Standard-Terms Contracting in the Global Electronic Age: European Alternatives[1]

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I. INTRODUCTION

The issue of standard terms in contracts is a roadblock on the road to reform of American contract law in the era of electronic commerce. In the

1. The title draws on that of Robert A. Hillman & Jeffrey J. Rachlinski, *Standard Form Contracting in the Electronic Age*, 77 N.Y.U. L. REV. 429 (2002).

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1990s the two sponsors of the Uniform Commercial Code ("U.C.C.")—the American Law Institute ("ALI") and the National Conference of Commissioners on Uniform State Laws ("NCCUSL")—decided to modernize Article 2 of the U.C.C., which deals with sales of goods, and to create a new Article 2B, to govern licensing of "computer information," i.e., information in electronic form, including software.[2] By the end of the decade this ambitious project lay in shambles. In April 1999, ALI rejected Proposed Article in part because it did *not* make major changes in existing law governing standard terms. In July 1999 NCCUSL rejected the proposed Revised Article 2—Sales in part because it *did* seek to change existing law. This continuing controversy is discussed below in Part II.C.

Standard terms are contract terms that one party formulates for use in its contracts generally and provides to other parties for use in their mutual transactions. Typically they are not negotiated but are presented to customers at the conclusion of bargaining over the contract's principal subject matter. Standard terms are often referred to pejoratively as "boilerplate." Their legal importance is that they alter default solutions provided by law. That is, the law provides one solution that applies "unless the parties agree otherwise." In standard terms, the parties "agree" otherwise. For example, in a standard term the buyer may "agree" with the seller to negate a warranty that contract law would otherwise imply. Standard terms are a feature of the vast majority of written contracts. Since only one party participates in their formulation, they offer opportunity for that party to introduce terms that the other might not willingly agree to in negotiations.[3] In the words of a popular song, "the large print giveth, and the small print taketh away."[4]

For over forty years American law has authorized courts to decline to enforce "unconscionable" terms. This unconscionability control is not limited to standard terms, although it has its principal application there. How necessary and how successful it has been is controversial. While some observers believe that economic self-interest largely prevents standard terms drafters from overreaching and that a control limited to the rare "unconscionable" term is sufficient,[5] others complain that the current control is awkward at best and woefully inadequate at worst.[6]

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2. ALI is the source of the noted "Restatements" of the law; it is composed of several thousand leading jurists. NCUSSL is responsible for most Uniform Acts and consists of several commissioners per state, usually appointed by the governor of the state, that represent the state. *See* Richard E. Speidel, *Revising Article 2: A View from the Trenches*, 52 HASTINGS L.J. 607, 608-09 (2001).

3. To name a few examples: a term in a contract for new electronic equipment disclaims all warranties; the terms of a trial subscription to a magazine provide that if not cancelled at the end of the thirty-day trial, a five-year subscription will be entered; a software license provides that in no circumstance may the licensee transfer the program to another computer.

4. TOM WAITS, *Step Right Up*, *on* SMALL CHANGE (Elektra Entertainment 1976), *lyrics available at* http://www.yimpan.com/Songsite/Lyric/index.asp?sid=2335. *See* Waits v. Frito-Lay, Inc., 978 F.2d 1093 (9th Cir. 1991) (upholding songwriter's claim for misappropriation of the song).

5. *See infra* text accompanying notes 78 to 80.

6. *See, e.g.*, Bates, *infra* note 15, at 105 ("[A]dequate consumer protection against unfair terms in form contracts [is] not being provided by the American legal system"); Mark Klock, *Unconscionability and Price Discrimination*, 69 TENN. L. REV. 317, 350 (2002) (describing the American approach as "a complete failure when it comes to deterring unconscionable contracts"). *See also* Swanson, *infra* note 17, at 370.

