Chapter 19. Unconscionability

19.0. Introduction

Consider for a moment what might justify using the coercive power of the state to enforce private promises. From a moral perspective, we might think that choosing to make a promise creates a duty to perform. Imagine that Cheryl promises Albert that she will prepare his tax return in exchange for $200. The promisor Cheryl exercises her autonomy to establish a new relationship in which the promisee Albert can rely on her promise and adjust his plans accordingly. We show respect for the autonomy of both parties by enforcing the promise. Enforcement enables Cheryl to bind herself to perform if she chooses to do so. At the same time, enforcement respects Albert's autonomy by protecting his reliance on Cheryl's promise.

An alternative economic or "instrumental" approach to enforcement also focuses on the parties' choices and reliance. From an economic perspective, one goal of promise making is mutually beneficial trade. People make promises to enable others to rely. Promises also allow parties to trade risks. Thus, Cheryl assumes the risk that the market price for tax preparation will rise or that she will find it inconvenient or difficult to fulfill her promise to complete Albert's tax return by the filing deadline. At the same time, Albert accepts the risk that someone else will offer to do his taxes for less or that he would prefer to prepare the return himself. Each party faces a different bundle of risks than he or she did before making or receiving the promise. On this account, the purpose of promissory enforcement is to maximize the social benefits that flow from these exchanges of risk.

Both justifications for enforcement have in common the assumption that parties make promises and enter into bargains voluntarily. It follows that if Cheryl holds

a gun to Albert's head and forces him to contract for her services, then Albert should be free to disavow the deal and use H&R Block instead. More difficult and subtle questions arise when a promisor claims that she lacked essential information about the terms of a bargain or that she was for some other reason unable to exercise a meaningful choice. Even more controversial are claims that the terms of the deal are so unfavorable that a court should simply refuse to enforce them.

19.1. Uniform Commercial Code Unconscionability Provisions

The Uniform Commercial Code empowers a court to refuse to enforce unconscionable contracts in the following terms:

> § 2-302. Unconscionable Contract or Clause
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> (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.
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> (2) When it is claimed or appears to the court that the contract or any clause thereof may be unconscionable the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose and effect to aid the court in making the determination.
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> Official Comment
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> 1. This section is intended to make it possible for the courts to police explicitly against the contracts or clauses which they find to be unconscionable. In the past such policing has been accomplished by adverse construction of language, by manipulation of the rules of offer and acceptance or by determinations that the clause is contrary to public policy or to the dominant purpose of the contract. This section is intended to allow the court to pass directly on the unconscionability of the contract or particular clause therein and to make a conclusion of law as to its unconscionability. The basic test is whether, in light of the general commercial background and the commercial needs of the particular trade or case, the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract. Subsection (2) makes it clear that it

is proper for the court to hear evidence on these questions. The principle is one of the prevention of oppression and unfair surprise. (Cf. Campbell Soup Co. v. Wentz, 172 F.2d 80, 3d Cir. 1948) and not of disturbance of allocation of risks because of superior bargaining power.

19.2.1. Case: *Williams v. Walker-Thomas Furniture I*

Williams v. Walker-Thomas Furniture Co. I

District of Columbia Court of Appeals
1964

198 A.2d 914

QUINN, Associate Judge:

[1] Appellant, a person of limited education separated from her husband, is maintaining herself and her seven children by means of public assistance. During the period 1957-1962 she had a continuous course of dealings with appellee from which she purchased many household articles on the installment plan. These included sheets, curtains, rugs, chairs, a chest of drawers, beds, mattresses, a washing machine, and a stereo set. In 1963 appellee filed a complaint in replevin for possession of all the items purchased by appellant, alleging that her payments were in default and that it retained title to the goods according to the sales contracts. By the writ of replevin appellee obtained a bed, chest of drawers, washing machine, and the stereo set. After hearing testimony and examining the contracts, the trial court entered judgment for appellee.

[2] Appellant's principal contentions on appeal are (1) there was a lack of meeting of the minds, and (2) the contracts were against public policy.

[3] Appellant signed fourteen contracts in all. They were approximately six inches in length and each contained a long paragraph in extremely fine print. One of the sentences in this paragraph provided that payments, after the first purchase, were to be prorated on all purchases then outstanding. Mathematically, this had the effect of keeping a balance due on all items until the time balance was completely eliminated. It meant that title to the first purchase, remained in appellee until the fourteenth purchase, made some five years later, was fully paid.

