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Viewing Unconscionability through a Market Lens

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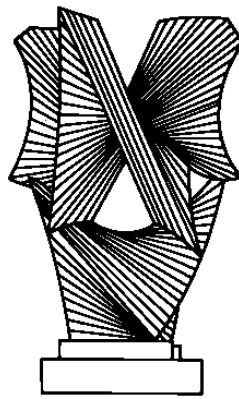
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David Gilo & Ariel Porat, "Viewing Unconscionability through a Market Lens" (John M. Olin Program in Law and Economics Working Paper No. 489, 2009).

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CHICAGO

JOHN M. OLIN LAW & ECONOMICS WORKING PAPER NO. 489
(2D SERIES)



Viewing Unconscionability through a Market Lens

David Gilo and Ariel Porat

THE LAW SCHOOL
THE UNIVERSITY OF CHICAGO

October 2009

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VIEWING UNCONSCIONABILITY THROUGH A MARKET LENS

David Gilo and Ariel Porat*

This Article calls for a move to the third phase in courts' attitudes toward consumer contracts. In the first phase, consumer contracts were considered ordinary contracts by courts thus requiring no special treatment. In the second phase, courts and legislatures became suspicious of consumer contracts and developed several tools for handling them, focusing on the characteristics of the parties and the transaction. In this Article, we suggest that it is time to introduce a third phase: Rather than examining each consumer contract in isolation, courts need to acknowledge that consumer contracts are a market-phenomenon which calls for a market-based approach. Instead of focusing on the characteristics of the parties and the transaction, courts should inquire whether there is competition, or potential competition, over contracts in the supplier's market. In order to do so, courts should look at the particular features of the supplier's market, that we identify, and also on the potential strategic interaction among competitors. We argue that when competition over contracts, or the threat of such competition, is sufficiently strong, consumer contracts should be deemed efficient and fair, and courts should not strike down clauses incorporated in such contracts. Interestingly, and counter-intuitively, this conclusion holds even where consumers are uninformed. We offer workable guidelines for courts as to how they could implement the market-based approach proposed in this Article and show how this approach could produce outcomes opposite to, but more efficient and fair, than the ones conventionally adopted by courts or offered by legal scholars.

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INTRODUCTION

Suppose you buy a computer from a manufacturer of electronic equipment, and after a few days of use the computer breaks down. Even though you had purchased a warranty from the seller you find out that it does not cover your losses. The reason is that a clause in the fine print limits recovery to losses caused by some components of the computer but not by others. The question of whether to strike down such a clause is generally determined by courts according to a combination of three considerations, mostly under the doctrine of unconscionability:¹ first, the information gap between the supplier and his consumers, which exists when consumers are not aware of the full value loss the clause entails;² second, whether the supplier enjoys superior bargaining power;³ third, the degree of harshness, or one-sidedness, of the clause.⁴

Law and economics scholars have argued that only the consideration regarding the information gap should matter. The reason is that even if a supplier possessed superior bargaining power, it would not incorporate an inefficient clause into its standard form contract if consumers were aware of the clause and its full cost to them; the supplier would always prefer to have an efficient contract. To the extent that the supplier had superior bargaining power it would use it to raise the price rather than to impose an inefficient clause.⁵ It is only when consumers are unaware of the clause or of the full cost it is imposing upon them that the supplier can extract value from consumers by incorporating inefficient terms into its standard form contracts.⁶ Therefore, the law and economics literature concludes that intervention is justified if, and only if, consumers lack sufficient information.⁷

Surprisingly, however, the question of *how* courts should verify whether consumers are informed remained under-explored in legal writings. As a result, courts conduct a transaction-specific analysis as to whether there is a gap of information between the supplier in question and his consumers and reach decisions accordingly. Determining whether consumers are sufficiently informed in a particular case, or in a particular market, however, is an extremely formidable task for courts.

¹ *Infra* Section III.A.

² *Infra* note 99 and accompanying text.

³ *Infra* note 99 and accompanying text.

⁴ *Infra* note 101 and accompanying text.

⁵ *Infra* note 13 and accompanying text.

⁶ *Infra* note 15 and accompanying text.

⁷ As shown by Alan Schwartz and Louis L. Wilde, *Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis*, 127 U. Pa. L. Rev. 630 (1979), if there are enough sophisticated consumers who shop and compare the terms of suppliers' deals, suppliers will be motivated to offer efficient contracts. See also Alan Schwartz, *How Much Irrationality Does the Market Permit?* 37 J. LEGAL STUD. 131 (2008) (showing that when the number of informed consumers is sufficiently large, suppliers would refrain from including inefficient terms in their contracts). It remains to be asked what a court should do when it is claimed that a large portion of consumers is uninformed. Our article provides a tool to deal with such cases.

This Article offers a new method for courts to consider whether to strike down an oppressive term. The Article's claim is that instead of trying to explore directly whether there is a gap of information between the supplier and his consumers, courts should inquire whether market forces have the potential to close this gap. In particular, we develop tools according to which courts should determine whether the supplier's market encourages competing suppliers, or other parties, to draw consumers' attention to inefficient or unfair terms in the supplier's contract.⁸ If the answer is "yes" the contract should be deemed efficient and fair and courts should not intervene against it; if the answer is "no", courts should be suspicious of oppressive terms in the contract and apply the transaction-specific analysis they currently apply to such contracts. Thus, in the computer example mentioned above, it is very difficult for a court to determine whether the buyer of the computer, or many of the supplier's consumers, are sufficiently informed. Nevertheless, we claim that courts should not intervene if they are convinced that the computer supplier's market encourages its competitors, or other parties, to expose to consumers inefficient or unfair exclusionary clauses in the supplier's contracts.

The virtue of our proposed market-based method is not only that it circumvents the prohibitive costs of inquiring whether consumers are informed. It also helps identify cases where consumers are known or presumed to be uninformed but where nevertheless court intervention is unwarranted. In particular, if consumers are uninformed, as long as there is a credible threat that competitors or other parties allude consumers' attention to suppliers' inefficient or unfair terms, no supplier would incorporate such terms in its contract in the first place. Thus, in equilibrium, when the threat of competition over contracts is credible, contracts should be deemed efficient and fair and any court intervention is unwarranted. To illustrate, in the computer example above, courts should not strike down the exclusionary clause if they are convinced that in the relevant computer market, had the clause been inefficient or unfair, competitors or other parties would have criticized it, and the supplier would have lost market share.⁹

⁸ In our terminology, fairness in a contract exists when the bargain is consistent with both parties' reasonable expectations. According to this terminology, any fair contract is also efficient, since, when both parties to a contract are informed, the contract is not only fair, but also efficient. Not every efficient contract is necessarily fair, however. For example, if the contract allocates risks efficiently, and the consumer values the product more than the product's marginal cost, the contract is efficient. The same contract, however, could still be unfair if the supplier reaps most of the contract's surplus by using deceptive techniques, thereby frustrating the consumer's reasonable expectations. *See, e.g.,* W. David Slawson, *Standard Form Contracts and Democratic Control of Lawmaking Power*, 84 HARV. L. REV. 529, 531 (1971) ("An unfair form will not deter sales because the seller can easily arrange his sales so that few if any buyers will read his forms, whatever their terms ...").

⁹ Previous authors have mentioned, in specific contexts, that competition among suppliers could educate consumers about inefficient terms in consumer contracts. *See, e.g.,* Lee Goldman, *My Way and the Highway: The Law and Economics of Choice of Forum Clauses in Consumer Form Contracts*, 86 NW. U. L. REV. 700, 716 (1992) (stating, in the context of choice of forum clauses in consumer contracts, that if a firm uses inefficient terms with a low price, a rival firm offering efficient terms with a higher price would want to highlight this fact); Richard A. Epstein, *Behavioral Economics: Human Errors and Market Corrections*, 73 U. CHI. L. REV. 111, 111 (2006) (arguing that when consumers overvalue a product, a

As we show, the effectiveness of competition over contracts in deterring suppliers from using inefficient or unfair standard form contracts crucially depends on the nature of the oppressive techniques used by suppliers. We distinguish between four oppressive techniques, only the first one has been attracting courts' scrutiny and attention, while the other three have been, for the most part, ignored by courts, even though they are very common and could be very harmful. The first and most familiar technique is to incorporate terms into the contract which deprive the consumer of a right or a remedy to which she would have been entitled but for the oppressive terms (hereinafter: "traditional oppressive term" or "TOT"). Clauses limiting the supplier's liability such as the one described in the above-mentioned computer example are illustrative of such terms. The second technique is to incorporate terms into the contract which are oppressive only for some consumers but not for others. Typically, those who are not offended by the terms are consumers who were aware of their existence, and made some effort to avoid their adverse effects (hereinafter: "selectively oppressive term" or "SOT"). An example of a SOT is a term that deprives consumers of a remedy, but allows consumers who carefully read the contract to relieve themselves of the oppressive term.¹⁰ The third technique is to incorporate contract terms which confer benefits on some consumers but not on others (hereinafter: "selectively beneficial term" or "SBT"). As in the case of a SOT, with an SBT only those consumers who make some effort to attain the benefits will receive them. A typical example is a term, included in the fine print, allowing a discount only for a consumer who is aware of the term and is willing to fill out a certain form to receive the discount.¹¹ The *fourth and last oppressive technique* that we identify is artificial complication of contracts. Under this technique, by making contracts more complex, suppliers can extract benefits from consumers.¹²

seller of a better product is expected to draw away such consumers by trumpeting their mistake); David Gilo & Ariel Porat, *The Hidden Roles of Boilerplate and Standard-Form Contracts: Strategic Imposition of Transaction Costs, Segmentation of Consumers, and Anticompetitive Effects*, 104 MICH. L. REV. 983, 1009, at note 64 (2006) (mentioning that "the saliency of terms is, for the most part, endogenous: a supplier could snatch business from his rival by highlighting the rival's harsh nonsalient terms."); Xavier Gabaix & David Laibson, *Shrouded Attributes, Consumer Myopia, and Information Suppression in Competitive Markets*, 121 Q.J. ECON. 505, 506 (2006) (identifying that when suppliers try to exploit consumers' mistakes, competing suppliers may wish to expose such exploitation). But see Florencia Marotta-Wurgler, *Competition and the Quality of Standard Form Contracts: The Case of Software License Agreements* 5 J. OF EMPIRICAL LEGAL STUD. 447, 468 (2008) (finding no statistically significant relationship between the degree of competition in software markets and the incidence of pro-supplier fine print.) To the best of our knowledge, however, ours is the first article to formulate this basic notion into a systematic methodology courts should pursue when assessing consumer contracts.

¹⁰ For example, a contract which states that the supplier bears no liability for a delay in delivery of up to 90 days, unless the consumer asks otherwise at the time of purchase and fills out the requisite forms. For further discussion, see *infra* Section I.B.1.

¹¹ For further discussion see *infra* Section I.C.1.

¹² For example, a supplier of services, who provides several different plans, in a way that makes it difficult for a consumer to evaluate which plan best suits him. For further discussion, see *infra* Section I.D.1. See Gilo and Porat, *supra* note 9, at 1004-1005 (showing how suppliers can use complexity of their consumer contracts in order to stifle competition); Oren Bar-Gill, *The Law, Economics and Psychology of Subprime Mortgage Contracts*, 94 CORNELL LAW REVIEW 1073, 1102-6 (2009) (showing how complex

The Article demonstrates how among the four oppressive techniques, only the traditional one, the TOT, is sufficiently affected by competition over contracts. We show how such competition cannot deter suppliers from using inefficient or unfair SOTs, SBTs or artificial complexity. Courts should therefore be particularly suspicious of SOTs, SBTs and artificial complexity, and analyze them on a case by case basis, disregarding the degree of competition over contracts in the market.

TOTs, however, should be assessed differently. Since inefficient or unfair TOTs could be effectively eliminated by competition over contracts, they should be analyzed according to the market-based method we develop here. Rather than analyzing TOTs on the basis of the parties to the contract and their characteristics, as courts currently do, according to this Article's proposal courts should explore the structure of the supplier's market and the nature and capabilities of the supplier's rivals. Furthermore, the Article lists four factors that could hinder the ability of competition to expose TOTs. When these factors are particularly strong, competition over contracts cannot be counted upon and courts should scrutinize consumer contracts according to the transaction-specific analysis they currently apply. The four factors are:

- (1) *Backfiring*: sometimes suppliers might avoid criticizing their rivals' TOT so as to avoid a negative backfiring effect on themselves. There are three types of backfiring: *Consumers' backfiring on the product* occurs when criticizing a rival's oppressive technique could expose weaknesses in the criticizer's own product or service;¹³ *Consumers' backfiring on the contract* occurs when exposing a rival's TOT requires the criticizing supplier to stop using similar TOTs himself; *rivals' backfiring* occurs when the criticized supplier is driven to retaliate.
- (2) *Attracting Unwanted Consumers*: At times when a supplier exposes TOTs in his rivals' contracts he ends up "gaining" unwanted, high-cost consumers.¹⁴ This could be a reason not to engage in such an exposition in the first place.
- (3) *Benefit Externalization*: A supplier might avoid criticizing his competitors' TOTs because the benefits of such efforts would be shared by other rival suppliers, while the criticizing supplier would shoulder the entire cost.¹⁵

sub-prime mortgage contracts are and explaining accordingly that competition could not solve inefficiencies in such contracts).

¹³ See Jon D. Hanson & Douglas A. Kysar, *Taking Behavioralism Seriously: A Response to Market Manipulation*, 6 ROGER WILLIAMS U. L. REV. 259, 339 (2000) (arguing that firms may not want to advertise the safety of their product because this raises consumers' awareness to the risk in all such products and reduces their demand); Jeff Sovern, *Toward a New Model of Consumer Protection: The Problem of Inflated Transaction Costs*, 47 WM. & MARY L. REV. 1635, 1680-81 (2006) (arguing that a firm may not want to highlight that it does not bind arbitration in a distant forum so as not to draw consumers' attention to the probability of disputes).

¹⁴ See Russell Korobkin, *Bounded Rationality, Standard Form Contracts, and Unconscionability*, 70 U. CHI. L. REV. 1203, 1242-43 (2003) (arguing that a firm would not want to brag about its lack of an arbitration clause because this might attract consumers liable to sue the firm).

¹⁵ See Howard Beales et al., *The Efficient Regulation of Consumer Information*, 24 J.L. & ECON. 491, 527 (1981) (claiming that firms may not have suitable incentives to disclose to consumers positive information about their product when rivals selling the same product would share the benefits from such

(4) *Irresponsive consumers*: In certain situations many consumers would not change their consumption decisions even if competition exposing the TOT were to take place. In such cases highlighting a rival supplier's TOT could be unrewarding.¹⁶

This Article offers to courts a coherent and systematic method for assessing TOTs based on these insights. For example, it shows how, contrary to the conventional wisdom, a TOT is more likely to be efficient and fair in a (competitive) market in which most suppliers adopt it. It also shows how a (competitive) market for a product or service that is essential to consumers justifies less intervention against TOTs than a market in which the product or service is non-essential. Also, in many instances, TOTs that qualify a right granted by the supplier himself should be treated more leniently than TOTs that qualify a default rule imposed by law. Accordingly, the Article offers courts workable guidelines according to which they can shape their intervention policies against consumers' contracts.

The Article also demonstrates how competition over contracts takes place in the real world. It provides numerous examples of suppliers' campaigns criticizing their rivals' contracts.¹⁷ The incidence of such campaigns actually understates the true impact of competition over contracts for two reasons. First, it is expected that many suppliers engage in covert efforts to criticize their rivals, e.g., through their sales representatives. Second, in a market in which a credible threat of competition over contracts exists, TOTs are expected to be efficient and fair even where no such competition is actually observed: In such markets, suppliers would be deterred from employing inefficient or unfair TOTs.