The development of information in electronic form and of software (collectively, "computer information") has given standard terms new and increased importance. Computer information contracts are hardly imaginable without standard terms. Computer information contracts are "licenses." The standard terms of these licenses set out what the parties contracting for the information, i.e., the licensees, may do with it. Typically these licenses limit the number of users the licensee may permit to use the information, restrict the uses that the licensee may put the information to, and control the circle of recipients to whom the licensee may distribute the information. The wish for legal validation of standard terms computer information licenses, "shrink-wrap" and "click-wrap" licenses,[7] was a major goal of the backers of the Uniform Computer Information Transactions Act ("UCITA").

Thanks to development of the Internet, standard terms are a global issue. Parties from different countries meet on the Internet. They enter into online license agreements that govern use of Internet sites and transactions in computer information. They reach contracts for international sales of goods that utilize standard terms. As a result, standard terms designed for use in one country are subject to laws for which they were not designed. Dozens of terms in common use by American Internet service providers such as AOL and CompuServe have been struck down abroad as unlawful. Even mighty Microsoft has bowed to consumer associations rewriting its standard license for Windows 2000.[8]

Ever more countries are adopting standard terms laws. In 1993, on the eve of the commercialization of the Internet and just as the United States began revising the U.C.C., the European Union ("E.U.") introduced controls on standard terms. It adopted Council Directive 93/13/EEC of April 5, 1993 on unfair terms in consumer contracts (hereinafter, the "Unfair Terms Directive"). The directive requires Member States to have unfair terms statutes that meet certain minimum standards. Those standards are more restrictive than American law. Other countries outside Europe have also adopted standard terms statutes.[9]

The E.U. Unfair Terms Directive did not appear out of nowhere. Perhaps its most important source of inspiration was the German Standard Terms Statute of 1976 [*Gesetz zur Regelung des Rechts der Allgemeinen*

7. "Shrink-wrap" licenses are licenses printed on the packaging of software and other computer information delivered to licensees in tangible media (e.g., computer diskettes of some kind). The package is wrapped in a clear-read-through shrink-wrap plastic. The buyer of the computer information is deemed to have assented to the terms of the license by ripping open the shrink-wrap. "Click-wrap" licenses are licenses shown in electronic form or made available to users on computer screens to users. Before the user is permitted to use the online service or the computer program, the user must agree to the license terms. The user assents to the standard terms by clicking with the mouse. The term "click-wrap" arose by analogy to "shrink-wrap." Online licenses are typically in "click-wrap" form, but there is yet another form of online license that is asserted: "browse-wrap." The theory of a browse-wrap license is that the user is informed that use of the Internet site amounts to the user's assent to the site's stated terms.

8. *See infra* text accompanying note 346. The same trio seems to have lost only one term to legal action in the United States. *See* Specht v. Netscape Communications Corp. and America Online, Inc., 306 F.3d 17 (2nd Cir. 2002).

9. *See, e.g.*, The Consumer Contract Act [Japan 2001]; Adhesion Contract Act [Korea 1986, amended 1992], both available in English translation at Asia Pacific Consumer Law, http://www.ciroap.org/apcl/index.html.

Geschäftsbedingungen].[10] That statute itself seems to have had a common origin with present day American law. In the 1950s, just as both the U.C.C. and the Common Market were being launched, German and American legal systems were both working on new approaches to standard terms. The approaches in the two countries were strikingly similar. This seems to have been a product of a flow of ideas across the Atlantic.[11] In any case, by the 1960s and 1970s the courts in the two countries were working to give form to those new rules. In Germany the courts were sufficiently successful that the legislature could codify the rules in a new statute, the Standard Terms Statute of 1976.

Already in the 1950s when the U.C.C. was first under consideration, Rudolf B. Schlesinger called for a "serious study of the advantages and disadvantages" of the methods undertaken to control oppressive clauses in Europe and America.[12] Schlesinger had an essentially legislative rationale for his proposal—such a study would bring critical perspective to drafting American laws. In 1976, on the eve of adoption of the German Standard Terms Statute, John P. Dawson published such a study of the then existing German case law. He found much to admire in German law and counseled that "German experience can be a guide."[13] Two decades later, when ALI and NCCUSL took up revisions to the U.C.C., Professor Peter Winship reminded them of Schlesinger's invocation that "[t]he civilians have faced the same issue and resolved it with a variety of devices," and he renewed the call for a systematic study.[14] The comparativists' call for systematic study has gone unheeded, even though now there is also a highly practical reason to study foreign standard terms law.[15]

The goal of this article is to begin at long last such systematic comparative studies of foreign standard terms laws from an American perspective. Its aims are at the same time both highly practical—facilitation of compliance with foreign law—and highly scientific—improved comprehension of the issues and approaches available to deal with standard terms.