[4] At trial appellant testified that she understood the agreements to mean that when payments on the running account were sufficient to balance the amount due on an individual item, the item became hers. She testified that most of the purchases were made at her home; that the contracts were signed in blank; that she did not read the instruments; and that she was not provided with a copy. She admitted, however, that she did not ask anyone to read or explain the contracts to her.

[5] We have stated that "one who refrains from reading a contract and in conscious ignorance of its terms voluntarily assents thereto will not be relieved from his bad bargain." *Bob Wilson, Inc. v. Swann*, D.C.Mun.App., 168 A.2d 198, 199 (1961). "One who signs a contract has a duty to read it and is obligated according to its terms." *Hollywood Credit Clothing Co. v. Gibson*, D.C.App., 188 A.2d 348, 349 (1963). "It is as much the duty of a person who cannot read the language in which a contract is written to have someone read it to him before he signs it, as it is the duty of one who can read to peruse it himself before signing it." Stern v. Moneyweight Scale Co., 42 App.D.C. 162, 165 (1914).

[6] A careful review of the record shows that appellant's assent was not obtained "by fraud or even misrepresentation falling short of fraud." *Hollywood Credit Clothing Co. v. Gibson, supra*. This is not a case of mutual misunderstanding but a unilateral mistake. Under these circumstances, appellant's first contention is without merit.

[7] Appellant's second argument presents a more serious question. The record reveals that prior to the last purchase appellant had reduced the balance in her account to $164. The last purchase, a stereo set, raised the balance due to $678. Significantly, at the time of this and the preceding purchases, appellee was aware of appellant's financial position. The reverse side of the stereo contract listed the name of appellant's social worker and her $218 monthly stipend from the government. Nevertheless, with full knowledge that appellant had to feed, clothe and support both herself and seven children on this amount, appellee sold her a $514 stereo set.

[8] We cannot condemn too strongly appellee's conduct. It raises serious questions of sharp practice and irresponsible business dealings. A review of the legislation in the District of Columbia affecting retail sales and the pertinent decisions of the highest court in this jurisdiction disclose, however, no ground upon which this court can declare the contracts in question contrary to public policy. We note that were the Maryland Retail Installment Sales Act, Art. 83 §§ 128-153, or its equivalent, in force in the District of Columbia, we could grant appellant appropriate relief. We think Congress

should consider corrective legislation to protect the public from such exploitive contracts as were utilized in the case at bar.

19.2.2. Case: *Williams v. Walker-Thomas Furniture II*

Williams v. Walker-Thomas Furniture Co. II

United States Court of Appeals, District of Columbia Circuit
1965

121 U.S. App. D.C. 315, 350 F.2d 445 [Note: Some footnotes were eliminated without notation; others were put in the above-the-line text as surrounded by ᵕᵕ symbols. – EEJ, ed.]

J. SKELLY WRIGHT, Circuit Judge:

[1] Appellee, Walker-Thomas Furniture Company, operates a retail furniture store in the District of Columbia. During the period from 1957 to 1962 each appellant in these cases purchased a number of household items from Walker-Thomas, for which payment was to be made in installments. The terms of each purchase were contained in a printed form contract which set forth the value of the purchased item and purported to lease the item to appellant for a stipulated monthly rent payment. The contract then provided, in substance, that title would remain in Walker-Thomas until the total of all the monthly payments made equaled the stated value of the item, at which time appellants could take title. In the event of a default in the payment of any monthly installment, Walker-Thomas could repossess the item.

[2] The contract further provided that "the amount of each periodical installment payment to be made by (purchaser) to the Company under this present lease shall be inclusive of and not in addition to the amount of each installment payment to be made by (purchaser) under such prior leases, bills or accounts; and all payments now and hereafter made by (purchaser) shall be credited pro rata on all outstanding leases, bills and accounts due the Company by (purchaser) at the time each such payment is made." The effect of this rather obscure provision was to keep a balance due on every item purchased until the balance due on all items, whenever purchased, was liquidated. As a result, the debt incurred at the time of purchase of each item was secured by the right to repossess all the items previously purchased by the same purchaser, and each new item purchased automatically became subject to a security interest arising out of the previous dealings.

[3] On May 12, 1962, appellant Thorne purchased an item described as a Daveno, three tables, and two lamps, having total stated value of $391.10. Shortly thereafter, he defaulted on his monthly payments and appellee sought to replevy all the items purchased since the first transaction in 1958. Similarly, on April 17, 1962, appellant Williams bought a stereo set of stated value of $514.95. [5]At the time of this purchase her account showed a balance of $164 still owing from her prior purchases. The total of all the purchases made over the years in question came to $1,800. The total payments amounted to $1,400.[6] She too defaulted shortly thereafter, and appellee sought to replevy all the items purchased since December, 1957. The Court of General Sessions granted judgment for appellee. The District of Columbia Court of Appeals affirmed, and we granted appellants' motion for leave to appeal to this court.