The Article is organized as follows: In *Part I* we describe the four oppressive techniques, discuss the motivations for suppliers to use them, and also expose their potential welfare-reducing and welfare-enhancing effects. In this part, we shall ignore the corrective potential of competition over contracts. *Part II* considers how competition affects the efficiency and fairness of each of the four oppressive techniques identified in Part I. As we show, intense competition over contracts could expose inefficient and unfair TOTs, but not SOTs, SBTs and Complexity. As a result, we propose that SOTs, SBTs and artificial complexity, which are not subject to market discipline, be analyzed according to strict case by case scrutiny. In this part we also analyze the factors that could prevent competition over contracts from guaranteeing efficient TOTs. *Part III* draws workable guidelines from the results obtained in Parts I and II as to how courts could employ the market-based methodology to TOTs. *Conclusions* follow.

disclosure); Ted Cruz & Jeffrey J. Hinck, *Not My Brother's Keeper: The Inability of an Informed Minority to Correct for Imperfect Information*, 47 HASTINGS L.J. 635, 659 (1996) (same).

¹⁶ See Korobkin, *supra* note 14 (claiming that highlighting the existence of a forum selection clause is not likely to change consumers' purchase decisions).

¹⁷ See *infra* notes 74-82 and accompanying text.

I. OPPRESSIVE TECHNIQUES

In this Part we present four oppressive techniques used by suppliers in their contracts with consumers. Only the first one was discussed in court decisions. With regard to each technique we expose suppliers' motivations for employing it and evaluate it from a social perspective. The effects of competition on each technique are ignored at this stage.

A. Traditional Oppressive Terms

1. *The Technique*

Many standard form contracts contain terms which deprive consumers of rights or remedies to which they would be entitled but for these terms. We call such terms "Traditional Oppressive Terms" (or "TOTs"). Example 1 illustrates a TOT.

Example 1. TV Set. In a contract for the provision of a TV set, the time of delivery is set for January 1, 2009. In the boilerplate, however, there is a clause stating that "the supplier bears no liability for a delay in delivery of up to 90 days."¹⁸

While in Example 1 the TOT exempts the supplier from contractual liability, in the next example, the TOT caps tort damages.

Example 2. The Dry Cleaner. A Dry Cleaner offers its consumers a standard form contract which contains a term stating that "the Dry Cleaner's liability per item is limited to 15 times the fee paid for the damaged or lost item."¹⁹

2. *Suppliers' Possible Motivations*

In order to understand why suppliers use TOTs one should distinguish between two states of the world: one, where there is no gap of information between the suppliers and the consumers; the other, where there is such a gap. Absent an information gap between the supplier and his consumers, there is a solid basis for assuming that the supplier incorporated the TOT into the contract in order to increase the value of the contract to

¹⁸ See *Corinno Civetta Constr. Corp. v. New York*, 67 N.Y.2d 297, 306 (1986) (stating that "damages resulting from unanticipated delays caused by the contractee may be recovered despite the existence of a broad exculpatory clause relieving the contractee from liability"); In *Fowler, Rodriguez, Kingsmill, Flint, Gray & Chalos, LLP v. Island Properties, LLC*, 833 N.Y.S.2d 146, 148 (2007) the Court ruled that "[G]enerally, even with such a [broad exculpatory] clause, damages may be recovered for: (1) delays caused by the contractee's bad faith or its willful, malicious, or grossly negligent conduct, (2) unanticipated delays, (3) delays so unreasonable that they constitute an intentional abandonment of the contract by the contractee, and (4) delays resulting from the contractee's breach of a fundamental obligation of the contract."

¹⁹ See MICHAEL J. TREBILCOCK, *THE LIMITS OF FREEDOM OF CONTRACT* 119-120 (1993) (saying that standard form contracts are common in markets which are highly competitive, dry cleaning being a typical example).

himself as well as to consumers. The explanation is that when both parties to a contract possess all relevant information, they strive to incorporate efficient terms into their contract, which increase their mutual benefit.²⁰ This reasoning applies even when one of the parties (the supplier) enjoys superior bargaining power vis à vis the other party (the consumer).²¹ In contrast, when consumers are not fully aware of the loss of value the TOT imposes upon them, there is a risk that the supplier will incorporate a TOT into his standard form contracts so as to extract value from consumers, without the latter being aware of it, and even induce some consumers to buy a product they would not have bought had they been aware of its true cost to them.²²

It is often hard to know by just looking at a TOT whether it is welfare-reducing, or rather welfare-enhancing. To illustrate, let's return to Example 2 (The Dry Cleaner). At first glance the TOT in this example seems welfare-reducing: the Dry Cleaner, rather than the consumer, is in a position to take the necessary precautions to prevent damage to consumers' clothes. If the Dry Cleaner bears the harm in its entirety, it will take efficient precautions to prevent such harm. With the TOT, the supplier's liability for damaged clothes is capped, so that he lacks appropriate incentives to take care. But notwithstanding first appearances, the following subtle point should be considered. Suppose everyone pays the same fee per item of laundry regardless of its value. With no cap on damages owed by the Dry Cleaner, consumers owning cheap items would find themselves subsidizing owners of expensive items. In the long run, many owners of cheap items would drop out, prices would go up, and eventually the entire service might

²⁰ For the case without an information gap see Michael I. Meyerson, *The Efficient Consumer Form Contract: Law and Economics Meets the Real World*, 24 GA. L. REV. 583, 586 (1990) ("In a free market, exchanges among knowledgeable rational people are expected to result in Pareto superior results..."); Richard Craswell, *Passing on the Costs of Legal Rules: Efficiency and Distribution in Buyer-Seller Relationships*, 43 STAN. L. REV. 361, 363 (1991) (mentioning that sellers have incentives to select an efficient rule on their own). For the case with an information gap see Robert Cooter & Thomas Ulen, *Law & Economics* 208 (5th ed. 2008) ("the presence of asymmetric information can sometimes preclude otherwise mutually beneficial exchanges from taking place."); *Handbook of Law and Economics Vol. 1* 34 (A. Mitchell Polinsky & Steven Shavell eds., 2007) (hereinafter: *Handbook of Law and Economics Vol. 1*) ("asymmetric information between the parties at the time a contract is negotiated can lead to distortions in the resulting contract vis-à-vis the contract that would have been negotiated under symmetric information.").

²¹ See A. Michael Spence, *Monopoly, Quality, and Regulation*, 6 BELL J. OF ECON. 417–29 (1975) (showing that a monopolist prefers to offer quality preferred by the "marginal consumer" – the first consumer to leave the supplier when price goes up -- and elect price so as to maximize its profits); Douglas G. Baird, *The Boilerplate Puzzle*, 104 MICH. L. REV. 933, 941 (2006) (explaining that even a monopolist looks for efficient warranty terms).

²² See Korobkin, *supra* note 14, at 1217-8 ("Efficiency requires not only that buyers be aware of the content of form contracts, but also that they fully incorporate that information into their purchase decisions. Because buyers are boundedly rational rather than fully rational decisionmakers, they will infrequently satisfy this requirement. ... "); Steven P. Croley & D. Hanson, *Rescuing the Revolution: The Revived Case for Enterprise Liability*, 91 MICH. L. REV. 683, 770 (1993) (arguing that without full information consumers are unable to make consumption and warranty decisions that reflect their true preferences); Meyerson, *supra* note 13, at 585 (same).

disappear from the market.²³ This concern—which a cap on damages mitigates—is the result of a gap of information between suppliers and consumers, but in a direction opposite to the one discussed so far. Here it is the suppliers rather than consumers who lack sufficient information. Suppliers are often ignorant as to whether the consumer with whom they transact is a high risk (expensive clothes) or low risk (inexpensive clothes) type. Had the supplier been able to distinguish between high and low risk consumers, the supplier would have charged each consumer in Example 2 a fee reflecting the value of his or her item, and a cap on damages would not have been necessary. However, given the above-mentioned gap of information, the supplier must charge all consumers a uniform price and a limitation on damages will be necessary for facilitating the provision of the service to consumers of all types.²⁴

An important lesson to be learned from the example above is that it is difficult for courts to judge a TOT merely according to its perceived “harshness” or “one-sidedness”. Thus it is all the more important to provide courts with manageable tools for determining whether a supplier would want to include a welfare-reducing TOT in his contracts, without having to assess the TOT’s merits directly. As shown in part II, the market-based method we propose constitutes such a tool. Before presenting our market-based approach to TOTs, however, the next section describes the welfare concerns stemming from TOTs.

3. Welfare Concerns

As demonstrated above, absent information gaps in which consumers lack sufficient information, all terms in standard form contracts should be deemed welfare enhancing and therefore efficient. There is no need to particularly explore whether a term is efficient, because, regardless of his bargaining position, the supplier only loses from including inefficient terms in his contract. As demonstrated, this could be so even with terms that, at first blush, seem inefficient. Also, no particular fairness concern emerges when there is no gap of information between the parties, because the consumer got exactly what he expected, or reasonably could expect, to get.

If, however, consumers are not informed enough as to the oppressive term or its cost to them, three kinds of efficiency concerns arise. First, suppliers may incorporate terms into the contract that allocate risks between the parties inefficiently (“*inefficient allocation of risks*”). For example, the TV supplier of Example 1 might include the TOT relieving him from liability for late delivery even when it saves him less than the cost it imposes on the consumer. Second, regardless of whether the term involves inefficient

²³ See RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 110-111 (7th ed., 2007) (Describing a similar phenomenon in the case of insurance); Richard A. Epstein, *Beyond Foreseeability: Consequential Damages in the Law of Contract*, 18 J. LEG. STUD. 105, 137-8 (1989) (justifying reducing damages in order to prevent the cross-subsidization of some plaintiffs by others).

²⁴ See also Baird, *supra* note 21, at 940 (arguing that a disclaimer of liability for consequential damages could be motivated by the supplier's goal of avoiding liability for harms caused by the carelessness of others).

allocation of risks, a second form of inefficiency may evolve: many uninformed consumers might buy products and services they should not have bought (*"inefficient contracting"*). For example, regardless of the TOT's efficiency, some consumers who bought the TV would not have bought it had they been aware of the TOT. Third, and, again, regardless of whether the TOT allocates risks efficiently, *informed* consumers might refrain from buying the product due to the TOT (*"inefficient non-contracting"*).²⁵ In example 1, the TOT imposes a cost on consumers (due to late delivery) yet this is not reflected in the TV's price. A consumer who understands this may well refrain from buying the TV, although it would have been socially warranted for him to buy it for its fair price.

The normative concerns with TOTs are not limited to inefficiencies. TOTs also raise fairness concerns, since they enable suppliers to extract value from consumers without them being aware of it, and induce consumers to buy products and services they do not really want. As such, TOTs constitute a form of deception.

Accordingly, when consumers are not well-enough informed, both inefficiency and unfairness could result. It is here, however, that two crucial questions arise: First, how can we know whether consumers are well-enough informed? Second, what happens if consumers are *not* well-enough informed – should it then be presumed that the TOT creates inefficient allocation of risks, inefficient contracting, inefficient non-contracting or unfairness? As we will see in the next parts of the Article, a useful way to answer these two important questions is to explore the degree and type of competition over contracts in the supplier's market.

B. Selectively Oppressive Terms

1. The Technique

As opposed to TOTs, Selectively Oppressive Terms ("SOTs") are oppressive only for some consumers. Consider the following variation of Example 1.

Example 3. TV Set II. In a contract for the provision of a TV set, the time of delivery is set for January 1, 2009. In the boilerplate, however, there is a clause stating that "the supplier bears no liability for a delay in delivery of up to 90 days, *unless the consumer asks otherwise at the time of purchase and fills out the requisite forms.*" Filling out the requisite forms takes no more than a couple of minutes and entails no benefit to the supplier.

As opposed to Example 1, in Example 3 any consumer who carefully reads the standard form contract will understand that she can request the removal of the

²⁵ See, e.g., Robert H. Lande, *Wealth Transfers as the Original and Primary Concern of Antitrust: The Efficiency Interpretation Challenged*, 34 HASTINGS L. J. 65, 72-74 (1983) ("[The] misallocation of resources results in diminished satisfaction of society's wants, and thus, in terms of what society values, a reduction of society's total wealth.").

exclusionary clause at no additional costs to her. The only reason for not doing so would be if the consumer were not aware of the exclusionary clause and her easy way out of it. Thus, with the type of SOT illustrated in Example 3, there is always an information gap between the supplier and *some* of his consumers. Only consumers who bear the transaction costs involved in a careful reading of the fine print will learn of the SOT and take costless steps to avoid it.²⁶

An example of a SOT is a term in a contract for the sale of a product, according to which the product's warranty is conditioned upon the buyer keeping the original receipt.²⁷ Only buyers who read the contract and remember to retain the receipt enjoy the warranty, other buyers forfeit it.²⁸ Another example of a SOT is a term in a travel insurance policy in which coverage of losses due to theft is conditioned upon reporting the theft to the police within 24 hours.²⁹ Insureds who either do not read the terms of the policy carefully or fail to comply with this specific term for other reasons, are denied compensation, while those who bear the transaction costs of reading the term and complying with it get fully compensated.³⁰ A third example concerns granting benefits to consumers, but limiting, in the fine print, eligibility for the benefit to a short period of time. Many consumers assume they will receive the benefit, while in fact this is so only if they act promptly.³¹ A fourth and final example is a term in a car rental contract which

²⁶ Not every SOT is characterized by consumers not being aware that there is a way out of the oppressive term. To illustrate, suppose that in Example 3, filling out the requisite forms does not take just a couple of minutes as in the original example, but rather is time consuming. With such a SOT, even if all consumers are aware of its existence, some of them will give up on filling out the forms so as to save time, knowing they will then have to bear the costs of the exclusionary clause. Interestingly, in this variation of Example 3 there is no information gap between any consumer and the supplier. Nevertheless the oppressive term is selective: some consumers are willing to fill out the forms and relieve themselves of the oppressive clause, and some are not willing to do so and thus remain subject to this clause.

²⁷ See, e.g., Sagemax's insurance contract for LCD televisions, instructing that the receipt is "an integral part" of the contract, and the consumer "may be required to reference it to obtain service.", www.bhphotovideo.com/find/sagemaxTC.jsp.

²⁸ Arguably, asking for the original receipt could be motivated by the supplier's desire to save verification costs as to the validity of the warranty. It seems, however, that other means of verification – certainly in the computer age – could be at least as effective and almost costless.

²⁹ See, e.g., Access America – Travel Insurance & Assistance, Individual Travel Insurance Policy No. 52.201NY 13-14, http://www.worldnomads.com/policy_wording.aspx?uid=7d4701fdcb8f487dbef849f8673502f1 (offering coverage for baggage, which states that "[y]ou must notify the appropriate local authorities at the place of the loss occurred and inform them of the value and description of your property within 24 hours after the loss.").

³⁰ Here too an argument can be made that reporting to the police immediately serves the insurer's interests in reducing risks. But it is quite obvious that for many types of thefts, in many countries, reporting to the police is almost useless, and in any case, the penalty for failing to report within 24 hours—deprivation of entitlement to any compensation, is allegedly draconian.

³¹ For example, American Airlines offers a "Low Fare Promise," according to which if the consumer provides a lower rate on another airline she receives a \$50 coupon from American Airlines. In order to receive such a benefit, among other conditions, the claim must be submitted by midnight on the same day of the purchase from American Airlines. See <http://www.studentscrooge.com/2008/10/09/the-american-airlines-low-fare-guarantee/> (a students' blog describing the fine print behind American Airlines' low-fare-guarantee).

penalizes the consumer for not picking up the car she has reserved, but then includes in the fine print a process for partly waiving the penalty.³² Only consumers who are well-aware of this particular term and who are willing to bear the transaction costs involved in getting the partial waiver will receive it, many others will not.³³

2. Suppliers' Possible Motivations

Suppliers may want to use SOTs for several reasons. To begin with, SOTs involve benefits for the supplier that resemble those derived from using TOTs: SOTs allow suppliers to extract value from uninformed consumers. Notwithstanding this similarity between TOTs and SOTs, a very important distinction between them should be made: With a TOT, the supplier takes the risk of losing *informed* consumers who find the TOT in the fine print and consequently decide not to buy the product. With a SOT, the supplier can enjoy both worlds: he manages to deceive consumers vulnerable to deception while retaining consumers who cannot be fooled – informed consumers can buy from the supplier while escaping the oppressive term.³⁴

Accordingly, SOTs allow suppliers to benefit informed consumers at the expense of uninformed consumers, thereby discriminating in favor of the former. Such a strategy could induce informed consumers to buy the supplier's product or service even when they would not have bought it otherwise.