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10. BGBI. I S. 3317 [*hereinafter* AGB-Gesetz]. *See* Thomas Wilhelmsson, *Standard Form Conditions, in* TOWARDS A EUROPEAN CIVIL CODE 255, 258 (Arthur Hartkamp et al. eds., 2d ed. 1998); Carl Baudenbacher, *Some Remarks on the Method of Civil Law*, 34 TEX. INT'L L.J. 333, 341 (1999).

11. *See infra* text accompanying notes 37-42, 197.

12. Rudolf B. Schlesinger, *The Uniform Commercial Code in the Light of Comparative Law*, 1 INTER-AM. L. REV. 11, 33 (1959). Schlesinger's article first appeared in a government document in 1955. *Id.* at 11.

13. John P. Dawson, *Unconscionable Coercion: The German Version*, 89 HARV. L. REV. 1041, 1125 (1976).

14. Peter Winship, *As the World Turns: Revisiting Rudolf Schlesinger's Study of the Uniform Commercial Code "In the Light of Comparative Law,"* 29 LOY. L.A. L. REV. 1143, 1156-58 (1996).

15. There is no study in American legal literature of the E.U.'s Unfair Terms Directive and no study based on primary sources of German Standard Terms law since Dawson's study made before the German statute was adopted. The closest article there is to such a study is Larry Bates's recently published work, *Administrative Regulation of Terms in Form Contracts: A Comparative Analysis of Consumer Protection*, 16 EMORY INT'L L. REV. 1 (2002) (surveying law in Germany, Sweden and the United Kingdom before the directive, as well as the law of Israel, for models for American law). Unfortunately, Professor Bates's article does not treat the Unfair Terms Directive, and for its discussion of German standard terms law, the article relies exclusively on secondary, English-language sources published more than fifteen years ago.

This article examines American, European Union, and German law. It considers not only current law, but significant aspects of the development of these bodies of law. Awareness of the latter furthers understanding of the former. Part II sets out general issues involved in standard terms laws and summarizes American law. It notes the possible origin of American concepts in Europe and examines standard terms in the struggle over revision of the Uniform Commercial Code. Part III looks at the law of the European Union and its origin in the consumer movement. Part IV considers in detail the law of one Member State as an example, that of Germany.[16] Finally, the conclusion summarizes the results of the examination and notes insights into American practice that European experiences suggest.

II. AMERICAN LAW

Part II first examines standard terms in contracts as a general issue. It then summarizes standard terms in American law[17] and notes the possible origins of the American law in the German law of the day. Finally, it examines the treatment of standard terms in the reform of the Uniform Commercial Code.

A. *Standard Terms Generally as a Legal Problem*

Standard terms have been used for well over a century. The issues involved in their use have long been known. Contract law in Western countries is based on the principle of freedom of contract. Thus, to varying extents, but generally as much as is widely acceptable in any one system, contract law is default law. That is, it is law that applies unless the parties agree otherwise.

The nineteenth century brought not only mass production, but also mass distribution, and with mass distribution, form contracts. In form contracts the party supplying a product or service (referred to here as "user") spells out the terms on which the party does business and which it expects the other party to accept (referred to here often as the "other party"). Standard terms permit suppliers to rationalize their offerings, to control their agents, and to avoid wasting time negotiating terms that they are not prepared to vary. Standard terms can provide answers to questions on which the law is silent.[18] Yet just

16. *See infra* text accompanying note 197.

