the next day to find the school's doors padlocked.

Key Bank and Student Loan Xpress, the school's preferred lenders, demanded that students pay back their loans for degrees they never received. About 2,700 students, including Mr. Kilgore, joined in class actions against the two lenders, accusing them of ignoring financial signs that the school was in trouble.

Student Loan Xpress, whose contracts did not have an arbitration clause, agreed to settle and forgave more than $100 million in student loans. Key Bank, whose contracts did, used the clause to get Mr. Kilgore's lawsuit dismissed in 2013.

Key Bank declined to comment on Mr. Kilgore's case, but said the bank had forgiven a portion of many students' loans.

Mr. Kilgore has not been able to pay back his loan, which with interest has swelled to $110,000. With his credit ruined, he and his wife cannot buy a house and he has abandoned his dream of becoming a pilot.

"It's the worst decision I ever made," he said.

Bargaining Power Fades

A hunter whose trophies are mounted on the walls of his chambers in Philadelphia's federal courthouse, Judge Berle M. Schiller prefers to use a bow to catch his prey. He has stalked deer through the Pennsylvania woods, tracked caribou in Quebec and pursued fleet-footed impala through South Africa.

Judge Berle Schiller reluctantly enforced a class-action ban in Applebee's employment contracts in 2013, noting the "lamentable" state of legal affairs.CreditMark Makela for The New York Times

Hunting with a rifle is "not a fair fight," said Judge Schiller, 71, who applies the same philosophy to his courtroom. Or at least he did until December 2013, when he had to rule on a lawsuit against the owner of 39 Applebee's restaurants in Pennsylvania.

The class action was brought by a former waiter on behalf of other low-wage employees. The waiter, Charles Walton, said Applebee's made workers sweep floors, stock silverware, scrub booths and empty trash cans, but did not pay them a fair wage for the extra tasks. The Applebee's employees, who relied on tips, often ended up making less than minimum wage. Employment lawyers said these practices were widespread in the restaurant industry.

The Rose Group, which owned the restaurants, defended its practices and urged Judge Schiller to dismiss the lawsuit since Mr. Walton signed an employee contract that included "a mutual promise to resolve claims by binding arbitration."

The request troubled Judge Schiller. "It is just these kinds of cases where it's important to have a jury," he said.

Applebee's franchises, run by different owners, have faced similar class actions in Alabama, Florida, Illinois, Kentucky, Missouri, New York, South Carolina and Rhode Island.

In 2014, Ronnie Del Toro brought a case while working as a waiter in the Bronx. Once again, Applebee's sought to have it thrown out.

In the meantime, Mr. Del Toro said the restaurant's owner and two hulking men, including one who went by "Big Drew," confronted him on the job. They warned him to "stop being a little bitch" and withdraw his lawsuit, according to an application for a restraining order that Mr. Del Toro filed in a Bronx court.

"I didn't wait to hear anymore," said Mr. Del Toro, who moved to Brooklyn and got the restraining order.

Apple-Metro Inc., which owns the Bronx Applebee's, did not return requests for comment.

Mr. Del Toro now works at P.F. Chang's, another restaurant chain. He had to sign an employment contract with an arbitration clause to get the job.

Class-action bans are also widely included in the employment policies of retailers, including Macy's, Kmart and Sears.

Even some N.F.L. cheerleaders have had to agree to them. When a group of cheerleaders sued the Oakland Raiders over working conditions, they discovered that Roger Goodell, the N.F.L. commissioner, would preside over the arbitration. The Raiders later agreed to use someone else.

The use of class-action bans is spreading far beyond low-wage industries to Silicon Valley and Wall Street, where banks like Goldman Sachs require some executives to sign contracts containing the clauses.

Civil rights experts worry that discriminatory labor practices will go unchecked as class actions disappear.

Cases brought by African-American employees against Nike in 2003 and Walgreens in 2005, for example, led the companies to change their policies. The drug company Novartis paid $175 million to settle a class action brought by female employees over promotions and pay.

Jenny Yang, chairwoman of the Equal Employment Opportunity Commission, said arbitration allowed "root causes" to persist. Part of the problem, Ms. Yang said, is that arbitration keeps any discussion of discriminatory practices hidden from other workers "who might be experiencing the same thing."

The point was not lost on Judge Schiller in Philadelphia, who has handled many employment cases in his 15 years on the bench. Once an arbitrator himself for disputes between companies, the judge said he had nothing against the forum, as long as both sides wanted to go.

Among thousands of employees at Applebee's franchises, only four took the company to arbitration between 2010 and 2014, according to The Times's review of arbitration data.

When lawyers for Applebee's argued before Judge Schiller to have the lawsuit thrown out, they assured him that Mr. Walton, who brought the suit, could have turned down the job and not agreed to the arbitration clause.

Judge Schiller was not persuaded. "To suggest that he had bargaining power because he could wait tables elsewhere ignores reality," the judge wrote in court papers. The Applebee's workers, the judge wrote, must "chew on a distasteful dilemma" of whether to "give up certain rights or give up the job."

Despite his own objections, Judge Schiller said he was bound by the Supreme Court decisions. In his ruling, he noted the "lamentable" state of legal affairs and dismissed the case.

With no other option, Mr. Walton took his case to arbitration. In April, he lost.

Dewayne HUBBERT, Elden L. Craft, Chris Grout, and Rhonda Byington, Individually and on Behalf of Others Similarly Situated, Plaintiffs–Appellees,
v. DELL CORPORATION, Defendant–Appellant.

359 Ill.App.3d 976, 835 N.E.2d 113, 296 Ill.Dec. 258 (2005)

Justice HOPKINS delivered the opinion of the court:

The defendant, Dell Corp., appeals the trial court's order denying its motion to compel arbitration and the court's related orders denying its motion to strike certain exhibits and an affidavit submitted by the plaintiffs, Dewayne Hubbert, Elden Craft, Chris Grout, and Rhonda Byington, in opposition to the defendant's motion to compel arbitration. Because a ruling on a motion to compel arbitration is in the nature of injunctive relief, the trial court's orders are reviewable under Supreme Court Rule 307(a)(1). On appeal, the defendant argues that the trial court erred in finding that its arbitration clause was not a part of the contract between the defendant and the plaintiffs and that the court erred in finding that if the arbitration clause was a part of the contract between the parties, then the arbitration clause was unenforceable because it was procedurally and substantively unconscionable.

BACKGROUND

In 2000 and 2001, the plaintiffs purchased computers online through the defendant's Web site. Before purchasing their computers, each of the plaintiffs configured the model and type of computer he or she wished to purchase from the defendant's Web pages. To make their purchases, each of the plaintiffs completed online forms on five of the defendant's Web pages. On each of the five Web pages, the defendant's "Terms and Conditions of Sale" were accessible by clicking on a blue hyperlink. The terms and conditions were also printed on the back of the plaintiffs' invoices, which were sent, along with separate documents containing the "Terms and Conditions of Sale," in the shipping boxes with the plaintiffs' computers, and the terms and conditions could be obtained by calling the defendant's toll-free number and requesting a copy. On the last three forms the plaintiffs completed online, the following statement appeared: "All sales are subject to Dell's Term[s] and Conditions of Sale." The defendant included in the boxes in which the computers were shipped its "total satisfaction" return policy, which provided that purchasers would receive a full refund or credit if the computers were returned within 30 days. None of the plaintiffs returned his or her computers within 30 days.

On June 3, 2002, the plaintiffs filed their complaint, both as individuals and on behalf of others similarly situated, *i.e.*, a putative class action lawsuit, against the defendant. In their complaint, the plaintiffs—three Illinois residents and one Missouri resident—alleged that they had purchased computers online from the defendant, whose principal place of business was in Texas; that the computers contained Pentium 4 microprocessors, which the defendant had asserted were the fastest, most powerful Intel Pentium processor available; that the Pentium 4 microprocessor was slower and less powerful and provided less performance than either a Pentium III or an AMD Athlon, but at a greater cost; and that the defendant's marketing of its Pentium 4 computers was false, misleading, and deceptive. The plaintiffs' complaint includes

three counts alleging that the defendant violated the Texas Deceptive Trade Practices—Consumer Protection Act (Tex. Bus. & Com.Code Ann. § 17.41 *et seq.* (Vernon 1994)) and one count alleging that the defendant violated the Illinois Consumer Fraud and Deceptive Business Practices Act (815 ILCS 505/1 *et seq.* (West 2002)). The plaintiffs allege that their damages are less than $75,000 per person.

After the plaintiffs filed their complaint, the defendant made a demand for arbitration, but the plaintiffs did not respond. On September 13, 2002, the defendant filed a motion to dismiss the plaintiffs' complaint pursuant to section 2–619 of the Code of Civil Procedure (735 ILCS 5/2–619 (West 2002)) or, alternatively, to stay the proceedings and to compel arbitration. In the defendant's motion, it alleged that as a part of the online contract, the plaintiffs agreed to a binding arbitration clause, which was contained in the defendant's "Terms and Conditions of Sale."

The beginning of the "Terms and Conditions of Sale" stated:

"PLEASE READ THIS DOCUMENT CAREFULLY! IT CONTAINS VERY IMPORTANT INFORMATION ABOUT YOUR RIGHTS AND OBLIGATIONS, AS WELL AS LIMITATIONS AND EXCLUSIONS THAT MAY APPLY TO YOU. THIS DOCUMENT CONTAINS A DISPUTE RESOLUTION CLAUSE.

This Agreement contains the terms and conditions that apply to purchases by Home, Home Office, and Small Business customers from the Dell entity named on the invoice ('*Dell*') that will be provided to you ('*Customer*') on orders for computer systems and/or related products sold in the United States. You agree to be bound by and accept this agreement as applicable to your purchase of product(s) or service(s) from Dell. By accepting delivery of the computer systems and/or other products described on that invoice, Customer agrees to be bound by and accepts these terms and conditions." (Emphasis in original.)

The "Terms and Conditions of Sale" also contained a choice-of-law provision, which stated that Texas law governed the sale of the computers and the agreement.

The arbitration clause contained in the defendant's "Terms and Conditions of Sale" stated:

"12. **Binding Arbitration.** ANY CLAIM, DISPUTE, OR CONTROVERSY (WHETHER IN CONTRACT, TORT, OR OTHERWISE, WHETHER PREEXISTING, PRESENT[,] OR FUTURE, AND INCLUDING STATUTORY, COMMON LAW, INTENTIONAL TORT[,] AND EQUITABLE CLAIMS) AGAINST DELL, its agents, employees, successors, assigns[,] or affiliates (collectively for purposes of this paragraph, '*Dell*'[ ),] arising from or relating to this Agreement, its interpretation, or the breach, termination [,] or validity thereof, the relationships which result from this Agreement (including, to the full extent permitted by applicable law, relationships with third parties who are not signatories to this Agreement), Dell's advertising, or any related purchase SHALL BE RESOLVED EXCLUSIVELY AND FINALLY BY BINDING ARBITRATION ADMINISTERED BY THE NATIONAL ARBITRATION FORUM (NAF) under its Code of Procedure then in effect (available via the Internet at **http://**

www.arb-forum.com[ ], or via telephone at 1–800–474–2371). The arbitration will be conducted before a single arbitrator and will be limited solely to the dispute or controversy between Customer and Dell. The arbitration shall be held in a mutually agreed upon location in person, by telephone, or online. Any award of the arbitrator(s) shall be final and binding on each of the parties[ ] and may be entered as a judgment in any court of competent jurisdiction. Information may be obtained and claims may be filed at any office of the NAF or at P.O. Box 50191, Minneapolis, MN 55405." (Emphasis in original.)

At a hearing, the plaintiffs agreed that a contract had been formed by their online purchase of the defendant's computers, but they denied that the binding arbitration clause in the "Terms and Conditions of Sale" was a part of the contract. The defendant moved to strike certain exhibits and an affidavit filed by the plaintiffs in opposition to the defendant's motion to compel arbitration. The court denied the defendant's motion to dismiss or, alternatively, to compel arbitration and the defendant's motions to strike. The defendant filed this interlocutory appeal.

ANALYSIS

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Validity of Arbitration Agreement

The defendant argues that the trial court erred in finding that its arbitration clause, contained in the "Terms and Conditions of Sale," was not a part of the parties' contract. The defendant argues that by making the "Terms and Conditions of Sale" available on its Web pages pursuant to a blue hyperlink, by stating on several of the Web pages completed by the plaintiffs that all sales are subject to the defendant's "Terms and Conditions of Sale," and by sending a copy of the "Terms and Conditions of Sale" in the boxes in which the computers were shipped, it sufficiently created a binding arbitration agreement with the plaintiffs. The plaintiffs argue that simply making the "Terms and Conditions of Sale" available online was insufficient and that a clear manifestation of assent to the "Terms and Conditions of Sale" was needed to create a binding arbitration agreement. The plaintiffs argue that the defendant should have displayed on its order-confirmation-confirmation Web page an "I accept" box, on which the plaintiffs must click to manifest assent to the agreement before the purchase proceeded. The plaintiffs also argue that the "Terms and Conditions of Sale" contained in the shipping boxes were "additional terms" and were governed by section 2.207 of the Texas Uniform Commercial Code (Tex. Bus. & Com.Code Ann. § 2.207 (Vernon 1994)), which requires clear assent to make the additional terms binding on the plaintiffs. The plaintiffs do not allege that they did not see or that they did not read the "Terms and Conditions of Sale."

Federal and state law strongly favors arbitration, and a presumption exists in favor of arbitration agreements. 9 U.S.C. § 2 (2000); *AutoNation USA Corp. v. Leroy,* 105 S.W.3d 190, 195 (Tex.App.2003). Courts are to resolve any doubts concerning an arbitration agreement in favor of arbitration. *AutoNation USA Corp.,* 105 S.W.3d at 195. A party cannot be required to arbitrate unless the party has agreed to do so, and the parties' arbitration agreement must be clear. *Mohamed v. Auto Nation USA Corp.,* 89 S.W.3d 830, 835 (Tex.App.2002). If a valid arbitration agreement exists and the claims raised are within the scope of the agreement, a trial court has no discretion but to compel arbitration. *AutoNation USA Corp.,* 105 S.W.3d at 195.

The party seeking to compel arbitration has the burden of proving that an arbitration agreement exists and that the claims raised are within the agreement's scope. *Cantella & Co. v. Goodwin,* 924 S.W.2d 943, 944 (Tex.1996). If an arbitration agreement is valid, the party opposing the agreement has the burden of defeating it. *Cantella & Co.,* 924 S.W.2d at 944.

In the present case, the court found that the defendant's online terms and conditions had not been "adequately communicated" to the plaintiffs because the defendant did not provide a display text on the Web site that manifested a clear assent to the terms and conditions before the order could proceed, because the terms and conditions were not displayed on a Web page that the plaintiffs had completed in placing their orders, and because there was no language on the Web pages placing the plaintiffs on notice that they were performing an affirmative act that would bind them to submit their claims to arbitration. The court held that the defendant's "Terms and Conditions of Sale," and, therefore, the arbitration clause, were not a part of the online sales contract.

We find that the online contract included the "Terms and Conditions of Sale." The blue hyperlink entitled "Terms and Conditions of Sale" appeared on numerous Web pages the plaintiffs completed in the ordering process. The blue hyperlinks for the "Terms and Conditions of Sale" also appeared on the defendant's marketing Web pages, copies of which the plaintiffs attached to their complaint. The blue hyperlinks on the defendant's Web pages, constituting the five-step process for ordering the computers, should be treated the same as a multipage written paper contract. The blue hyperlink simply takes a person to another page of the contract, similar to turning the page of a written paper contract. Although there is no conspicuousness requirement, the hyperlink's contrasting blue type makes it conspicuous. Common sense dictates that because the plaintiffs were purchasing computers online, they were not novices when using computers. A person using a computer quickly learns that more information is available by clicking on a blue hyperlink.

Additionally, on three of the defendant's Web pages that the plaintiffs completed to make their purchases, the following statement appeared: "All sales are subject to Dell's Term[s] and Conditions of Sale." This statement would place a reasonable person on notice that there were terms and conditions attached to the purchase and that it would be wise to find out what the terms and conditions were before making a purchase. The statement that the sales were subject to the defendant's "Terms and Conditions of Sale," combined with making the "Terms and Conditions of Sale" accessible online by blue hyperlinks, was sufficient notice to the plaintiffs that purchasing the computers online would make the "Terms and Conditions of Sale" binding on them. Because the "Terms and Conditions of Sale" were a part of the online contract and because the plaintiffs did not argue that their claims were not within the scope of the arbitration agreement, they were bound by the "Terms and Conditions of Sale," including the arbitration clause.

Because we conclude that the "Terms and Conditions of Sale" were a part of the online contract formed at the time of the plaintiffs' purchase of the computers, we need not consider what effect the copies of the "Terms and Conditions of Sale" enclosed in the shipping boxes have on the contract…

Arbitration Agreement Unconscionable

The defendant also argues that the trial court erred in finding that if the arbitration agreement was binding, it was unenforceable because it was procedurally and substantively unconscionable. This finding assumed that the arbitration agreement was otherwise valid.

The doctrine of unconscionability applies to arbitration agreements just as it applies to other contracts. *AutoNation USA Corp.*, 105 S.W.3d at 198. If an arbitration agreement is unconscionable, it is unenforceable. *In re Turner Brothers Trucking Co.*, 8 S.W.3d 370, 376 (Tex.App.1999). The test of unconscionability is whether, "given the parties' general commercial background and the commercial needs of the particular trade or case, the clause involved is so one-sided that it is unconscionable under the circumstances existing when the parties made the contract." *AutoNation USA Corp.*, 105 S.W.3d at 198. The purpose of the doctrine of unconscionability is to prevent oppression and unfair surprise. *AutoNation USA Corp.*, 105 S.W.3d at 198. Unconscionability is a question of law (*Pony Express Courier Corp. v. Morris*, 921 S.W.2d 817, 820 (Tex.App.1996)) and is determined on a case-by-case basis (*In re H.E. Butt Grocery Co.*, 17 S.W.3d 360, 371 (Tex.App.2000)).

There are two aspects to unconscionability. Procedural unconscionability refers to the circumstances surrounding the adoption of the arbitration provision. *AutoNation USA Corp.*, 105 S.W.3d at 198. Substantive unconscionability refers to the fairness of the arbitration provision itself. *AutoNation USA Corp.*, 105 S.W.3d at 198. The party asserting unconscionability has the burden of proving both procedural and substantive unconscionability. *In re Turner Brothers Trucking Co.*, 8 S.W.3d at 376–77.

Here, the trial court found that the arbitration agreement was procedurally unconscionable for the following reasons:

> "The manner in which the existence of the arbitration provision was minimized as to not to [*sic*] attract the attention of the customer, as well as the other aspects of the sale relating to the lack of disclosure of the terms and conditions as previously discussed, make [*sic*] it fundamentally unfair. This is particularly apparent when one considers the adhesive nature of sales between Dell and the consumer and the significance of the right of a party to present his claims in court[.]"

When it ruled that the arbitration clause was procedurally unconscionable, the trial court held that the arbitration agreement should have been conspicuous. "Texas law invalidates only certain types of clauses if they are inconspicuous" and an arbitration agreement is not one of those. Further, the Uniform Commercial Code, as adopted in Texas, provides that a term or clause is conspicuous when it is written so that a reasonable person against whom it is to operate ought to have noticed it. Tex. Bus. & Com.Code Ann. § 1.201(10) (Vernon 1994); *Arthur's Garage, Inc. v. Racal–Chubb Security Systems, Inc.*, 997 S.W.2d 803, 814 (Tex.App.1999). A term or clause is conspicuous if it is written in capital letters or if it is written in larger or other contrasting type or color print. Tex. Bus. & Com.Code Ann. § 1.201(10) (Vernon 1994); *Arthur's Garage, Inc.*, 997 S.W.2d at 814.

In the instant case, the hyperlinks for the "Terms and Conditions of Sale" were in a contrasting blue color. On the linked Web page for the "Terms and Conditions of Sale," the arbitration clause was partially in capital letters, thereby drawing attention to the clause. Also, the beginning of the "Terms and Conditions of Sale" stated in bold, capital letters that the terms and conditions contained a dispute-resolution clause. Thus, although we do not hold that an arbitration clause must be conspicuous, in this case the "Terms and Conditions of Sale" and the arbitration clause were conspicuous.