Let us illustrate in more detail how SOTs allow suppliers to improve the deal they offer informed consumers at the expense of the uninformed consumers. Suppose the price of a supplier's TV sets when all consumers are fully informed (i.e., without hiding a SOT in the contract) is 10. A supplier who chooses to incorporate the SOT of Example 3 into his contracts could exploit uninformed consumers in the following way: he could charge all consumers a price of 9, but extract a value of 2 from uninformed consumers through the SOT. In such a scenario, uninformed consumers would be subject to the oppressive

³² Hertz car rental agency, for example, partly refunds the prepayment in case of "No Show", but only "if you write to us within 90 days of the Pick Up Date at Hertz Prepaid Accounting Department...", <http://www.hertz.com.ro/qualifications.php?topic=Amendments,+Cancellation,+No+Show++Lost+Rental>.

³³ There could also be *ex post* SOTs, namely, oppressive terms which are applied in a discriminatory manner by suppliers: See Lucian A. Bebchuk & Richard A. Posner, *One-Sided Contracts in Competitive Consumer Markets*, 104 MICH. L. REV. 827 (2006) (explaining the efficiencies of many one-sided terms in consumer contracts, which are selectively applied). Also, "add-ons" – expensive services or products that are added on to the original deal, bear some resemblance to SOTs. See Gabaix & Laibson, *supra* note 9 (analyzing the case of avoidable add-ons, such as the minibar or other services at a hotel). As with SOTs, some consumers manage to avoid the add-ons, by not using them, and some end up using them. The difference between an avoidable add-on (such as a hotel mini bar) and a SOT is that most consumers are aware of the oppressive add-on before they decide whether to use it. With a SOT, on the other hand, uninformed consumers are simply unaware of the oppressive term hidden in the fine print, and unaware of the ability to avoid it.

³⁴ Note that some informed consumers would have entered the contract even if they hadn't been able to remove the oppressive term. Supposedly, the supplier could have offered such consumers the same deal with a TOT and earned more. But for the supplier, it is often more important to retain the more sensitive informed consumers, who would not have bought the product if they were subject to the oppressive term.

term hidden in the fine print, relieving the supplier of liability for late delivery. Informed consumers, who see the SOT and fill out the forms to escape the oppressive term, pay 9 and receive the TV on time. As a result, *de facto*, it is as if informed consumers pay 9, while uninformed consumers pay 11. The supplier saves the costs of having to deliver on time to uninformed consumers. These profits, made at the expense of uninformed consumers, can be used to enable the price reduction from 10 to 9. Accordingly, informed consumers, who pay 9 and receive the TV on time, are subsidized by the uninformed consumers. This benefits the supplier, because informed consumers are typically more sensitive to the terms of the deal, and many of them would not have bought the TV at the original price of 10.

Why are informed consumers typically more sensitive to the terms of the deal than uninformed consumers? Informed consumers are those who waive the SOT and incur the transaction costs of reading the contract carefully, filling out the requisite forms (as in Example 3), and so forth. Their willingness to do so can serve as a proxy for their sensitivity to the terms of the deal.³⁵

In particular, consumers who are willing to pay attention to the fine print and escape the oppressive term are typically characterized as one (or more) of the following: (a) those who value their time less and their money more compared to others. Such consumers are also typically more sensitive to what they receive for their money; (b) large or repeat buyers, for whom investing the transaction costs involved in a careful reading and understanding of the contract and filling out the forms is worthwhile given the high volume of their business with the supplier. Such consumers too are typically sensitive to oppressive terms in the contract; (c) sophisticated consumers for whom the transaction costs are relatively low, because they are trained in reading and understanding such contracts and also in filling out the forms. To the extent that sophisticated consumers are also those better aware of alternative products, they too are often “trigger happy” with regard to rejecting the supplier’s product.³⁶

Another reason for suppliers to employ SOTs is that a contract with a SOT may look more fair than the same contract with a TOT. Suppliers use TOTs to extract value from uninformed consumers. They bear the risk, however, of courts striking the term down.³⁷ If suppliers use a SOT instead, as in Example 3, they benefit from both worlds: on the one hand many consumers would shoulder the consequences of the oppressive term without being aware of it, as with a TOT; but on the other hand, the term cannot be easily challenged in court because it appears to be fair. After all, in Example 3, a consumer could easily avoid the exclusionary clause if she filled out the requisite forms. The supplier could easily come up with an explanation justifying the requirement to fill out

³⁵ Gilo & Porat, *supra* note 9, at 996-7 (discussing the imposition of transaction costs on consumers to distinguish between those who are more price sensitive from those who are less sensitive to price).

³⁶ *See id.* at 997.

³⁷ *Infra* Section III.A.

forms. The above-mentioned car rental example³⁸ could also be explained in this way: the damages imposed upon the consumer for late delivery could be considered unreasonable by courts and struck down. However, the court may change its mind if it assumes that most of the penalty could "easily" be waived in favor of consumers who ask for it to be waived. The car rental company could come up with a reason for imposing the damages in the first place, and allowing a subsequent refund at a later stage.

The innocent appearance of the contract could also protect the supplier from public opinion critics, as well as from his own consumers who might later realize that they ended up with the worst deal. Such consumers, when acknowledging they could have easily received the better deal, might tend to blame themselves, not the supplier.³⁹

A final reason suppliers might prefer to use SOTs rather than TOTs is that TOTs, as we shall see in Part II, could at times expose the supplier to criticism by his rivals, and cause the supplier to lose market share. As we show, this is not the case with a SOT. A rival supplier would derive little benefit from criticizing the supplier's SOT.

3. Welfare Concerns

When consumers are not informed enough, using SOTs could be at least as problematic as using TOTs: in both cases the supplier extracts value from consumers, without the latter being aware of it. As with TOTs, SOTs too raise fairness concerns, could allocate risks inefficiently and might create inefficient contracting by causing uninformed consumers to buy a product that they don't really want.⁴⁰

However, as noted, and unlike TOTs, SOTs can facilitate "price discrimination" between informed (often more sensitive to the terms of the deal) and uninformed (often less sensitive to the terms of the deal) consumers. The upside of such discrimination, from an efficiency perspective, is that it may allow the supplier to improve the terms it grants to consumers who have waived the SOT and prevent them from deciding to not buy the product at all.⁴¹ Let us label this welfare-enhancing feature of SOTs "*bringing consumers on board*." That is, absent the SOT, efficient transactions between the supplier and some informed consumers would not have taken place.⁴²

³⁸ *Supra* text accompanying notes 28-9.

³⁹ But occasionally the reverse would be true: consumers may develop antagonism toward a supplier who failed to make the SOT more salient.

⁴⁰ *See supra* section I.A.3.

⁴¹ *See, e.g.,* JEAN TIROLE, *THE THEORY OF INDUSTRIAL ORGANIZATION* 139 (1988) (showing how price discrimination could improve welfare by inducing consumers who are more sensitive to price to buy the product).

⁴² SOTs' ability to discriminate between informed and uninformed consumers could also serve as an anticompetitive device that facilitates collusion among competing suppliers. The reasons for this resemble those of Selectively Beneficial Terms ("SBTs"), which will be discussed below *See infra* note 55 and accompanying text.

SOTs could also involve a distributional justice concern.⁴³ Because SOTs enable price discrimination, they cause inequality among consumers: some consumers get better deals than others.⁴⁴ However, under a SOT, consumers who enjoy the better deal are often the less wealthy ones: those who value their time less and their money more compared to others, and therefore are willing to incur the transaction costs required for waiving the SOTs.⁴⁵ This could mitigate, or even overrule, the distributional justice concerns in using SOTs.

Finally, another important difference between SOTs and TOTs relates to the higher sustainability of SOTs. If many consumers were informed, socially harmful TOTs would not survive.⁴⁶ This is not the case with SOTs, since even with a mass of informed consumers, the supplier would not remove a socially unwarranted SOT: He would still be able to exploit the uninformed consumers while keeping the informed consumers happy.⁴⁷

In Part II, we show that competition cannot be counted upon to deter suppliers from using inefficient and unfair SOTs. Hence, in stark contrast to courts' complete disregard of SOTs, they actually deserve strict legal scrutiny, even more so than TOTs. While, as shown in Part II, inefficient or unfair TOTs may be competed away under certain circumstances, this is shown not to be the case with SOTs.

C. Selectively Beneficial Terms

1. The Technique

The mirror image of a SOT is a Selectively Beneficial Term ("SBT"). While SOTs are *oppressive* for only some consumers, SBTs are *beneficial* for only some consumers. Example 4 illustrates how an SBT works.

⁴³ It is a controversial question whether the distribution of wealth should be a concern for legal rules or rather should be left to the tax system. See Louis Kaplow & Stephen Shavell, *Should Legal Rules Favor the Poor? Clarifying the Roles of Legal Rules and the Income Tax in Redistributing Income*, 29 J. LEG. STUD. 821 (2000) (arguing for the superiority of the tax system in this respect); TSACHI KEREN-PAZ, TORTS, EGALITARIANISM AND DISTRIBUTIVE JUSTICE 14-66 (2007) (arguing that distributive justice should be a concern when defining tort rules). In the context of our discussion, we merely wish to point out, as a positive matter, that distributive effects exist, without taking sides as to whether these effects also have normative implications.

⁴⁴ On the other hand, one could claim that SOTs enhance distributional justice among consumers to the extent that they cause consumers who value the product more to pay more. Arguably, those who benefit more from the product should indeed pay more.

⁴⁵ *Supra* text accompanying notes 31-2.

⁴⁶ *Supra* Section I.A.1; Schwartz & Wilde, *supra* note 7 at 673 (showing that intervention against contract terms is undesirable when a mass of consumers is sufficiently informed).

⁴⁷ As noted, Schwartz and Wilde, *id.* show that when a large enough percentage of consumers are informed, suppliers are induced to include efficient terms in their contract. They assume, however, that suppliers offer the same contractual terms to all consumers. In contrast, with a SOT, informed consumers are relieved from the oppressive term while uninformed consumers are not. This is why a mass of informed consumers would not suffice to deter the supplier from using a SOT.

Example 4. Special Discount. A supplier who sells computers offers, in the fine print, a special discount to consumers who fill out a certain form and mail it back to the supplier. Only consumers who read the fine print carefully and remember to fill out the form and mail it, enjoy the special discount.

As opposed to TOTs and SOTs, which create a bad surprise for uninformed and no surprise for informed consumers, an SBT does not create a surprise for either informed or uninformed consumers. In Example 4, consumers who do not read the contract and therefore do not get the special discount are not misled by the supplier: they received exactly what they had expected! However, with SBTs consumers who bear certain transaction costs get better deals than others. In this respect SBTs resemble SOTs. To illustrate, if in the above-mentioned example the posted price for a computer is 11 and there is a special discount of 2 in the fine print, uninformed consumers end up paying 11, while informed consumers end up paying only 9.⁴⁸

There are many real life cases in which consumers who are willing to incur the transaction costs of reading and understanding their contracts with their suppliers receive greater benefits. One example is hiding a best price guarantee in the fine-print.⁴⁹ Another example is common in subscription sales. Internet service providers often have a provision in the fine print granting customers signing up an option to cancel within a certain period of time and get their money back.⁵⁰ Many consumers are not aware of this option, and therefore do not execute it. Probably those who are more hesitant about signing up would tend to incur the transaction costs of exploring all the terms of the contract offered to them. They are the ones who would utilize the benefit.⁵¹

⁴⁸ As with SOTs, it is possible to distinguish between two types of SBTs: In the first type the transaction costs a consumer needs to incur in order to receive the benefits consist merely of the time spent in reading and understanding the contract. The other type of SBT is one where consumers know they are required to bear transaction costs—such as filling out time-consuming forms—in order to be entitled to the benefits.

⁴⁹ In this example the supplier undertakes in the fine print to match any competing offer given by another supplier. See Aaron S. Edlin, *Do Guaranteed-Low-Price Policies Guarantee High Prices, and Can Antitrust Rise to the Challenge?*, 111 HARV. L. REV. 528 (1997). Edlin points out that low-price guarantees enable price discrimination between customers who cite a competing price and other consumers. Our additional insight is that suppliers may want to "hide" their low-price guarantees in the fine print, rather than making them salient, so that only the particularly price-sensitive consumers will take advantage of the guarantees.

⁵⁰ See, for example, the terms of sale of Speakeasy, which offers broadband Internet services: "Speakeasy offers a 25-day Trial Period on all ADSL services... If you feel that you must cancel within 25 calendar days of your Activation Date you may do so without being subject to a Disconnection Fee." Speakeasy, Terms of Service, <http://www.speakeasy.net/tos>.

⁵¹ Cf. Jason Scott Johnston, *The Return of Bargain: An Economic Theory of How Standard-Form Contracts Enable Cooperative Negotiation Between Business and Consumers*, 104 MICH. L. REV. 857 (2006) (arguing that suppliers often extend benefits beyond standard-form consumer-contract terms and explaining their motivations for doing so).

2. Suppliers' Possible Motivations

As is evident from the examples above, the idea behind an SBTs is to confer benefits only on consumers who appreciate them. Hence, as with SOTs, SBTs extract more value from uninformed consumers while at the same time attracting informed consumers, who incur the transaction costs of reading the contract and, as in Example 4, filling out the forms. These latter consumers are typically more sensitive to the terms of the deal and many of them would not buy the product without the beneficial term. But there is an important difference between SOTs and SBTs in this respect. As noted, suppliers might use SOTs in order to fool uninformed consumers into buying a product under terms they would not have accepted had they know about them. This is not the case with SBTs, where even uninformed consumers buy what they aimed to buy, namely, the product without the special benefit.

This also illuminates how SOTs and SBTs feature two different modes of price discrimination. With SBTs all consumers know how much they are paying and what they are receiving; by contrast, with SOTs only informed consumers have it right. This difference bears on the potential profits a supplier could derive from each of these two techniques. With an SBT, since uninformed consumers know of the high price they are paying (say, a posted price of 11 in Example 4) they might refrain from buying the supplier's product. This is not the case with a SOT, in which uninformed consumers mistakenly believe they are paying a relatively low price for a contract without the oppressive term. Hence the supplier does not lose their business.

Finally, as with SOTs, the supplier can use SBTs to make the contract appear fair, thereby immunizing it from both courts' and consumers' scrutiny. The supplier may have wanted to use a TOT, but is well aware that a TOT could be struck down by courts as unfair. To avoid this, in addition to the TOT, the supplier could incorporate an SBT into the contract in order to set the stage for the argument that the contract is balanced and fair. By using an SBT and not a beneficial term which applies to all consumers, the supplier gains more: only some consumers receive the benefits, while the argument that the contract is balanced and fair may still be accepted by courts. Thus, suppose that in Example 4 there was a TOT, immunizing the supplier from liability for a delay of up to 90 days in delivery (as in Example 1). Such a TOT is at risk of invalidation by courts. The supplier could argue, however, that because of the TOT he offered consumers a special discount, in an SBT, which makes the price lower than that of his competitors. As explained, this strategy could protect the supplier from courts' and others' scrutiny, even though most consumers, being uninformed, would pay the full price *and* bear the costs of the oppressive clause.

3. Welfare Concerns

From a social welfare perspective, SBTs are less problematic than TOTs or SOTs. As noted, TOTs and SOTs present a "bad surprise"⁵² for uninformed consumers. This is not the case with SBTs, in which uninformed consumers receive what they expected to get. Unlike TOTs and SOTs, SBTs cannot cause consumers to buy products they do not really want. This implies that TOTs and SOTs possess greater potential for inefficiencies.