17. A comprehensive review is beyond the scope of this article. For recent fuller examinations of standard terms in American law, see E. ALAN FARNSWORTH, CONTRACTS § 4.28 (3d ed. 1999); W. DAVID SLAWSON, BINDING PROMISES: THE LATE 20TH-CENTURY REFORMATION OF CONTRACT LAW 142 (1996); JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE 151-77 (5th ed. 2000); Hillman & Rachlinski, *supra* note 1; Carol B. Swanson, *Unconscionable Quandary: U.C.C. Article 2 and the Unconscionability Doctrine*, 31 N.M. L. REV. 359, 367 (2001). For a listing of still others, *see* Bates, *supra* note 15, at 2 n.2, 14 n.38 (2002).

18. For discussions of the costs and benefits of enforcing standard forms, see Hein Kötz, *Welche gesetzgeberischen Maßnahmen empfehlen sich zum Schutze des Endverbrauchers gegenüber Allgemeinen Geschäftsbedingungen und Formularverträgen?*, *in* 1 VERHANDLUNGEN DES FÜNFZIGSTEN DEUTSCHEN JURISTENTAGES, A9, A21-A25 (1974); Hillman & Rachlinski, *supra* note 1, at 437-41 (2002). Standard terms make up standard form contracts. Standard form contracts are themselves sometimes called contracts of adhesion.

as form contracts provide benefits, so too, they produce problems. Karl N. Llewellyn observed that users of standard terms may "turn[] out a form of contract which resolves all questions in advance in favor of the one party."[19] What controls, if any, should a legal system place on such terms?

In contract law, terms become parts of contracts because parties assent to them. Typically where standard terms are used, however, parties are asked to submit to them unread or, if read, not necessarily understood.[20] Moreover, when parties do read and understand standard terms and object to them, the parties imposing them may refuse any alteration. Where standard terms are inalterable, parties asked to "agree" to the terms in some instances will have no easy alternatives other than to submit. That is most obviously the case where the supplier has a monopoly or where all other suppliers use the same terms. But practically—at least in smaller matters—it may also be the case where the inconvenience of seeking out alternatives is disproportionate to the dangers involved in accepting the terms. Users of standard terms act in their own interests.[21] Ask in house counsels to speak candidly and they will acknowledge, as one general counsel advised senior management of a Fortune 500 company, that "[t]he purpose of form contracts is primarily to protect the needs of our [internal] clients, not to protect the interests of our customers."[22] But when users provide terms in their own self-interest, and parties submitting to them do not read them or have no choice but to accept them, possibilities for abuse arise.

Recognition that contract law should provide some measure of protection against overreaching in contract terms is near universal in modern legal systems.[23] Comparative law questions relate to how different legal systems perceive and define the problem and how they seek to resolve it.[24] Perceptions of the problem mostly lie between two points of view. One view sees the issue as a contract law question of how the general contract law requirement of assent applies to standard terms; the other view sees the problem as an issue of protection of weaker parties to contracts. Actions taken to resolve the problem tend to address one or both of two principal questions. One question is whether and what formal or procedural requirements should determine whether terms become parts of contracts (referred to here as "incorporation control"). The other question is whether and how the content or

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19. Karl N. Llewellyn, *Contract—Institutional Aspects*, *in* 4 ENCYCLOPEDIA OF THE SOCIAL SCIENCES 329, 335 (Edwin R.A. Seligman ed., 1931).

20. For a discussion of the economic, social, and cognitive reasons parties do not read forms, see Hillman & Rachlinski, *supra* note 1, at 445-54.

21. While users are usually suppliers, sometimes they are customers, particularly large ones. They also may be trade associations or even government bodies. They frequently seek to transfer all risks to the other parties. *See* Kötz, *supra* note 18, at A26-A29 (rejecting the argument that the risk transfer produces lower prices).

22. This quotation is from a company internal communication on file with the author. While this might seem obvious to a lawyer, it is not always obvious to laymen. The author had the in house lawyer's nightmare come true: an internal client used the company form when the company was, exceptionally, on the other side of the transaction.