The court also determined that the arbitration clause was procedurally unconscionable because it was a contract of adhesion. A contract of adhesion exists where one party has absolutely no bargaining power or ability to change the contract terms. *In re H.E. Butt Grocery Co.*, 17 S.W.3d at 370–71. However, a contract of adhesion is not automatically unconscionable. *In re H.E. Butt Grocery Co.,* 17 S.W.3d at 371. Because the court engaged in no other analysis and simply found that the defendant's arbitration clause was unconscionable because it was a contract of adhesion, the court erred in finding that the arbitration agreement was procedurally unconscionable.

The court also determined that the arbitration agreement was substantively unconscionable because the agreement provided that "the exclusive arbitrator of any dispute is one which compensates its arbitrators in a way that has been found to 'impinge on neutrality and fundamental fairness.' *Toppings v. Meritech Mortgage Services, Inc.,* 212 W.Va. 73, 569 S.E.2d 149 (2002)." The court also found that the plaintiffs' action could only proceed as a class action, that the arbitration clause prohibited arbitration on a class-wide basis, and that enforcement of the arbitration clause would substantively deny the plaintiffs and the class members any chance of recovery. The trial court concluded:

> "While parties are free to agree to submit their disputes to arbitration, Dell is seeking to impose its unilateral choice of the use of arbitration as well as its selection of the actual arbitrator on its customers. The record suggests that the result of this arrangement is an arbitration process which, among other things, results in favorable results for defendants on an inordinate basis, limits remedies available to the customer, requires the customer to potentially incur greater costs than the amount he can recover, and exposes the customer to the possibility of paying the fees and costs of Dell. The Court finds the arbitration provision is both procedurally and substantively unconscionable."

The plaintiffs argue that the defendant's arbitration agreement is substantively unconscionable because the arbitration agreement deprives them of their statutory rights and remedies. Specifically, the plaintiffs argue that NAF's rules have a "loser pays" rule, which contravenes the mandates of the Texas and Illinois consumer protection statutes, and that NAF's rules deprive the plaintiffs of punitive damages, again in contravention of their statutory rights under the consumer laws of Texas and Illinois. The plaintiffs also argue that the defendant's arbitration agreement prevents arbitration on a class-wide basis.

With regard to the plaintiffs' argument that the arbitration agreement deprives them of their statutory rights by imposing a "loser pays" rule, we note that NAF's code of procedure states in Rule 37C: "An

Award may include fees and costs awarded by an Arbitrator in favor of any Party *only as permitted by law* or in favor of the Forum for fees due." (Emphasis added.) Nat'l Arbitration Forum Code of Procedure R. 37C, eff. July 1, 2000. The complete rule belies the plaintiffs' argument. If the statute does not provide for awarding fees and costs (or attorney fees), NAF's arbitrator will not do so. Additionally, the rule states that the arbitrator "may" impose fees and costs, which implies that the imposition of fees and costs is discretionary and not mandatory. The plaintiffs' arguments in the trial court and on appeal are couched in generalities. Because the plaintiffs failed to prove their argument in the trial court and have not shown on appeal that the arbitrators would impose such fees and costs on them, their argument fails. See *In re FirstMerit Bank, N.A.*, 52 S.W.3d 749, 756–57 (Tex.2001) (the arbitration clause was not substantively unconscionable where no specific evidence was presented that excessive fees and costs would actually be charged to effectively deny the plaintiffs access to arbitration).

The plaintiffs argue that the arbitration clause prevents punitive damages because the amount of filing fees in the arbitral forum rests upon the amount of damages asserted in a claim. Therefore, in order for the plaintiffs to assert a claim for punitive damages, they would have to pay an excessive filing fee, making a request for punitive damages prohibitive. Again, the plaintiffs have not shown that NAF would impose such fees upon them. NAF's code of procedure states in Rule 44F, "Issues regarding filing fees, including the value of relief sought, may be raised by any Party and shall be resolved by the Director or by an Arbitrator." Nat'l Arbitration Forum Code of Procedure R. 44F, eff. July 1, 2000. The plaintiffs did not show in the trial court and have not shown on appeal how NAF's code of procedure, when considered as a whole, prevents them from recovering punitive damages. It is the plaintiffs' burden to prove that the arbitration agreement is unconscionable (see *In re Turner Brothers Trucking Co.*, 8 S.W.3d at 376–77), and the plaintiffs have not shown that it could not collect punitive damages because of the size of NAF's filing fees.

The plaintiffs argue and the trial court held that the defendant's arbitration agreement was unconscionable because it prevented the plaintiffs from proceeding with a class action lawsuit. We find the language of the court in *AutoNation USA Corp.*, 105 S.W.3d at 200, to be instructive. The court stated:

> "This assumes that the right to proceed on a class-wide basis supercedes a contracting party's right to arbitrate under the FAA [(Federal Arbitration Act)]. However, the primary purpose of the FAA is to overcome courts' refusals to enforce agreements to arbitrate and to ensure that private agreements to arbitrate are enforced according to their terms. The Texas Supreme Court has made it clear that the FAA is part of [the] substantive law of Texas and has stressed that ' [p]rocedural devises,' such as Rule 42[']s provision for class actions, 'may " not be construed to enlarge or diminish any sustantive rights or obligations of any parties to any civil action." ' Accordingly, there is no entitlement to proceed as a class action..

In *AutoNation USA Corp.*, the plaintiff alleged that the arbitration provision in his agreement was substantively unconscionable because it prohibited class actions for small-damage consumer claims. The court in *AutoNation USA Corp.* found that even though the plaintiff argued that "without the class action device, consumers will be disinclined to pursue individual remedies for small damages," the plaintiff had

failed to demonstrate that the arbitration provision was substantively unconscionable. *AutoNation USA Corp.*, 105 S.W.3d at 200.

Here, too, the plaintiffs' generalized arguments that they would be deprived of a remedy if they were forced to arbitrate are insufficient to sustain the burden of proving that the arbitration provision is unconscionable.

Finally, the court found that the defendant's arbitration agreement results in favorable decisions for the defendant "on an inordinate basis." The defendant provided evidence to the trial court that in a three-year period, 5 disputes out of 20 went to arbitration. Of the five disputes that were arbitrated, the defendant won two and lost three of the disputes. These do not appear to be results favorable to the defendant on an inordinate basis. The trial court's finding that the defendant's arbitration agreement was unconscionable was error.

CONCLUSION

In conclusion, the trial court erred in determining that the defendant's arbitration agreement was not a part of the parties' online contract, in denying the defendant's motion to strike, and in holding that the arbitration agreement was both procedurally and substantively unconscionable. Therefore, we reverse the trial court's order denying the defendant's motion to compel arbitration and remand this case to the trial court with directions for the court to either stay or dismiss the proceedings and order the parties to arbitrate their disputes.

For the foregoing reasons, the judgment of the circuit court of Madison County is reversed, and the cause is remanded with directions.

Reversed; cause remanded with directions.

DONOVAN, P.J., and McGLYNN [FN1], J., concur.

Case 8: a requirements contract

Case

Alloy, a steel manufacturer, promised to sell Motor Works, a car manufacturer, as much steel as it ordered during the coming year for a set price per ton. Is the promise binding (a) if the market price rises to 20 per cent more than the contract price, and Motor Works orders the amount of steel it usually needs? (b) if the market price rises to 20 per cent more than the contract price, and Motor Works orders twice the steel it usually needs? (c) if the market price falls to 20 per cent below the contract price, and Motor Works buys no steel from Alloy, buying its requirements of steel on the market instead?

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Discussions

FRANCE

The arrangement between Alloy and Motor Works seems to be aimed at fixing the general conditions of sale, which will be the subject of later orders. Under French law, such a contract would be considered a framework contract (*contrat cadre*) as opposed to the sales contracts (*contrats d'application*) which implement the initial contract. It is probably more accurate to view the *contrat cadre* as a convenient and practical category which scholarly opinion (*doctrine*) has constructed so that it will not be necessary to analyse each sale as a new contract with its own conditions. This construction is more elegant.

The only other possible analysis, in our view, would be to consider the arrangement to be a unilateral promise to sell (*promesse unilatérale de vente*) since Alloy is already bound to sell at a fixed price while Motor Works may or may not decide to purchase. Such a promise to sell may be void here

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because Alloy's own obligation to deliver is uncertain: the amount to be delivered has not been determined. Such an obligation may be void under art. 1129 of the Civil Code[1] and kindred articles which require a contractual obligation to be definite. In any event, such an analysis would require the promise to be transformed into a contract of sale each time Motor Works exercised its option to purchase. It is impracticable to imagine Motor Works repeating such an operation each time it sends an order.

We therefore prefer to analyse the agreement as a framework contract to supply the amount of steel subsequently ordered. Nevertheless, this analysis does not get rid of the difficulty of how to quantify Alloy's obligation: how many tons of steel is it obliged to deliver to Motor Works? If the answer remains 'as many as Motor Works orders', then the contract may still fall foul of the provisions of art. 1129 and related articles of the Civil Code.

These articles require a contractual obligation to be definite. Under art. 1108,[2] the object of the contract must be certain. Under art. 1129, the subject matter of the obligations must be determined or determinable. Similarly, under arts. 1583[3] and 1591,[4] in a sale, if the price of the goods or the amount to be delivered is undetermined or undeterminable, and the contract includes no mechanism for determination, the contract is void for uncertainty (*l'indétermination de l'objet*). If the contract were for the sale of specific goods, the contract would not have to contain any special provision as to quantity. It would be enough to specify the goods. But where, as here, generic goods are sold by quantity, both the type of goods (steel) and the quantity must be determined or determinable. The type of goods must be determined at formation of the contract; the quantity may be set later or may be determinable at the time of performance.

If determining the quantity required a new agreement by both of the parties, then the initial contract would be void for uncertainty. The judge has no power to set a price in the absence of contractual agreement. These principles have been applied by case law to framework contracts.

If the quantity were to be determined at the sole discretion of the promisor under the obligation, who could therefore decide whether or

[1] It is necessary that the subject matter of an obligation is at least determinable as to its kind. The quantity of the thing can be uncertain provided that it can be determined.

[2] Article 1108: 'Four conditions are essential for the validity of an agreement (*convention*): the consent of the person who obligates himself; his capacity to contract; certainty of the object which is the subject matter of the undertaking; a licit *cause* for the obligation.'

[3] Article 1583: 'The sale is perfect as between the parties, and the buyer obtains title as of right from the seller, as soon as they have agreed on the thing and the price sold, even if the thing has not yet been delivered nor the price paid.'

[4] Article 1591: 'The price of the sale must be determined and fixed by the parties.'

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not to be contractually obligated, it would constitute a *condition potestative*. The contract would then be void under art. 1174 of the Civil Code.[5] This is not the case, as the quantity ordered does not depend on Alloy (the promisor of the relevant obligation) but on Motor Works.

Here, the quantity depends on the sole discretion of the promisee. The cases most closely in point concern contracts in which the price depends on the discretion of one of the parties. For a long time, the *Cour de cassation* held such a contract void for uncertainty under arts. 1129 or 1583 of the Civil Code. Recently, however, the Court overruled its prior decisions by holding that such indeterminacy no longer voids the contract. Nevertheless, a remedy will be granted if there is an abuse in setting the price. Damages may be awarded. Alternatively, or in addition, the contract may be terminated as to the future, although, despite the general rule of French law,[6] it will be deemed valid as to past transactions.[7] Therefore, a party complaining of indeterminacy will now claim relief on the grounds of an abuse of a right.

This result is an application of the theory of 'abuse of right' developed by the case law and by legal scholars which limits the exercise of a right by its owner. Although an abuse of right is most obviously characterized by an intention to harm another person, the concept extends to any behaviour deemed to be illegitimate.[8] Assessing such behaviour is left to the lower court judges but they are subject to review by the *Cour de cassation* as the question raised is one of law: whether a right has been abused by infringing the liberty of another person.

In contracts in which the price is set by one of the parties, the traditional approach which voided the contract for uncertainty was an attempt to deal with the same basic problem as the new one which looks for an abuse of right. It is the problem of fairness. It is self-evident that some degree of certainty is necessary if an agreement is to be enforced. But the requirement of certainty also constitutes a guarantee for the parties, and particularly the promisee, that the other party cannot impose an excessive or unsatisfactory obligation on him.[9] This need for protection has led

[5] Article 1174: 'Every obligation is void when it is made under the *condition potestative* of the promisor.'

[6] A. Colin and H. Capitant, *Cours élémentaires de droit civil français*, 3rd edn, vol. II (1920–1), no. 2, p. 350; Ghestin, Jamin, and Billau, *Traité de droit civil* nos. 482 ff.

[7] Ass. plén., 1 Dec. 1995, JCP 1996, II, 22565, concl. Jeol, note J. Ghestin; D 1996, 13, concl. Jeol, note L. Aynès.

[8] Ghestin, Gorbeaux, and Fabre-Magnan, *Traité de droit civil* no. 761, pp. 747 f.; C. Jamin, 'Réseaux intégrés de distribution', JCP, 1996, I, 3959.

[9] See Flour and Aubert, *Droit civil* 1; A. Colin, *L'acte juridique*, 7th edn (1996), no. 244, p. 165.

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the courts to refuse to enforce contracts in which a price depends on the sole discretion of one of the parties, for example, in franchising and in contracts for exclusive distribution. Imposing such a requirement in a framework contract might seem artificial since these contracts do not actually include prices, but merely an agreement for future sales contracts. However, the imposition of a limit on the discretion of a party over the content of the contract, and especially the price, was a recognition that in such a situation, the position of the promisee is weak. The policing of the manner in which the parties set the contract price was an indirect way of avoiding economic imbalance. It prevents the weaker party from being subject to the arbitrary economic power of the other.

The new approach to policing unfairness in such contracts by asking if a right has been abused has received both criticism and approval from scholars.[10] It is clear, however, that the remedies it makes available – damages and non-retrospective termination – are easier to administer and more satisfactory in practice. The older approach – voiding the contract for indeterminacy – led to serious practical difficulties concerning restitution, and was not necessarily the appropriate corrective remedy that the promisee was really looking for.

If the cases on an indeterminate price are applied here by analogy,[11] then the contractual obligation to deliver an undetermined quantity of steel will be valid but subject to a claim of abuse of right.

The consequence, in Case 8(a), is that Motor Works may validly order the amount of steel which it usually orders even if the market price has risen 20 per cent above the contract price. It will not have abused its right to determine the quantity it buys. The theory of *imprévision* or relief for changed and unforeseen circumstances is not accepted in French private law and therefore would not be applicable even if a rise in the market price constituted such a change. The French rejection of this theory is based on a strict interpretation by the courts of art. 1134 of the Civil Code. French law does grant relief for *force majeure*, but that is a quite different doctrine which applies only when performance has become impossible.[12]

In Case 8(b), in contrast, Alloy could receive a remedy for abuse of right if it succeeds in proving that Motor Works ordered twice as much steel

[10] For the diversity of opinions, see 'Le contrat-cadre de distribution', JCP 1997, ed. E., and particularly, J. Ghestin, 'La notion de contrat-cadre et les enjeux théoriques et pratiques qui s'y attachent' 7 f.; L. Aynès, 'La question de la détermination du prix', 16 f.

[11] Terré, Simler, and Lequette, *Les obligations* no. 262, p. 219.

[12] For an explanation and criticism of the refusal of French law to accept the theory of *imprévision*, see Ghestin, Jamin, and Billau, *Traité de droit civil* no. 260, pp. 288 ff.

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with an intention to do harm (for example, to get rid of a competitor) or for an illegitimate reason. It would then be able to obtain termination of the contract and/or damages for the breach. Characterizing such behaviour as illegitimate is tricky. It would be up to the judges of the lower courts to decide. Although trying to make a profit is not in itself illegitimate, it could be argued that if Motor Works ordered twice as much in order to resell the steel and thus be in competition with Alloy, it would be changing the purpose of their framework contract, which was intended as a supply contract and not a distribution contract.

In Case 8(c), however, where the market price has fallen, Motor Works would be under no obligation to buy any steel. The contract does not contain an exclusive dealing clause, and it imposes an obligation only on Alloy. Under French law, it would be a unilateral contract as opposed to one that is bilateral or synallagmatic (*synallagmatique*) where both parties are under an obligation. It follows that Motor Works need not buy any steel, and obviously will not if the market price is lower than the contract price.

We have already explained why the contract is less likely to be analysed as a unilateral offer to sell, on the part of Alloy, with an option for Motor Works to order as much steel as it wants. Even if this analysis were preferred, it is interesting that a court might then take the traditional approach and void the contract because its content is uncertain. It would probably be held to be uncertain, and therefore void under arts. 1129 and 1583 of the Civil Code, because the quantity to be delivered depends upon the sole discretion of Motor Works.[13]

BELGIUM

The agreement in this case is a supply contract (*contrat d'approvisionnement*). This contract is perfectly valid. The fact that the quantity term is left open does not raise any difficulty under art. 1129 of the Belgian Civil Code (identical to art. 1129 of the French Civil Code) which requires that the object of the contract be certain. The controversy never arose in Belgium, as it did in France, as to the need for complete certainty in quantity (under art. 1129) and price (under art. 1591, also identical in the French and Belgian Civil Codes). Belgian law has always clearly distinguished between a contract that provides a framework for future transactions and the contracts

[13] Terré, Simler, and Lequette, *Les obligations* no. 279–3, p. 235; Collart-Dutilleul and Delebecque, *Contrats* no. 148, p. 131.

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Uniform Law for International Sales under the 1980 United Nations Convention

Second Edition

by

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freedom under the Convention to shape the transaction to meet their needs supports the view that exchanges of goods are not excluded unless the parties so choose (Art. 6, *infra*).[13] On the other hand, some "counter-trade" arrangements, primarily concerned with the balance of payments, may not describe the goods or other obligations of the parties with sufficient definiteness to constitute a contract of sale. See §56.2 and Article 14, §133 *infra*. See Draft UNCITRAL Legal Guide on Drawing up Contracts in International Countertrade Transactions (Ch. III of 1990 draft considers alternative approaches to contract. A/CN.9/332); *Kritzer Manual* Ch. 25; Loeber in *Weidring Conf.* (1986) 299–315.

56.2 **(3) Framework Agreements for Future Orders and Deliveries; Franchise Agreements.**

Example 2B. A supplier (S) and a distributor (D) make a "framework" agreement that will govern any orders and deliveries by S to D but does not require D to order or S to deliver any specified quantity of goods.

This agreement, without more, does not constitute a "contract of sale" under Article 1 and is not governed by the Convention. (The definiteness required of offers is discussed under Article 14 at §§134–137, *infra*.) However, if orders are thereafter made and accepted, the "framework" agreement can supply the detailed terms of the transaction to supplement or modify the provisions of the Convention. See Article 6, §§74–84. If the "framework" agreement was made before the date of the Convention's entry into force, under Article 99 the Convention would govern orders and contracts made after that date but not before.

The arrangements and practices involved in franchise and dealership relationships are too varied for thorough treatment here. Dealers sometimes sue for losses incurred in preparing for a franchise arrangement that is expected on the basis of representations that fall short of promises. These claims present some of the problems presented by outlays during negotiations that fail to ripen into contract -- the problem known in some legal systems as *culpa in contrahendo*.

13. Professor Schlechtriem, on the other hand, suggests that barter transactions are not "contracts of sale" under Article 1. Schlechtriem, *1986 Commentary* 24 and n. 41b. The present writer would agree that the complexity of some barter or counter-trade arrangements may suggest exclusion of the Convention based on the parties implied intent. See Arts. 6 and 8, *infra*.

These problems arise from such diverse settings that they are dealt with or excluded by provisions of Part II on Formation of the Contract. Other problems arise out of termination clauses in franchise agreements that are challenged as so harsh as to violate standards of conscionability -- problems of contract validity that Article 4(a) leaves to domestic law. See §§64–69 (validity) and §§94–95 (good faith). In addition, close examination of the facts may show that the issue does not arise out of a "contract of sale of goods" and therefore falls outside of the scope of the Convention.

56.3 (4) Undivided Shares of Fungible Goods

Efficient handling of some types of goods (*e.g.* oil, grain) calls for their storage or their shipment in quantities greater than the units needed for sale. Units of such goods (*e.g.* bushels of No. 2 Durham wheat, barrels of No. 3 heating oil) are sufficiently uniform ("fungible") throughout a tank or bulk carrier that contracts of sale may be framed not merely in quantities of generic goods (*e.g.* 1,000 bushels of No. 1 Durham wheat) but instead in terms of quantities or shares of the contents of an identified bulk ("tank #63"; "tanker North Star sailing June 1").

These transactions are clearly "contracts of sale of goods" within Article 1 and no provision excludes them from the Convention.[14] Thus, failure to deliver goods of the agreed quality or quantity and failure to receive and pay for the goods and many related questions are governed by the Convention. The only substantial question is whether sales of quantities or shares in an identified bulk of fungible goods can satisfy the "identification" requirements of Articles 67(1) and 69(3) governing risk of loss. See §§371, 378, *infra*.