The efficiency implications of an SBT depend on the social outcome of the price discrimination it allows, which is generally ambiguous. On the one hand, the SBT effectively reduces the price paid by informed consumers and this could induce such consumers to buy the product. That is, an SBT features the social advantage of "*bringing consumers on board*." This effect promotes social welfare.⁵³ On the other hand, the price uninformed consumers pay under an SBT is typically higher than the price consumers would pay absent such price discrimination. This could cause some uninformed consumers not to buy the product. Accordingly, SBTs also feature "*inefficient non-contracting*" – they could cause efficient transactions not to take place. The latter effect has a negative effect on social welfare.⁵⁴ Furthermore, as we show elsewhere, SBTs could hinder competition in certain cases, by making tacit or explicit collusion between competitors more likely.⁵⁵

From a fairness perspective, SBTs are much less problematic – if at all – than TOTs and SOTs: consumers are not deceived by suppliers, since they receive what they expected to get. The situation could be different where there is a special relationship between the supplier and the consumer. At times, a special relationship warrants the recognition of a duty on the part of the supplier to explicitly disclose to consumers the existence of an SBT in his standard form contracts.⁵⁶ SBTs could also create a distributional justice concern, since they create inequality among consumers. Still, as

⁵² An important criterion for courts' intervention in consumer contracts is whether the arguably problematic terms posed a bad surprise for the consumer. *See infra* note 108.

⁵³ *See* TIROLE, *supra* note 41, at 137-142 ("... [A] necessary condition for price discrimination to be preferred socially is that it raise total output ..."); HANDBOOK OF LAW AND ECONOMICS Vol. 2 1089 (A. Mitchell Polinsky & Steven Shavell eds., 2007) ("price discrimination generates greater seller profits yet may well be benign or even favorable on average for consumers.").

⁵⁴ *Supra* Section I.B.3.

⁵⁵ *See* Gilo & Porat, *supra* note 9, at 1025-29.

⁵⁶ *See, e.g.* United States use of Bussen Quarries, Inc. v. Thomas, 938 F.2d 831, 834 (8th Cir. 1991) ("The duty to disclose may arise from inequality of position, a fiduciary relationship between the parties, or a demonstration of superior knowledge on the part of one party that is not within the fair and reasonable reach of the other party."); Merrill Lynch, Pierce, Fenner & Smith, Inc. v. First Nat'l Bank of Little Rock, Ark., 774 F.2d 909, 913 (8th Cir. 1985) ("The duty to speak may be based on special circumstances, such as a confidential relationship, in which one party knows that another is relying on a misrepresentation to his detriment.").

with SOTs, in the case of SBTs consumers who enjoy better deals are often the less wealthy ones. This helps alleviate, or even remove, distributive justice concerns.⁵⁷

In Part II we show how competition over contracts cannot really be trusted to remove SBTs.

D. Complexity

1. The Technique

The fourth and final oppressive technique often used by suppliers is artificial complication of the contract. The next example is illustrative.

Example 5. Combined Internet and Multichannel TV Plans. An Internet provider who also supplies multichannel TV offers a menu of plans: each plan is different than the others with regard to general monthly fee, fee per special channels or group of channels, pay per view, video on demand services, band width, modes of payment, and all of the permutations among the above parameters, in ways that make it difficult for a consumer to evaluate the plans.

There are numerous examples where there is good reason to suspect complication of contracts of being artificial. Contracts with cellular phone companies⁵⁸, with credit card firms⁵⁹ for mortgages,⁶⁰ and for car rentals⁶¹ are common examples.

2. Suppliers' Possible Motivations

The complexity of the provider's contracts in Example 5 creates a distinction among consumers similar to that of SOTs or SBTs. It is often the case that consumers who better understand these complexities, and hence could opt for the best deals, are the same consumers who delve into a supplier's fine print to avoid SOTs or to look for SBTs. Other consumers, because they find the transaction costs of understanding complex contracts prohibitively high, might get a poorer deal. Accordingly, complexity, like SBTs and SOTs, can serve as a tool for *price discrimination* in favor of the better informed group of consumers.

In addition to price discrimination, artificially complicated contracts could benefit the supplier in other ways. In particular, complicating contracts is sometimes necessary for the success of the other oppressive techniques used by suppliers. TOTs, SOTs and

⁵⁷ *Supra* note 44 and accompanying text.

⁵⁸ Several websites offer comprehensive comparisons between cellular phone companies, and cellular plans. *See, e.g.*, <http://www.cellphones.ca/cell-plans>; <http://www.myrateplan.com>.

⁵⁹ For a comparison between the different packages offered by various credit card firms *see* <http://www.creditcards.com>.

⁶⁰ *See* Bar-Gill, *supra* note 12.

⁶¹ *See* Ronald J. Mann, "Contracting" for Credit, 104 MICH. L. REV. 899, 903 (2006) (describing the complexity of car rental contracts).

SBTs are typically hidden in the fine print and their effectiveness often depends on consumers' difficulties in locating and understanding them. The degree of the contract's complexity affects the quantity of uninformed consumers. The level of the contract's artificial complexity therefore depends on how many consumers the supplier wishes to keep uninformed. If the supplier wishes to exploit uninformed consumers as much as possible with a TOT or SOT, he will probably artificially make his contracts particularly complex. If he wishes to allow some consumers to enjoy a special benefit (as with an SBT) the artificial complexity of his contracts will probably be more moderate.

3. Welfare Concerns

Complexity used to hide a TOT or a SOT could extract value from uninformed consumers and also induce some of them to buy products they would not have bought but for the complex nature of the contract. Hence artificial complexity, in such cases, could feature inefficiencies (inefficient allocation of risks, inefficient contracting (by uninformed consumers), inefficient non-contracting (by informed consumers)), as well as unfairness and distributive justice concerns similar to those created by TOTs and SOTs.

Complexity not used to hide TOTs or SOTs (i.e., complexity per se), could create price discrimination, the efficiency of which is ambiguous (as with SBTs the upside of such discrimination is *bringing consumers on board* but the downside is *inefficient non-contracting*.) In addition, such complexity could create *inefficient contracting*. That is, complexity per se could lure consumers to enter contracts they would not have entered had they been informed. To illustrate, in Example 5, where uninformed consumers cannot really pick the package of multi-channel TV and Internet services most suitable to their needs, they may well find themselves with an unsuitable package which they would never have chosen had they understood the contract.

Price discrimination enabled by complexity per se also raises distributive justice issues, but they are less of a concern to the extent that consumers discriminated against are the rich. Contract complexity could also stifle competition in the market, as it makes it harder for consumers to compare among competing suppliers.⁶² This makes suppliers less likely to try to compete for consumers.⁶³ Note that as in the case of SOTs, socially

⁶² Indeed, Bruce Cran, president of the Consumers Association of Canada, was quoted last summer as saying that "They (wireless carriers) deliberately make it very difficult to make comparisons," See Gillian Shaw, *iPhone Data Pricing Draws Fire; 35¢ for Brief email. Bell Mobility Might Feed Off Backlash*, THE GAZETTE, July 9, 2008, at B5. In the same vein, Natalie Woodroffe, spokesman for UK credit card issuer Nationwide, said that: "In the current market, it is very difficult for British consumers to make an informed choice. There are 1,300 credit card brands available in the UK, offering a range of different rates, fees and complex terms and conditions." See Nina Montagu-Smith, *Lay Cards on The Table, Nationwide Tells Rivals Building Society Wants Clarity on Fees*, TELEGRAPH.CO.UK, Nov. 1, 2002, <http://www.telegraph.co.uk/finance/personalfinance/borrowing/creditcards/2832161/Lay-cards-on-the-table-Nationwide-tells-rivals.html>.

⁶³ See Gilo & Porat, *supra* note 9, at 997-8; Bar-Gill, *supra* note 12 at 1102-6.

harmful complexity would not disappear even if many informed consumers existed, because informed consumers are not particularly harmed by complexity.

As shown in Part II, competition would often have a negligible deterrent effect against artificial complexity of standard form contracts. Hence this technique, like SOTs, should be strictly scrutinized by courts.

E. Summary

The following table summarizes the welfare concerns stemming from the four oppressive techniques.

TABLE 1: WELFARE CONCERNS FROM THE OPPRESSIVE TECHNIQUES

	<i>Inefficient Allocation of Risks</i>	<i>Inefficient Contracting</i>	<i>Inefficient Non-Contracting</i>	<i>Efficiently Bringing Consumers on Board</i>	<i>Unfair</i>
<i>TOT</i>	yes	yes (non-informed)	yes (informed)	no	yes
<i>SOT</i>	yes (non-informed)	yes (non-informed)	no	yes	yes
<i>SBT</i>	no	no	yes (non-informed)	yes	no
<i>Complex</i>	yes (non-informed)	yes (non-informed)	yes (non-informed)	yes	yes

II. COMPETITION OVER CONTRACTS AND THE INFORMATION GAP

In Part I, we presented four oppressive techniques used by suppliers in standard form contracts. We explored suppliers' possible motivations in employing these techniques and discussed the possible policy concerns stemming from each technique. In Part I, we purposely ignored the impact of competition. In the current part of the Article we introduce competition into the discussion. We explore to what extent competition over contracts can contribute to closing the gap of information between suppliers and their uninformed consumers. This is a crucial question because the oppressive techniques could not be inefficient or unfair without an information gap. Hence competition's ability to close the information gap should be a central consideration in evaluating whether a particular oppressive technique is efficient and fair, and, accordingly, whether it warrants the court's intervention in the standard form contract.

Of course, for competition over contracts to exist, competition over price, or at least over quality, must be shown to exist. For example, if a supplier who uses a TOT is a monopolist – the only supplier in his market – his product or service faces no competition, so there is no competition with regard to his contract either. Competition could also be lacking altogether when there are only a few suppliers in the market (an

oligopolistic market) and the market is susceptible to collusion.⁶⁴ In a market prone to tacit or explicit collusion, suppliers might collude also over the imposition of oppressive terms. In what follows, we assume that the supplier's market is competitive enough to foster competition over price and quality, and we focus on the question whether and when *competition over contracts* exists.

Competition over contracts can inform consumers who were previously uninformed.⁶⁵ When consumers are informed, suppliers would not want to place inefficient terms in their fine print.⁶⁶ The same is true when consumers are uninformed, but there is a credible *threat* of competition over contracts, which could inform them. This would suffice to deter suppliers from hiding inefficient or unfair terms in their standard form contracts. Hence *competition over contracts*, in our framework, involves suppliers' credible threats to *actively* expose each other's oppressive techniques, thereby informing uninformed consumers.⁶⁷ After all, if suppliers have already exhausted price and quality competition, and a supplier wishes to raise its market share at the expense of other suppliers, he may wish to find hidden flaws in his rival's contracts and make them salient to consumers. As we shall see below, however, this particular form of competition does not always exist.

A. How Can Competition over Contracts Close the Information Gap?

Suppose the market in which a supplier operates is competitive. How can competition the supplier faces help inform consumers about the supplier's oppressive techniques, thereby deterring the supplier from employing inefficient and unfair terms in his contract? In this section we answer this question. In sum, it all depends on whether competitive tension among rivals in the market triggers not only competition over price or quality, but also *competition over contracts*; only then, suppliers would be effectively deterred from using inefficient and unfair techniques in their standard form contracts.

In the meantime, we purposely ignore special factors, explored in detail in section B below, which could stand in the way of competition closing the information gap. In the current section we show that even before considering these special factors the effects of competition on the information gap crucially depend on the type of oppressive technique

⁶⁴ See, e.g., TIROLE, *supra* note, 41 at 240, 247-51 (showing when competitors could collude, even tacitly, and what market conditions foster such behavior); See also F.M. SCHERER & DAVID ROSS, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE (3d ed. 1990) 235-75 (same).

⁶⁵ See *supra* note 9. Ezra Friedman, *Competition and Unconscionability* ((May 2009) (unpublished paper presented at Am. L. & Econ. Ass'n, on file with authors) claims that a more competitive market may be more prone to exploitation, because firms then earn less money on informed consumers than in a non-competitive market. He takes the naiveness of consumers as given, however. In our framework, in a competitive market, suppliers may want to steal market share by educating consumers.

⁶⁶ See *supra* note 20.

⁶⁷ Absent such competition, standard-form contracts could be regulated to make their terms more salient. Cf. Mann, *supra* note 57, at 927-32 (proposing to foster competition among credit card issuers, by standardization of most of the terms offered to consumers).

used by the supplier. Let us examine these effects separately for each of the four oppressive techniques.

1. Traditional Oppressive Terms

Consider a supplier ("Supplier X") employing the TOT described in Example 1: His standard form contract contains a provision, in the fine print, according to which "the supplier bears no liability for a delay in delivery of up to 90 days." But now suppose that the supplier is not the only one in his market, but rather faces intense competition from several rival suppliers who sell TV sets too. Intense competition means that if a supplier is offering consumers either a relatively high price or a relatively poor deal, competing suppliers can and will offer better deals and/or lower prices.⁶⁸ But if consumers remain in the dark as to Supplier X's TOT hidden in the fine print, simply offering them a deal without such a TOT would not suffice in order to persuade them to switch to a competing supplier. Hence competing suppliers would often want to let consumers know about Supplier X's hidden TOT, in order to entice them away from Supplier X.⁶⁹ This is a simple case where competition could close the information gap between Supplier X and his consumers.

At times, consumers might learn of a supplier's inefficient or unfair TOT from sources other than the supplier's rivals. In particular, consumer-oriented web sites could provide some information regarding oppressive terms in consumer contracts in certain industries.⁷⁰ In appropriate cases, where an industry is under close scrutiny of reliable watchdogs that are committed to protect consumers, a supplier could claim that the threat

⁶⁸ By "intense competition" we do not necessarily mean competition that drives prices all the way down to marginal cost (the cost of supplying the marginal unit). We acknowledge that in real life, in most markets competition is not that perfect. *See, e.g.,* ANDREU MAS-COLELL, MICHAEL D. WHINSTON & JERRY R. GREEN, MICROECONOMIC THEORY 387-400 (1995); TIROLE, *supra* note 41, at 209-236. Subject to this caveat, we assume that competition is intense enough to induce suppliers to try and fight each other for market share. In other words, we assume that competitive tension is too intense to sustain tacit or express collusion among suppliers.

⁶⁹ For examples of such behavior, *see infra* notes 71-79 and accompanying text.

⁷⁰ For example, ConsumerReports.org reported a survey of contracts regarding extended warranties for cars, and recommended that consumers pay attention to "exclusions and limitations" in the fine print, stressing that in order to learn about them, "you need to delve into the contract." *See* <http://www.consumerreports.org:80/cro/cars/new-cars/buying-advice/extended-warranties-4-08/how-they-work/how-they-work-continued/extended-warranties-how-they-work-terms-and-coverage.htm>. *See also* Omri Ben-Shahar, *The Myth of 'Opportunity to Read' in Contract*, 4 EUR. REV. OF CONT. L. 428 (2008) (Proposing non-legal approaches to making the contract terms more transparent, by building on market devices such as ratings and labeling). In addition, independent bloggers or industry analysts occasionally highlight the existence of harsh terms in the fine print of particular suppliers. For example, Telecom Analyst Bruce Kushnick has revealed allegedly oppressive terms in the fine print regarding the use of iPhones. *See What's Hidden in iPhone's Fine Print?*, July 9, 2007, <http://directorblue.blogspot.com/2007/07/whats-hidden-in-iphones-fine-print.html>; *See also* <http://www.newnetworks.com/attwirelessfineprint.htm>; Also, blogger Ken Fisher has alleged that a term in AT&T's contract for Internet connection is oppressive. *See infra* note 92.

of such exposure would suffice in order to deter him from including inefficient or unfair TOTs in his contracts, much like competition over contracts would.