[4] Appellants' principal contention, rejected by both the trial and the appellate courts below, is that these contracts, or at least some of them, are unconscionable and, hence, not enforceable. In its opinion in *Williams v. Walker-Thomas Furniture Company*, 198 A.2d 914, 916 (1964), the District of Columbia Court of Appeals explained its rejection of this contention as follows:

> Appellant's second argument presents a more serious question. The record reveals that prior to the last purchase appellant had reduced the balance in her account to $164. The last purchase, a stereo set, raised the balance due to $678. Significantly, at the time of this and the preceding purchases, appellee was aware of appellant's financial position. The reverse side of the stereo contract listed the name of appellant's social worker and her $218 monthly stipend from the government. Nevertheless, with full knowledge that appellant had to feed, clothe and support both herself and seven children on this amount, appellee sold her a $514 stereo set.
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> We cannot condemn too strongly appellee's conduct. It raises serious questions of sharp practice and irresponsible business dealings. A review of the legislation in the District of Columbia affecting retail sales and the pertinent decisions of the highest court in this jurisdiction disclose, however, no ground upon which this court can declare the contracts in question contrary to public policy. We note that were the Maryland Retail Installment Sales Act, Art. 83 §§ 128-153, or its equivalent, in force in the District of Columbia, we could grant appellant appropriate relief. We think Congress should consider corrective legislation to protect the public from such exploitive contracts as were utilized in the case at bar.

[5] We do not agree that the court lacked the power to refuse enforcement to contracts found to be unconscionable. In other jurisdictions, it has been held as a matter of common law that unconscionable contracts are not enforceable. While no decision of this court so holding has been found, the notion that an unconscionable bargain should not be given full enforcement is by no means novel. In *Scott v. United States*, 79 U.S. (12 Wall.) 443, 445 (1870), the Supreme Court stated:

> …If a contract be unreasonable and unconscionable, but not void for fraud, a court of law will give to the party who sues for its breach damages, not according to its letter, but only such as he is equitably entitled to….

Since we have never adopted or rejected such a rule, the question here presented is actually one of first impression.

[6] Congress has recently enacted the Uniform Commercial Code, which specifically provides that the court may refuse to enforce a contract which it finds to be unconscionable at the time it was made. 28 D.C.CODE § 2-302 (Supp. IV 1965). The enactment of this section, which occurred subsequent to the contracts here in suit, does not mean that the common law of the District of Columbia was otherwise at the time of enactment, nor does it preclude the court from adopting a similar rule in the exercise of its powers to develop the common law for the District of Columbia. In fact, in view of the absence of prior authority on the point, we consider the congressional adoption of § 2-302 persuasive authority for following the rationale of the cases from which the section is explicitly derived. Accordingly, we hold that where the element of unconscionability is present at the time a contract is made, the contract should not be enforced.

[7] 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. Whether a meaningful choice is present in a particular case can only be determined by consideration of all the circumstances surrounding the transaction. In many cases the meaningfulness of the choice is negated by a gross inequality of bargaining power. ⮑See *Henningsen v. Bloomfield Motors, Inc.*, *supra* Note 2, 161 A.2d at 86,, and authorities there cited. Inquiry into the relative bargaining power of the two parties is not an inquiry wholly divorced from the general question of unconscionability, since a one-sided bargain is itself evidence of the inequality of the bargaining parties. This fact was vaguely recognized in the common law doctrine of intrinsic fraud, that is, fraud which can be presumed from the grossly unfair nature of the terms of the contract. See the