14. The question would scarcely be worth mentioning but for the fact that language of the (U. K.) Sale of Goods Act has led to doubt of its applicability to such transactions. *Benjamin* §§119. *Contra*: *Ont. L. Ref. Com.* I, 44–45; Draft Uniform Sale of Goods Act §8, Uniform Law Conference of Canada (Proceedings, 1982) 537; (U. S. A.) UCC2–105(4), 1–201 (definition of "fungible").

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Why Does America Not Recognize Framework Contracts When Civil Law Countries Do?

In recent decades, the dominant legal form of sale of goods transactions between businesses in America and around the world has undergone a profound transformation. In the 1950s, when the Uniform Commercial Code was completed, business buyers and sellers typically formed sales contracts through the exchange of different standard types of business documents such as purchase orders and invoices. This practice has declined in recent decades and been supplanted by a new practice: the parties to the transaction enter into a formal agreement establishing a common set of terms and conditions that will govern their relationship. Then individual sale of goods transactions take place under that framework. While this new concept of a "framework contract" is recognized in the case law that has developed under the 1980 Vienna Convention on the International Sale of Goods and in many European civil law systems, its emergence has generally been overlooked in common law countries, notwithstanding its widespread use among contracting parties.[1]

The business practice that preceded the use of framework contracts was captured in Uniform Commercial Code § 2-207, a provision that is colloquially known as the "Battle of the Forms" provision. Sophisticated businesses rarely suffer from battle of the forms problems because they changed their business model, which in turn made the battle of the forms provision of American sale of goods law largely irrelevant. Businesses are increasingly embracing networks of relational contracts and turning away from both public markets and corporate bureaucracies. Management experts have commented on the disaggregation of large-scale corporate bureaucracies into business networks; increased competition triggered by the disintegration of national markets into local and global markets; and the furious pace of technological innovation in communication, production and distribution systems. These structural changes have driven the growth of global supply chains, and within successful supply chains, framework contracts are the preferred governance mechanism for collaborative business networks.

Sales law in common law countries was first codified with the English Sale of Goods Act of 1893 followed by the American Sale of Goods Act of 1906. Within the broader effort to codifying American commercial law, Karl Llewellyn recreated the formalist Sale of Goods Act in quintessentially realist form as Uniform Commercial Code Article 2. One of the pivotal provisions was UCC § 2-204 governing the formation of sale of goods contracts which provides in part, "A contract for sale of goods may be made in any manner sufficient to show agreement, including conduct by both parties which recognizes the existence of such a contract." Llewellyn's objective was to turn attention away from the abstract, formalist mechanics of offer and acceptance and turn attention toward the realities of contemporary commercial practice. While this new approach to contract formation may have seemed radical when it was first proposed in the 1940s, it soon became the new orthodoxy. When the formalist 1932 Restatement of Contracts was revised during the 1970s, it was infused throughout with the spirit of Llewellyn's realism.

[1] UK article

The open-ended approach to contract formation enshrined in Article 2 was intended to allow American sales law to adapt effortlessly to changing commercial practice, but with regard to the rise of supply chains and framework contracts, it has made it more difficult for U.S. courts to keep U.S. law aligned with commercial practice. Although Llewellyn succeeded in draining the structure out of the primary contract formation provisions of Article 2, he inadvertently created a byzantine alternative contract formation provision in UCC § 2-207. Llewellyn drafted UCC § 2-207 to address a relatively narrow issue that had emerged in some pre-code cases, and there is no evidence he ever anticipated it would be used to address what became known as the Battle of the Forms problem.[2] In the decades following the promulgation of the Uniform Commercial Code, however, the influence of what is now known as the Battle of the Forms provision of the UCC has grown to such a degree that at times it seems to overshadow Llewellyn's primary contract formation provision. By contrast, sales law in European civil law jurisdictions which lack both the realist excesses of UCC § 2-204 and the byzantine formalism of UCC § 2-207, have had no problem in recognizing and accommodating the rise of framework contracts.

The rise of "supply chain management" as a new source of competitive advantage in global markets is a reflection of a much larger transformation taking place throughout systems of business administration at the beginning of the 21st century. By the time historian Chandler published The Visible Hand: The Managerial Revolution in American Business in 1977, "Managerial Capitalism" was already beginning to crumble under the weight of globalization and accelerating technological innovation. Academics in business schools have studied the rise of supply chains extensively from the point of view of operations research but they have not student the rise of framework contracts as governance mechanisms.

The purposes of the UCC include simplifying, clarifying and modernizing the law governing commercial transactions, and permitting continued expansion of commercial practices through custom, usage and agreement. UCC § 1-103. When U.C.C. Article 2 was finalized in the 1950s, paper purchase orders were also widely used by American businesses. The purchase order originated with the rise of large corporations and modern accounting systems in the late 19th century. Purchase orders were a pivotal element in control systems used to prevent unauthorized transactions using corporate resources: no one outside the purchasing department could make a major purchase unless someone inside purchasing confirmed their authority and budget before issuing a "purchase order number," and no one inside the purchasing department could buy things except in response to requests from other departments.

Purchasing clerks used marketing materials such as paper catalogues or price lists to fulfill requests from other departments for goods and services. In addition to pictures and text descriptions, catalogues also included item numbers for each product that could be added to purchase orders to reduce the likelihood that the vendor would make mistakes filling the order. The terms specific to a single transaction—such as price, quantity, item description, shipping terms, and date—were normally hand written or typed on the face of the paper purchase order while the standard boilerplate terms and conditions were normally printed on the back of it.

[2] White & Summers, "Like the amphibious tank that was originally designed to fight in the swamps, but was ultimately sent to fight in the desert."

A copy of the purchase order would also be sent to the accounting department in addition to the vendor to await the vendor's invoice. After the receiving department had taken delivery of the goods described in the purchase order and send a receiving report to accounting, accounting would collect the three documents and try to make a "three way match" before it paid for the goods. If the vendor's invoice did not match the purchase order or receiving report, then someone in accounts payable would have to figure out why the three documents didn't match and resolve the conflict before payment could be made. For example, if purchasing issued a purchase order for 3 units and receiving took delivery of 3 but the vendor's invoice billed for 4 units, then the vendor might be required to reissue the invoice for the correct amount before payment would be sent.

If a single purchaser and a single supplier engaged in a steady stream of transactions involving a limited number of products or services, then the parties might agree that they could dispense with some of the administrative formalities of the basic purchase order and instead use a single "blanket" purchase order for a number of transactions. The purchasing department can issue a single purchase order number for a series of transactions within a specified period of time and up to a maximum volume of goods or money spent. Individual transactions under a blanket purchase order are referred to as "releases" and the supplier is authorized to invoice the purchaser for each release rather than for each purchase order. A framework contract resembles a blanket purchase order in that they both provide a framework for a series of sale of goods contracts between two parties, but framework contracts are normally broader in scope than blanket purchase orders. ***In addition, framework contracts are normally signed by both parties, not just the purchaser.***

Beginning in the 1970s, many organizations discontinued the use of basic purchase orders or blanket purchase orders to govern their relationships with their most important customers or suppliers and adopted framework contracts instead. Consolidating a series of transactions under a single contract may allow the buyer to negotiate more favorable terms than would be possible if it simply placed a series of separate orders for goods at catalogue prices. Under a framework contract, individual purchase orders incorporating by reference the terms of the framework contract may be used to document the terms of individual transactions. Even an organization that framework contracts to govern its relationships with most of its suppliers and largely discontinued the use of ad hoc purchase orders will still need to use ad hoc purchase orders from time to time. For example, even a large, sophisticated organization that largely relies on framework contracts to manage its relationships with suppliers might need to issue ad hoc purchase orders for relatively large but non-recurring purchases.

By contrast, many if not most small businesses continue to rely on purchase orders as the primary mechanism for documenting contracts with suppliers. This is because small businesses usually have simpler accounting and management systems than large businesses as well as less market power as purchasers. As a result, the cost of negotiating framework contracts would outweigh the benefits to most small businesses. So many small businesses continue to follow the 1950s model of issuing individual purchase orders for all their major purchases, although those purchase orders may be in electronic form rather than on paper. If a small business's supplier is a large, sophisticated business then that supplier may be able to require its customers to use the supplier's website to place orders, and thus prevent its customers from attaching any terms and conditions to their orders that would

conflict with the supplier's standard terms and conditions. On the other hand, if both the buyer and the supplier are small businesses with informal management systems, then the supplier accept from the buyer purchase orders formatted as spreadsheets attached to emails. One risk to a firm using an ad hoc purchase order is that the supplier will send back an acknowledgement with different standard terms and conditions, triggering a "Battle of the Forms" and the application of U.C.C. § 2-207 if a dispute arises the parties cannot resolve amicably.

Let's assume that each purchase order issued under a framework contract is deemed to be a separate sale of goods transaction. That still leaves unanswered the question of what kind of a contract the framework contract is. Would it make sense to interpret a framework contract as an "option" that the seller grants the buyer?

Restatement 2d of Contracts, § 25: An option is a promise which meets the requirements for the formation of a contract and limits the promisor's power to revoke an offer.

An option "contract" still requires some consideration in order to be effective. What consideration does the buyer provide its supplier in return for entering into a framework contract?

> Restatement 2d of Contracts, § 77 Illusory promises are not consideration, but recognition of the supplier as a possible strategic partner of the purchaser is consideration (e.g., it might be formalized as membership in purchaser's vendor qualification program, or not)
>
> Restatement 2d of Contracts, § 79 Adequacy of consideration: Ordinarily, courts do not inquire into the adequacy of consideration (therefore proof of an objective gain, advantage or benefit to promisor or detriment to the promisee is NOT required)

If the framework contract is an option, then the buyer exercises the option by issuing a purchase order that incorporates the framework contract's terms by reference.

Under UCC § 2-204, a contact for the sale of goods may be made in any manner sufficient to show agreement. A sale of goods contract normally includes the price, quantity and description of the goods; here, the purchase order specifies the price, quantity and description.

Because the framework contract creates a unified, coherent framework within which the rights and obligations of the parties can be clearly defined (opting out of UCC Article 2 defaults for specific terms), contract formation should be under UCC § 2-204, not UCC § 2-207.

Parties cannot expressly "opt out" of UCC Article 2 contract formation provisions like UCC § 2-207 provisions on contract formation the same way they can opt out of default contract terms provisions, contract formation is governed by objective standards applied by the court.

But there is no need to expressly "opt out" of UCC § 2-207 because contract formation is governed by Restatement 2d of Contracts § 25 on option contracts (Supply Agreement) and UCC § 2-204 on sale of goods contract (purchase order).

A New Approach to Contracts

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When Dell originally selected FedEx, in 2005, to handle all aspects of its hardware return-and-repair process, the companies drew up a traditional supplier contract. The 100-page-plus document was filled with "supplier shall" statements that detailed FedEx's obligations and outlined dozens of metrics for how Dell would measure success. For nearly a decade, FedEx met all its contractual obligations—but neither party was happy in the relationship. Dell felt that FedEx was not proactive in driving continuous improvement and innovative solutions; FedEx was frustrated by onerous requirements that wasted resources and forced it to operate within a restrictive statement of work. Dell's attempts to lower costs, including bidding out the work three times during the eight-year relationship, ate into FedEx's profits.

By the eighth year, the parties were at the breaking point. Each lacked trust and confidence in the other, yet neither could afford to end the relationship. Dell's cost of switching to another company would be high, and FedEx would have trouble replacing the revenue and profits the contract generated. It was a lose-lose scenario.

Unfortunately, this story is not unique. Companies understand that their suppliers are critical partners in lowering costs, increasing quality, and driving innovation, and leaders routinely talk about the need for strategic relationships with shared goals and risks. But when contract negotiations begin, they default to an adversarial mindset and a transactional contracting approach. They agonize over every conceivable scenario and then try to put everything in black-and-white. A variety of contractual clauses—such as "termination for convenience," which grants one party total freedom to end the contract after a specified period—are used to try to gain the upper hand. However, these tactics not only confer a false sense of security (because both firms' switching costs are too high to actually invoke the clauses) but also foster negative behaviors that undermine the relationship and the contract itself.

We argue that the remedy is to adopt a totally different kind of arrangement: a *formal relational contract* that specifies mutual goals and establishes governance structures to keep the parties' expectations and interests aligned over the long term. Designed from the outset to foster trust and collaboration, this legally enforceable contract is especially useful for highly complex relationships in which it is impossible to predict every what-if scenario. These include complicated outsourcing and purchasing arrangements, strategic alliances, joint ventures, franchises, public-private partnerships, major construction projects, and

collective bargaining agreements. A growing number of large organizations—such as the Canadian government, Dell, Intel, AstraZeneca, and the Swedish telecommunications firm Telia—are successfully using this approach.

In this article, we look at the theoretical underpinnings of formal relational contracts and lay out a five-step methodology for negotiating them.

Hold-Ups, Incomplete Contracts, and Shading

Companies have traditionally used contracts as protection against the possibility that one party will abuse its power to extract benefits at the expense of the other—for example, by unilaterally raising or lowering prices, changing delivery dates, or requiring more-onerous employment terms. Economists call this the *hold-up problem*: the fear that one party will be held up by the other. The fact that virtually all contracts contain gaps, omissions, and ambiguities—despite companies' best efforts to anticipate every scenario—only exacerbates hold-up behavior.

Leaders employ a range of tactics to try to ensure that they are not taken advantage of by a powerful partner. These include contracting with multiple suppliers, forcing suppliers to lock in prices, using termination-for-convenience clauses, or obligating suppliers to cover activities that might arise after the initial contracting phase. Some companies go so far as to install a "shadow organization" to micromanage the supplier.

Early research by one of us (Oliver, who won the 2016 Nobel Prize in economics for his work on contracts) predicted that in response to the combined problems of hold-ups and incomplete contracts, companies are very likely to make distorted investments that produce poor outcomes. Using multiple suppliers instead of only one, for example, increases costs; so does operating a shadow organization. Termination-for-convenience clauses create perverse incentives for suppliers to not invest in buyer relationships. "A 60-day termination for convenience translates to a 60-day contract," one CFO at a supplier told us. "It would be against our fiduciary responsibility to our shareholders to invest in any program for a client with a 60-day termination clause that required longer than two months to generate a return." The implications for innovation are obvious. "Buyers are crazy to expect us to invest in innovation if they do the math."

In 2008, Oliver, together with economic theorist John Moore, revisited his work on contracts. They realized that an equally important problem is *shading*, a retaliatory behavior in which one party stops cooperating, ceases to be proactive, or makes countermoves. Shading happens when a party isn't getting the outcome it expected from the deal and feels the other party is to blame or has not acted reasonably to mitigate the losses. The aggrieved party often cuts back on performance in subtle ways, sometimes even unconsciously, to compensate.

Imagine that a supplier of engineering services submits a proposal in a competitive bidding process and wins the contract. If demand is lower during the term of the contract than the buyer stated in the RFP or the scope expands in an unanticipated area, the supplier's profit will take a hit. If the buyer refuses to adjust the supplier's fee or the statement of work, the supplier may try to recoup losses by, for example, replacing the expensive A team it currently has on the project with its less costly C team. In long-term, complex deals, shading can be so pervasive that the tit-for-tat behavior becomes a death spiral. Oliver and Moore's expanded theory focuses on contracts as reference points, a new perspective that emphasizes the need for mechanisms to continually align expectations—or update reference points—as unanticipated events occur and needs change over time.

A New Approach

At the same time that Oliver and Moore were looking at the contracting problem from an economics perspective, University of Tennessee researchers (including two of us, Kate and David) were working with companies to come up with a new approach that would produce healthier and more sustainable partnerships. Their efforts led to the vested methodology for creating formal relational contracts—a process that establishes a "what's in it for we" partnership mentality. (It's called vested because the parties have a vested interest in each other's success.) Written contracts that are legally enforceable (which is why we call them formal), they include many components of a traditional contract but also contain relationship-building elements such as a shared vision, guiding principles, and robust governance structures to keep the parties' expectations and interests aligned.

Relational contracts that rely on parties' making choices in their mutual self-interest are nothing new, of course. The benefits of informal "handshake" deals have been studied and promoted over the decades; legal scholars Stewart Macaulay and Ian Macneil were early advocates in the 1960s. Japanese *keiretsu*, an arrangement in which buyers form close associations with (and often own stakes in) suppliers, is a type of relational contract (see "The New, Improved Keiretsu," HBR, September 2013).

Perhaps unsurprisingly, most companies—and their legal counsels in particular—are uncomfortable with informal handshake deals, especially when the stakes are high. In fact, many companies now believe that even the vaunted keiretsu model, which Toyota and Nissan, among others, used so successfully, ties up capital and limits flexibility. The formal relational contract addresses these deficiencies.

Shading happens when one party isn't getting the outcome it expected.

When Dell and FedEx reached their breaking point, they chose to abandon their existing contracting process and create a formal relational contract that specified desired outcomes and defined relationship-management processes at the operational, management, and executive levels. In the first two years, Dell and FedEx were able to reduce costs by 42%,

scrap by 67%, and defective parts per million to record-low levels. Both companies now consider the contracting approach a best practice and have applied it in other relationships.

To date, 57 companies have employed the vested methodology. (David and Kate have consulted on many of these projects, including several mentioned in this article.) Results have not been tracked for all of them, but many have told us that they and their partners are happy with the approach and cite benefits including cost savings, improved profitability, higher levels of service, and a better relationship.

Putting It into Practice

Before jumping into a formal relational contract process, companies must determine whether it is right for them. Some relationships, such as those involving the purchase of commodity products and services, are truly transactional and only need traditional contracts. But many organizations require long-term, complex relationships for which the vested methodology is well suited.

Buyers must consider three key factors when deciding what type of contracting arrangement is right for each supplier relationship. They should analyze their dependency on the particular supplier, the strategic value of its product, and the impact of nonperformance on a buyer's operations.

	TRANSACTIONAL CONTRACT	**FORMAL RELATIONAL CONTRACT**
BUYER'S DEPENDENCY ON THE SUPPLIER		
Switching costs:	—	—
Overall cost to switch suppliers	Low	Medium to high
Physical asset specificity (location, machinery, processes)	Low	Medium to high
Skill level of supplier's personnel	Unskilled to semiskilled	Skilled to professional
Level of integration required with supplier's systems or processes	None to low	Medium to high

What is the availability of substitutes in the marketplace?	—	—
Supplier services or products	Plentiful	Moderate to scarce
Qualified and skilled personnel	Plentiful	Moderate to scarce
Technology	Off-the-shelf	Custom
STRATEGIC IMPACT		
Is the supplier's product or service a strategic differentiator for the buyer?	No	Yes
Does the buyer benefit from access to the supplier's critical systems and processes (and vice versa)?	Very little	Moderately to very much
RISKS DUE TO SUPPLIER NONPERFORMANCE		
Lost profits	None to low	Medium to high
Damage to the buyer's customer or brand experience	None to low	Medium to high
Damage to the buyer's employee experience	None to low	Medium to high
Regulatory compliance penalties	None to low	Medium to high
Impact on demand management	None	Medium to high

Note: This table is based on material presented in *Strategic Sourcing in the New Economy* (Palgrave Macmillan, 2016).

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A case in point is Vancouver Island Health Authority and South Island Hospitalists, a partnership of administrators and doctors who work together to provide inpatient care for patients with the most complex medical issues in British Columbia. The entities decided to explore relational contracting in 2016, two years after their conventional contract had expired and countless hours of contentious negotiations had failed to replace it. Working with the University of Tennessee (including Kate), they embarked on the five-step process.

Step 1: Lay the foundation.

The primary goal of Step 1 is to establish a partnership mentality. Both parties must make a conscious effort to create an environment of trust—one in which they are transparent about their high-level aspirations, specific goals, and concerns. And if their previous contracting process led to distrust and a vicious cycle of shading, they should reflect on how and why that happened.

At Island Health and South Island, the parties tossed out the old contract and chartered a team of 12 administrators and 12 hospitalists to design a formal relational contract. Each individual worked with a counterpart from the other organization to establish connections in key areas. For example, Spencer Cleave, a hospitalist from South Island, and Kim Kerrone, Island Health's vice president for finance, legal, and risk, led a small group focused on rethinking the conventional fee-for-billable-service-hour payment structure.

"We were no longer interested in just developing a contract," recalled Jean Maskey, a hospitalist at South Island who coheaded the contracting team, "but in building excellent relationships at multiple levels that would allow all of us to be leaders in Canadian health care, whether as administrators or hospitalists."