There are various examples of firms criticizing terms hidden in the fine print of their rivals' contracts: To give only a few, in its commercials Capital One, a rewards credit card firm, mocks competing reward credit card companies, for hiding various limitations to receiving rewards in their fine print, such as minimum card use requirements, expiration and inalienability provisions, as well as blackout dates during which rewards cannot be used.⁷¹ Nationwide, a provider of loans, mortgages and credit cards, has emphasized that its rivals' fine print contains "hidden features" such as the paying off of the cheapest debt first and stressed in an Internet publication, that "We think that is unfair, so we allow customers to pay off the most expensive debt first."⁷² In a TV commercial, Nationwide highlights how its rivals in the mortgage market hide an "HLC," or "Higher Lending Charge" in their contract that kicks in when the amount borrowed exceeds a given percentage of the value of the property.⁷³ Broadband Internet Service Provider PlusNet criticized its competitors, and specifically its rival Tiscali, for misleading customers into believing they had "unlimited connectivity," whereas the fine print of their standard form contracts includes a "fair usage" clause that is designed to ease congestion at peak traffic times but effectively serves as a cap on connectivity.⁷⁴ Cheap TV Spots, a company which offers TV advertising for small businesses, attacked the oppressive fine print of its rivals that sell automated ads.⁷⁵ Wireless carrier Alltel broadcast a TV commercial criticizing rivals AT&T, T-Mobile, Sprint and Verizon (the companies' representatives each wear a T-shirt with the name of the competing carrier marked on it) for their fine print preventing customers from changing their wireless plan without extending their contract.⁷⁶ Virgin Mobile too has extensively published critiques

⁷¹ See <http://www.youtube.com/watch?v=IFn4cxy05HA> (Capital One commercial in which reward limitations are allegorized through a princess kissing a frog and receiving a rat instead, who quotes the fine print); <http://www.youtube.com/watch?v=Kxpx4HnPCtS> (Capital One commercial where limitations are allegorized through a tooth fairy quoting the fine print explaining why a child receives merely a nickel for her tooth); <http://www.youtube.com/watch?v=WAGJkRh8rXA> (Capital One commercial implicitly comparing rival's fine print to living Hell while Capital One causes Hell to freeze out with the slogan "Capital One: takes all of the surprises out of reward mile redemption ... no hidden fees, no expiration, no blackouts.")

⁷² See Nina Montagu-Smith, *supra* note 62.

⁷³ See <http://www.youtube.com/watch?v=8Lgbs6A2glk&feature=related> (Nationwide commercial featuring a couple, frustrated by the provision while the rival bank's representative tries to distract them); For a definition of an HLC, see http://www.home.co.uk/guides/mortgage_glossary.htm?hlc; See also http://www.youtube.com/watch?v=qFZV3y-p_NY (another Nationwide commercial criticizing rivals for first offering low introductory rates so as to "hoike people in" and then exploit them with larger hidden fees.)

⁷⁴ See David Meyer, *PlusNet Accuses Broadband Rivals of Misleading Customers*, ZDNET.CO.UK, Sept. 1 2006, <http://news.zdnet.co.uk/communications/0,1000000085,39282114,00.htm>.

⁷⁵ See <http://cheaptvcommercial.com/> (Cheap TV Spots Internet ad calling consumers who choose rivals "suckers" due to rivals' oppressive fine print).

⁷⁶ See <http://www.youtube.com/watch?v=E1h0KaaOkFM>. Following Alltel's campaign, Verizon Wireless and Sprint Nextel announced that they too would alter their contracts to enable customers to switch plans without extending the contract's period. See Matt Kapko, *VZW Sues Alltel over Ad Claims*;

about its rivals' fine print, including "hidden fees,"⁷⁷ charging for services the customer does not need,⁷⁸ as well as lock-in periods.⁷⁹

2. *Selectively Oppressive Terms*

Consider now the SOT of Example 3 above, where Supplier X's standard form contract provides that "the supplier bears no liability for a delay in delivery of up to 90 days, *unless the consumer asks otherwise at the time of purchase and fills out the requisite forms.*" Suppose now that Supplier X faces intense competition from other TV suppliers. To what extent would other suppliers, who vigorously compete with Supplier X, have the incentive to inform consumers about Supplier X's SOT? Unlike the case of a TOT, with a SOT, Supplier X's informed consumers, who have no particular problem carefully reading the fine print and filling out the forms, are not subject to the oppressive term. Where the transaction costs required from informed consumers to escape the oppressive term are negligible, competing suppliers could not entice such informed consumers away from Supplier X by highlighting the existence of the SOT. A competing supplier could allegedly only steal Supplier X's potential uninformed consumers – those who are subject to the oppressive term. But when a competing supplier reveals the existence of the SOT to them, even they may well buy Supplier X's product, now that they know from the competing supplier how to easily relieve themselves from Supplier X's oppressive term. Hence competing suppliers might be unsure how many consumers

Fight Centers on Ability to Change Plans without Impacting Contracts, RCR WIRELESS NEWS, Jan. 7, 2008, at 4. See also <http://www.youtube.com/watch?v=xgnSgW-xz3c> (where another Alltel commercial highlights how customers of its four rivals (represented again by these four representatives) are "stuck" with contracts that do not match their individual needs).

⁷⁷ See Maryanna Lewyckij, *Cellphone Fee Furor; System Access Charges Subject of Lawsuit*, THE TORONTO SUN, March 5, 2005, at 48. (Founder of Virgin Mobile quoted saying that his rival cellular carriers have been hiding fees in their fine print.); See also <http://www.youtube.com/watch?v=sWMsZLk0mfc> (a news bulletin describing the PR strategy behind the launching of Virgin Mobile, featuring "Nothing to Hide," "no contracts" and "no hidden fees."); Also, Bell Mobility, a Canadian rival of Rogers, the network associated with iPhones, has broadcast a commercial criticizing the fees hidden in rivals' contracts. The ad features customers of rival cell phone companies as victims of a crime. See <http://www.youtube.com/watch?v=IS4QMYZhcI8>. Indeed, the Canadian network associated with iPhone has been reported as using oppressive and unfair techniques in its fine print, and Bell Mobility was named by reporters as the carrier most likely to feed off the exposure of Rogers' behavior. See Gillian Shaw, *supra* note 62.

⁷⁸ See <http://www.youtube.com/watch?v=-4aNgTXjf5c>. (A Virgin Mobile commercial entitled "Don't Get Hosed").

⁷⁹ See <http://www.youtube.com/watch?v=mZW8VlnGgQQ>. (A Virgin Mobile ad entitled "don't get sucked in"); <http://www.youtube.com/watch?v=nfjczPVyddI>. (Ad with the slogan "Had enough? Get Virgin Mobile. No ripoffs, no lock-ins."); <http://www.youtube.com/watch?v=Q0jMAu45vas>. (Virgin Mobile commercial criticizing "the mobile phone companies that tempt you with the so called 'free phones,' they don't explain all the costs ... "). Several additional examples of firms criticizing their rivals' fine print exist on file with authors.

they could really steal from Supplier X by closing the consumers' information gap, and this lack of certainty could stifle their incentive to do so.⁸⁰

Accordingly competition has a weak deterrent effect on Supplier X's incentive to include an inefficient or unfair SOT in his contract.⁸¹

3. Selectively Beneficial Terms

Will suppliers want to make their rivals' SBTs salient to consumers? Suppose Supplier X adopts the SBT mentioned in Example 4: His fine print provides a special discount for consumers who fill out a certain form and mail it back to the supplier. Will competing suppliers, engaged in vigorous competition with Supplier X, have an incentive to highlight to consumers the existence of Supplier X's SBT? The analysis here is similar to that of SOTs: First, the competing supplier would not necessarily succeed in enticing Supplier X's informed consumers away, since they already enjoy the special discount from Supplier X. Second, the rival supplier might not even be able to entice uninformed consumers away from Supplier X, since the latter, following the rival's advertisement about Supplier X's SBT, might simply choose Supplier X's product and fill out the requisite forms.⁸² As in the case of SOTs, then, there are no substantial benefits from exposing a rival's SBT.⁸³

⁸⁰ The situation could be different when the transaction costs required in order to neutralize the oppressive term are non-negligible. If, for example, filling out the forms in Example 3 is time consuming, a competing supplier could steal more of Supplier X's consumers by highlighting that when buying his TVs, no oppressive terms exist, with no need for time consuming filling-out of forms.

⁸¹ See Gabaix & Laibson, *supra* note 9 (showing that competition cannot deter suppliers from using avoidable add-ons, that were shown above to resemble SOTs). To be sure, at times competing suppliers could derive certain long-term benefits from closing consumers' information gaps as to Supplier X's SOT. First, if for some reason the rival supplier is not able to discriminate in favor of informed consumers (as the SOT enables Supplier X to do) the rival may want to expose the SOT in order to erode Supplier X's ability to discriminate. Second, emphasizing the existence of Supplier X's SOT to consumers could erode Supplier X's profits, leaving him fewer funds to invest in improving his product. Still, these subtle long-run competitive motivations could not be counted upon to guarantee the rival's incentives to expose the SOT. Criticizing SOTs might become more likely where the SOT binds the consumer to his supplier and makes it hard for her to switch to a competing supplier. For example, UK telecom company British Telecom has criticized its rival, TalkTalk, alleging that its "customer agreements are unfair because they include a 'negative opt-out term' which allows TalkTalk to move customers [to its own network] without their permission." A British Telecom executive was quoted as saying that "[t]hese clauses are unfair on customers and are a shady practice. I am surprised they would ever be considered by a major industry operator." The criticized term is a SOT, since, according to TalkTalk's contract, a consumer can ask, in writing, to disqualify TalkTalk from unilaterally moving his telephone line to TalkTalk's network. See Damian Reece, *BT Accuses Talktalk of Shady Sales Practice*, THE INDEPENDENT, Feb. 26, 2005, at 49. Finally, when third impartial parties, such as consumer-oriented web sites, closely scrutinize the supplier's market, such parties could also deter suppliers from using inefficient or unfair SOTs. See *supra* note 70 and accompanying text.

⁸² As with SOTs, a rival supplier could try to attract consumers by showing them they can receive the same special discount with a smaller hassle. He could lure informed consumers from Supplier X if the transaction costs consumers need to bear for receiving the discount from Supplier X are significant.

⁸³ Edlin, *supra* note 49, at 538 shows how entry into the market does not alleviate the price-increasing effect of price matching policies. Price matching (promising to match a rival's lower price) bears some

4. Complexity

Suppose now that Supplier X is the provider of multichannel TV and Internet mentioned in Example 5, who offers complex contracts, the value of which is hard for consumers to assess. Can a rival of Supplier X gain from closing the consumers' information gap caused by this complexity? The answer depends on what Supplier X is trying to accomplish by using complexity. Naturally, if complexity is used to disguise a TOT, rival suppliers may want to help consumers see through the complexity and realize the existence of Supplier X's TOT. As in the case of highlighting the existence of any TOT, the rival supplier could, in this way, steal consumers from Supplier X.

Suppose now, on the other hand, that Supplier X's complexity is not used to hide a TOT but rather to facilitate discrimination by Supplier X, or to facilitate the application of SOTs or SBTs. Here rival suppliers' incentives to neutralize the complexity and emphasize this fact could be weaker. Supplier X's informed and sophisticated consumers may well be satisfied with Supplier X, since they know their way through Supplier X's contractual maze. Furthermore, they may be subsidized by Supplier X's uninformed and less sophisticated consumers, who end up with worse deals.⁸⁴

B. Factors Preventing Competition from Closing the Information Gap

As we saw in the previous section, competition has the potential of closing the information gap between suppliers and consumers mainly when suppliers use TOTs. With the other oppressive techniques competition over contracts is expected to be minor or non-existent. In this section we discuss several factors that may prevent competition from closing the information gap even with respect to TOTs. Each of these factors could cause suppliers not to inform consumers about the TOTs used by their rivals.

1. Backfiring Competition

One reason suppliers might avoid criticizing their rivals' oppressive techniques is that by doing so they would expose themselves to consumers' negative reactions toward their

resemblance to SBTs, since it too enables suppliers to discriminate between informed and uninformed consumers. As in the case of SOTs, discussed *supra* note 81, in certain cases there could be long-run, more subtle profits derived by a competing supplier from highlighting Supplier X's SBT. Such subtle competitive drives cannot be counted upon, however, to close the information gap. Also, when third impartial parties, such as consumer-oriented web sites, closely scrutinize the supplier's market, such parties could deter suppliers from using inefficient or unfair SBTs. See *supra* note 70 and accompanying text.

⁸⁴ To be sure, if a rival supplier offers consumers a simple deal with terms equivalent to those informed consumers could receive from Supplier X, they may nevertheless switch to the rival supplier, so as to relieve themselves from the transaction costs. Also, in certain circumstances, rivals may have long-run incentives to dissipate Supplier X's ability to discriminate (via complexity) or his ability to make profits in this fashion. See *supra* note 81. Finally, when impartial parties, such as consumer-oriented web sites, closely scrutinize the supplier's market, such parties could simplify complex contracts for the benefit of consumers. See *supra* note 70 and accompanying text.

own products (*consumers' backfiring on product*)⁸⁵ or contracts (*consumers' backfiring on contract*) or to rivals' retaliation (*rivals' backfiring*). To illustrate, suppose that in Example 2 (the Dry Cleaner) the TOT limiting the Dry Cleaner's liability for damage to the customer's clothes was adopted by Dry Cleaner X and is inefficient. Dry Cleaner X's competitors are therefore supposedly expected to expose the TOT and make consumers understand its drawback: a high risk of exposure to non-recoverable losses. But despite the existence of intense competition in Dry Cleaner X's market, competing dry cleaners may avoid exposing the TOT and its adverse effect on consumers, because this exposition may backfire on them. Consumers' backfiring on the product occurs because by illuminating Dry Cleaner X's TOT a rival supplier may create the impression in consumers' minds that dry cleaning as such may result in harm to consumers' clothes. Absent such exposition by rival dry cleaners, the possibility of damage to their clothes (as the existence of the TOT itself) may not have been salient to consumers.⁸⁶ Once consumers become aware of the possible harm, their consumption of dry cleaning services, including the services of the criticizing dry cleaner, may go down.

The second type of backfiring, consumers' backfiring on the contract, can occur because when a rival dry cleaner exposes Dry Cleaner X's TOT this sharpens the consumers' attention and increases their aversion toward exclusionary clauses used by dry cleaners in general, including the criticizing dry cleaner's exclusionary clauses. That is, if a dry cleaner criticizes Dry Cleaner X's exclusionary clause, he too would probably have to stop using exclusionary clauses, since due to his campaign against Dry Cleaner X's oppressive clauses, consumers would become more sensitive to such clauses.⁸⁷

The third type of backfiring, rivals' backfiring, takes place because when Supplier X's TOT is criticized by a competing supplier, Supplier X is usually expected to retaliate. By definition, criticizing a rival's contract involves "negative advertising." That is, rather than praising his own product, a supplier has something bad to say or imply about his rival's contracts with consumers. Such negative advertising could be costly to the criticizing supplier, because it usually invites retaliation by the criticized supplier.⁸⁸

⁸⁵ See *supra* note 13.

⁸⁶ See Korobkin, *supra* note 22, at 1229-1230 ("For a product's attribute to be salient to buyers, the attribute must capture the limited attention of those buyers.").

⁸⁷ Consumers' backfiring on the product and on the contract are stronger the longer suppliers expect to operate in the market. When such backfiring occurs, its damage is usually long lived. If a rival supplier has a TOT similar to Supplier X's TOT and this supplier criticizes Supplier X's TOT, the criticizing supplier would probably need to stop using such a TOT for an indefinite period. Similarly, if such criticism reduces the demand for the product, the reduction in demand could last for a considerable period.

⁸⁸ See Ming-Jer Chen & Danny Miller, *Competitive Attack, Retaliation and Performance: An Expectancy-Valence Framework*, 15 STRATEGIC MGMT. J. 85, 86 (1994) ("If a firm's actions represent a threat that is obvious, easy to match, and significant, its alert rivals will be motivated to counter that attack, and thus perhaps, to negate its potential benefits"). Retaliation could be a rational strategy if the criticized supplier wishes to show consumers that he is not worse than the criticizing supplier and/or when the criticized supplier wishes to win back market share enticed away from him by the criticizing supplier. Chen and Miller, *id.* at 88, claim that "[a]n action is more likely to evoke a response if it is easy to imitate, that is, if it can be countered simply, economically and without much organizational disruption...".

Retaliation against the criticizing supplier is expected to be harsher the more severe the critique.⁸⁹

While the threat of consumer backfiring on the product varies from case to case, and is at times compelling, suppliers' fear of rivals' backfiring always exists to a certain extent. Furthermore, consumer backfiring on the contract exists whenever the criticizing supplier himself employs oppressive techniques similar to the criticized one. In a market in which competition over price and quality is strong, however, consumer backfiring on the contract and rivals' backfiring are not expected, in and of themselves, to stop suppliers from criticizing their rivals' TOTs. In general, *any* competitive move by a supplier involves the need to become competitive himself (as in the case of consumer backfiring on the contract) and involves, to a certain extent, retaliation by the suppliers' rivals, who wish to compete back (as in the case of rivals' backfiring). Nevertheless, in a competitive market, these two forms of backfiring are usually presumed not to block competition.

