

January 10, 2018

Council Members  
American Law Institute  
4025 Chestnut Street  
Philadelphia, PA 19104-3099

Re: Council Draft No. 4 of the Restatement of Consumer Contracts (Dec. 18, 2017)

Dear Members of the ALI Council:

We understand that the American Law Institute is engaged in a project to draft a Restatement of Consumer Contracts. As we understand it, the goal of any ALI Restatement is to adopt a clear formulation of the common law as it presently stands or might appropriately be stated by a court. Restatements are intended to be respectful of precedent and to weigh the competing views of courts that have addressed the issues.

We are writing to express our deep concerns regarding the current Council Draft of this proposed Restatement. If followed by courts, it would tilt the marketplace dramatically toward businesses at the expense of consumers. Instead of respecting precedent, it undermines the well-accepted factors that courts and legislatures have developed to determine whether contract terms are procedurally unconscionable, and replaces them with a theory spun out in a law review article that cites not a single judicial decision in its support.

We write as organizations that work to protect consumers from unfairness in the marketplace every day. We have a keen on-the-ground feel for how some businesses treat consumers fairly and reasonably and how other businesses do not. We are also painfully aware of the dearth of legal resources available to consumers to defend themselves from mistreatment by businesses. The combined legal resources available to assist consumers are very limited and are able to help very few people.

We have a number of concerns about the assent, addition of new terms, and modification of terms provisions (Sections 2-4).<sup>1</sup> These sections take an extremely loose view of the terms to which the consumer has agreed. Moreover, the Draft would allow a business to insert new terms after the fact as long as the consumer was told beforehand that it might do so, and the consumer has an opportunity to review the new terms and either continue under the existing terms or terminate the contract. Notably, the consumer is *not* given the same right to impose new terms upon the business.

The Draft justifies these lenient standards for courts to construct consumer assent on the ground that the doctrines of unconscionability and deception will act as a counterbalance to predatory terms, abuse, and overreaching by businesses. The entire premise of this proposed Restatement is that the unconscionability and deception doctrines are essential to “police” the

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<sup>1</sup> See Council Draft No. 4, at 4-5 (describing the rationale for the permissive assent provisions).

market in light of the permissive assent rules found throughout.<sup>2</sup> However, Sections 5 and 6 of the Draft undermine rather than strengthen these doctrines.

There are four primary problems with the Draft's approach: (1) the definitions of procedural and substantive unconscionability are too restrictive; (2) the Draft fails to state that unconscionability and deception can be raised affirmatively to challenge the specific terms or the contract as a whole; (3) the Draft severely limits the remedies available once a court finds a term or contract to be unconscionable or that the business engaged in deception; and 4) the Draft places the burden of proof on consumers even though only businesses have access to most of that proof. In sum, the proposed Restatement embodies an expressly preferential treatment of businesses over consumers.

## **I. The Draft Undermines the Critically Important Doctrine of Unconscionability**

Restatements consist of three parts: the “black letter,” which is intended to be the essential law on the subject; the Comments, which are regarded as an integral part of the section to which they belong and are consulted in order to understand the background and rationale of the black letter and the details of its application; and the Reporters' Notes, which are regarded as the product of the Reporters (not the Institute) and discuss the legal and other sources they relied upon in formulating the black letter and the comments.

The black letter of the current Draft states that a term is procedurally unconscionable—*i.e.* that consumer's agreement to the term was obtained in an unconscionable way—when it causes unfair surprise or results from the lack of meaningful choice of the part of the consumer. Section 5(b)(2). We do not object to this general statement. However, the Restatement also proposes to abandon—or drastically recast—the well-accepted set of factors that courts use to determine procedural unconscionability: (1) the consumer's lack of financial sophistication (including cognitive biases); (2) the business's exploitation of consumer disadvantages; (3) unequal bargaining power; (4) the use of incomprehensible language; (5) high pressure tactics and misrepresentations; and (5) whether economic, social, or practical duress compelled a party to execute the contract. Comment 6 and the Reporters' Notes seek to *replace* this set of factors with a new concept, “salience.”<sup>3</sup>

The Reporters' Notes define a contract term as salient “if it can affect the contracting decisions of a substantial number of consumers,” and then take the remarkable position that, if a term *can* affect the contracting decisions of a substantial number of consumers, then the market will police the term and the courts need not evaluate whether it was imposed on the consumer in

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<sup>2</sup> Council Draft No. 4, at 33, 58, 76, 79, 90.