Step 2: Co-create a shared vision and objectives.

To keep expectations aligned in a complex and changing environment, both parties—not just the one with greater power—need to explain their vision and goals for the relationship.

The Island Health and South Island team held a three-day off-site to craft their vision: "Together, we are a team that celebrates and advances excellence in care for our patients and ourselves through shared responsibility, collaborative innovation, mutual understanding, and the courage to act, in a safe and supportive environment." They further established a set of four desired outcomes that flowed from the shared vision:

- Excellence in patient care (develop a formal and robust quality structure)
- A sustainable and resilient hospitalist service (strengthen recruitment, mentorship, and retention processes; create an efficient and flexible hospitalist scheduling model; clearly define hospitalist services and workload; develop stronger interdepartmental working relationships; and train and develop current and future hospitalist leaders)

- A strong partnership (continue to build a healthy relationship between Island Health and South Island)
- A best-value hospitalist service (proactively manage the budget, optimize billing, review workload, and increase operational efficiencies)

In a subsequent workshop the team delved deeper, crafting four high-level desired outcomes, seven goals, and 22 tactical and measurable objectives. One objective, for example, called for improving physicians' billing to the provincial Medical Services Plan (MSP) for cost recovery for the hospitalist fees. The parties created a joint project collaboratively working with billing support and IT technologists to develop an electronic billing program to maximize billing submissions, ultimately improving cost recovery from 87% to 100%.

Step 3: Adopt guiding principles.

Value-eroding friction and shading occur because one or both parties feel unfairly treated. This risk is highest when there are many unknowns about what will occur after the contract is signed. In Step 3, parties commit to six guiding principles that contractually prohibit opportunistic tit-for-tat moves.

The six principles—reciprocity, autonomy, honesty, loyalty, equity, and integrity—form the basis for all contracts using the vested methodology and provide a framework for resolving potential misalignments when unforeseen circumstances occur.

Formal relational contracts are built on a foundation of trust and are shaped by a shared vision and six universal guiding principles. The wording crafted by Island Health and South Island, which they embedded in the preamble of their contract, can be used by other companies as a model for drafting their own guiding principles.

Shared Vision

- Together, we are a team that celebrates and advances excellence in care for our patients and ourselves through shared responsibility, collaborative innovation, mutual understanding, and the courage to act, in a safe and supportive environment.
- We will be recognized leaders in health care.
- We will achieve this vision by building relationships grounded in trust and respect, and anchored in the following Guiding Principles and Intended Behaviors.

Guiding Principles & Intended Behaviors

- **Reciprocity:** We conduct ourselves in the spirit of achieving mutual benefit and understanding. We recognize that this requires ongoing give-and-take. We each will bring unique strengths and resources that will enable us to overcome our challenges and celebrate our successes.

- **Autonomy:** We give each other the freedom to manage and make decisions within the framework of our unique skills, training, and professional responsibilities. We individually commit to make decisions and take actions that respect and strengthen the collective interest to achieve our Shared Vision.
- **Honesty:** We will be truthful and authentic even when that makes us vulnerable or uncomfortable. This includes honesty about facts, unknowns, feelings, intentions, perceptions, and preferred outcomes.
- **Loyalty:** We are committed to our relationship. We will value each other's interests as we value our own. Standing together through adversity, we will achieve our Shared Vision.
- **Equity:** We are committed to fairness, which does not always mean equality. We will make decisions based on a balanced assessment of needs, risks, and resources.
- **Integrity:** Our actions will be intentionally consistent with our words and agreements. Decisions will not be made arbitrarily but will align with our Shared Vision and Guiding Principles. Our collective words and actions will be for the greater good of the relationship and the provision of patient-centered care.

Island Health and South Island formally embedded their interpretations of the principles in the preamble of their contract. Each was crafted to establish a new norm for the partnership. Under "reciprocity," for example, they highlighted the need to "conduct ourselves in the spirit of achieving mutual benefit and understanding." Under "equity," they acknowledged the unavoidable imbalances that arise in contracts: "We are committed to fairness, which does not always mean equality. We will make decisions based on a balanced assessment of needs, risks, and resources."

Again, it's important to note that these guiding principles have teeth. Although the contractual language may be vague, courts are obligated to interpret it should there be a dispute. Indeed, the Canadian supreme court recently took up a case in which a franchisee alleged that it was not being treated fairly by the franchise owner. And therein lies the beauty of the formal relational contract. Few companies will want to risk an expensive court case for breaching the guiding principles; thus the contract becomes a deterrent against counterproductive behavior.

Step 4: Align expectations and interests.

Having set the foundation for the relationship in the first three steps, parties hammer out the terms of "the deal"—for example, responsibilities, pricing, and metrics. It is crucial that all terms and conditions of the formal relational contract are aligned with the guiding principles. With the right mindset, the development of the contract becomes a joint problem-solving exercise rather than an adversarial contest.

Consider how the Island Health administrators and South Island hospitalists tackled pricing, which had always been their sticking point. Historically, the two parties had operated under a shroud of opaqueness. For example, Island Health never shared the budget with the hospitalists. And South Island's less-than-optimal reporting processes meant inevitable bickering over billable hours.

Kim Kerrone, of Island Health, described how the vested methodology broke the impasse. "We consciously approached the economics of the relationship with full transparency and a problem-solving mentality instead of a negotiations mentality," she told us. "We put everything on the table, and we challenged the contracting team to figure out ways to work with the money we've got."

The parties ultimately came up with an alternative to the standard fee-for-billable-hours method. They designed a hybrid pricing model with a combination of fixed and variable rates, coupled with incentives to improve efficiencies. The model also gave the hospitalists autonomy in scheduling. After all, the team realized, who better to optimize the scheduling for superior patient care than the doctors on the front lines? Under the new pricing model, when the inpatient population is low, the hospitalists can opt to take time off and save Island Health money. When the population is high, they manage their hours in a way that's within the budget and optimizes patient care. South Island has the opportunity to earn incentives if they improve efficiency and billing, which they can invest in research and quality-of-care initiatives they are passionate about. Both parties felt that the new model was a win-win solution that would have been unachievable under previous contracts.

Step 5: Stay aligned.

In this step, contracting parties go beyond crafting the terms of the agreement and establish governance mechanisms that are formally embedded in the contract.

Island Health and South Island created four joint governance teams chartered to "live into" the relational contract:

- **The relationship team** focuses on monitoring the health of the relationship.
- **The excellence team** focuses on quality control, transformational initiatives, continuous improvement, and prioritization and tracking of innovation ideas.
- **The sustainability team** focuses on workload, scheduling, recruiting, and retention.
- **The best value team** focuses on finance, billing, workload optimization, and operational efficiencies.

Each team meets at regular intervals to review progress against the shared vision, goals, outcomes, and measures.

The contract also specifies a second governance mechanism—a “two in a box” communication approach in which an administrator is teamed with a hospitalist for each of the four governance teams. The approach encourages trust and honesty between the two sides, said Ken Smith, a hospitalist at South Island. “Before, we had no one to speak with [if concerns arose]. Now I have someone I know fairly well at a high level in administration. If I need to make an urgent decision or have a difficult issue that can’t wait for the next formal meeting, I can phone my two-in-a-box partner and ask to meet.”

Such pairings are also highly encouraged outside the governance teams to strengthen the relationship and build trust between parties at all levels. For example, Kim Kerrone and Jean Maskey, informal partners, both say that formal relational contracting was “transformational” for their respective organizations. Both point to the surveys conducted immediately before the process began and one year after the relational contract was in place: The number of people who expressed a positive attitude toward the relationship increased by 84% in just two years. Administrators and hospitalists who had called their relationship “broken,” “dysfunctional,” and “distrustful” now describe it as “collaborative,” “trusting,” and “supportive.”

Kerrone points to financial benefits as well. “For the first time, the administration and our doctors are innovating together to drive efficiencies and optimize for patient care with our limited budget,” she said. “We not only came in under budget, we also increased our revenue by improving our MSP billing process. And in a publicly funded health care environment, that is exactly what we need to be focusing on.”

The governance structure also helped the parties surmount the tricky problem of scope creep. While the contract was being developed, in 2016 and 2017, Canada passed a law legalizing medical assistance in dying. At the time, there were too many unknowns about how it would be implemented to address the issue formally. So the sustainability team came up with a pilot project to address how to fairly add the additional scope of work and new role for health care providers to the hospitalists’ schedule and pricing model. Gone were the battles of “not in scope”; instead, there was a spirit of “how can we accommodate this new reality given our statement of intent?”

The Future: Contracting for Competitive Advantage

Formal relational contracts will never completely replace traditional transactional contracts. Nor should they. But the process we have outlined should be part of the contracting tool kit to govern highly complex relationships that demand collaboration and flexibility.

Glenn Gallins, the attorney representing South Island Hospitalists and a law professor at the University of Victoria, offers the following advice when it comes to embracing formal relational contracts: “The focus on negotiating the foundation of the relationship first is brilliant. But the real power is it threads all the way down to core decisions on how the

parties would work." In a business world where strategic, long-term relationships are critical to competitive advantage, leaders have no choice but to overturn the status quo.

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Comment & Analysis

Christoph Busch, Hans Schulte-Nölke, Aneta Wiewiórowska-Domagalska, Fryderyk Zoll*

The Rise of the Platform Economy: A New Challenge for EU Consumer Law?

The aim of this paper is to reflect upon the need to adjust EU consumer contract law to take into account the changing market structure caused by the rise of online platforms such as Airbnb, Uber or Amazon Marketplace. It is argued that the existing regulatory framework is primarily focused on 'bipolar' transactions between businesses and consumers, and therefore does not provide adequate solutions for the growing number of 'triangular' transactions arising in the new platform economy. As a result, in many situations consumers concluding contracts through online platforms are left without effective consumer protection. One possible solution could be a new EU legislative instrument – possibly a 'Platform Directive' – clearly defining the criteria for distinguishing whether the platform operator is only a 'facilitator' or the actual supplier. In addition, a legislative instrument should specify the duties and obligations of the platform operator, making it clear under which conditions the platform operator is liable for a non-performance by the supplier.

I. Introduction

In recent years, companies using the platform business model have grown dramatically. Platform business models have emerged in various sectors, from retail (Ebay, Amazon Marketplace), travel (Airbnb), food home-delivery services (Delivery Hero), to transportation (Uber, BlaBlaCar) and banking (Zopa). The growth of the platform economy is closely linked with the digitalisation of products, services and business processes. Platforms are not only a challenge for existing business models, they have also given rise to regulatory controversy. There are concerns that platforms could attain a dominant market position and undermine competition by using the power of network effects.[1] There have also been concerns that, by classifying workers as independent contractors, platforms can circumvent the requirements of labour law.[2] In addition, from the perspective of consumer law, the rise of the platforms may cause the need for an adjustment to the existing regulatory framework.

The purpose of this short paper is to reflect on the question whether a reform of EU consumer contract law is necessary in order to ensure effective consumer protection and fair competition between businesses in the new platform economy. The structure of the paper is as follows. After some remarks on the multifaceted notion of 'platforms' (part II), the issue of whether the existing framework of EU consumer law provides adequate solutions for the new platform economy will be discussed (part III). Part IV provides some examples of problems that a future EU legislative instrument should address. This section focuses on information duties of the platform operator and the potential liability of the platform operator for non-performance by the supplier.

II. Online platforms – a new phenomenon?

When discussing the regulatory framework for 'platforms' in the Digital Single Market, some terminological clarifications are necessary. There are thousands of websites that call themselves a platform. The scope of this paper is limited to 'transaction platforms' enabling a customer, be it a consumer or not, to order goods or services in exchange for payment. As a result, online collaboration platforms, wikis and search engines are outside the scope. The same is true for business models such as dating platforms (e.g. Parship, Match.com) or online gaming platforms (e.g. World of Warcraft), which connect people with aims other than concluding a contract with other individuals.

Admittedly, the business model of platforms is not entirely new. Online marketplaces such as Ebay, which provide a possibility for non-professionals to sell used goods, have existed from the early days of the Internet. Moreover, what platforms do is also well known in the offline world. One example is the role of professional car dealers offering their help to consumers who want to sell their used cars. It is common practice that consumers ask a professional car dealer to advertise and sell a used car in their name and on their behalf. From a legal perspective, this business model usually does not result in a contract of sale between the professional car dealer and the buyer, but rather a contract between the consumer and the buyer, who is often also a consumer. At least under German law, this business model (commonly referred to as *Agenturgeschäft*) allows, if certain transparency requirements are met, the mandatory provisions of consumer sales law to be circumvented.[3] Although a professional trader was involved in the transaction, the contract of sale is considered to be a contract between two consumers, meaning that other consumer law provisions are also not applicable to this contract. The same is true for contracts concluded be-

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1 Monopolkommission, 'Special Report 68: Competition Policy: The Challenge of digital markets' (*Monopolkommission*, 1 June 2015) <http:// monopolkommission.de/index.php/en/reports/special-reports/284-special-report-68>; Bundeskartellamt, 'Digitale Ökonomie – Internetplattformen zwischen Wettbewerbsrecht, Privatsphäre und Verbraucherschutz' (*Bundeskartellamt*, 1 October 2015) <http://bundeskartellamt.de/SharedDocs/Publikation/DE/Diskussions_Hintergrundpapier/AK_Kartellrecht_2015_Digitale_Oekonomie.html?nn=3590858> (all websites last accessed 25 January 2016); see also R Podszun & S Kreifels, 'Digital Platforms and Competition Law' (in this issue).

2 See e. g. B Rogers, 'The Social Costs of Uber' [2015] 82 U Chi L Rev 85.

3 Bundesgerichtshof, Judgement of 26 January 2005, Case VIII ZR 175/04, NJW 2005, 1039; see also C Katzenmeier, 'Agenturgeschäfte im Gebrauchtwagenhandel' NJW 2004, 2632; F Maultzsch, 'Agenturgeschäfte im Gebrauchtwagenhandel und Gesetzesumgehung' ZGS 2005, 175.

Electronic copy available at: http://ssrn.com/abstract=2754100

tween two consumers via online marketplaces such as Ebay or Etsy.

While the basic idea behind the platform business model is not entirely new, the rise of digital technology has dramatically changed the quantitative and qualitative dimension of contracts concluded via online platforms. Some of the most successful online retailers have turned themselves into digital platforms. For example, Amazon.com has developed from the world's largest online bookstore into a huge online marketplace, where a broad range of products are available, not only from Amazon, but also from other suppliers.[4] Moreover, so-called 'sharing economy' platforms such as Uber, Airbnb or Book-a-tiger allow nearly everyone – including many consumers turned into 'prosumers' – to offer not only goods, but also services such as transportation, accommodation or cleaning services.

It is perhaps not a coincidence that economists, who are more used to thinking in quantitative categories than lawyers, were the first to discover that the emergence of platforms could lead to disruptive changes in many markets. Economists usually refer to platforms as two-sided markets.[5] One characteristic feature of platforms is the presence of network effects. Direct network effects occur when the value of joining the platform for the individual user increases with the number of users. Equally important are indirect network effects, which occur where more users on one side of the platform attract more users on the other side of the platform. This dynamic is one of the reasons for the spectacular growth of enterprises based on the platform business model.

III. Online platforms under the existing framework of EU consumer contract law

1. From 'bipolar' to 'triangular' relationships

The existing consumer contract law of the EU and its Member States seems to be rather outdated with respect to the dynamics of the platform economy. Consumer contract law primarily deals with 'bipolar' contractual relationships between a trader and a consumer. If a trader and a consumer conclude their contract via an online platform such as Ebay or Airbnb, the platform is usually not party to this contract between the consumer and the supplier of the goods or services. In such a 'triangular' situation, however, there are also legal relationships between the platform and the consumer, as well as between the platform and the supplier. It is, at best, unclear whether these legal relationships with the platform, usually also contracts, fall into the scope of the current (or forthcoming) EU consumer law directives.[6] If the supplier is not a business but a consumer, then EU consumer contract law certainly does not apply to such a consumer-to-consumer contract. As a result, many contracts, although concluded in the highly professional environment of an online platform, totally escape the scope of application of existing consumer contract law. In summary, it seems that EU consumer policy and consumer regulation have more or less ignored one of the most influential developments in the Digital Single Market.[7] As of today, there is no specific EU regulation addressing the legal issues raised by the growing platform economy. So far, the regulation of online platforms has been mainly left to the Member States. Whether and how Member State laws offer adequate protection for consumers is a matter for further research.[8]

In particular, the new set of legislative proposals[9] recently unveiled by the European Commission as part of the Digital Single Market strategy,[10] which can be understood as the successor or improved version of the Common European Sales Law, does not deal with platforms. This is rather surprising since, for more than ten years, a growing number of consumer contracts concluded online have been entered into via platforms. It is therefore promising that the European Commission has recently started a consultation that also deals with the issues of platforms. Another consultation, initiated by DG Communication Networks, Content & Technology concerning an update of the E-Commerce Directive, is also currently underway.[11]

2. The need for regulatory action at a European level: A plea for a Platform Directive

If it is agreed that the existing EU consumer law does not adequately cover the growing number of three-party situations, this does not automatically mean that regulatory action is necessary at a *European* level. One could argue that this issue should be left entirely for Member States to regulate. In a market environment where most transactions were two-party relationships, EU consumer law could indeed limit itself to regulating the rights of the consumer and the duties of the trader, i. e. the *content* of (pre-)contractual obligations. With the rise of the platform economy and the proliferation of three-party relationships, this approach is no longer sufficient. Determining the parties to the contract, and thus specifying who is the *addressee* of EU consumer law rules, becomes a necessary ingredient of a workable consumer law framework. This paper, therefore, pleads for an EU 'Platform Directive' to be drafted.

In order to avoid inconsistencies, the envisaged Platform Directive would have to be fitted into the existing regulatory framework contract, in particular, the directives concerning consumer law, the Services Directive and the E-Commerce Directive. Therefore, any draft for a Platform Directive would have to meet two requirements:

Firstly, it would have to be clarified whether the subject matter already falls into the scope of existing EU directives (e.g. information duties of platforms under the Services Directive, the E-Commerce Directive or the Consumer Rights Directive). In this case, it would have to be decided whether the envisaged specific platform legislation should be considered a *lex specialis* and stipulate specific information duties that would replace those from the other directives, or whether the new directive would merely add a complementary set of rules.

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4 B Stone, 'The Everything Store: Jeff Bezos and the Age of Amazon' (Little Brown 2013).

5 See the seminal work by JC Rochet & J Tirole, 'Platform Competition in Two-Sided Markets' [2003] Journal of the European Economic Association 990.

6 See C Wendehorst, 'Platform Intermediary Services and Duties under the E-Commerce Directive and the Consumer Rights Directive' (in this issue).

7 Cf. the critical remarks of the European Parliament resolution 'Towards a Digital Single Market Act' of 19 January 2016 (2015/2147(INI)), paras. 77-81.

8 See the contributions by Alberto De Franceschi, Irene Kull, Jerzy Pisulinski and Evelyne Terryn in this issue.

9 Proposal for a Directive of the European Parliament and of the Council on certain aspects concerning contracts for the supply of digital content COM(2015) 634 final; Proposal for a Directive of the European Parliament and of the Council on certain aspects concerning contracts for the online and other distance sales of goods COM(2015) 635 final

10 Communication from the Commission 'A Digital Single Market Strategy for Europe' COM(2015) 192 final.

11 Consultation 'Regulatory environment for platforms, online intermediaries, data and cloud computing and the collaborative economy'; published on 24/09/2015; <https://ec.europa.eu/digital-agenda/en/news/public-consultation-regulatory-environment-platforms-online-intermediaries-data-and-cloud>.

Secondly, it should be analysed to what extent the new platform directive could be built along the already existing lines in the Acquis, and whether it could make use of the legislative instruments developed for situations that have some similarities with platforms because they address the role of intermediaries. Probably the most prominent legislative examples falling into this category are the Commercial Agents Directive[12] and the recently revised Package Travel Directive.[13] However, these examples also illustrate that the regulatory issues arising from online platforms may involve rather different conflicts of interests to those regulated in these two directives. The Commercial Agents Directive contains instruments that seek to protect the agent against the principal. However, it is hard to imagine that platforms need a similar protection as agents against their principal. The situation is rather the opposite, i. e. suppliers may need protection against dominant platforms. By contrast, customers, in particular consumers, contracting via a platform may be faced with dangers similar to those of travellers booking a holiday from a tour operator under the Package Travel Directive. Tour operators may create the impression that they themselves undertake the obligation to provide the booked travel services, but try to stipulate in the small print that they only act as intermediaries for the individual service providers (e.g. hotels, airlines) and they do not take any responsibility for their proper performance. If platforms that only wish to be intermediaries do not clearly say so, the situation may be quite similar to package travel.