oft-quoted statement of Lord Hardwicke in Earl of Chesterfield v. Janssen, 28 Eng. Rep. 82, 100 (1751): "…(Fraud) may be apparent from the intrinsic nature and subject of the bargain itself; such as no man in his senses and not under delusion would make...." And *cf. Hume v. United States, supra* Note 3, 132 U.S. at 413, where the Court characterized the English cases as 'cases in which one party took advantage of the other's ignorance of arithmetic to impose upon him, and the fraud was apparent from the face of the contracts.' See also *Greer v. Tweed, supra* Note 3.↵ The manner in which the contract was entered is also relevant to this consideration. Did each party to the contract, considering his obvious education or lack of it, have a reasonable opportunity to understand the terms of the contract, or were the important terms hidden in a maze of fine print and minimized by deceptive sales practices? Ordinarily, one who signs an agreement without full knowledge of its terms might be held to assume the risk that he has entered a one-sided bargain. ↳See RESTATEMENT, CONTRACTS § 70 (1932); Note, 63 HARV. L. REV. 494 (1950). See also *Daley v. People's Building, Loan & Savings Ass'n*, 178 Mass. 13, 59 N.E. 452, 453 (1901), in which Mr. Justice Holmes, while sitting on the Supreme Judicial Court of Massachusetts, made this observation: "…Courts are less and less disposed to interfere with parties making such contracts as they choose, so long as they interfere with no one's welfare but their own….It will be understood that we are speaking of parties standing in an equal position where neither has any oppressive advantage or power…."↵ But when a party of little bargaining power, and hence little real choice, signs a commercially unreasonable contract with little or no knowledge of its terms, it is hardly likely that his consent, or even an objective manifestation of his consent, was ever given to all the terms. In such a case the usual rule that the terms of the agreement are not to be questioned should be abandoned and the court should consider whether the terms of the contract are so unfair that enforcement should be withheld.

[8] In determining reasonableness or fairness, the primary concern must be with the terms of the contract considered in light of the circumstances existing when the contract was made. The test is not simple, nor can it be mechanically applied. The terms are to be considered "in the light of the general commercial background and the commercial needs of the particular trade or case." ↳Comment, Uniform Commercial Code § 2-307.↵ Corbin suggests the test as being whether the terms are 'so extreme as to appear unconscionable according to the mores and business practices of the time and place." We think this formulation correctly states the test to be applied in those cases where no meaningful choice was exercised upon entering the contract.

[9] Because the trial court and the appellate court did not feel that enforcement could be refused, no findings were made on the possible unconscionability of the contracts in these cases. Since the record is not sufficient for our deciding the issue as a matter of law, the cases must be remanded to the trial court for further proceedings.

So ordered.

DANAHER, Circuit Judge (dissenting):

[10] The District of Columbia Court of Appeals obviously was as unhappy about the situation here presented as any of us can possibly be. Its opinion in the Williams case, quoted in the majority text, concludes: "We think Congress should consider corrective legislation to protect the public from such exploitive contracts as were utilized in the case at bar."

[11] My view is thus summed up by an able court which made no finding that there had actually been sharp practice. Rather the appellant seems to have known precisely where she stood.

[12] There are many aspects of public policy here involved. What is a luxury to some may seem an outright necessity to others. Is public oversight to be required of the expenditures of relief funds? A washing machine, e.g., in the hands of a relief client might become a fruitful source of income. Many relief clients may well need credit, and certain business establishments will take long chances on the sale of items, expecting their pricing policies will afford a degree of protection commensurate with the risk. Perhaps a remedy when necessary will be found within the provisions of the "Loan Shark" law, D.C.Code §§ 26-601 et seq. (1961).

[13] I mention such matters only to emphasize the desirability of a cautious approach to any such problem, particularly since the law for so long has allowed parties such great latitude in making their own contracts. I dare say there must annually be thousands upon thousands of installment credit transactions in this jurisdiction, and one can only speculate as to the effect the decision in these cases will have.13

[14] I join the District of Columbia Court of Appeals in its disposition of the issues.

19.3. Procedural and Substantive Unconscionability

Both judges and scholars ordinarily draw a distinction between "substantive" and "procedural" unconscionability. ***Substantive unconscionability*** focuses on

the contract terms themselves. This branch of the doctrine asks whether the terms of the agreement are so unfavorable to one of the parties that we should refuse enforcement. In this vein, courts may find that a manufacturer's clause limiting remedies for breach is contrary to the "essence of the bargain" or that a price or warranty term in a consumer contract is "unreasonable."

In contrast, ***procedural unconscionability*** focuses on the circumstances surrounding contract formation. Was there something about that process that prevented one party from understanding the agreement? Most courts consider a wide range of "factors related to the bargaining power of each party, including age, education, intelligence, business acumen, experience in similar transactions, whether the terms were explained to the weaker party, who drafted the contract, whether alterations in the printed terms were possible, and whether the party claiming unconscionability was represented by counsel at the time the contract was executed." *Roe v. Rent-A-Center, Inc.*, CA2007-09-224 (Ohio App. 2008). For example, a court might find an agreement procedurally unconscionable because a company's sales practices tended to obscure the true nature of the contract.