23. *See* 1 HEIN KÖTZ & AXEL FLESSNER, EUROPEAN CONTRACT LAW 138 (Tony Weir trans. 1997); KONRAD ZWEIGERT & HEIN KÖTZ, INTRODUCTION TO COMPARATIVE LAW 333 (Tony Weir trans., 3d ed. 1998)

24. This article is concerned only with overreaching through use of standard terms and not with other issues of overreaching, such as duress.

substance of terms should be subject to control (referred to here as "content control"). All of these concepts are found in American law.

B. *American Approaches to Standard Terms, Especially in the U.C.C.*

American treatments of standard terms have been dominated for over forty years by concepts identified with Llewellyn: "unconscionability" and "blanket assent." Llewellyn's influence is pervasive to this day.[25] As the leading commercial law scholar of the mid-twentieth century, principal architect of the U.C.C., and Reporter for Article 2, Llewellyn drafted section 2-302 of the U.C.C. It permits, but does not require, a court to decline to enforce a term that it finds "unconscionable."[26] While a precursor of section 2-302 drafted in the early 1940s applied only to standard terms,[27] section 2-302 is not limited to controlling standard terms. It applies to transactions between merchants as well as to transactions with consumers. Section 2-302 first became law in 1954 when Pennsylvania became the first state to adopt the U.C.C.; in the 1960s it became law throughout the land.[28] Llewellyn considered the section to be "perhaps the most valuable section in the entire Code."[29] Subject to much discussion[30] and criticism from the beginning, section 2-302 has never been amended. It almost certainly will remain essentially unchanged for the foreseeable future.[31]

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25. *See, e.g.*, FARNSWORTH, *supra* note 17, § 4.26, at 301-02 (highlighting Llewellyn's name in the margin); Hillman & Rachlinski, *supra* note 1 (in which Llewellyn's name appears 34 times). *Cf.* Dawson, *supra* note 13, at 1117.

26. U.C.C. § 2-302(1) (2002) provides:

> 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.

Official Comment 1 elaborates:

> 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. The 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 the 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 upon these questions. The principle is one of the prevention of oppression and unfair surprise and not of disturbance of allocation of risks because of superior bargaining power. *Id.* (internal citations omitted).

See also Kötz, *supra* note 18, at A49 (discussing the virtues of an open control of content in German law).

27. Allen R. Kamp, *Uptown Act: A History of the Uniform Commercial Code: 1940-49*, 51 SMU L. REV. 275, 299-302, 306-14, 334-36 (1998) (quoting the provision); *see also* Arthur Allen Leff, *Unconscionability and the Code—The Emperor's New Clause*, 115 U. PA. L. REV. 485, 509-10 (1967) (quoting the provision).

28. The history of the drafting of section 2-302 is set out in Leff, *supra* note 27, at 489-501, 509-16.

29. FARNSWORTH, *supra* note 17, § 4.28, at 307, *citing* New York Law Revision Commission, Hearings on the Uniform Commercial Code at 121 (1954).

30. JOHN D. CALAMARI & JOSEPH M. PERILLO, THE LAW OF CONTRACTS 365 (4th ed. 1998).

31. If the ALI Membership adopts the NCCUSL-ALI post-1999 compromise, already

Section 2-302 was not Llewellyn's last word on the subject. In the 1960s he introduced the concept of "blanket assent" to explain what happens in standard form contracts. He denied that there is assent to all the terms of a standard form contract. Assent, he argued, applies only to the few "dickered" terms, the broad type of the transaction, and "a blanket assent (not a specific assent) to any not unreasonable or indecent terms the seller may have on his form, which do not alter or eviscerate the reasonable meaning of the dickered terms."[32] The idea is said to dominate American treatment of standard forms.[33]

From this base the United States has dealt with standard terms. Court decisions and scholarship—there has been no legislation as such[34]—have built on this base, seeking to make sense of it, and working to make it effective. Competing or perhaps better described as complementary approaches, i.e., the doctrines of "reasonable expectations" and a somewhat similar scheme used in the Restatement of Contracts, have sought favor. The efforts have not been universally regarded as successful.[35]