IV. Legal questions to be addressed by a future EU legislative instrument

The following section provides some examples of topics to be covered by a future EU Platform Directive. The topics can be broadly divided into three categories. Firstly, the legislative instrument should clarify the role of the platform. A platform operator that intends to be only a 'facilitator' or intermediary, and not a party to a contract of sale or service, should say so in a clear and unambiguous manner. Secondly, an EU legislative instrument should define the duties and obligations of those platforms that are only intermediaries. For example, it should be made clear to what extent the platform operator has to a duty to inform the consumer about the goods and services available through the platform. In addition, the obligations of the platform as a communications intermediary between the consumer and supplier should be specified. Thirdly, the question should be addressed under which conditions a platform acting as an intermediary is liable for a non-performance by the supplier.

1. Clarification of the platform operator's role

Most online platforms present themselves as mere facilitators, brokers or 'digital clearinghouses' rather than as sellers or suppliers. The intention to act only as an intermediary is usually expressed in the platform operator's terms of service. Such statements can be found, for example, in the terms and conditions of Uber[14] and Airbnb.[15] It is doubtful, however, whether such a declaration is sufficient for reducing the role of the platform to an intermediary. Whether or not the platform operator is a party to the contract for the sale of goods or the supply of services concluded on the platform is to be decided by the applicable Member State's contract law. Identifying the parties to the sale or supply contract is basically a matter of interpretation, which will be determined from the perspective of the customer, i. e. the addressee of the declaration (*objektiver Empfängerhorizont*). The method of interpretation is an objective test taking into account not only the statement of intention in the terms of service, but also the context in which the statement was made.

It is not entirely clear to what extent the existing Acquis requires the platform operator to inform the consumer about its intended contractual role. According to Article 10(1) of the E-Commerce Directive 2000/31, the service provider must inform the recipient of the service about "the different technical steps to follow the contract." This information duty, however, relates to the technical process of contract formation, rather than the contract law aspects including the determination of the parties to the contract. The European legislator carefully avoided intruding into this area when drafting the E-Commerce Directive.[16]

A possible basis for a duty of the platform operator to disclose its intended contractual role could be Article 6(1)(a) of the Consumer Rights Directive. According to this provision, the trader must inform the consumer, before the conclusion of a distance contract, about the "main characteristics of the goods or services" offered by the trader. If the platform operator intends to act only as a facilitator, such a limitation of the service offered to the consumer has to be disclosed under Article 6(1)(a). The directive is, however, not very specific as to the legal consequences if the trader fails to comply with the information duty. A possible starting point could be Article 6(5) of the directive, which stipulates that the information referred to in Article 6(1) becomes "an integral part" of the distance contract. One could argue, therefore, that the limitation of the platform operator's role to a mere intermediary function does not become part of the contract if it is not stated in a clear and comprehensible manner. As a result, the platform operator would be considered as the supplier of the goods or services. Yet, such a reading of the directive would probably be inconsistent with Article 3(5) according to which the directive "shall not affect national general contract law such as the rules on the validity, formation or effect of a contract, in so far as general contract law aspects are not regulated in this Directive."

In summary, there seems to be a gap in the existing EU consumer law. This gap could be filled by introducing a

12 Council Directive 86/653/EEC of 18 December 1986 on the coordination of the laws of the Member States relating to self-employed commercial agents [1986] OJ L382/17.

13 Directive (EU) 2015/2302 of the European Parliament and oft he Council of 25 November 2015 on package travel and linked travel arrangements travel [2015] OJ L 326/1.

14 See Section 3 of the Terms and Conditions of Uber UK <https://www.uber.com/de/legal/gbr/terms> "Uber UK accepts PHV Bookings acting as disclosed agent for the Transportation Provider (as principal). Such acceptance by Uber UK as agent for the Transportation Provider gives rise to a contract for the provision to you of transportation services between you and the Transportation Provider (the "Transportation Contract"). For the avoidance of doubt: Uber UK does not itself provide transportation services, and is not a Transportation Provider. Uber UK acts as intermediary between you and the Transportation Provider. You acknowledge and agree that the provision to you of transportation services by the Transportation Provider is pursuant to the Transportation Contract and that Uber UK accepts your booking as agent for the Transportation Provider, but is not a party to that contract."

15 See the Terms of Service of Airbnb, Inc. <https://www.airbnb.co.uk/terms> "The site, application and services comprise an online platform through which hosts may create listings for accommodations and guests may learn about and book accommodations directly with the hosts. You understand and agree that Airbnb is not a party to any agreements entered into between hosts and guests, nor is Airbnb a real estate broker, agent or insurer. Airbnb has no control over the conduct of hosts, guests and other users of the site, application and services or any accommodations, and disclaims all liability in this regard to the maximum extent permitted by law."

16 H Schulte-Nölke, 'EC Law on the Formation of Contract – from the Common Frame of Reference to the 'Blue Button', European Review of Contract Law 2007, pp. 332, 336.

provision drafted along the lines of Article 7(1) of the Proposal for a Consumer Rights Directive,[17] which contained specific information requirements for intermediaries. The provision, which was dropped in the course of the legislative process, read as follows:

"Prior to the conclusion of the contract, the intermediary shall disclose to the consumer that he is acting in the name of or on behalf of another consumer, and that the contract concluded shall not be regarded as a contract between the consumer and the trader but rather as a contract between two consumers and as such falling outside the scope of this Directive."

According to Article 7(2) of the proposal, an intermediary that did not meet the disclosure duty under Article 7(1) would be deemed to have concluded the contract in its own name. It is doubtful, however, whether the violation of a pre-contractual information duty as such should be the only criterion for determining the contract party, or rather one element among others. However, the violation of an information duty about the intended contractual role could give rise to a claim for damages.

2. Duties of platform operators acting as intermediaries

If the platform operator successfully limits its role to only facilitating the conclusion of a contract between a consumer and a third party who supplies goods or services, the platform operator may still have a number of duties and obligations arising from its role as an intermediary.

a) Pre-contractual information duties on goods and services offered via the platform

Apart from the general duty to provide information about its intended role, as discussed above, the platform operator may have to meet pre-contractual information duties regarding the goods and services offered via the platform. This question was recently raised in a request for a preliminary ruling from the Finnish Supreme Court concerning a peer-to-peer lending platform that facilitates the conclusion of credit agreements between consumers.[18] The CJEU was asked to clarify whether a peer-to-peer lending platform should be regarded as a "creditor" under Article 3(b) of the Consumer Credit Directive, if the platform operator exercises the decision-making power with respect to the terms and conditions, the granting of credit and debt recovery, even though the funds for credits come from anonymous private individuals and are kept separate from the trader's own funds. If the operator of the peer-to-peer lending platform is regarded as a creditor, then this means that it has to meet the comprehensive information duties under the directive. If, however, the platform operator is not regarded as a creditor, this could mean that the information duties under the Consumer Credit Directive do not apply at all, if the funds for the credit come from private individuals. Unfortunately, the CJEU will not clarify this issue, as the case submitted by the Finnish Supreme Court has been deleted from the Court's register.[19]

The question to what extent an intermediary has to provide information about the services for which it serves only as broker is well known from the area of package travel. While the old Package Travel Directive 90/314/EEC was somewhat ambiguous, the new Directive (EU) 2015/2302 clearly states that "the organiser and, where the package is sold through a retailer, also the retailer, shall provide the traveller with the standard information" required under the directive. This approach, which imposes an information duty both on the supplier of the service and the intermediary, could be a model for online platforms in general.

b) Attribution of communications made by the platform operator

The platform operator often takes an active part in communications between the parties, for example, by advertising the goods and services offered through the platform. Such statements by the platform operator will shape the legitimate expectations of the consumer as to the quality of the goods or services offered through the platform. Consequently, the statements made by the platform operator must be taken into account when determining whether the goods or services offered via the platform are in conformity with the contract.

This is a well-known issue that has already been dealt with by the Consumer Sales Directive. According to Article 2(2)(d) of Directive 1999/44, "consumer goods are presumed to be in conformity with the contract if they […] show the quality and performance that are normal in goods of the same type and *which the consumer can reasonably expect*, given the nature of the goods and *taking into account any public statements* on the specific characteristics of the goods made about them *by the seller, the producer or his representative*, particularly in advertising or on labelling."

The wording of Article 2(2)(d) is probably too narrow to also cover statements made by the operator of an online platform. A more comprehensive approach is taken by the recent Proposal for a Directive on the online sale of goods. According to Article 5(c) of the proposal, "the goods shall […] possess qualities and performance capabilities that are normal in goods of the same type and that the consumer may expect given the nature of the goods, and *taking into account any public statement made by or on behalf of the seller or other persons in earlier links of the chain of transactions*, including the producer […]."

The expression "earlier links of the chain of transaction" still does not precisely cover the situation where such statements have been made by the operator of a platform who only facilitates the conclusion of a contract between the seller and the consumer. The wording should be extended to cover also "persons facilitating the conclusion of the contract between the seller and the consumer." Moreover, the scope of application should be extended to contracts for the supply of services.

c) Duties of the platform as a communication intermediary

Online platforms serving as facilitators to the conclusion of a contract between consumers and suppliers also play a key role in communications between the parties. Usually, all communications between the consumer and the supplier are channelled through the platform. This central role of the platform as "communication intermediary" comes, or should come, with certain responsibilities. The platform should make sure that messages sent by the consumer or the supplier are forwarded without delay. Moreover, receipt of messages

17 On similarities between this provision and earlier German case law see D Effer-Uhe, 'Das Gebrauchtwagen-Agenturgeschäft – Teilrezeption einer umstrittenen Rechtsprechung ins europäische Sekundärrecht?', Neue Juristische Online-Zeitschrift 2009, pp. 656-661.

18 Request for a preliminary ruling from the Korkein oikeus (Finland) lodged on 25 June 2015, *TrustBuddy AB v Lauri Pihjalaniemi* [2005] OJ C 294/38.

19 Order of the President of the Court of 23 October 2015, ECLI:EU:C:2015:759.

(e.g. a notice of withdrawal) by the platform should be considered as receipt by the supplier.

Neither the Consumer Rights Directive nor the recently unveiled legislative proposals on the supply of digital content[20] and the online sale of goods[21] address these issues. A possible model for a legislative instrument on contracts concluded via online platforms could be Article 15 of Directive (EU) 2015/2302. According to this provision "Member States shall ensure that the traveller may address messages, requests or complaints in relation to the performance of the package directly to the retailer through which it was purchased." Moreover, the retailer has a duty to forward those messages, requests or complaints to the organiser without undue delay. In addition, for the purpose of compliance with time-limits or limitation periods, receipt of the messages, requests or complaints by the retailer should be considered as receipt by the organiser.

d) Duties of the platform provider towards suppliers?

A platform operator acting as an intermediary does not only have duties and obligations towards the consumer side of the two-sided market, but also towards the supplier side. A supplier who registers at a platform in order to offer goods or services via the platform usually concludes a contract with the platform operator.[22] Within the framework of this 'platform use contract', the platform shapes the business environment in which the supplier operates. The supplier usually has to accept terms of use in which the platform operator tries to exclude its liability as far as possible.[23] Against this background, it is an open question whether an EU legislative instrument should limit itself to the consumer protection aspects of online platforms, or take a more holistic approach by regulating also the rights and obligations of platforms towards suppliers. In particular, if suppliers are consumers, one might ask whether EU consumer law should also protect these 'prosumers' against platform operators.

There is a broad range of issues that a Platform Directive could deal with. Obvious examples are the obligations of platforms regarding the handling of payments and the transmission of communications between the supplier and the customer. In some cases, platforms may also have a duty to ban customers who are known for not performing their obligations, or at least warn suppliers of such customers.

Much trickier is the question to what extent suppliers may need protection against the economic power of dominant platforms. For instance, contract terms that prohibit 'multi-homing' (i.e. offering the same products or services also on other, competing platforms) could be banned. So-called 'best price' clauses, which prohibit offering the same goods or services for a better price on another platform or on the supplier's own website, seem to clearly infringe (at least German) competition law.[24] One could argue that such questions should be exclusively left to competition law, and therefore specific legislation on contract terms is not necessary. At an EU level, however, a flanking and supplementary legislation on unfair terms in contracts between platform operators and supplier may have an additional value.[25]

Even more complex are questions relating to reputation systems of platforms (e.g. ratings, reviews).[26] A positive rating on a platform based on many transactions may have an enormous value for a supplier. If the platform deletes such data, the supplier's sales may dramatically decrease. It is, therefore, not implausible to assume that platforms are under an obligation to carefully manage their reputation system and that they may be liable for damages if a supplier suffers a reputational loss because of insufficient data security. Finally, issues of data portability may arise. If it is not possible to transfer a long-standing positive ranking from the reputation system of one platform to another platform, this may cause undesirable lock-in effects for suppliers.

3. Liability of the platform operator for non-performance by the supplier?

As mentioned before, many online platforms usually present themselves as intermediaries facilitating only the establishment of a contractual relationship between the supplier and the consumer.[27] The desire of the platform not to be treated as a party to the contract is understandable from an economic point of view.[28] The platform operator seeks to enter into a certain area of business activity and tap into a pool of revenue without being held responsible for the adequate performance of the contractual obligation rendered by a third-party supplier. From a legal perspective, there are, in principle, no objections against this business model. The guiding principle is that – as rule – an intermediary platform is not liable for the performance of the obligation by the supplier. It is, however, the core question to be solved by an EU Platform Directive, whether there are cases in which a platform operator may also be liable for non-performance by the supplier.

a) The role of the platform in the contractual triangle

Online platforms such as Airbnb, Uber or Amazon Marketplace regularly appear on the market in a very prominent role. Not only do they dominate the entire business model, they may also appear to the public as the actual supplier. It may be difficult for the consumer to discern who is his or her contractual counterpart. Platforms often present themselves as the main actor in the transaction. It is common practice that platforms even provide the standard terms for the contract of sale or service, thus exercising a 'remote control' over the contractual relationship between the customer and the supplier. Many platforms also take a pivotal role as payment service providers in the process of transferring customer payments to the supplier.[29] In addition, most platforms also provide some sort of reputation system (e.g. ratings, reviews)

20 Proposal for a Directive of the European Parliament and of the Council on certain aspects concerning contracts for the supply of digital content, COM(2015) 634 final.

21 Proposal for a Directive of the European Parliament and of the Council on certain aspects concerning contracts for the the online and other distance sale of goods, COM(2015) 635 final.

22 See as an example Amazon Marketplace <https://sellercentral.amazon.com/gp/homepage.html>.

23 Cf. the term and conditions of Amazon Marketplace <https://services.amazon.co.uk/standards/terms-and-conditions.html>.

24 Higher Regional Court Düsseldorf, Judgement of 9 January 2015, Case VI-Kart 1/14 (V); see also the recent decision of the *Bundeskartellamt* of 23 December 2015 against the platform Booking.com on 'best price' clauses <http://www.bundeskartellamt.de/SharedDocs/Meldung/EN/Pressemitteilungen/2015/23_12_2015_Booking.com.html>.

25 R Podszun & S Kreifels, 'Digital Platforms and Competition Law' (in this issue).

26 On the importance of reputation systems for online platforms see H Masum & M Tovey (eds), The Reputation Society: how online opinions are reshaping the offline world (MIT Press 2012).

27 See e.g. <https://pizza.de/info/nutzungsbedingungen> ("Vertragsschluss", "Bezahlung"); <https://www.lieferando.de/agb-kunden>.

28 H Kötz & B Schäfer, *Judex oeconomicus* (Mohr Siebeck 2003) pp. 58-62 (comment on Bundesgerichtshof, Judgment of 19 September 1985, Case II ZR 275/84, BGHZ 95, 330).

29 See e.g. <https://www.uber.com/de/legal/gbr/terms ("4. Payment"); <https://www.lieferando.de/agb-kunden> ("5. Zahlungsart"). On the role of online platforms as a payment service providers see also C Busch, 'Mobile Payment – Rechtliche und technische Rahmenbedingungen für Innovationen im Zahlungsverkehr' [2014] Wirtschaft und Verwaltung pp. 148-154.

for evaluating the parties to a transaction (usually not only the supplier but also the customer).[30]

As a result, from the consumer's perspective it is often the online platform that appears as the actual partner of the contractual relationship and not a third-party supplier. This is most obvious in the case of online platforms offering passenger transportation services. Here many platforms have been successful in developing well-known brands (e.g. Uber, Lyft). They standardise the requirements for the quality of performance and attract their clients with the promise of high quality services rendered by the suppliers under their uniform brand. Furthermore, in many cases communication between the client and the supplier is possible only through the technical facilities of the platform.

In those cases where the platform appears as a party of the contractual relationship, or where the client at least has good reason to perceive the platform as the actual contractual counter-part, the question arises whether the platform should be held liable in the event of non-performance or defective performance of the supplier's obligation.

b) Possible criteria for the liability of the platform operator

The essential question for the legislator to decide is whether there should be some sort of 'secondary liability' of the platform provider. This is not only a matter of policy regarding the nexus between regulation and innovation.[31] It must also be examined whether such a kind of liability – or rather a lack of liability – would be consistent with fundamental principles of contract law such as the 'reliance principle'.[32] It is arguably one of the essential assumptions of contract law that if somebody presents itself in such manner that the client's reliance in the performance of the platform is justified, the party that gave a reason for such reliance should be liable in one way or other.

Starting from this premise, different regulatory approaches are possible. The European legislator could merely stipulate the duty of the platform operator to provide clear and unambiguous information as to the role of the platform. In the event of a violation of such an information duty, various sanctions can be imposed. The most radical solution would be to regard the contract concluded via the platform as a contract with the platform operator itself.[33] This sanction could be appropriate when the platform appears, from the perspective of the consumer, as the one and only party to the contract that promises performance. In this case the actual supplier (e.g. the driver of an Uber car) would have no contractual obligations towards the consumer at all. Where, however, the consumer can be expected to realise that the actual supplier undertakes to perform the service or to deliver the goods as its own obligation towards the consumer, the platform may nevertheless be under a 'secondary liability', complementing the 'primary liability' of the supplier. Such a 'secondary' liability can take different forms, be it just reliance damages or an obligation of the platform to make the supplier perform (and, consequently, the platform's liability for expectation damages, if that fails).

Various regulatory models should be taken into consideration when drafting an EU legislative instrument. However, it is doubtful whether the issue of the platform operator's liability can be reduced only to a question of clear and unambiguous information. Such an approach would probably not fully reflect the role of the platform in the system of contract law. The legal relationships emerging from the platform's activity rather create a triangular structure, between the platform, the customer and the supplier. Within this contractual triangle, the platform very often has a pivotal role going far beyond a mere intermediary.

In its 'pointillistic' approach,[34] the European legislator has recently addressed the role of such intermediaries with a potentially dominant role in the revised Package Travel Directive.[35] According to the Article 13(1) sentence 2 of the new Package Travel Directive, Member States may provide the liability of intermediaries (or 'retailers' in the terminology of the directive) in case of the non-performance of the obligations arising from the package travel contract. If a Member State makes use of this regulatory option, the rules of the directive on liability for non-performance shall apply. The new Package Travel Directive also provides, in its Article 20, that the intermediary is liable according to the rules of the directive if the travel organiser is situated outside of the European Economic Area (EEA). The purpose of this rule is to prevent a circumvention of the directive by organising package travel tours from a location outside of the territorial scope of EU law with the help of intermediaries located within the European Union.

Both provisions from the new Package Travel Directive are based on the idea that the role of travel retailers is not confined to the role of an intermediary, but as a party that may be much more influential than the other persons involved. One could possibly argue that the existence of such a provision in the new Package Travel Directive is an indicator of a certain tendency in the development of EU law and could be a source of inspiration for future EU legislation on platforms.

Based on these considerations, an EU Online Platform Directive could contain a rule stipulating the liability of the platform operator if the consumer can reasonably rely on the control of the platform provider over the supplier. The conditions of such a liability should be set out in more detail, providing courts with some additional indications in order to assess whether the role of the platform goes beyond that of a mere intermediary. Such additional criteria could be, for example:

- the conclusion or initiation of the contract is exclusively executed through the technical facilities of the platform;
- payment mechanisms are exclusively provided by the platform;
- the content of the contract with the supplier is essentially regulated by the platform;

30 Aee H Masum & M Tovey (eds), The Reputation Society: how online opinions are reshaping the offline world (MIT Press 2012).