2. *Attracting Unwanted Consumers*

A supplier would hesitate to expose his rival's oppressive terms if he expected many of the consumers attracted by this exposition to be unwanted consumers.⁹⁰ Unwanted consumers are characterized by the fact that they are so costly to serve that, if possible, a supplier would prefer not to serve them at all.

Unwanted consumers could typically exist in markets for services, long-term contracts, sales of products with supplier warranties, and so forth, where consumers of certain types are prohibitively costly to serve.⁹¹ To illustrate, consider the example given in the introduction of a manufacturer of computers who employs a clause in his contracts exonerating himself from liability for losses caused by some of the computer's components. Assume now that these components malfunction half of the time due to the consumer's carelessness. A rival computer supplier criticizing this TOT must take into account that the first consumers the exposition of the TOT attracts are the careless consumers whose expected losses are relatively high. For such consumers the TOT is especially harmful. Naturally, the criticizing supplier could not employ a similar

⁸⁹ Chen & Miller, *id.*, examined the aviation industry in the United States and concluded that the more visible, more central and more easily imitated attacks by criticizing firms provoke more responses from the criticized.

⁹⁰ See *supra* note 14.

⁹¹ Suppliers often try to get rid of high cost consumers. See, e.g., Alisa Bralove, *Screening Clients Can Prevent Attorneys from Taking on Problem Clients*, THE DAILY RECORD, Aug. 15, http://findarticles.com/p/articles/mi_qn4183/is_20030815/ai_n10057488/pg_1 (quoting attorneys who advise their colleagues on how to identify and get rid of unwanted clients); Lucy Barrett, *How Admen Can Spot the 'Timewaster.com'*, MARKETING WEEK, Nov. 4, 1999, <http://www.mad.co.uk/Main/News/Disciplines/Digital/Articles/7f1953a8adc1428e8de91dcf36c7a7dd/How-admen-can-spot-the-timewastercom.html> (reporting how London's top advertising agencies turn down new Internet ventures due to their high insolvency rate).

exclusionary clause in his contract. Hence he may rightly fear that many of the consumers he would entice away would be "high risk," and therefore "high cost," consumers. This would weaken his incentives to expose his rival's TOT in the first place.

A similar effect could deter competitors from criticizing the Dry Cleaner's TOT in Example 2. The first consumers to leave the Dry Cleaner after they become aware of the TOT are those whose clothes are more vulnerable to damage or more expensive. A rival dry cleaner who does not limit his liability might hesitate to entice away such consumers, whose expected harm from dry-cleaning is on average relatively high.⁹²

3. *Benefit Externalization*

As the preceding sections show, the criticizing supplier at times bears costs when he exposes a rival's oppressive technique, particularly due to backfiring of the three above-mentioned types, and the attraction of unwanted consumers. At the same time, the benefits of exposing a rival's TOT could be shared by many of the other suppliers in the market, particularly those who do not use similar TOTs themselves. Consumers concerned with their supplier's exposed TOT might well leave their supplier in favor of another supplier who does not use such a TOT, and might not necessarily transfer to the criticizing supplier. If the criticizing supplier bears all costs when criticizing his rival and does not receive all of the benefits, his incentive to do so will be diminished.⁹³ Moreover, each of the suppliers who do not use TOTs may prefer to wait until another supplier among them decides to bear the costs of criticizing their rival.⁹⁴ Consequently, it may be that none of them ends up engaging in such criticism.

4. *Irresponsive Consumers*

In order for competitive pressure to close the information gap between consumers and a supplier, a large enough portion of consumers needs to be responsive to the information the rival supplier is trying to convey to them.⁹⁵ To be sure, not all consumers

⁹² For another example, consider Internet access provider AT&T's TOT, enabling it, at the time, to "immediately terminate ... your Service, any Member ID, electronic mail address, IP address, Universal Resource Locator or domain name used by you, without notice, for conduct that AT&T believes... tends to damage the name or reputation of AT&T, or its parents, affiliates and subsidiaries." Naturally, no rival of AT&T would wish to highlight the existence of this TOT, because the customers who care about such a term and who would likely transfer to the criticizing rival would be those most inclined to harm the reputation of their Internet provider. Fortunately, in this case the TOT has been revealed by a journalist. See Ken Fisher, *AT&T Vows to Use Terms of Service for Good, Not Censorship*, Oct. 2, 2007, <http://arstechnica.com/news.ars/post/20071002-att-vows-to-use-terms-of-service-for-good-not-censorship.html>.

⁹³ See *supra* note 15.

⁹⁴ To be sure, some of the costs created when a TOT is exposed are suffered by all rivals, and not only by the criticizing supplier. Such are the costs involved in consumers' backfiring on the product and on the contract, and in attracting unwanted consumers. A disproportionate part of these costs, however, are born by the criticizing supplier. The costs of rivals' backfiring are born exclusively by the criticizing supplier.

⁹⁵ See *supra* note 16.

need to respond to such information. It is sufficient that a critical mass of them might leave the supplier following the rival's advertisements in order to effectively deter the supplier from employing the TOT. Such a critical mass of responsive consumers may not exist, however. In certain cases, consumers are not only ignorant of the TOT hidden in their contract, but also indifferent to advertising by rival suppliers who try to emphasize its existence. After all, uninformed consumers are often those who are not willing to expend the transaction costs needed in order to read the fine print in their contracts. They may be equally unwilling to absorb and verify a rival supplier's claim that their contract is oppressive. Take the TOT of Example 1, for instance, in which Supplier X relieves himself from liability for late delivery of a TV set. If a rival supplier advertises, in written leaflets put in mailboxes or via Email, that Supplier X's contract includes a TOT in the fine print, consumers who do not read the fine print may also fail to read and absorb such an advertisement. In order to induce them to respond, the rival supplier would have to expend more resources in advertising. For example, he would have to emphasize Supplier X's TOT in television or radio commercials. But the latter form of advertisement is more costly, and therefore could be less profitable for the criticizing supplier. The criticizing supplier may well prefer to use the scarce and expensive advertising time he had purchased to convey information consumers are more likely to respond to.

The situation might be different when suppliers use sales representatives who have direct contact with consumers. Such sales representatives could try to convince consumers to buy their company's product or service by exposing rival suppliers' TOTs and emphasizing how the rivals' contract is unfair or draconian. Consumers' responses to such efforts might at times be stronger, making the efforts worth their while.⁹⁶ Also, consumers might be more responsive in cases in which their deal with the supplier is a larger one.⁹⁷

C. Sufficiency of a Competitive Threat

As noted, for competition over contracts to deter suppliers from using inefficient or unfair TOTs, rivals need not actually inform consumers about such TOTs. The threat that rivals may do so often suffices in order to provide such deterrence.⁹⁸ When a supplier

⁹⁶ See Arvind Rangaswamy, Prbhakant Sinha & Andris Zoltners, *An Integrated Model-Based Approach for Sales Force Structuring*, 9 MARKETING SCI. 279, 281 (1990) (examining the role of sales representatives and pointing out that on the one hand, short purchase cycle and a competitive environment support a constant presence of sales representatives. On the other hand, customers view the presence of sales representatives as an inconvenience).

⁹⁷ See *infra* section III.B.1.c.

⁹⁸ It is well known that when a market is competitive enough, the mere threat of competition assures competitive prices and good quality. See, e.g., TIROLE, *supra* note 41, at 101 (showing that in a competitive market, product quality will be optimal from the point of view of the average consumer in equilibrium, while a different level of quality would not evolve in equilibrium in the first place). This is why antitrust courts and agencies approve or disapprove of a transaction, such as a merger among competitors, on the basis of the number of viable competitors in the market. If the number and capacity of such rivals is large

considers employing an inefficient or unfair TOT, he balances the gains such a TOT might grant him with the expected losses from having rivals later criticize his TOTs. Even if, say, only a 20% chance of rivals criticizing his TOT existed, such criticism might involve such a large expected loss that it would outweigh the gains the supplier expected to make from the TOT. This implies that even in cases where one or more of the four factors discussed in the previous section *partially* hinders competition over contracts, the probable threat of such competition could suffice to remove inefficient or unfair TOTs.

It should be stressed that the supplier's expected losses from rivals' criticism is typically long-lived. When its inefficient or unfair TOT is exposed, many consumers may leave him in favor of rival suppliers. Even if the supplier stops using the TOT, consumers might not trust him anymore.

III. HOW SHOULD COURTS HANDLE TRADITIONAL OPPRESSIVE TECHNIQUES?

In this part of the Article we propose to courts how to implement the market-based approach and when to intervene in standard form consumer contracts based on our conclusions from Parts I and II.

As demonstrated in Part II, competition over contracts serves as a weak deterrent against the use of SOTs, SBTs and artificial complexity. Accordingly, these three techniques deserve special scrutiny and courts should be particularly suspicious about them. This result is striking, as to date courts have virtually ignored these techniques. Yet as Part I shows, they potentially pose significant efficiency and fairness concerns. As we show elsewhere,⁹⁹ a host of legal tools exist to cope with the welfare concerns stemming from SBTs. As to SOTs and artificial complexity, it would be worthwhile to explore how the unconscionability doctrine could be applied to such practices and what other legal tools might be available to mitigate their social harm.

Unlike in the cases of SOTs, SBTs and artificial complexity, where competition cannot be counted upon to prevent their social harm, Part II shows how at times competition—or even a threat of competition—could deter suppliers from using inefficient or unfair TOTs. Part III provides courts with guidelines for applying the proposed market-based approach to TOTs. We start by presenting courts' current

enough, the merger is approved, because the threat of competition is counted upon to produce competitive prices and quality. *See, e.g.,* Laura L. Stephens, *Nonprofit Hospital Mergers and Section 7 of The Clayton Act: Closing An Antitrust Loophole*, 75 B.U. L. REV. 477, 500 (1995) ("In analyzing mergers, economists assume that market concentration and market performance (i.e., price competition) tend to vary inversely."); *Irving Bank Corporation v. Board of Governors of the Federal Reserve System*, 845 F.2d 1035 (1988) (approving a merger among banks due to the low concentration of the market); Department of Justice and Federal Trade Commission's 1992 Horizontal Merger Guidelines, Statement Accompanying Release of Revised Merger Guidelines, 57 Fed. Reg. 41, 552; 41,559 (Sept. 10, 1992), at section 1.51 ("Mergers resulting in unconcentrated markets are unlikely to have adverse competitive effects and ordinarily require no further analysis.").

⁹⁹ *See* Gilo & Porat, *supra* note 9, at 1020-30.

methodology for assessing TOTs. We then continue to propose how courts might dramatically change their existing methodology by incorporating the insights of Part II into the analysis of TOTs.¹⁰⁰

A. Courts' Existing Attitude toward TOTs and the Proposed Change

Courts utilize various legal tools to deal with TOTs.¹⁰¹ At times, courts conclude that TOTs have not been accepted by consumers in the first place and therefore are not part of the contract.¹⁰² On other occasions, courts interpret TOTs in favor of consumers, applying the rule of interpretation against the draftsman.¹⁰³ Another way courts tackle TOTs is to find them unenforceable under public policy considerations.¹⁰⁴ At times, courts impose liability for misleading advertising, when a supplier publicly advertises only the beneficial, salient parts of his product, hiding the parts that make the supplier's real deal less attractive.¹⁰⁵ But the most familiar tool courts employ in dealing with TOTs is the doctrine of unconscionability.¹⁰⁶ According to this doctrine, courts take into account two types of unconscionability: procedural unconscionability and substantive

¹⁰⁰ For a different approach advocating various degrees of market regulation see Baird, *supra* note 14, at p. 947 (stating that "in mass markets in which there is little dickering or negotiating, legal rules should focus ... on ensuring the smooth operation of the market as a whole").

¹⁰¹ See Robert A. Hillman & Jeffrey J. Rachlinski, *Standard-Form Contracting in the Electronic Age*, 77 N.Y.U. L. REV. 429, 456-60 (2002) (discussing various legal tools to handle harsh terms in standard form contracts).

¹⁰² E. ALLAN FARNSWORTH, FARNSWORTH ON CONTRACTS 298-300 (1999) ("[a] judicial technique in dealing with standard forms is to refuse to hold a party to a term on the ground that, although the writing may plainly have been an offer, the term was not one that an uninitiated reader ought reasonably to have understood to be part of the offer."); *Nagrampa v. MailCoups, Inc.*, 469 F.3d 1257, 1267 (9th Cir. 2006) (deciding that the franchisee did not agree to the arbitration clause, and thus it is not a part of the agreement); *C&J Fertilizer, Inc. v. Allied Mut. Ins. Co.*, 227 N.W.2d 169, 181 (Iowa 1975) (refusing to enforce an escape clause in an insurance policy because "This escape clause..., was never read to or by plaintiff's personnel, nor was the substance explained by defendant's agent").

¹⁰³ See, e.g., *United States v. Seckinger*, 397 U.S. 203, 210 (1970) (applying the rule of interpretation against the draftsman to a construction contract). See also RESTATEMENT (SECOND) OF CONTRACTS §206 ("In choosing among the reasonable meanings of a promise or agreement or a term thereof, that meaning is generally preferred which operates against the party who supplies the words or from whom a writing otherwise proceeds.").

¹⁰⁴ See, e.g., *Armendariz v. Found. Health Psychcare Servs.*, 6 P.3d 669, 690 (Cal. 2000) ("Employing 'general contract law principles,' courts will refuse to enforce arbitration provisions that are 'unconscionable or contrary to public policy.'").

¹⁰⁵ See, e.g., *Colgan v. Leatherman Tool Group, Inc.*, 135 Cal. App. 663 (2006) (affirming a summary judgment imposing liability, since the defendant advertised its products as "Made in U.S.A.," although components were manufactured outside the United States); *Williams v. Gerber Prods. Co.*, 523 F.3d 934 (9th Cir. 2008) (ruling in favor of parents, who believed snacks for toddlers called "fruit juice snacks" were healthy for their children, although the two most prominent ingredients were corn syrup and sugar).

¹⁰⁶ UCC §2-302(1) ("If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result."); see JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE 151-177 (2000) (discussing the unconscionability doctrine); FARNSWORTH, *supra* note 102, at 908 (same).

unconscionability.¹⁰⁷ Procedural unconscionability exists when consumers are uninformed or when the supplier enjoys a superior bargaining position.¹⁰⁸ In such cases, consumers, as some courts have maintained, "do not have a meaningful choice."¹⁰⁹ Substantive unconscionability relates to the harshness of the TOT: the more oppressive it is the higher its chances of being struck down.¹¹⁰

Within procedural unconscionability courts often focus on whether the individual consumer claiming the application of the doctrine was informed. For example, a consumer who is not a native speaker of English might be considered uninformed and his TOT would be condemned, while English speaking consumers subject to the same TOT would be considered informed and their TOTs would remain valid.¹¹¹ An extreme case of substantive unconscionability is reflected in occasions in which a TOT is struck down because of its very nature. A common example is an exclusionary clause relating to personal injury, which is considered by the UCC as *prima facie* unconscionable.¹¹² At times, even exclusionary clauses concerning non-bodily harm, such as the one in

¹⁰⁷ See Arthur Allen Leff, *Unconscionability and the Code – The Emperor's New Clause*, 115 U. PA. L. REV. 485 (1967) (discussing both types of unconscionability and the interrelation between them); Korobkin, *supra* note 15, at 1254 ("Courts usually search for 'substantive unconscionability' only when there is evidence of a procedural defect in the bargaining process. Without evidence of 'procedural unconscionability', courts generally defer completely to seller-drafter terms."); Robert Hillman, *Online Boilerplate: Would Mandatory Website Disclosure of E-Standard Terms Backfire?*, 104 MICH. L. REV. 837, 854 (2006) (discussing the two forms of unconscionability).