<sup>3</sup> Although the concept is introduced in Comment 6, the noun “salience” and the adjective “salient” appear exclusively in the Reporters' Notes, with one exception in the last sentence of Comment 6(c). If the Reporters did not intend to replace these independent set of factors with “salience,” Comment 6 and their Notes should be clarified to state that the viability of the factors as independent bases for a finding of procedural unconscionability is not disturbed.

an unconscionable way.<sup>4</sup> The Reporters, however, do not cite any judicial decisions that define or apply the concept of “salience” in the unconscionability context, and there is not one reported or unreported decision on Westlaw that takes this approach. Instead, the Reporters’ Comments appear to rely entirely on a law review article that spins out this theory, again without citing any judicial decisions that support it.<sup>5</sup>

This attempt to inject an entirely new approach contravenes the methodology that ALI claims to follow of ascertaining the majority and minority rules, determining which rule is the better one, and providing the rationale for choosing it.<sup>6</sup> But of greater concern is its unfounded reliance on the marketplace to prevent overreaching and unfairness toward consumers. Recent history, including the vast wave of irresponsible lending that caused the mortgage meltdown ten years ago, demonstrates that overreaching and unfairness flourish in the marketplace.

The Draft also expresses an overly restrictive standard for whether a contract term is substantively unconscionable. While Section 5(b)(1) states that a term is substantively unconscionable if it is “fundamentally unfair” or “unreasonably one-sided,” the Comments state that: “the doctrine is to be used only when the one-sidedness of a term in the contract is extreme.”<sup>7</sup> This test sets an overly high standard. Many fine print terms in consumer contracts today are unreasonable and unfair, but might not be viewed as “unconscionable” under this definition. For example, a fine print \$35 charge might not seem “fundamentally” unfair in isolation. But when a \$35 charge is repeatedly imposed, is high when compared to the cost of the contract, exceeds the cost to the business that the charge is intended to offset, or is imposed repeatedly, the fee should be declared unreasonable and unfair even though a court might not find it “extreme.”

Moreover, non-mutual enforcement clauses—clauses that deny the consumer the right to a remedy that the business is allowed to invoke—were not added to the list of contract terms that are *prima facie* unconscionable in the text of Section 5. It is common for businesses to place non-mutual clauses in consumer contracts that allow the business to sue the consumer in court, but relegate the consumer to mandatory binding arbitration. Although court decisions are split on whether “one-sided” or “non-mutual” enforcement clauses are unconscionable in the arbitration context, the better rule is that they are *prima facie* substantively unconscionable. The role of a Restatement is to “propose the better rule and provide the rationale for choosing it.” The Draft’s failure to apply the presumption of substantive unconscionability to such clauses, whether or not they involve mandatory arbitration, also undermines the critical role that the unconscionability doctrine is supposed to contribute to the success of the Restatement’s approach.

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<sup>4</sup> Council Draft No. 4, at 76, 89-91.

<sup>5</sup> *Id.*

<sup>6</sup> Council Draft No. 4, at xi-xii.

<sup>7</sup> Council Draft No. 4, at 69-70. The Reporters use the adjective “extreme” to explain substantive unconscionability throughout the Draft. *Id.* at 4, 5, 33, 77, 81.

## II. The Draft Cripples the Enforcement of Unconscionability and Deception

Our second concern about the Draft's approach to the unconscionability doctrine is the failure to provide for robust consumer enforcement. The unconscionability doctrine will provide little or no counterweight to the permissive assent rules if consumers can raise it only as defense to a lawsuit to enforce the contract. Traditionally, common law unconscionability could be raised only as a defense to an action brought against a consumer. A court could permit a suit seeking a declaration that a term or the contract is unconscionable if the suit does not seek damages or other affirmative relief.<sup>8</sup> The black letter of this Draft does not address the limited enforcement options available to consumers.<sup>9</sup> Neither the Comments nor Reporters' Notes discuss any judicial rulings on this point. Enforcement of the doctrine of deception suffers the same fate.

In the context of state and federal statutory protections, optimal policing of marketplace behavior occurs when state, federal, and private attorneys are acting as cops on the beat. In the context of the common law, however, there is little or no governmental enforcement, leaving consumers and their attorneys to bear this burden. Consumers should not be put in the position of having to default on the contract and subject themselves to negative credit reporting in order to raise unconscionability or deception. Moreover, the threat of enforcement is insignificant and will not significantly affect market behavior if only a small percentage of consumers (those who default and are sued) can raise the issue. Businesses will be well aware that they have little to fear from consumers.

In light of these practical and legal restrictions to private enforcement found in this Draft, the pivotal roles that unconscionability and deception are called upon to play in policing the marketplace are severely undermined. To remedy this, the black letter of Sections 5 and 6 must include a provision stating that a consumer can raise unconscionability affirmatively and defensively by seeking a declaration that the contract is void in part or in its entirety, providing for restitution for the costs incurred by virtue of the void provisions,<sup>10</sup> and allowing class action relief.

The current Draft addresses this critical question just in Comment 12 to Section 5 and Comment 7 to Section 6, not in the black letter. And the two Comments are entirely inadequate. They reject the use of these doctrines affirmatively except in the limited circumstance where the consumer paid an unconscionable fee and seeks to recover it.

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<sup>8</sup> This limited suit proceeded in one case that we were able to find. *Carey v. Lincoln Loan Co.*, 125 P.3d 814, 829-30 (Or. Ct. App. 2005), *aff'd on other grounds*, 157 P.3d 775 (Or. 2007).

<sup>9</sup> The Draft does, however, severely limit remedies in Section 9. This issue is discussed in the next section.