31 On the nexus between regulation and innovation with a particular focus on the platform economy see M Cohen & A Sundararajan, 'Self-Regulation and Innovation in the Peer-to-Peer Sharing Economy', 82 U Chi L Rev Dialogue 116 (2015); S Ranchordás, 'Does Sharing Mean Caring? Regulating Innovation in the Sharing Economy', 16 Minn. J. L. Sci. & Tech. 413 (2015); see also W Hoffmann-Riem & JP Schneider (eds) *Rechtswissenschaftliche Innovationsforschung. Grundlagen, Forschungsansätze, Gegenstandsbereiche* (Nomos 1998); W Hoffmann-Riem, Innovationen durch Recht und im Recht, in: M Schulte (ed), *Technische Innovation und Recht* (CF Müller 1996).

32 Cf. the seminal work on the 'reliance principle' by *CW Canaris*, Die Vertrauenshaftung im deutschen Privatrecht (CH Beck 1971).

33 Such a solution was foreseen in Art 7(2) of the Commission Proposal for the Consumer Rights Directive, cf. *supra* IV.1.

34 H Kötz, *Europäisches Vertragsrecht* (Mohr Siebeck 2015) p. 12; on the Acquis see H Schulte-Nölke & F Zoll, 'Structure and values of the Acquis Principles: New Features and their possible use for political purposes', in Research Group on the Existing EC Private Law (ed), *Principles of the Existing EC Contract Law (Aquis Principles) – Contract II* (Sellier 2009), pp. xxiii – xxxv

35 Directive (EU) 2015/2302 of the European Parliament and of the Council of 25 November 2015 on package travel and linked travel arrangements [2015] OJ L326/1.

- the appearance of the supplier ("uniformisation" of the supplier, use of trademarks, marketing being focused on the platform, not the supplier).

These criteria should not be regarded as exclusive or cumulative conditions for the platform operator's liability, but only as indicators that may justify, if several or all of them are present, the assumption that the platform operator is so deeply involved in the contract between the supplier and the client that a 'secondary' liability is appropriate.

c) Possible alternative models

It should be clear from the outset that a 'secondary' liability as considered above is certainly not the only way how duties of online platforms could be regulated by the EU. An alternative approach could be to stipulate a general 'monitoring duty' of the platform operator or at least a duty to swiftly react to a complaint of a platform user. The possible need for such a regulatory approach is illustrated by a recent case where a German woman sued Airbnb and the hosts from whom she rented an apartment in California, on the grounds that a hidden camera had been present in the apartment.[36] Such behaviour would seem a blatant violation of privacy. While the case is still pending, Airbnb's response has been to update its Responsible Hosting policy with respect to guests' privacy. The policy now indicates that hosts should '[f]ully disclose whether there are security cameras or other surveillance equipment at or around your listing.'[37]

One may argue that a duty of the platform to influence suppliers to refrain from such practices, or to remove misleading product descriptions, would arise only where the platform has gained knowledge of such a case. This would mean that a platform has no general duty to monitor the suppliers' conduct, but rather to act only if there is a concrete complaint. This model resembles the approach taken by Article 15 of the E-Commerce Directive which expressly states that providers are not subject to a general obligation to monitor the information they transmit or store, nor a general obligation actively to seek circumstances indicating facts or circumstances indicating illegal activity. A simple transfer of this model would, however, neglect that the E-Commerce Directive deals with tortious infringements of personality or IP rights, whereas in the case of platforms also contractual rights of customers in case of unconscionable conduct of suppliers are at stake. Moreover, platforms may make general promises on the quality of the goods and services themselves.[38] In such case, the platform may have – at least – a general duty to take reasonable steps to ensure that the suppliers deliver the promised level of quality. Depending on the kind of promise the platform makes, it may also itself be considered liable for the promised quality, irrespective whether any duty to monitor the suppliers' conduct has been breached or not.

One may even raise the question whether the regulation of the platform economy should be left entirely to markets, or – more precisely – the self-regulation mechanisms provided by most platform operators. Indeed, as mentioned before, online platforms frequently come with built-in regulatory devices, most prominently some sort of reputation system (e.g. ratings, reviews). Some argue that these reputation systems ensure a high level of consumer protection and could thus make traditional methods of regulation superfluous.[39] It is questionable, however, whether rankings based on reviews by other customers can fully replace regulatory intervention. Recent empirical research casts some doubts on the validity of customer reviews.[40] Indeed, there seems to be a serious problem with the quality of information provided by such reviews, as recent problems with shill reviews on online shopping websites like Amazon.com show.[41] Moreover, there are indications that the design of reputation systems can inadvertently promote discriminatory behaviour.[42] In summary, it seems that ratings and reviews can only play a complementary role in the regulatory framework for online platforms. In order to strengthen the role of such self-regulatory mechanisms it could even be helpful if a future Platform Directive stipulates that the platform operator has a duty to ensure a certain transparency and minimum quality standards for the reputation system.

V. Conclusion

The emerging platform economy gives rise to new regulatory issues that make it necessary to adjust EU contract law to the changing market structure. In particular, adequate solutions have to be developed for the 'triangular' contractual relationships that are a characteristic feature of the platform business model. This paper calls for the preparation of a new EU legislative instrument – possibly a 'Platform Directive'. Although much more groundwork needs to be done, some contours of the content of the envisaged directive have been outlined.The Platform Directive could set out transparency requirements regarding the role of the platform in relation to consumers and other customers, and in particular clarify in which cases the platform operator is only to be considered a 'facilitator' and which as the actual supplier. If such transparency requirements are not met, the directive may even make the platform operator liable for a non-performance by the supplier in cases where the platform intended to only act as intermediary, but failed to make its role clear enough. Moreover, the Platform Directive could regulate to what extent platforms are subject to a general duty to screen or monitor suppliers and customers active on the platform, and may even be liable for a breach of contract by suppliers or customers.

The regulatory issues are not limited to questions of consumer protection in a traditional sense. A legislative instrument that is adequate for the regulation of two-sided markets may also seek to protect the suppliers' side, taking into consideration that in the so-called 'sharing economy' the suppliers are often consumers, or rather 'prosumers'. Such issues cannot be left to the market. Self-regulation mechanisms, in particu-

36 A brief summary of the case can be found in the *Los Angeles Times* (17 December 2015), http://www.latimes.com/socal/daily-pilot/news/tn-dpt-me-1218-airbnb-lawsuit-20151217-story.html>; further summary (in German) in *Süddeutsche Zeitung* (14 January 2016), 'Deutsche Touristin entdeckt versteckte Kamera in Airbnb-Wohnung.' For the complaint filed with the court, see <http://ia801508.us.archive.org/24/items/gov.uscourts.cand.293740/gov.uscourts.cand.293740.1.0.pdf>.

37 <www.airbnb.com/help/responsible-hosting>.

38 See, for example, the far-reaching promises by Uber on safety <https://www.uber.com/safety>.

39 For such a rather optimistic view see C Koopman, M Mitchell and A Thierer, 'The Sharing Economy and Consumer Protection Regulation: The Case for Policy Change' 8 J.Bus. Entrepreneurship & L. 529 (2015); see also A Thierer, C Koopman, A Hobson and C Kuiper, 'How the Internet, the Sharing Economy, and Reputational Feedback Mechanisms Solve the "Lemons Problem"', Mercatus Working Paper (26 May 2015), available at SSRN: http://ssrn.com/abstract=2610255;

40 B de Langhe et al., 'Navigating by the Stars: Investigating the Actual and Perceived Validity of Online User Ratings', <http://jcr.oxfordjournals.org/content/early/2015/09/10/jcr.ucv047>.

41 'Amazon sues 1000 'fake reviewers" (*The Guardian* 18 October 2015) <http://www.theguardian.com/technology/2015/oct/18/amazon-sues-1000-fake-reviewers>; see also F Marotta-Wurgler, 'Even More Than You Wanted to Know About the Failures of Disclosure' (2015) 11 Jerusalem Review of Legal Studies pp. 63, 71.

42 V Katz, 'Regulating the Sharing Economy', 30 Berkeley Tech. L.J. 1067 (2015) at 1118.

lar reputation systems such as ratings and reviews, can have an important complementary function, though it is doubtful whether they can fully replace regulatory intervention.

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The other contributions to this special issue of EuCML, which are based on papers presented at a conference on 'Platform Services in the Digital Single Market' hosted by the European Legal Studies Institute at Osnabrück in November 2015, may be a rich source of further inspiration. The authors of this article will invite the contributors to this issue and the general public to a follow-up conference at Krakow on 7 and 8 April 2016, where a more detailed draft of an EU Platform Directive will be presented and discussed. ■

THE SECESSION OF THE SUCCESSFUL: THE RISE OF AMAZON AS PRIVATE GLOBAL CONSUMER PROTECTION REGULATOR

Jane K. Winn*

In 2005, the Americans for Fair Electronic Commerce Transactions ("AFFECT") coalition issued a list of 12 principles it hoped would contribute to a new consensus about what constitutes fairness in online consumer transactions. A decade later, a cursory review of different jurisdictions indicates that, while there has been little discernable progress in the direction of the principles in the United States, other jurisdictions such as the European Union have made more progress. However, the one jurisdiction in the world that comes closest to implementing all 12 principles across the full spectrum of consumer transactions is not a government at all, but Amazon acting as a private regulator. Amazon's status as a regulator arises out of its ownership of a "multi-sided platform" that acts as a global retail marketplace. The rise of global platforms such as Amazon, Google, Apple, Facebook, and Microsoft that own global online marketplaces and simultaneously act as their primary regulators calls to mind the "Secession of the Successful" described by Robert Reich in 1991—the withdrawal from civil society of the wealthy and powerful into private gated communities. Amazon's status as the primary de facto regulator of the marketplace it owns combined with its single-minded pursuit of customer satisfaction contributes to relations with its employees and suppliers that are often profoundly problematic. When a platform operator is also the primary regulator of the market it creates, negative spillover effects may occur: squeezing employees and suppliers to insure that consumers get whatever they want merely pushes conflict from one part of the platform "ecosystem" to another. When this occurs, it does not make online commerce fairer overall, which was the implicit goal of the 12 principles. Although transaction-level norms such as those found in the 12 principles cannot ensure that all stakeholders in online marketplaces are treated fairly, other forms of regulation might be more effective in contributing to that goal.

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TABLE OF CONTENTS

INTRODUCTION 194
I. PLATFORM AS GOVERNANCE 198
II. REGULATORY GOVERNANCE AND PLATFORMS 199
III. NEW BASICS IN THE SHADOW OF PLATFORM GOVERNANCE 203
IV. ACCOUNTABILITY OF PLATFORM GOVERNANCE 209
CONCLUSION 211

INTRODUCTION

In 2005, Americans for Fair Electronic Commerce Transactions ("AFFECT") issued a list of 12 principles that it hoped would renew public dialogue about how the legal framework of electronic commerce could promote fairness in online consumer transactions.[1] Jean Braucher played a leading role in the development of the principles and in their subsequent dissemination.[2] This Article revisits those principles a decade later in light of the rise of global platforms such as Amazon that now dominate online retail markets. It also explores the question of which regulatory strategies would be best suited to advance the broader social justice ideals that Professor Braucher championed, and that underlie the 12 principles, in light of these changed circumstances. This Article was first presented at a symposium at the University of Arizona James E. Rogers College of Law celebrating Professor Braucher's life and work.

The AFFECT coalition was formed by opponents of the Uniform Computer Information Transaction Act, a legislative project that started out as part of the Uniform Commercial Code ("UCC") revision process but was later completed as a separate uniform law.[3] When the original version of the UCC was completed in the 1950s, "software" as something separate from the hardware of computing machinery had not been invented, let alone become the subject of a major category of commercial transactions.[4] After efforts during the 1990s to create a commercial law governing software and information transactions became hopelessly bogged down in political controversy, almost all state legislatures rejected it.[5] The 12 principles of fair electronic commerce represented an effort to shift the focus of

1. Jean Braucher, *New Basics: Twelve Principles for Fair Commerce in Mass-Market Software and Other Digital Products*, *in* CONSUMER PROTECTION IN THE AGE OF THE 'INFORMATION ECONOMY' 183 (Jane K. Winn ed., 2006).

2. *Id.* at 178.

3. UNIF. ELEC. TRANSACTIONS ACT (NAT'L CONFERENCE OF COMM'RS ON UNIF. STATE LAWS 2002), http://www.uniformlaws.org/shared/docs/computer_information_transactions/ucita_final_02.pdf.

4. *Id.* at 1.

5. Braucher, *supra* note 1, at 180–82.

debate away from that debacle and toward building a consensus regarding what constitutes "fair dealing" for trade in digital products and electronic commerce.[6]

A decade after the 12 principles were issued, a cursory review of different legal systems indicates that progress in the direction of the 12 principles has been modest at best. While American consumer protection laws have generally been subject to creeping obsolescence as a result of technological innovation, the European Union has repeatedly revised its consumer and data protection laws to ensure their continued efficacy.[7] Neither jurisdiction, however, has clearly embraced the principles. By contrast, the one jurisdiction that arguably comes closest to implementing all of the 12 principles in online consumer transactions generally is not a government at all, but Amazon acting as a private regulator.

Amazon is the largest American Internet retailer by a large margin, as well as one of the largest retailers in America.[8] In addition, Amazon operates the Amazon Marketplace where independent retailers offer products for sale. It has one of the most efficient logistics systems in the world for its own products, and also provides logistical support—including order fulfillment, delivery, payment processing, and web hosting services—for Amazon Marketplace sellers. As part of its brand management strategy, Amazon maintains an intense focus on customer satisfaction and requires participants in the Amazon Marketplace to do the same.[9] In other words, Amazon's customers do not need to worry about whether their national consumer protection laws have been updated to address online commerce issues because they know Amazon has staked its reputation on making sure that its customers are always treated fairly. The same cannot be said of Amazon's suppliers or employees, however. Amazon has been criticized for abusing its power as a monopsonist in some markets and for the harsh treatment of its employees.[10]

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6. *Id.* at 182–83.

7. *See* Directive 2011/83/EU of the European Parliament and of the Council of 25 October 2011 on Consumer Rights, Amending Council Directive 93/13/EEC and Directive 1999/44/EC of the European Parliament and of the Council and repealing Council Directive 85/577/EEC and Directive 97/7/EC of the European Parliament and of the Council, 2011 O.J. (L 304/64); *see also Proposal for a Regulation of the European Parliament and of the Council on the Protection of Individuals with Regard to the Processing of Personal Data and on the Free Movement of Such Data (General Data Protection Regulation)*, COM (2012) 11 final (Jan. 25, 2012), http://www.europarl.europa.eu/meetdocs/2009_2014/documents/libe/dv/comp_am_art_30-91/comp_am_art_30-91en.pdf.

8. Phil Wahba, *Amazon Ranks Among Retail's 10 Biggest Companies for the First Time*, FORTUNE (July 1, 2014, 4:50 PM), http://fortune.com/2014/07/01/10-largest-retailers-amazon/; *Running Away*, WALL ST. J., http://www.wsj.com/articles/SB10001424127887323324904579041300287558882.

9. George Anders, *Jeff Bezos Reveals His No. 1 Leadership Secret*, FORBES (Apr. 4, 2012, 6:00 PM), http://www.forbes.com/forbes/2012/0423/ceo-compensation-12-amazon-technology-jeff-bezos-gets-it.html; Joe Nocera, *Put Buyers First? What a Concept*, N.Y. TIMES, Jan. 5, 2008, at C1.

10. Paul Krugman, *Amazon's Monopsony Is Not O.K.*, N.Y. TIMES, Oct. 20, 2014, at A25; Spencer Soper, *Amazon Worker Forces Changes as Labor Board Settles Claim*, BLOOMBERG (Nov. 18, 2014, 3:56 PM), http://www.bloomberg.com/news/articles/2014-11-18/amazon-settles-labor-board-complaint-on-workers-rights; David Streitfeld, *Inside*

In 1991, Robert Reich published an essay in the *New York Times Sunday Magazin*e entitled *The Secession of the Successful*.[11] Reich described the growing concentration of wealth in American society in the hands of what he called the "fortunate top fifth" of the population, and this group's increasing withdrawal into private gated communities, private schools, private security forces, and private infrastructure.[12] This withdrawal, in turn, impoverishes civil society in America, making the political challenges it faces even more intractable. While Reich was describing the migration of wealthy individuals into private geographical spaces, a similar migration occurs when economically powerful players withdraw into private regulatory orders that define global markets. Due to a limited interface between those private regulatory orders and the national legal systems from which they grew, private regulators can focus on maximizing value to shareholders while avoiding the broad range of duties a national legal system must accommodate.

This rise of private global regulators and erosion of national legal systems has been studied through various lenses, including transnational business governance,[13] global administrative law,[14] global legal pluralism,[15] transnational legal orders,[16] new governance and smart regulation,[17] global private regulation,[18] and democratic experimentalism.[19] These studies have highlighted many different aspects of the transformation of legal systems in response to the rise of global markets and accelerating pace of technological innovation. However, none of these

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Amazon's Very Hot Warehouse, N.Y. TIMES: BITS (Sept. 19, 2011, 6:12 PM), http://bits.blogs.nytimes.com/2011/09/19/inside-amazons-very-hot-warehouse/.

11. Robert B. Reich, *Secession of the Successful*, N.Y. TIMES MAG. (Jan. 20, 1991), http://www.nytimes.com/1991/01/20/magazine/secession-of-the-successful.html?pagewanted=all.

12. *Id.*

13. Burkard Eberlein et al., *Transnational Business Governance Interactions: Conceptualization and Framework for Analysis*, 8 REG. & GOVERNANCE 1, 1–21 (2014).

14. *See* Benedict Kingsbury et al., *The Emergence of Global Administrative Law*, 68 LAW & CONTEMP. PROBS. 15, 27–29 (2005).

15. Paul Schiff Berman, *From Legal Pluralism to Global Legal Pluralism*, *in* LAW, SOCIETY AND COMMUNITY: SOCIO-LEGAL ESSAYS IN HONOUR OF ROGER COTTERRELL 255 (Richard Nobels & David Schiff eds., 2014); Ralf Michaels, *Globalization and Law: Law Beyond the State*, *in* LAW AND SOCIAL THEORY 287 (Reza Banakar & Max Travers eds., 2d ed. 2013); Brian Z. Tamanaha, *Understanding Legal Pluralism: Past to Present, Local to Global*, 30 SYDNEY L. REV. 375 (2008).

16. *See* Terence C. Halliday & Gregory Shaffer, *Transnational Legal Orders*, *in* TRANSNATIONAL LEGAL ORDERS 3–6 (Terence C. Halliday & Gregory Shaffer eds., 2015).

17. IAN AYRES & JOHN BRAITHWAITE, RESPONSIVE REGULATION: TRANSCENDING THE DEREGULATION DEBATE 4 (1992); NEIL GUNNINGHAM & PETER GRABOSKY, SMART REGULATION: DESIGNING ENVIRONMENTAL POLICY (1998); LESTER M. SALAMON, *The New Governance and the Tools of Public Action: An Introduction*, *in* THE TOOLS OF GOVERNMENT: A GUIDE TO THE NEW GOVERNANCE 1 (Lester M. Salamon ed., 2002).

18. *See* TIM BÜTHE & WALTER MATTLI, THE NEW GLOBAL RULERS: THE PRIVATIZATION OF REGULATION IN THE WORLD ECONOMY (2011); M. Patrick Cottrell & David M. Trubek, *Law as Problem Solving: Standards, Networks, Experimentation, and Deliberation in Global Space*, 21 TRANSNAT'L L. & CONTEMP. PROBS. 359 (2012).

19. *See* Michael C. Dorf & Charles F. Sabel, *A Constitution of Democratic Experimentalism*, 98 COLUM. L. REV. 267 (1998).

studies have focused on the role of information and communication technology ("ICT") networks or global "multi-sided platforms" in the governance of global markets.[20] Once ICT networks have been launched successfully, they are difficult to unseat, an advantage that may give the operator of a successful network considerable leverage over users of that network.[21] Global technology companies—such as Amazon, Google, Apple, Facebook, and Microsoft—have rapidly achieved enormous market power as ICT networks. They have further amplified that power by adopting a multi-sided platform business model, which requires complementary "sides" such as consumers and retailers, or users and advertisers, to participate in their platforms.[22] These platform operators can exercise considerable private regulatory authority over the global "ecosystems" that the operation of their platforms has spawned.

The ability of these platform operators to act as private regulators with authority over the global online marketplaces they have created calls to mind Reich's description in 1991 of the withdrawal of the wealthy and powerful from civil society into private gated communities.[23] Amazon's status as the primary regulator of its own marketplace combined with its single-minded pursuit of customer satisfaction often produces profoundly problematic relations with employees and suppliers.[24] When a platform operator is also its primary regulator, negative spillover effects may occur. In particular, squeezing employees and suppliers to ensure that consumers get whatever they want merely pushes conflict from one part of the platform "ecosystem" to another; it does not make online commerce fairer, which was the goal of the 12 principles.