¹⁰⁸ See, e.g., *Washington Mutual Finance Group, LLC v. Bailey*, 364 F.3d 260, 268 (5th Cir. 2004) (Procedural unconscionability is proven by showing "a lack of knowledge, lack of voluntariness, inconspicuous print, the use of complex legalistic language, disparity in sophistication or bargaining power of the parties and/or a lack of opportunity to study the contract and inquire about the contract terms."); *Flores v. Transamerica HomeFirst, Inc.*, 113 Cal. Rptr. 2d 376, 381-82 (Cal. App. 2001) ("Procedural unconscionability analysis focuses on 'oppression' or 'surprise.'"); *First Financial Ins. Co. v. Purolator Secur., Inc.*, 69 Ill. App. 3d 413, 419 (1979) ("The unconscionability doctrine has been applied most often to prevent instances of commercial sharp practices by parties possessing superior bargaining power.").

¹⁰⁹ See *Williams v. Walker-Thomas Furniture Co.* 350 F.2d 445, 449 (D.C. Circ. 1965) ("Unconscionability has generally been recognized to include 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."); *Abramson v. Juniper Networks, Inc.*, 115 Cal. App. 4th 638, 651 (2004) ("The oppression component arises from an inequality of bargaining power of the parties to the contract and an absence of real negotiation or a meaningful choice on the part of the weaker party.").

¹¹⁰ See, e.g., *Kinney v. UnitedHealth Care Services, Inc.*, 70 Cal. App. 1322, 1330 ("Substantive unconscionability' focuses on the terms of the agreement and whether those terms are so one-sided as to 'shock the conscience.'"); *Nagrampa v. MailCoups, Inc.*, 469 F.3d 1257, 1267 (9th Cir. 2006) ("In other words, the more substantively oppressive the contract term, the less evidence of procedural unconscionability is required to come to the conclusion that the term is unenforceable"); *Abramson v. Juniper Networks, Inc.*, 115 Cal. App. 4th 638, 651 (2004) ("Substantively unconscionable terms may take various forms, but may generally be described as unfairly one-sided.").

¹¹¹ See, e.g., *Jefferson Credit Corp. v. Marciano*, 302 N.Y.S.2d 390, 393 (holding that a contract was unconscionable, since the defendant, because of his poor English, could not understand that he had waived the implied warranties of fitness and merchantability.).

¹¹² UCC §2-719(3) ("Limitation of consequential damages for injury to the person in the case of consumer goods is *prima facie* unconscionable...").

Example 2 (The Dry Cleaner), may be considered unconscionable regardless of whether consumers are informed or not.¹¹³

In addition to courts conducting case by case adjudication, legislatures in several states have enacted laws prohibiting the use of certain types of TOTs. For example, several states have banned suppliers from disclaiming implied warranties of fitness and merchantability of the product or service.¹¹⁴ In many states, suppliers are subject to duties of disclosure with respect to certain terms of the deal, including TOTs, thereby closing the gap of information between them and consumers.¹¹⁵ At times suppliers are required by legislators to clearly disclose to consumers whether they are providing them with a limited or a full warranty, yet once the disclosure requirement is met suppliers are free to provide a limited warranty.¹¹⁶

In sum, the brief description above suggests that courts take account of three main considerations when deciding whether to strike down a TOT: to what extent consumers are informed; the supplier's bargaining power vis a vis consumers; and the harshness of the term in question. Yet it is hard to identify a clear and unified theory guiding courts when dealing with TOTs.¹¹⁷

By contrast, the law and economics literature has shown that the main focus of courts should be on procedural, rather than substantive unconscionability, and that even within procedural unconscionability, only the information gap between suppliers and consumers matters, rather than the supplier's superior bargaining power.¹¹⁸ In particular, when consumers are sufficiently informed, it is safe to assume that the policy concerns discussed in Part I above are small, i.e., the TOT efficiently allocates risks, creates efficient contracting, and does not entail inefficient non-contracting. Moreover, absent an information gap, TOTs should also be presumed to be fair. The law and economics literature's conclusion, therefore, is that a TOT's efficiency hinges solely on whether consumers are sufficiently informed. The problem, however, is that it is hard to know whether a large enough number of consumers is sufficiently informed. Moreover, even if such an information gap is somehow proven to exist, that by itself, as we demonstrate, does not mean that the TOT is inefficient. Accordingly, the focus on whether consumers

¹¹³ UCC §2-719(3) ("Consequential damages may be limited or excluded unless the limitation or exclusion is unconscionable.").

¹¹⁴ See Farnsworth, *supra* note 102, at 318 (providing examples of statutes prohibiting disclaimers of implied warranties).

¹¹⁵ See Ben-Shahar, *supra* note 70 (describing how legislatures impose duties of disclosure on suppliers, and arguing that those endeavors are useless).

¹¹⁶ See, the Magnuson-Moss Warranty-Federal Trade Commission Improvement Act, 15 U.S.C. §§ 2301-2312 (requiring a supplier who grants a written warranty to designate it as either a "full" or a "limited" warranty).

¹¹⁷ See Mann, *supra* note 57, at 918-9 (arguing that courts that apply the unconscionability doctrine with sufficient vigor "are likely to do a poor job of sorting provisions that make economic sense from those that reflect overreaching.").

¹¹⁸ *Supra* Section I.A.2.

are informed or not, demanded by the law and economics literature, to a large extent leads to a dead end.

We propose a totally different methodology for assessing TOTs that circumvents this problem: When applying the unconscionability doctrine, courts should look not directly at whether an information gap exists, but rather at whether competition in the supplier's market is expected to close the information gap. The virtue of this new methodology is that courts have useful tools to observe the strength of such competition, even when they cannot assess whether there is an information gap.

Moreover, existing literature focusing on the question of whether consumers are informed overlooks the fact that even the proven existence of an information gap is insufficient to justify intervention, because the mere *threat* of competition, in a given case, could incentivize suppliers to adopt only efficient and fair TOTs even when consumers are uninformed. That is, even in markets in which suppliers have not actually exposed each other's TOTs, the mere threat of such competitive actions would deter suppliers from employing TOTs that cause inefficiency or unfairness. On the other hand, in cases where competition over contracts is not strong enough to close the information gap, courts should be suspicious of TOTs and take a closer look at them.

In the next sections, we provide workable guidelines for courts regarding the application of this new methodology.

B. Guidelines for Intervention under the Market-Based Method

In the case of TOTs, competition has the *potential* of closing the information gap between suppliers and consumers. But the question of whether this potential will be realized in a particular case depends on the type of the TOT or the transaction, and most importantly, the characteristics of the supplier's market. Naturally, before exploring the degree of *competition over contracts* (the kind of competition that could close the information gap), the court should examine how intense *competition over price or quality* is. If the supplier is a monopolist, for example, the TOT should be assessed according to the courts' existing methodology.¹¹⁹ The same is true if the supplier operates in a market with only a few firms, and, in addition, the court finds that the market is susceptible to tacit or explicit collusive behavior.¹²⁰ In such a case too, competition cannot be counted upon to close the information gap, since suppliers in such a market lack sufficient

¹¹⁹ See *Rozeboom v. Northwestern Bell Tel. Co.*, 358 N.W.2d 241, 242, 242–45 (S.D. 1984) (striking down a term because the seller was monopolistic).

¹²⁰ In *Henningsen v. Bloomsfield Motors*, 32 N. J. 358, 391 (1960), for example, the New Jersey Supreme Court, in striking down Chrysler's restrictive warranty, emphasized the fact that only three manufacturers, including Chrysler, controlled over 90 percent of the passenger car market. Furthermore, the TOT in question was actually drafted by the "Automobile Manufacturers Association" and hence could have constituted explicit collusion (*id.* at 390); See also Lewis Kornhauser, *Unconscionability in Standard Forms*, 64 CAL. L. REV. 1151, 1169 (1976) (arguing that suppliers in concentrated markets may tacitly collude on terms such as warranty coverage so as to facilitate an anticompetitive price).

incentives to act so as to entice away customers from one another. This preliminary examination of the degree of competition in the supplier's market is similar to the way federal courts deal with antitrust cases.¹²¹

Once the court finds that the supplier is not a monopolist in his market and that the market is not susceptible to collusive behavior, it should examine whether competition over contracts might be blocked in this market due to one or more of the four factors discussed in Part II: backfire, unwanted consumers, externalization of benefits and irresponsible consumers. In this section we propose a set of observable characteristics which courts could look at, and through them determine to what extent the four factors prevent suppliers from revealing TOTs in their rivals' contracts.¹²² As demonstrated, the implementation of these insights provides several counterintuitive results.

If, after taking account of these characteristics, a court finds that competition over contracts is able to close the information gap, it should not intervene against the TOT. If, on the other hand, the court finds that competition over contracts is unable to close the information gap, it should be particularly suspicious of the TOT: We propose that in such a case, the burden of proof be transferred to the supplier to show that the TOT is nevertheless efficient and fair. If this burden is not met, the court should intervene against the TOT under the doctrine of unconscionability.

In what follows, we first consider observable characteristics related to the TOT or the transaction itself that shed light on the expected intensity of competition over contracts. These characteristics concern the *type* of TOT and the *type* of transaction rather than the particular attributes of the parties involved. Then we portray observable characteristics related to the market in which the supplier is operating.

1. The Type of TOT or Transaction

a. Does Exposing the TOT Reveal Information about the Product or Service?

Recall that consumers' backfire on the product occurs only when criticizing the oppressive technique reveals negative information as to the *product or service* sold by the criticizing supplier. Such backfiring does not occur when the criticism reveals negative

¹²¹ See, e.g., *United States v. CBS, Inc.*, 459 F. Supp. 832 (1978) (examining the commercial television markets and its submarkets); *New York v. Kraft Gen. Foods*, 926 F. Supp. 321 (1995) (examining the implications of a merger in the market for breakfast cereals). See also Scherer & Ross, *supra* note 64, at Ch. 7 (discussing the characteristics that make a market prone to tacit collusion); Tirole, *supra* note 41, at Ch. 6 (same); Department of Justice and Federal Trade Commission's 1992 Horizontal Merger Guidelines, *supra* note 98, at section 2.1 (same); The merger guidelines also demonstrate how the market in which the supplier operates needs to be defined. See *id.* at section 1.

¹²² An interesting question is whether competition over contracts could pressure suppliers into giving up on efficient TOTs and not only on inefficient ones. See Todd D. Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96 HARV. L. REV. 1174 (1983) (arguing that the competitive outcome does not reflect consumers' preferences, when they are unable to understand their contracts). Apparently, this could occur only if such competition did not perfectly inform consumers. But even if that could happen, it should not affect courts' decisions when they assess a TOT actually included in a contract.

information only about the criticized *supplier*. To illustrate, in Example 1, where the TOT relieves the supplier from liability for late delivery, exposing the TOT does not involve negative information about TVs or their supply in general, but only negative information about the supplier who employed this TOT. Furthermore, even when criticism about a TOT seems to reveal negative information about the product or service, consumers' backfire on the product is not always triggered. To illustrate, in Example 2 (The Dry Cleaner) if the risk of damage to clothes from dry cleaning is already salient to consumers anyway, or if a competing dry cleaner uses a different technology than Dry Cleaner X in which there is hardly any risk to clothes, the competing dry cleaner would hesitate less to expose Dry Cleaner X's oppressive term. In such cases the information implied by the criticism does not affect the demand for the criticizing supplier's product or service. On the other hand, if harm to clothes is a possibility at any dry cleaner's facility, and consumers are not aware of this possibility, a rival dry cleaner may hesitate to criticize Dry Cleaner X's TOT.

b. Effects of Exposing the TOT on High-cost Consumers

As we have explained, sometimes it is possible to predict which consumers would be the first to leave their supplier if they were to be informed of his TOT. In Example 2 (The Dry Cleaner) the first to leave are consumers whose clothes are expensive. These are typically high cost consumers. Rival dry cleaners might find these consumers unattractive and accordingly might avoid criticizing the TOT in the first place. This is typically the case with many exclusionary clauses, which cap the supplier's liability for harm. The first consumers to leave the supplier when they become informed of the TOT are those who pose the greatest risk of harm.

Another typical example of a TOT the exposing of which could attract high-cost consumers is a TOT dealing with litigation over complications in the contract, such as arbitration, jurisdiction and so forth.¹²³ The first consumers to react to the exposition of such a TOT in their contract are consumers who believe they will be more likely to be involved in litigation with the supplier. These are typically high cost consumers. A similar problem could exist with TOTs that improve the supplier's ability to enforce the consumer's contractual obligations.¹²⁴ When a rival exposes such a TOT, the first consumers who would react and switch to the criticizing supplier are consumers who believe they might not fulfill all of their contractual obligations. Obviously, these are

¹²³ See, e.g., *Italian Colors Rest. v. Am. Express Travel Related Servs. Co.* (In re Am. Express Mierchants' Litig.), 2009 U.S. App. Lexis 1646, 33-34 (2d Cir. N.Y. Jan. 30, 2009) (holding that a class action waiver provision is "incompatible with the federal substantive law of arbitration."); *Matterhorn, Inc. v. NCR Corp.*, 763 F.2d 866 (7th Cir., 1985) (denying a seller's motion to compel arbitration because the buyer did not clearly intend to be bound by arbitration).

¹²⁴ See WHITE & SUMMERS, *supra* note 106, at 163-167 ("Seller may also include a waiver of defense clause, and if the sale is on secured credit, may include a clause that gives the seller a right to repossess if it 'deems itself insecure.'")

unwanted consumers. These insights could justify courts' relatively strict treatment of TOTs dealing with exclusionary clauses, litigation or arbitration, or with suppliers' tools to enforce consumers' obligations,¹²⁵ but for reasons different than those currently given by courts. Courts' justifications for intervention in such cases hinge mainly on "substantive unconscionability" i.e., the TOTs in question seem particularly one-sided, draconian or harsh.¹²⁶ We claim that the justification for intervention here is not the harshness of the TOTs, but rather the fact that such TOTs are unlikely to be competed away, due to rivals' fear of attracting unwanted consumers.¹²⁷

c. Scope of Transactions

When the transaction size is large, consumers are expected to be more responsive to criticism of TOTs. For example, if instead of the TV sets in Example 1, Supplier X's TOT referred to the sale of a car, even consumers who had failed to read Supplier X's fine print might be alert to rivals' ads exposing Supplier X's TOT. Here rivals' incentives to engage in such criticism would be enhanced, because consumers would be more responsive to their efforts.¹²⁸

d. Does the TOT Qualify a Default Rule or a Contractual Benefit?

Our proposed market-based approach explains why a TOT qualifying a default rule (such as an implied warranty) should be treated more strictly than a TOT qualifying a benefit granted by the supplier himself (such as an express warranty). This can be demonstrated through a variation of example 2 (the dry cleaner). Suppose that the dry cleaner offers consumers, in the salient part of his contract, an express warranty covering "any damage to cloths". The TOT in question, in the fine print, qualifies the express warranty and says that "cloths will be covered for damage not exceeding \$50". At first blush, it seems that such a TOT should be treated strictly, since consumers who only read

¹²⁵ *Supra* note 104.

¹²⁶ *See, e.g.* *Haprer v. Ultimo*, 113 Cal. App. 4th 1402, 1410 (2003) ("if an arbitration clause does not achieve 'minimum levels of integrity' it would 'be denied enforcement in any circumstances,' but all the more so where it is in a contract of adhesion... That is, adhesion was not essential to a finding of unconscionability."); *Affholter v. Franklin County Water Dist.*, 2008 U.S. Dist. LEXIS 106254 (2008) (granting defendants' motion to compel arbitration since the arbitration provision was not substantively unconscionable).

¹²⁷ Another example, borrowed from Bebchuk & Posner, *supra* note 29, at 830-1, is a term in a contract between a publisher and authors, according to which the publisher is allowed to publish the book, after the time scheduled for authors' final approval of proofs, even if the authors have failed to meet the deadline for approval. This example demonstrates Bebchuk & Posner's argument that one-sided terms in consumer contracts allow selective enforcement by suppliers, which could be efficient. *Id.* We suggest that if the term is inefficient, competition over contracts among publishers is unlikely to touch upon such a term, since rival publishers understand that the first authors to leave the publisher using the one-sided term would be those who expect to be late in approving their book's proofs.