<sup>10</sup> See Restatement (Third) of Restitution and Unjust Enrichment (2011).

### **III. The Draft Severely Limits Remedies Related to Unconscionability and Deception**

The only remedies available in this Draft in the event of a finding of unconscionability or deception are found in Section 9. This Section instructs the courts to refuse to enforce the offending term or the contract or replace the offending provisions with other terms. These provisions, without more, do not realistically deter business overreaching at contract inception or police the marketplace after the fact. These remedies are especially feeble when considered in conjunction with the lack of affirmative enforcement, the burdens of proof imposed on consumers, and silence regarding standards of proof.

### **IV. The Drafts Fails to Address Burdens of Proof and Standards of Proof**

The allocation of burdens of proof and the level of evidence the consumer must present to prove unconscionability and deception also reduce the effectiveness of the roles that these doctrines are supposed to play. According to the Draft, the consumer bears the initial burden of proving the elements of unconscionability. Businesses, however, have access to nearly all of the relevant evidence. For example, only businesses are “recording this call to for quality assurance,” and therefore control the recordings which would show that telemarketers pressure and deceive consumers into agreeing to bad deals. Only businesses draft the contracts and only they know “the commercial setting, purpose, and effect” of the terms they impose on consumers.<sup>11</sup>

Regarding procedural unconscionability related to a contract term, the Draft takes the position that a consumer must show that the term did not affect the contracting decisions of a substantial group of consumers, *i.e.*, the term is not salient.<sup>12</sup> To meet this burden a consumer would have to commission a study of consumers—an unrealistic task for a consumer to perform given the cost involved. Such a study lacks validity in any event because, if conducted by consumers once unconscionability has become an issue, the study would take place well after consummation of the contract, rather than at the time of contracting. A prior draft added a Comment to Section 5 that placed the burden on the business to prove that the standard contract terms were presented in a way that affected consumers’ contracting decisions to rebut a finding of procedural unconscionability. It also addressed burdens related to substantive unconscionability. Council Draft No. 4 *removed* that Comment, taking a big step backwards.<sup>13</sup>

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<sup>11</sup> Similarly, only businesses know the relationship between price and one-sided terms, yet the Comments state—without citing any support for the proposition—that “a contract that provides few rights to a consumer may not be problematic if a low price reflects those minimal rights, but might be problematic without the corresponding benefit of a low price.” Council Comparison Draft No. 4, § 5 at 75.

<sup>12</sup> See discussion of salience in Section I above.

<sup>13</sup> Council Comparison Draft No. 4, § 5 at 87-88. Preliminary Draft No 3, § 5 cmt 10 stated: “*Burden of proof.* If a term is presumed to be substantively unconscionable under subsection (d), the burden is on the business to prove that the presumption is rebutted in the particular case. In addition, if a standard contract term is substantively unconscionable, the burden is on the business to prove that there is no procedural unconscionability (namely, that the term can affect the contracting decisions of a substantial

Neither Section 5 nor Section 6 address the standard of proof a court should apply in cases raising these claims. In both contexts, the black letter should state that the standard of proof is preponderance of the evidence. The application of a stricter standard reduces the deterrence and policing role of these doctrines. This is especially so where the remedy is limited to unenforceability and replacement with a substitute term and deterrence damages are not available for business deception, as would be the case with common law fraud.

#### **IV. Conclusion**

Unfortunately, this Draft unnecessarily restricts the scope of procedural and substantive unconscionability, fails to provide that unconscionability and deception can be raised affirmatively, circumscribes the remedies available for violations of these doctrines well beyond what the general common law otherwise provides, and fails to address burdens and standards of proof. As a result, the Restatement collapses under the weight of “freedom to contract” due to the lack of any meaningful consumer protections.

For these reasons, we urge the Council to not approve this Draft. Thank you for your consideration.

Alliance for Justice	Consumers for Auto Reliability and Safety (California)
Allied Progress	Crandall Law firm, SC (Wisconsin)
Arkansans Against Abusive Payday Lending	D.C. Consumer Rights Coalition
Berkeley Law Consumer Advocacy & Protection Society (California)	East Bay Community Law Center (California)
Center for Responsible Lending	Equal Justice Society (California)
Consumer Action	Kentucky Equal Justice Center
Consumer Federation of America	Legal Services NYC

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number of consumers). As noted in Comment 6, it is presumed that standard contract terms do not affect the contracting decisions of a substantial number of consumers and are, therefore, procedurally unconscionable. The burden is on the business to rebut the presumption and prove that the standard contract terms were presented in a way that affected consumers’ contracting decisions.” At 72.

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Maryland Consumer Rights Coalition	Public Citizen
National Association of Consumer Advocates	Public Justice Center (Maryland)
National Center for Law and Economic Justice	Southern Poverty Law Center
National Consumer Law Center (on behalf of low-income consumers)	U.S. PIRG
National Fair Housing Alliance	Virginia Poverty Law Center
Progressive Congress Action Fund	Woodstock Institute (Illinois)