Although transaction-level norms such as those found in the 12 principles cannot ensure that all stakeholders in online markets are treated fairly, other forms of regulation might be more effective in achieving that goal. Shifting the focus of efforts to make markets operate more fairly from the level of specific contract terms to the broader relationship between national legal systems and global private regulators might be a more effective regulatory strategy. For example, the California Transparency in Supply Chains Act of 2010 promotes fairness in global commerce by mandating disclosure of efforts to abolish forced labor in global production networks. If global retailers such as Amazon and Walmart were required to disclose to consumers whether their employees and suppliers had earned a "living wage,"

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20. OZ SHY, THE ECONOMICS OF NETWORK INDUSTRIES (2001).

21. *See id.* at 155–59; *see also* HAL R. VARIAN ET AL., THE ECONOMICS OF INFORMATION TECHNOLOGY: AN INTRODUCTION 21–25 (2004).

22. Andrei Hagiu & Julian Wright, *Multi-Sided Platforms*, 43 INT'L J. INDUS. ORG. 162, 162–63 (2015); Marc Rysman, *The Economics of Two-Sided Markets*, 23 J. ECON. PERSP. 125, 126–29 (2009).

23. Reich, *supra* note 11.

24. Jodi Kantor & David Streitfeld, *Inside Amazon: Wrestling Big Ideas in a Bruising Workplace*, N.Y. TIMES, Aug. 16, 2015, at A1. *But see* Krishnadev Calamur, *A Blistering Response from Amazon*, ATLANTIC (Oct. 19, 2015, 3:15 PM), http://www.theatlantic.com/business/archive/2015/10/amazon-responds-new-york-times/411232/ (noting that Amazon questioned the accuracy of the *New York Times*' reporting and provided evidence calling into question the reliability of some sources).

then these global retailers might have stronger incentives to ensure that the treatment of different stakeholder groups was more balanced.

I. PLATFORM AS GOVERNANCE

In 2015, Amazon together with Google, Apple, Facebook, Microsoft, and Alibaba, comprised a small, elite group of businesses that operated global platforms. The word platform in this sense has been defined in the following terms:

> The platform, created and maintained by one or more intermediaries, encompasses components and rules employed by users in most of their interactions. Users' interactions are subject to network effects, which are demand-side economies of scale: the value of platform affiliation for any given user depends upon the number of other users with whom they can interact.[25]

A platform business strategy has been defined as, "the mobilization of a networked business platform to expand into and operate in a given market. A business platform, in turn, is a nexus of rules and infrastructure that facilitate interactions among network users."[26]

Out of the five most valuable brands in the world in 2015, four were platforms in this sense: Apple, Google, IBM, and Microsoft.[27] Samsung, Facebook, Amazon, Cisco, Oracle, and Intel were included in the top 20 most valuable brands of 2015, and are also considered platforms in this sense.[28]

Computer networks are an essential element of platforms. Economists have defined networks as markets characterized by complementarity (i.e., what consumers value are systems made up of multiple products), compatibility (i.e., the different products making up a system are interoperable), and interoperability standards.[29] Markets based on networks have certain special characteristics that make launching a viable network very difficult, which in turn makes displacing a successful network difficult once it is in place.[30] These special characteristics include consumption externalities—i.e., the utility of a product to one consumer depends on how many other consumers are using the same product.[31] Another special characteristic is the high risk of user "lock-in" once a network has been launched successfully: If the switching costs involved in moving from one system to another are high, then users may find themselves "locked in" to the old system even if a new, better system becomes available.[32] Networks are also subject to

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25. Thomas R. Eisenmann et al., *Platform Envelopment*, 32 STRATEGIC MGMT. J. 1270, 1273 (2011).

26. Geoffrey Parker & Marshall W. Van Alstyne, *Platform Strategy* 1 (Bos. U. Sch. of Mgmt., Research Paper No. 2439323, 2014), http://ssrn.com/abstract=2439323.

27. *The World's Most Valuable Brands*, FORBES, http://www.forbes.com/powerful-brands/list/ (last visited Jan. 16, 2015).

28. *Id.*

29. SHY, *supra* note 20, at 1–2.

30. *Id.* at 3–6.

31. *Id.* at 3–4; *see also* VARIAN ET AL., *supra* note 21, at 33–37.

32. Examples of switching costs include the cost of researching alternatives to the current system and weighing the costs and benefits of switching ("search costs"); the human

significant economies of scale in production. Many products distributed over networks such as software or digital media also have extremely high up-front development costs but a marginal production cost approaching zero.[33]

As a result of innovations in the technology of computer networks, what were once public marketplaces can now be operated as privately owned multi-sided platforms, in effect privatizing a public good.[34] A platform is an "institution" as that term was used by economist Douglass C. North:

> Institutions are the rules of the game in a society, or more formally, are the humanly devised constraints that shape human interaction. In consequence they structure incentives in human exchange, whether political, social, or economic. Institutional change shapes the way societies evolve through time and hence is the key to understanding historical change.[35]

A successful platform operator is not merely the manager of activity taking place on the platform, but also one of the regulators governing that activity.[36] A platform operator's power as a private regulator may be amplified by network effects, and because it is exercised through global ICT networks, the impact can be direct and immediate.[37]

II. REGULATORY GOVERNANCE AND PLATFORMS

Although it may be conventional to think of enterprises such as Amazon as subjects of nation-state regulation, the role of such enterprises in regulating economic activity by displacing public marketplaces has also long been recognized.[38] In recent decades, however, governance activities undertaken by businesses have expanded beyond the market/hierarchy distinction and now include interactions with a range of private sector, civil society, multi-stakeholder, and hybrid public-private institutions.[39] The rise of Amazon as the de facto consumer protection authority with jurisdiction over its marketplace is an example of business acting as a source and not merely a target of regulation. The interaction among nation states, international organizations, and business institutions produces what

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effort of learning a new system; converting data stored in the old system to formats that can be used with the new system; and contractual restrictions that would make switching networks a breach of contract. SHY, *supra* note 20, at 4–5.

33. *Id.* at 5; *see also* VARIAN ET AL., *supra* note 21, at 25.

34. *See generally* Robert J. Staaf, *Privatization of Public Goods*, 41 PUB. CHOICE 435, 435–36 (1983) (noting how technological innovation makes privatization of public goods possible).

35. DOUGLASS C. NORTH, INSTITUTIONS, INSTITUTIONAL CHANGE, AND ECONOMIC PERFORMANCE 3 (James Alt & Douglass C. North eds., rev. ed.1999).

36. *See* Kevin S. Boudreau & Andrei Hagiu, *Platform Rules: Multi-sided Platforms as Regulators*, *in* PLATFORMS, MARKETS AND INNOVATION 163 (Anabelle Gawer ed., 2009); *see also* David S. Evans, *Governing Bad Behavior by Users of Multi-sided Platforms*, 27 BERKELEY TECH. L.J. 1201, 1210 (2012).

37. Jane K. Winn, *Technical Standards as Data Protection Regulation*, *in* REINVENTING DATA PROTECTION 191 (Serge Gutwirth et al. eds., 2009).

38. Ronald H. Coase, *The Nature of the Firm*, 4 ECONOMICA 386, 401–05 (1937).

39. Eberlein et al., *supra* note 13, at 13.

Eberlein et al., describe as "regulatory governance."[40] By focusing on institutions that maintain accountability, legitimacy, and rights rather than on traditional conceptions of "law," Eberlein et al., have developed a framework to analyze the dynamics of regulatory governance without regard to its roots in the nation state or elsewhere. This framework breaks down the lifecycle of regulatory governance into the following stages: agenda setting, norm formation, implementation, monitoring, enforcement, and review.[41]

Amazon derives its authority as a private regulator in part from its ownership of the ICT platform on which its marketplaces operate and in part from its status as a private business enterprise under the law of each country, as well as the status of its interactions with its customers, suppliers, and employees *based on* contracts. Moreover, Amazon's market power as one of the world's most ferocious competitors and successful platform operators enhances its de facto regulatory authority derived from traditional legal relations. In terms of the taxonomy of regulatory governance activities, Amazon is engaged in the following:

Problem Definition and Agenda Setting	Prioritize customer experience; omni-channel commerce; ubiquitous computing
Norm Formation	"One-Click" contracting; A-to-Z Guarantee
Implementation	Terms and Conditions; Privacy Policy
Monitoring and Information Gathering	Data analytics from activity on Amazon Marketplace; Amazon Web Services; Kindle
Enforcement	Exclude stakeholders from platform; chargeback contested transactions to merchants; plus contract and property enforcement in national legal systems
Review and Evaluation	Internal review; national government oversight

When Amazon was founded in 1994, its business model was simply online retailer rather than multi-sided platform, as it only sold to consumers the products that it owned.[42] In 1999, it launched a service originally called zShops to allow third parties to sell their products on its platform, a service that was later rebranded as Amazon Marketplace.[43] Third-party sellers pay nothing to list items but 15–45% in

40. *Id.* at 3.
41. *Id.* at 6.
42. Hagiu & Wright, *supra* note 22, at 163.
43. John Fredrick Moore, *Amazon Adds Merchants*, CNNMONEY (Sept. 29, 1999, 5:06 PM), http://money.cnn.com/1999/09/29/technology/amazon/; *Selling at Amazon.com: zShops Storefront*, AMAZON, http://www.amazon.com/gp/help/customer/display.html?nodeId=1161442 (last visited Jan. 16, 2016).

"referral fees" and other charges to Amazon when an item is sold.[44] In 2015, 40% of all products sold on Amazon were sold by Amazon Marketplace sellers.[45]

With regard to consumer transactions taking place within the Amazon Marketplace, Amazon both defines and enforces the norms that apply to third-party merchants.[46] In order to inspire consumer confidence, Amazon provides Amazon Marketplace buyers with a comprehensive "A-to-Z Guarantee" that in effect forces third-party merchants to match its fanatical pursuit of customer satisfaction. The A-to-Z Guarantee provides refunds up to $2,500 for buyers who claim an item they received was damaged, defective, or materially different from the item represented on the product detail page.[47] Refunds may also be provided for items that did not arrive within the delivery window, if the seller has not voluntarily issued the refund.[48] Amazon can enforce its buyer guarantee policy by charging back refunds against the seller, or even excluding the seller from the Amazon Marketplace: "Sellers with excessive guarantee claims and/or service chargebacks may be subject to warnings, suspensions, and account termination."[49]

Although Amazon has considerable clout as a private regulator, it nevertheless must rely on national legal systems for support in dealing with the worst offenders. For example, in 2015, Amazon filed suit in Washington State against 1,000 individuals it said were selling fake reviews to Amazon Marketplace merchants.[50] The lawsuit involved trademark disparagement and breach of contract claims based on the reviewers' assent to Amazon's terms of service.

Given Amazon's strong tilt in favor of retail customers, it is not surprising that reports of buyer fraud are widespread, as are reports of seller frustration with

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44. *Selling on Amazon Fee Schedule*, AMAZON, http://sellercentral.amazon.com/gp/seller/registration/participationAgreement.html?itemID=200336920&language=en_US&ld=SCSOAStriplogin (last visited Jan. 16, 2016); Mary Weinstein, *See on Amazon: How Much Does It Cost to Sell on Amazon?*, CPC STRATEGY: BLOG (June 23, 2014), http://www.cpcstrategy.com/blog/2014/06/sell-on-amazon-pricing/.

45. *Technologies Transforming Transportation: Is the Government Keeping Up?*, *Hearing Before the Subcomm. On Surface Transp. And Merch. Marine Infrastructure, and Sec.*, 114th Cong. 1 (2015) (statement of Paul Misener, Vice President for Global Public Policy, Amazon).

46. *Seller Protection & Best Practices*, AMAZON, http://www.amazon.com/gp/help/customer/display.html/ref=hp_left_cn?ie=UTF8&nodeId=13832211 (last visited Jan. 16, 2016).

47. *About A-to-Z Guarantee*, AMAZON, http://www.amazon.com/gp/help/customer/display.html?nodeId=200783670 (last visited Jan. 16, 2016).

48. *A-to-Z Guarantee Claims Program*, AMAZON, http://www.amazon.com/gp/help/customer/display.html?ie=UTF8&nodeId=13832181 (last visited Jan. 16, 2016).

49. *Id.*

50. Mae Anderson, *Crackdown: Amazon Sues to Stop Phony Product Reviews*, ASSOCIATED PRESS (Oct. 19, 2015, 7:05 PM), http://bigstory.ap.org/article/c2bc7f2e4b64490db4291ed5619ff2b2/amazon-sues-review-sellers-salvo-against-bogus-reviewers.

Amazon's dispute resolution procedures.[51] Amazon provides the following guidance for sellers concerned about this type of fraud on its website:

> If a seller follows the Amazon Marketplace Community Rules when listing, selling and shipping their item and, can document shipment to the customer or that the buyer received the correct item, Amazon usually does not hold the seller responsible for the reimbursement of the claim. Otherwise, reimbursement for the claim will usually be debited from the seller's account.[52]

Discussion among sellers on Amazon's own seller discussion forums indicates that sellers are in fact penalized by Amazon for any A-to-Z claims, even if the buyer later withdraws the claim, such as when a package that was delayed finally arrives.[53] While buyers are allowed to review seller performance, sellers are not permitted to comment publicly on misconduct by buyers, leading one seller to lament:

> I've found that recently more buyers are using [the A-to-Z Guarantee] to specifically get free product. I mean, it's not a secret Amazon will send a refund for any lame reason . . . but if Amazon is going to expect that their sellers give a FULL REFUND without returning an item AND downgrade a seller's reputation, then there should be an aspect of seller protection tied to it, be it buyer ratings or some method to know how often the customer has asked for a refund in the past . . . [54]

In the absence of a violation of national antitrust or competition law, merchants who are dissatisfied with Amazon's enforcement of its rules have no choice but to exit:

> In the end, it is Amazon's playing field. By selling on Amazon you have to accept that Amazon will always put the customer first.

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51. *See* Jake Seilger, *Is Amazon's Marketplace Encouraging Buyers to Scam Sellers by Filing a Refund Claim?*, STORY'S STORY (Feb. 16, 2013), http://jakeseliger.com/2013/02/16/is-amazon-coms-marketplace-encouraging-buyers-to-scam-sellers-by-filing-a-refund-claim/; *see also* Richard Stubbings, *The Dreaded A-Z Claim*, PRACTICAL ECOMMERCE (May 6, 2013), http://www.practicalecommerce.com/columns/the-view-from-england/11034-The-dreaded-Amazon-A-Z-claim-; *cf.* Better than Outlet, Reply to *Buyer Return Different Item Scam*, AMAZON SERVICES SELLER FORUMS (July 12, 2013, 8:05 AM), http://sellercentral.amazon.com/forums/message.jspa?messageID=2489867 (Amazon Marketplace seller reporting on Seller Forum that Amazon denied a fraudulent buyer claim).

52. *Seller Protection*, AMAZON.COM, http://www.Amazon/gp/help/customer/display.html?nodeId=13832211 (last visited Jan. 17, 2016).

53. Philips Light Lounge-Ved Electricals, *A-Z Guarantee Claim: Penalized for a Claim Withdrawn by the Buyer?*, AMAZON SERVICES INDIA SELLER FORUMS (Nov. 25, 2014, 5:06 PM), http://sellercentral.amazon.in/forums/message.jspa?messageID=1236715 ("We recently had an A-Z Guarantee Claim opened by a buyer and the buyer withdrew/cancelled his claim and yet we were penalized for the same. When we contacted Amazon, the customer service rep replied that even if a buyer withdraws or cancels his claim, the seller will still be penalized. This is however contradictory to Amazon's own online help article information.").

54. krlpuretone, *Seller Discussion - Amazon A to Z Guarantee Claims*, STEVE HOFFMAN MUSIC FORUMS (June 7, 2014), http://forums.stevehoffman.tv/threads/seller-discussion-amazon-a-to-z-guarantee-claims.359879/.

> You have to accept the way in which they judge their sellers. No matter how unfair or unreasonable it seems, it is their playground, their rules. It is better to accept this and find a way to play within these rules, or get out before you are forced out.[55]

III. NEW BASICS IN THE SHADOW OF PLATFORM GOVERNANCE

In 2005, Professor Braucher published a paper describing the 12 principles developed by AFFECT as guidelines for electronic commerce involving consumers.[56] She first outlined the challenges facing consumers in markets dominated by networks and platforms.[57] Professor Braucher and all those who contributed to the principles hoped they might be the catalyst for major reforms:

> Given all these market weaknesses, a good place to begin law reform efforts concerning software and digital content deals is with a focus on mass-market transactions in digital projects. To do this job well, we need to have basic principles in mind. Although law reform could begin at either the state or federal level, ultimately federal legislation will probably be desirable because of the connection to federal intellectual property law and policy involved in addressing the overreaching in non-negotiated terms for mass-market digital products. Some state statutory experiments could lead the way to this outcome.[58]

In terms of the transnational business government framework described above, the principles were intended to be an exercise in agenda-setting and norm formation.

The 12 principles were developed in two forms, a concise form designed to be comprehensible to consumers and a more elaborate form intended for lawyers and legislators. In their simplified form, they are:

> I. Customers are entitled to readily find, review, and understand proposed terms when they shop.
>
> II. Customers are entitled to actively accept proposed terms before they make the deal.
>
> III. Customers are entitled to information about all known nontrivial defects in a product before committing to the deal.
>
> IV. Customers are entitled to a refund when the product is not of reasonable quality.
>
> V. Customers are entitled to have their disputes settled in a local convenient venue.
>
> VI. Customers are entitled to control their own computer systems.
>
> VII. Customers are entitled to control their own data.

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55. Stubbings, *supra* note 51.
56. *See* Braucher, *supra* note 1.
57. *Id.* at 2.
58. *Id.* at 2–3.

> VIII. Customers are entitled to fair use, including library or classroom use, of digital products to the extent permitted by federal copyright law.
>
> IX. Customers are entitled to study how a product works.
>
> X. Customers are entitled to express opinions about products and report their experiences with them.
>
> XI. Customers are entitled to the free use of public domain information.
>
> XII. Customers are entitled to transfer products as long as they do not retain access to them.[59]

In the decade following publication of the principles, progress toward enshrining them in U.S. law is difficult to detect. While principles I and II may often be observed in U.S. cases involving consumers and electronic commerce,[60] the controversial but influential *Hill v. Gateway*[61] case remains good law and arguably violates both principles.[62] With regard to principles III and IV, American sellers generally remain free to disclaim warranty liability for the products they sell and are generally under no duty beyond that imposed by tort law to disclose defects.[63] The use of arbitration terms in consumer contracts is even more widespread in America in 2015 than it was in 2005.[64] In 2011, the U.S. Supreme Court resoundingly rejected the idea that American consumers have any right to have their disputes heard in a local, convenient venue in *AT&T Mobility Inc. v. Concepcion*.[65]

American information privacy and computer security rights remain fragmented and weak and continue to lag behind those of other jurisdictions such as the European Union.[66] The scope of the fair use defense under copyright law with regard to digital products and electronic commerce also remains uncertain, although

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59. *Id.* at 8.

60. *See, e.g.*, Knutson v. Sirius XM Radio Inc., Civil No. 12cv418 AJB (NLS), 2012 WL 1965337 (S.D. Cal. May 31, 2012), *rev'd and remanded*, 771 F.3d 559 (9th Cir. 2014).

61. Hill v. Gateway 2000, Inc., 105 F.3d 1147 (7th Cir. 1997) (validating "pay now, terms later" or "rolling contracts" contract formation mechanisms while rejecting an attempt by consumers to commence a class action against Gateway 2000 for defective computers and enforcing the arbitration term that had not been mentioned when the Hills placed their order by telephone but instead had been shipped in the box with the computer).

62. The reporters of an American Law Institute project, which aimed to harmonize consumer contract law in areas including electronic commerce, found that, in the 20 years following the *Hill v. Gateway* case, it had been followed 80% of the time that similar issues had been considered by American courts. RESTATEMENT OF THE LAW, CONSUMER CONTRACTS 27 (AM. LAW INST., Preliminary Draft No. 2, 2015).

63. *See generally* U.C.C. § 2-316 (AM. LAW INST. & UNIF. LAW COMM'N 1977).

64. Jessica Silver-Greenberg & Robert Gebeloff, *Arbitration Everywhere, Stacking the Deck of Justice*, N.Y. TIMES, Nov. 1, 2015, at A1.