¹²⁸ *Cf.* Mann, *supra* note 57, at 900 (explaining consumers' inattentiveness to credit transactions by the small size of the transactions).

the salient part of the contract are deceived by the TOT. But if the supplier's market is competitive the conclusion could change, in light of the proposed market-based method. Since the express warranty is offered in the salient part of the contract, it must mean that backfiring on the product and attraction of unwanted customers are relatively weak: Had they been strong, the supplier would not have wanted to highlight the existence of the express warranty. Emphasizing that damage to cloths is covered informs consumers that such damage is possible (possibly causing backfiring on the product) and could attract high cost consumers (who particularly appreciate such a warranty). Hence when such an express warranty exists, these two factors can be presumed to be insignificant. For the same reason, rival suppliers would not be deterred from highlighting the existence of the TOT qualifying the express warranty. They too will not fear from backfiring on the product and attraction of unwanted consumers. The same is true for consumer irresponsiveness: If the supplier makes an effort to make his warranty salient, this must mean that such a warranty is important to consumers. Hence consumers are also expected to be alert to rivals' ads stressing that the warranty is actually qualified. Accordingly, competition over contracts is relatively strong in this case (subject to benefit externalization), and intervention is less justified.

Suppose now that the TOT qualifies an *implied* warranty, set in a default rule, rather than qualifying an express warranty, granted by the supplier himself. In such a case, backfiring on the product, attraction of unwanted consumers and consumer irresponsiveness may well be strong, thereby stifling competition over contracts. Therefore, such a TOT may deserve closer scrutiny than the TOT qualifying the express warranty.¹²⁹

2. Characteristics of the Supplier's Market

a. Number of Suppliers in the Market Not Using the TOT

Suppose Supplier X is a dry cleaner in a certain area of New York City using a TOT like the one in Example 2, capping his liability for damaged clothes. Imagine this TOT is attacked in court. The court could often use the number of other suppliers in the market (all dry cleaners in the above-mentioned area of New York City) not using a similar TOT in order to assess the strength of the *benefit externalization* factor.¹³⁰ If rival suppliers not using a similar TOT are too numerous, a supplier who exposes Supplier X's TOT may fear that the benefits from such exposition would be shared by all suppliers not using the

¹²⁹ The analysis could change in particular circumstances. For example, a computer supplier could have an express warranty for "any damage or loss" and qualify it with a TOT saying that the warranty "does not cover damage due to fire caused by a defect in the computer." Here the express warranty itself could be too general to cause backfiring on the product. Still rivals may hesitate to highlight the existence of the TOT, so as not to inform consumers that defects in computers could cause fire.

¹³⁰ To this end, the court needs to define the relevant market in which Dry Cleaner X operates, i.e., answer the question who are Dry Cleaner X's rivals? This is a task routinely fulfilled by courts in antitrust cases. See *supra* note 121.

TOT: Consumers might leave Supplier X in favor of another supplier not using the TOT, and not necessarily in favor of the criticizing supplier. Suppose, for example, that the TOT is used only by Dry Cleaner X and is not used by five competing dry cleaners. Here benefit externalization is particularly great and the chance that one of Supplier X's five rivals would want to expose X's TOT are slight.

This further implies that benefit externalization is smaller (and hence competition over contracts is stronger) the more suppliers in the market use similar TOTs. This result stands in stark contrast to courts' and scholars' conventional premise, according to which if many or all suppliers in a market use an oppressive term, it has greater chances of being stricken down.¹³¹ The analysis above shows that the contrary may be true: If most suppliers use a similar TOT, and the market is competitive in other respects,¹³² benefit externalization is small, and competition over contracts may well be strong. In such a market, had the TOT been inefficient or unfair, any of the suppliers, and especially those not using the TOT, may well have had a strong incentive to expose it (subject to the other three factors that may hinder such incentives), since the benefits from such an exposition would not be externalized. This could support a conclusion that the TOT is actually efficient and fair, notwithstanding its harsh appearance.

Conversely, courts often treat a supplier's TOT leniently when the consumer is shown to have a choice of rival suppliers who do not use a similar TOT.¹³³ But again, the

¹³¹ See, e.g., *Weaver v. American Oil Co.*, 276 N.E.2d 144, 147 (Ind. 1971) (quoting *United States v. Bethlehem Steel Corp.*, 315 U.S. 289, 326 (Frankfurter, J. dissenting)) ("The weaker party, in need of the goods or services, is frequently not in a position to shop around for better terms, either because the author of the standard contract has a monopoly or because all competitors use the same clauses."); *Lloyd v. Service Corp. of Ala.*, 453 So.2d 735, 739 (Ala. 1984) (same); *Taylor v. Leedy and Co.*, 412 So. 2d 763, 766 (Ala. 1982) (striking down an exculpatory clause in a lease because "almost all leases contain these exculpatory clauses."); See also Friedrich Kessler, *Contracts of Adhesion—Some Thoughts About Freedom of Contract*, 43 COLUM. L. REV. 629, 632 (1943) ("The weaker party, in need of goods and services, is frequently not in a position to shop around for better terms ... because all competitors used the same clauses."); ; Julian S. Lim, Comment: *Tongue-Tied in the Market: The Relevance of Contract Law to Racial-Language Minorities*, 91 CALIF. L. REV. 579, 616 (2003) (same); John P. Little, Note: *Managed Care Contracts of Adhesion: Terminating The Doctor-Patient Relationship And Endangering Patient Health*, 49 RUTGERS L. REV. 1397 (1997) ("While MCOs compete with each other on price and benefits, most MCOs employ standard form contracts with remarkably similar terms.")

¹³² If there are only a few suppliers in the market, and it is prone to collusive behavior (*supra* notes 120-121 and accompanying text) courts should be mindful of the concern that all or most suppliers in a market use a similar TOT because suppliers are tacitly or expressly colluding. This was probably the case in *Henningsen*, 32 N. J. at 391, where the market was extremely concentrated and the TOT had been dictated by an association comprised of the suppliers (see *supra* note 120).

¹³³ See, e.g., *Dean Witter Reynolds v. Superior Court*, 211 Cal. App. 3d 758 (Cal. Ct. App. 1989) ("... the 'oppression' factor of the procedural element of unconscionability may be defeated, if the complaining party has a meaningful choice of reasonably available alternative sources of supply from which to obtain the desired goods and services free of the terms claimed to be unconscionable."); *Bradberry v. T-Mobile USA, Inc.*, 2007 WL 1241936 (N.D. Cal. Apr. 27, 2007) (where the court implied that had the defendant brought evidence "regarding the availability of alternative sources of cellular phone service without the allegedly unconscionable terms" it might have prevailed); *Pack v. Damon Corp.*, 320 F. Supp. 2d 545, 556 (E.D. Mich. 2004) (finding no procedural unconscionability in an arbitration clause because the "[p]laintiff

preceding analysis shows that this sort of reasoning is flawed: the more numerous are the supplier's rivals who do not use the TOT, the less likely is the TOT to be competed away, and the more suspicious courts should be toward it. In such cases, rivals will be less likely to expose the supplier's TOT, because they will fear that the benefits from such an exposition will be externalized to the other suppliers not using the oppressive term.

To be sure, if *all* suppliers in the market use the TOT, or similar TOTs, although benefit externalization does not exist, all such suppliers would fear *consumer backfiring on the contract*: They might hesitate to expose rivals' TOTs so as not to have to stop using their own TOTs. Therefore, the ideal market in this respect is one in which *almost all* suppliers use the TOT (or similar practices). In such a case, the few suppliers not using the TOT, or similar TOTs, are not exposed to consumer backfiring on the contract (since they are not using such TOTs to begin with) *and* benefit externalization remains particularly small (since the number of rivals not using such TOTs is small).

b. The Existence of Sales Representatives in Contact with Consumers

The analysis of Part II reveals that when Supplier X's rivals employ sales representatives, who are in direct contact with consumers, these rivals are more likely to expose Supplier X's TOTs. Suppose again that Supplier X is the dry cleaner employing the TOT from Example 2. Assume Dry Cleaner X has a rival, Dry Cleaner Y. Dry Cleaner Y's employees, operating Y's facility, are in direct contact with customers. They could use this direct contact to highlight the existence of Dry Cleaner X's TOT.

Such direct interaction could help overcome consumer irresponsiveness and could mitigate the fear of rivals' backfiring. It could alleviate consumers' irresponsiveness because consumers present at Y's facility are more alert to the direct messages conveyed to them by Y's employees and agents. Direct contact also relieves some of Y's fear of retaliation from Supplier X because, unlike criticism made via public advertising, Supplier X need not know that Supplier Y's employees have criticized him in this manner.

Conversely, if Supplier X's rivals do not have such direct contact with consumers, they are less likely to expose Supplier X's TOT. Suppose, for example, that Supplier X, like his rivals, sell electronic products over the Internet.¹³⁴ Absent direct contact between Supplier X's rivals and consumers, consumer irresponsiveness and the fear of Supplier X's retaliation may, in certain cases, deter X's rivals from criticizing his contracts.¹³⁵

has not shown that [defendant] was his only source for buying a new motor home, or that other potential sources required submitting disputes to arbitration").

¹³⁴ See Hillman, *supra* note 107, at 840-2 (explaining that on-line consumers tend not to read their contracts, because negotiation is impossible).

¹³⁵ While the absence of sales representatives does not necessarily imply that consumers are irresponsive, it demands that the question of consumers' responsiveness be further examined.

c. Is the Product or Service Essential to Consumers?

Suppose the product or service sold by the supplier using the TOT is essential to consumers, such as a drug that cures a certain illness, but the supplier's market is nevertheless competitive. For example, there are several other suppliers who sell drugs that cure the same illness. How should courts treat a TOT exempting a supplier from liability for the drug's side effects? Courts treat such TOTs with particular suspicion, and often strike them down as unconscionable.¹³⁶

In contrast, our analysis reveals that such TOTs are actually less susceptible to "backfiring on the product" and in this sense are more exposed to competition over contracts. The reason is that when a product or service is essential to consumers they would not easily give up purchasing it. As a result, rival suppliers of such products or services would not hesitate to criticize a supplier using such a TOT (subject to the other factors that could hinder competition over contracts). These rival suppliers know that even if their criticism would reveal unpleasant information about the product or service, consumers would still buy it. In the above-mentioned drug example, rival suppliers would not hesitate to highlight that their rival exempts itself, in the fine print from liability for the drug's side effects. If the drug is essential to consumers, demand for the drug would not substantially go down, in spite of consumers becoming aware of its side effects. Therefore, under our approach, with essential products or services (sold by a competitive industry) courts should actually count more on competition over contracts, and intervene less, than with other products and services in which there is a threat of backfiring on the product..

d. Alternative Parties Likely to Expose the TOT

As noted, at times the exposition of a supplier's inefficient or unfair TOT could come from parties other than the supplier's rivals, such as consumer organizations or websites.¹³⁷ Such parties could play a role similar to that of competition over contracts in deterring suppliers from placing inefficient or unfair TOTs in their fine print. Note that this deterrent effect is not subject to backfiring, attraction of unwanted consumers or benefit externalization. These are factors that restrain only *rivals'* criticism of the supplier's TOT and not criticism by objective parties from outside the supplier's market.

Accordingly, if the court finds that in the supplier's market, oppressive terms in consumer contracts are subject to close scrutiny by reliable parties, whose interests

¹³⁶ See, e.g., *Tunkl v. Regents of Univ. of Cal.*, 383 P.2d 441, 445-46 (Cal. 1963) ("As a result of the essential nature of [medical services], in the economic setting of the transaction, the party invoking exculpation possesses a decisive advantage of bargaining strength against any member of the public who seeks his services."); *Ransburg D/B/A Twin Lakes Apartments v. Richards*, 770 N.E.2d 393 (Ct. App. Indiana, 5th Dist., 2002) (striking down an exculpatory clause due to the essential nature of the service); *Crawford v. Buckner*, 839 S.W.2d 754 (Tenn. 1992) (same).

¹³⁷ *Supra* note 70 and accompanying text.

coincide with those of consumers, and in addition many consumers are likely to become informed by such parties, court intervention is unnecessary.

The above-mentioned guidelines for courts are summarized in the following table.

TABLE 2: GUIDELINES FOR COURTS

<i>Prima Facie Case for Intervention</i>	<i>No Intervention</i>
Criticizing TOT provides negative information about the product/service (consumers' backfiring on product)	Criticizing TOT provides negative information about the supplier (no consumers' backfiring on product)
Criticizing TOT attracts high-cost consumers (unwanted consumers)	Criticizing TOT attracts low-cost or average consumers (wanted consumers)
Small transactions (irresponsive consumers)	Large transactions (responsive consumers)
TOT qualifies a default rule (backfiring on the product, attraction of unwanted consumers, and consumer irresponsiveness could be strong)	TOT qualifies an express benefit granted by the supplier (backfiring on the product, attraction of unwanted consumers, and consumer irresponsiveness usually weak)
Few suppliers use similar TOTs (benefit externalization)	Almost all suppliers use similar TOTs (most benefits internalized and no concern of backfire on the contract)
No sales representatives (rivals' backfiring, risk of irresponsive consumers)	Sales representatives exist (less rivals' backfiring, consumers more responsive)
Product is inessential (backfiring on the product possible)	Product is essential (no backfiring on the product)
No alternative parties likely to expose the TOT (no alternative to competition over contracts)	Alternative parties likely to expose the TOT (an alternative to competition over contracts)

To finalize our guidelines, it should be noted that our market-based approach could also be employed *ex ante*, rather than *ex post*.¹³⁸ That is, an agency could decide *ex ante* whether a standard consumer contract was efficient according to our proposed guidelines, and once the agency decided affirmatively, the contract would be immune from courts' scrutiny for a certain period of time. There are several advantages to *ex ante* scrutiny. First, it would save litigation costs, since the contract would be litigated only once, while with *ex post* intervention litigation reoccurs whenever consumers sue the supplier. Second a specialized agency conducting *ex ante* scrutiny would likely be more apt and skillful than courts in applying the market-based guidelines we propose. Finally, *ex ante* scrutiny would promote certainty: once a contract was approved by the agency, the supplier could be confident that none of his contract's clauses would be struck down.

¹³⁸ Cf. Shmuel I. Becher, *Asymmetric Information in Consumer Contracts: The Challenge That Is Yet to Be Met*, 45 AM. BUS. L.J. 723 (2008). (arguing for *ex ante* scrutiny of consumer contracts).

CONCLUSION

The Article presents four oppressive techniques which suppliers often use in their standard-form contracts to extract value from uninformed consumers: TOTs, SOTs, SBTs and complexity. Only the first technique is closely scrutinized by courts. Ironically, courts' attention is much more needed with respect to the other three techniques, which are currently ignored by them, since these techniques are expected to survive even fierce competition among suppliers. Especially two of these practices – SOTs and complexity – could lead to substantial social harm if not closely scrutinized.

TOTs, on the other hand, are potentially affected by competition. The type of competition that affects TOTs is competition over contracts, rather than over price or quality. When competition over contracts exists it has the potential to close the information gap between suppliers and consumers, thereby securing efficient and fair contracts. Furthermore, even a threat of such competition would suffice in order to assure the efficiency and fairness of suppliers' contracts.

Accordingly, we suggest the application of a market-based approach to TOTs in consumer contracts, instead of scrutinizing them on the basis of the discrete transaction and its particular characteristics, as courts currently do. According to the market-based approach, TOTs should be assessed in light of the intensity of competition over contracts in the supplier's market. The Article reveals the observable characteristics of the supplier's market, and of the type of TOT or transaction, which determine the viability of competition over contracts in this market. When competition over contracts is shown to be able to close the information gap, intervention against the TOT is unwarranted. When competition over contracts cannot be counted upon to inform consumers, the burden should be transferred to the supplier to show that her TOT is nevertheless efficient and fair, as otherwise the TOT will be struck down.

This Article thus presents a third phase in courts' attitudes toward consumer contracts. In the first phase, consumer contracts were considered by courts as ordinary contracts, requiring no special treatment. In the second phase, courts became suspicious of consumer contracts and developed several tools for handling them, focusing on the particular characteristics of the transaction. In this Article, we suggest that it is time to introduce a third phase: Rather than examining each consumer contract in isolation, courts need to acknowledge that consumer contracts are a market-phenomenon which calls for a market-based approach.

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