Each strand of unconscionability doctrine stands in some tension with other contract doctrines that favor the enforcement of all voluntary bargains. Thus, the "duty to read" doctrine holds that a person who signs a contract without reading it will be bound despite his lack of knowledge of its terms. Courts have even refused to excuse illiterate and non-English-speaking promisors, explaining that they should have asked someone to read and explain the agreement before signing it. See, e.g. *Morales v. Sun Constructors, Inc.*, No. 07-3806 (3d Cir. 2008); *Upton v. Tribilcock*, 91 U.S. 45 (1875). As we saw in *Williams I* and *Williams II*, a procedural unconscionability claim must first overcome judicial reluctance to depart from the strict "duty to read" precedents.

Similarly, arguments about substantive unconscionability conflict with the general contractual principle that courts should let the parties' judge for themselves whether to accept a particular bargain. For example, courts do not scrutinize the adequacy of consideration. Each party is free to make a good bargain or a bad bargain, and judges ordinarily respect the private ordering these agreements seek to create. Finding a contract substantively unconscionable rejects the parties' bargain and prevents them from forming an enforceable agreement on those terms. Perhaps as a result of this fundamental tension, judicial decisions hardly ever invalidate an agreement solely on grounds of substantive unconscionability. And many jurisdictions formally require courts to find an agreement both procedurally and substantively unconscionable before refusing to enforce it. See, e.g., *Roe v. Rent-A-Center, Inc.*, CA2007-09-224 (Ohio App. 2008).

19.4. Rent-to-Own Industry and Consumer Protection Laws

In *Williams I*, the court concluded its opinion by calling attention to questionable practices in the rent-to-own industry. Walker-Thomas's conduct evidently raised "serious questions of sharp practice and irresponsible business dealings." The court also issued a plea for "corrective legislation" along the lines of provisions contained in the Maryland Retail Installment Sales Act.

Some years later, The Wall Street Journal published a highly critical feature story on the rent-to-own industry. In extensive interviews, former Rent-A-Center managers described high-pressure sales tactics, misleading pricing practices, and coercive methods of repossessing goods from defaulting renters. Repo calls sometimes included demands for "couch payments" – sexual favors extorted in lieu of cash. However, the article also revealed that many renters could not afford to buy the items and had "nowhere else to go." See Alix Freedman, *Peddling Dreams: A Marketing Giant Uses Its Sales Prowess to Profit on Poverty*, THE WALL STREET JOURNAL A1 (Sept. 22, 1993).

More recently the industry has fought off efforts to enact legislation classifying rent-to-own transactions as credit sales. The typical "rental" agreement provides for total payments several times the normal retail value of the goods, and thus an implied annual interest rate of 200-300 percent. Redefining these deals as credit transactions would make state usury laws applicable and prohibit firms from charging such a high implicit interest rate. The industry argues, however, that rent to own customers assume no debt and always have an option to return the goods with no further obligation. Moreover, a 1999 Federal Trade Commission customer survey found that most are satisfied with their rent-to-own transactions. See John Seward, *Tales of the Tape: Rent-To-Owns Seek Definition in Law*, DOW JONES NEWSWIRES (Oct. 17, 2003).

In one respect at least, the *Williams I* court's wish was fulfilled. The District of Columbia Code now contains a provision prohibiting the sort of pro-rata payment arrangement contained in Walker-Thomas Furniture Company's contract. See D.C. Code § 28-3805. Under the statute, payments must be credited towards the first item purchased until that item has been paid off and the seller's security interest in that item is then extinguished.

19.5. Discussion of Unconscionability

Why does the D.C. Court of Appeals (reluctantly) decide, in *Williams I*, to enforce the pro-rata payment clause in the Walker-Thomas Furniture Company's form contract?

The D.C. Circuit reaches a decidedly different decision about the prevailing legal rule. Does that court hold that the pro-rata-payment clause is unconscionable? If not, then what doctrinal standard will determine whether the clause is unconscionable?

Judge Wright talks extensively about unequal bargaining power. What do you suppose he means by that term?

Consider the following language from the Uniform Commercial Code provision concerning unconscionability: "The principle is one of the prevention of unfair surprise and not of disturbance of risks because of superior bargaining power." U.C.C. § 2-302 Comment 1. Can you reconcile this comment with Judge Wright's discussion of bargaining power in *Williams II*?

The prospective effects of procedural and substantive unconscionability are likely to differ. How would you expect sellers to respond to a ruling that the Walker-Thomas Furniture Company's form contract is procedurally unconscionable? Suppose that a court instead holds that pro-rata-payment clauses and cross-collateral clauses are substantively unconscionable. Will people in Ms. Williams's circumstances be able to obtain furniture on the same payment plan?

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