65. 563 U.S. 333 (2011); *accord* DIRECTV, Inc. v. Imburgia, 136 S. Ct. 463 (2015).

66. *See generally* Paul M. Schwartz, *The EU-U.S. Privacy Collision: A Turn to Institutions and Procedures*, 126 HARV. L. REV. 1966, 1978 (2013).

the Ninth Circuit recently affirmed that before issuing takedown notices to website operators pursuant to the Digital Millennium Copyright Act, copyright owners must first consider whether the person posting the allegedly infringing content might have a fair use defense.[67]

While American consumers are generally free to post negative reviews of products and services, they do so at the risk of being sued for defamation.[68] On the other hand, sellers who try to prohibit leaving truthful negative reviews may be found to have engaged in unfair trade practices.[69] While nonprofit organizations such as Creative Commons[70] and Public.Resource.Org[71] may have increased the volume of online materials available to the public royalty free, there is no general right of free access to public-domain materials. The 12 principles proposed that copies of digital media should be as freely transferable as hard copies so long as the transferor did not retain a copy, but U.S. law today still does not recognize such a right unless the license granted by the copyright owner includes permission to make such transfers.

By contrast, Amazon's focus on customer satisfaction has led it to comply voluntarily or come close to complying with almost all of the 12 principles:

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67. Lenz v. Universal Music Corp., 801 F.3d 1126, 1129 (9th Cir. 2015).

68. With regard to state law defamation claims for negative reviews, see, e.g., Rahbar v. Batoon, A136463, 2014 WL 346910, at *4–5 (Cal. Ct. App. Jan. 31, 2014). *But cf.* Pham v. Lee, H039184, 2014 WL 6992251, at *4–7 (Cal. Ct. App. Dec. 11, 2014); Adi Kamdar, *Amid Further Lawsuits, a Federal Anti-SLAPP Law Is Sorely Needed*, ELEC. FRONTIER FOUND. (Jan. 9, 2013), http://www.eff.org/deeplinks/2013/01/amid-further-lawsuits-federal-anti-slapp-law-sorely-needed.

69. The FTC has recently taken action against vendors who tried to prohibit consumers from posting negative reviews about their products. Press Release, Fed. Trade Commission, FTC Sues Marketers Who Used "Gag Clauses," Monetary Threats, and Lawsuits to Stop Negative Consumer Reviews for Unproven Weight-Loss Products (Sept. 28, 2015), http://www.ftc.gov/news-events/press-releases/2015/09/ftc-sues-marketers-who-used-gag-clauses-monetary-threats-lawsuits.

70. CREATIVE COMMONS, http://www.creativecommons.org/about/ (last visited Jan. 17, 2016).

71. PUBLIC.RESOURCE.ORG, http://www.public.resource.org (last visited Jan. 17, 2016).

	New Basics	Amazon
II	Accessible, Comprehensible Terms	Posted on the bottom of every page; links to relevant content prominently displayed and embedded in purchase and return processes
III	Actively accept terms before being bound	Unambiguous order placement interface
IIII	Right to information about defects before purchase	Customer reviews provide information about defects before purchase
IIV	Right to a refund if not reasonable quality	Right to a refund in most cases without regard to quality
VV	Right to settle disputes at convenient venue	Right to use local small-claims court preserved
VVI	Customer controls own computer	No use of spyware
VVII	Customer controls own data	Right to opt-out of interest based ads, information sharing, communications
VVIII	Freedom to enjoy fair use rights	Entitled to download digital content to unlimited number of devices; Kindle Online Lending Library for Prime members
IIX	Freedom to study how products work	Reverse engineering of Kindle was not blocked until recently
XX	Freedom to express opinions and report experiences	Freedom to express opinions and report experiences
XXI	Free use of public domain material	Free access to public domain materials in Kindle
XXII	Entitled to transfer if no copy retained	Entitled to download digital content to unlimited number of devices

Amazon is clearly in compliance with principles I, II, III, and IV.

Although its customers are generally required to arbitrate disputes, thus reducing the risk of class-action lawsuits, Amazon agrees to appear in the local small-claims court of any individual buyer who prefers that route to arbitration.[72]

Given that Amazon Web Services is the largest provider of cloud computing services in America,[73] Amazon is presumably subjecting all its own customer data to intense scrutiny using "Big Data" analytics.[74] Amazon provides mechanisms for any customer that prefers not to be subject to that kind of scrutiny to "opt out" of it, however.[75] While Amazon became embroiled in some high profile information-privacy-breach litigation in the 1990s,[76] it has since maintained a low profile and managed to avoid further controversy in the area of information privacy.[77]

Amazon protects the one-sided right of buyers to review sellers so vigorously that some sellers believe they cannot defend themselves from buyer fraud.[78] Through the Kindle e-book reader, Amazon has made it easier than ever before for consumers to access public domain works. While Amazon does not literally allow licensees of digital content to transfer copies to nonlicensees, Amazon Prime service subscribers may achieve a similar result with the ability to download content to an unlimited number of devices.[79]

While Amazon might once have tolerated "jailbreaks" of its Kindle e-reader, it is now very serious about locking down the device to prevent tinkering.[80] Thus, the only one of the 12 principles for which Amazon is clearly out of compliance is principle IX governing reverse engineering.

Not only has Amazon come closer to compliance with the 12 principles than any country in the world, it has also served as a transmission vector by bringing

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72. *Conditions of Use*, AMAZON, http://www.amazon.com/gp/help/customer/display.html/ref=ap_desktop_footer_cou?ie=UTF8&nodeId=508088 (last visited Feb. 27, 2016).

73. Barb Darrow, *Shocker! Amazon Remains the Top Dog in Cloud by Far, but Microsoft, Google Make Strides*, FORTUNE (May 19, 2015, 10:28 AM), http://fortune.com/2015/05/19/amazon-tops-in-cloud/.

74. J.P. Mangalindan, *Amazon's Recommendation Secret*, FORTUNE (July 30, 2012, 11:09 AM), http://fortune.com/2012/07/30/amazons-recommendation-secret/.

75. *Amazon.com Privacy Notice*, AMAZON, http://www.amazon.com/gp/help/customer/display.html/ref=ap_desktop_footer_privacy_notice?ie=UTF8&nodeId=468496 (last visited Feb. 27, 2016).

76. *See, e.g.*, Sklare v. Alexa Internet (In re Amazon.com/Alexa Internet Privacy Litig.), No. 1346, 2000 U.S. Dist. LEXIS 8201, at *2–4 (J.P.M.L. June 7, 2000).

77. John P. Mello, Jr., *Data Requests Put Amazon Between Rock, Hard Place*, E-COM. TIMES (June 23, 2015, 1:45 PM), http://www.ecommercetimes.com/story/82207.html.

78. *See, e.g.*, Stubbings, *supra* note 51.

79. Marshall Honorof, *What Is Amazon Prime?*, TOM'S GUIDE (Dec. 28, 2015, 10:07 AM), http://www.tomsguide.com/us/what-is-amazon-prime,news-18041.html ("Amazon Households allow two adults and up to four children to share digital Amazon content.").

80. *Amazon Quietly Bricked Jailbroken Kindle Devices Last Year*, TECHDIRT (May 24, 2015), http://www.techdirt.com/articles/20150321/13350230396/while-bricking-jailbroken-fire-tvs-last-year-amazon-did-same-to-kindle-devices.shtml.

European consumer rights into the American market.[81] In 2000, the EU E-Commerce Directive mandated that online vendors in Europe make clear to website visitors what technical steps were required to form an online contract as well as the means for identifying and correcting errors prior to placing an order.[82] To comply, Amazon was among the first American retailers to display a visual representation of the transaction flow across the top of the screen during the order process, highlighting the current step in the process while making all steps visible. This visual cue has now become ubiquitous in American online commerce in the absence of any legislative mandate, suggesting that Amazon's competitors may have followed its lead. Amazon's 30-day return policy exceeds the mandatory 14-day right of return imposed by Consumer Rights Directive.[83]

Amazon's unflagging attention to customer satisfaction, however, comes at the cost of profoundly problematic relations with its employees and suppliers.[84] It has repeatedly been criticized for the grueling conditions to which its workers are subjected in its distribution and logistics network.[85] The intensity and harshness of Amazon's culture apparently extends all the way up the hierarchy to top management.[86] Amazon enjoys a virtual monopsony in many markets such as online book sales, and has been criticized for abusing that market power.[87] While Walmart was once the world leader in the relentless pursuit of efficiency to bring "everyday

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81. Jane K. Winn & Mark Webber, *The Impact of EU Unfair Contract Terms Law on US Business-to-Consumer Internet Merchants*, 62 BUS. LAW. 209 (2006).

82. Directive 2000/31/EC of the European Parliament and of the Council of 8 June, 2000 on Certain Legal Aspects of Information Society Services, in Particular Electronic Commerce, in the Internal Market, O.J. (L. 178) 1–16.

83. Directive 2011/83/EU of the European Parliament and of the Council of 25 Oct., 2011 on consumer rights, amending Council Directive 93/13/EEC and Directive 1999/44/EC of the European Parliament and of the Council and Repealing Council Directive 85/577/EEC and Directive 97/7/EC of the European Parliament and of the Council Text with EEA Relevance, O.J. (L 304), art. 9 ("Right of withdrawal 1. Save where the exceptions provided for in Article 16 apply, the consumer shall have a period of 14 days to withdraw from a distance or off-premises contract, without giving any reason, and without incurring any costs other than those provided for in Article 13(2) and Article 14."). Under the former Distance Selling Directive, the right of return was for 7 days.

84. *See* Kantor & Streitfeld, *supra* note 24; Calamur, *supra* note 24.

85. Hal Bernton & Susan Kelleher, *Amazon Warehouse Jobs Push Workers to Physical Limit*, SEATTLE TIMES (Apr. 3, 2012, 9:30 PM), http://www.seattletimes.com/business/amazon-warehouse-jobs-push-workers-to-physical-limit/; Nathaniel Mott, *Don't Be Surprised at how Amazon Treats Its Workers*, GIGAOM (Aug. 18, 2015, 9:15 AM), http://gigaom.com/2015/08/18/dont-be-surprised-at-how-amazon-treats-its-workers/; Spencer Soper, *Inside Amazon's Warehouse*, MORNING CALL (Aug. 17, 2015, 12:13 PM), http://www.mcall.com/news/local/amazon/mc-allentown-amazon-complaints-20110917-story.html. *But see Working at Amazon*, AMAZON, www.amazon.com/fcpractices (last visited Jan. 16, 2016) (pointing out that wages and benefits for workers in Amazon fulfillment centers are above the national average for retailer workers)

86. Kantor & Streitfeld, *supra* note 24; Calamur, *supra* note 24.

87. *See* Joshua Gans, *Amazon: It's Not the Power, It's the Lost Focus*, DIGITOPOLY (Oct. 20, 2014), http://www.digitopoly.org/2014/10/20/amazon-its-not-the-power-its-the-lost-focus; *see also* Krugman, *supra* note 10. *But cf.* R.A., *Big Bad Amazon*, ECONOMIST (Oct. 20, 2014, 8:19 PM), http://www.economist.com/blogs/freeexchange/2014/10/market-power.

low prices" to its customers, that mantle has now passed to Amazon, whose market capitalization exceeded Walmart's for the first time in 2015.[88] While Walmart's unfair or even illegal labor practices have attracted widespread attention, the fact that Amazon's labor practices do not appear to be any better than those of Walmart has not been as widely noted.[89]

IV. ACCOUNTABILITY OF PLATFORM GOVERNANCE

With regard to activities that take place within the "ecosystem" of the platform, the regulatory authority exercised by global platform operators may rival that of national governments. However, the exercise of that regulatory authority is not normally legitimated by the same mechanisms as government regulation: representative democracy or judicial review. Any legitimacy that platform operators enjoy as regulators of activity taking place on the platform is derived from their power in markets, as well as contract and property rights established under national legal systems. The power and authority of national governments—the traditional nexus of legitimate authority in modern societies—is declining, but widely recognized measures of political legitimacy for platform governance equivalent to representative democracy or judicial review have not yet emerged.[90] Amazon's intense focus on customer satisfaction combined with its status as a private regulator currently permit it to externalize many of the costs of achieving high levels of customer satisfaction onto those stakeholder groups most excluded from its governance processes.

If increased enforcement efforts increase compliance in one area by triggering an increase in violations in another area, the result of such negative spillover effects is like squeezing a balloon. Although the term "balloon effect" was first used with reference to the failure of the U.S. War on Drugs to stem the tide of drug trafficking in North and South America,[91] a similar dynamic may be at play when the 12 principles are applied to private regulators such as Amazon. While the explicit goal of the 12 principles was fairness to consumers, the implicit goal was to make the operation of markets fairer generally. If the rights of workers and suppliers were not addressed explicitly in the 12 principles, it was doubtless because the drafters assumed that there would be other laws in place to maintain an acceptable

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88. Matt Krantz, *Amazon Just Surpassed Walmart in Market Cap*, USA TODAY (July 23, 2015, 6:44 PM), http://www.usatoday.com/story/money/markets/2015/07/23/amazon-worth-more-walmart/30588783/.

89. *See* Rob Cox, *Why Amazon May Take a Page from Walmart's Labor Playbook*, N.Y. TIMES (Aug. 17, 2015), http://www.nytimes.com/2015/08/18/business/dealbook/why-amazon-may-take-a-page-from-walmarts-labor-playbook.html; *see also* Alex Planes, *To Win the Holidays, Amazon.com Pushes Employees to the Limit*, THE MOTLEY FOOL (Nov. 23, 2014, 4:00 PM), http://www.fool.com/investing/general/2014/11/23/to-win-the-holidays-amazoncom-strips-its-workers-o.aspx.

90. Anne Peters et al., *Toward Non-State Actors as Effective, Legitimate and Accountable Standard-Setters*, *in* NON-STATE ACTORS AS STANDARD SETTERS 492, 502 (Anne Peters et al. eds., 2009).

91. *Balloon Effect*, WIKIPEDIA, http://en.wikipedia.org/wiki/Balloon_effect (last visited Jan. 17, 2016).

minimum level of protection for workers and suppliers. If the drafters of the 12 principles could have foreseen that significant progress in implementation could only be achieved by the "Walmartization" of labor and producer markets, they might have drafted the principles differently.

The California Supply Chain Transparency Act of 2010 requires large retailers and manufacturers to provide consumers with information regarding their efforts to eradicate slavery and human trafficking from their supply chains and to educate consumers on how to purchase goods that are produced by companies that responsibly manage their supply chains.[92] Accordingly, retailers and manufacturers doing business in California with worldwide gross receipts in excess of $100 million are required to publish annual reports describing their anti-slavery and anti-trafficking efforts.[93] The legislative purpose of the California law is to keep global supply chains free of products whose production involved human rights abuses.[94] A modified form of the California Supply Chain Transparency Act might help consumers understand whether the pricing policies of domestic American platforms like Amazon are based on unfair labor and trading practices.

Although few would claim that the business practices of Walmart or Amazon's operations in the United States violate the human rights of their employees or suppliers, many might argue that there is an unacceptably high social cost to the relentless pursuit of lower retail prices.[95] In recent years, the concept of a "living wage" has gained prominence in American politics and could be substituted for slavery and human trafficking in a mandatory disclosure law imposed on employers such as Amazon and Walmart.[96] Major employers including Facebook and Ikea have recently announced voluntary commitments to ensuring that their employees and contractors receive a living wage.[97] Massachusetts Institute of Technology has created an online living wage calculator to make it easy to estimate the cost of living in different locations around the country.[98] If living wage disclosures calibrated to variations in local cost of living were provided to American

92. Transparency in Supply Chains Act, S.B. 657, 2009–2010 Leg. Reg. Sess. (Cal. 2009–2010), codified as CAL. CIV. CODE § 1714.43 (West 2010).

93. *Id.*

94. Norman L. Greene & Eric Beinhart, *Combating Human Trafficking—The U.S. Government's Response*, 20 ILSA J. INT'L & COMP. L. 49, 79 (2013).

95. CHARLES FISHMAN, THE WAL-MART EFFECT: HOW THE WORLD'S MOST POWERFUL COMPANY REALLY WORKS, AND HOW IT'S TRANSFORMING THE AMERICAN ECONOMY (2006); Vern Kopytoff, *How Amazon Crushed the Union Movement*, TIME (Jan. 16, 2014), http://time.com/956/how-amazon-crushed-the-union-movement/.

96. Melena Ryzik, *'I, Too, Am America' Shares Snapshots from Workers Living on the Edge*, N.Y. TIMES, May 2, 2015, at C1.

97. *See* Jean McGregor, *Ikea to Raise Workers' Pay to a 'Living Wage,'* WASH. POST (June 26, 2014), http://www.washingtonpost.com/news/on-leadership/wp/2014/06/26/ikea-to-raise-workers-pay-to-a-living-wage/; *see also* Rebecca R. Ruiz, *White House and Labor Advocates Praise Move by Facebook for Higher Wages*, N.Y. TIMES, May 13, 2015, at B4.

98. Amy K. Glasmeier, MASS. INST. OF TECH., http://www.livingwage.mit.edu/ (last visited Jan. 17, 2016).

consumers pursuing "everyday low prices," they might be in a better position to assess the impact their consumption decisions may have.[99]

While it is unclear precisely how much impact disclosure laws alone can have on consumer behavior,[100] it is clear that simply mandating the public disclosure of information likely to be viewed unfavorably by a significant proportion of the public might have some effect on the behavior of companies concerned about their brand.[101] On the other hand, any attempt by governments to impose "command and control" mandates dictating the terms and conditions under which transactions take place within "multi-sided platforms" would be almost certain to fail.[102]

CONCLUSION

The 12 principles of fair electronic commerce published by AFFECT in 2005 focused on empowering consumers acting in information markets. They were informed by public debate triggered by the drafting project first known as UCC Article 2B and later finalized as the Uniform Computer Information Transactions Act. They were drafted in broad, general terms in the hope of influencing public debate and law reform in the future. In the decade following publication of the 12 principles, there has been very little evidence that law reform efforts in the United States are moving generally in the direction of strengthening legal guarantees of the substantive fairness of online consumer transactions.

Even in the absence of law reform, however, many American consumers are treated very fairly either because they shop on Amazon or they shop at a different online retail site competing to provide the same high level of customer service that Amazon has achieved. Not only has Amazon as a private global regulator made more progress in implementing the 12 principles than any government has, it has also put pressure on American competitors to comply with European online consumer protection laws by its own example of voluntary compliance in America. At one level, the triumph of market-driven consumer protection in the absence of government mandates validates American confidence in the free market. At another level, however, if Amazon's zeal for customer satisfaction is being paid for by unfair treatment of its employees and suppliers, then that contradicts the social justice objectives underlying the 12 principles.

A global "secession of the successful" away from national commercial and consumer laws applied in public markets to private regulation applied in global platforms may not be inevitable, however. If the drafters of the 12 principles were given the opportunity to reframe their project in light of the last decade of experience

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99. *See* Ruiz, *supra* note 97.

100. Lauren Willis, *When Nudges Fail: Slippery Defaults*, 80 U. CHI. L. REV. 1155, 1162–63 (2013).

101. Cory Bennett, *SEC Weighs Cybersecurity Disclosure Rules*, HILL (Jan. 14, 2015, 6:00 AM), http://thehill.com/policy/cybersecurity/229431-sec-weighs-cybersecurity-disclosure-rules.

102. *See* Christine Parker & Vibeke Lehmann Nielsen, *Introduction* to EXPLAINING COMPLIANCE: BUSINESS RESPONSES TO REGULATION 1 (Christine Parker & Vibeke Lehmann Nielsen eds., 2011); *see also* Robert Baldwin & Julia Black, *Really Responsive Regulation*, 71 MOD. L. REV. 59 (2008).

with global platform operators, they might wish to complement the transactional focus of the principles with a focus on insuring that all stakeholder groups participating in global business "ecosystems" such as Amazon are treated fairly. One such complimentary strategy might involve incentives for businesses—especially those with business models focused on relentlessly lowering prices—to disclose publicly whether those low prices were compatible with their employees and suppliers earning a living wage.

This Article commemorates the life and work of Professor Jean Braucher, a tireless advocate for the application of social justice norms to the operation of markets. She helped develop principles aimed at assuring fair treatment for consumers engaged in transactions online or for digital products. She might have been surprised to learn that the first jurisdiction to implement systematically almost all of the principles she advocated was a private enterprise operating as a global platform. In any event, she would have expected global private regulators to be held to the same social justice norms as the governments whose national legal systems they displace.