Llewellyn considered the authority bestowed on courts by section 2-302 to be novel in American law.[36] Comparative law scholars believe that Llewellyn drew his inspiration for section 2-302 from the practice of controlling standard terms in Germany under the general clauses of the German Civil Code.[37] Although in the latter part of his life Llewellyn

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approved by both NCCUSL and by the ALI Council, see Report of ALI Council Consideration of U.C.C. Projects, *available at* http://www.ali.org/forum4/ALIReport_Liebman1002.htm (last visited Nov. 11, 2002), the only change will be to substitute the word "term" for the word "clause." *See* American Law Institute, Uniform Commercial Code—Proposed Amendments to Article 2. Sales & Proposed Amendments to Article 2A. Leases—Council Draft No. 2 (October 8, 2002) § 2-302 (2002). If that draft is defeated, which seems unlikely, there will be no change at all.

32. KARL N. LLEWELLYN, THE COMMON LAW TRADITION—DECIDING APPEALS 370 (1960).

33. Hillman & Rachlinski, *supra* note 1, at 461. *See also* MARTIN MUNZ, ALLGEMEINE GESCHÄFTSBEDINGUNGEN IN DEN USA UND DEUTSCHLAND IM HANDELSVERKEHR 70 (1992).

34. At least there has been no general legislation. There have been consumer protection laws that affect standard terms in certain types of contracts and sectors.

35. *See, e.g.*, Bates, *supra* note 15, at 2 n.2, 14 n.40 (concluding that there is an "absence of any sort of consensus among legal commentators" and "[t]he case law is full of inconsistencies, contradictions, and lacks any sort of unifying theme"); Hillman & Rachlinski, *supra* note 1, at 434 (noting that "[t]he doctrine governing contract enforcement has long been criticized as vague, ill-defined, and easily muddled").

36. This is clear from the official comment, quoted in *supra* note 26. *Cf.* FARNSWORTH, *supra* note 17, § 4.28, at 307 (calling it "one of the [U.C.C.'s] most innovative sections").

37. RUDOLF B. SCHLESINGER ET AL., COMPARATIVE LAW: CASES—TEXT—MATERIALS 20-21 (6th ed. 1998); JUTTA KLAPISCH, DER EINFLUß DER DEUTSCHEN UND ÖSTERREICHISCHEN EMIGRANTEN AUF CONTRACTS OF ADHESION UND BARGAINING IN GOOD FAITH IM US-AMERIKANISCHEN RECHT 66 (1991) (citing views of Eike von Hippel). The inspirational sections would be Section 138 (prohibiting *sittenwidrige* transactions, i.e., those against good morals), and Section 242 (requiring *Treu und Glauben, i.e.*, "good faith" in carrying out contracts). But not everyone sees its origin in German law. *See, e.g.*, Kamp, *supra* note 27, at 299-302, 306-14, 334-36 (1998) (discussing origin of Section 2-302 with no mention of a German connection). Those who see the origin elsewhere find it in the practice of the courts of equity. The concept of unconscionability is said to have "deep roots in law and equity." *See* CALAMARI & PERILLO, *supra* note 30, § 9.38, at 366. *But see* United States v. Bethlehem Steel Corp., 315 U.S. 289, 300 (1942) (suggesting skepticism in referring to an "asserted doctrine of unconscionability"). What mix of influences may have directed Llewellyn's drafting of § 2-302 may never be known, but that the German Civil Code was a direct influence on him is generally believed. *See* E. Allan Farnsworth, *Duties of Good Faith and Fair Dealing Under the UNIDROIT Principles, Relevant International Conventions, and National Laws*, 3 TUL. J. INT'L & COMP. L. 47, 52 (1995) (noting that the obligation of good faith in U.C.C. Section 1-304, former Section 1-203, comes directly from Section 242 of the German Civil Code).

preferred to downplay, if not conceal, the importance of foreign ideas on his thinking,[38] his familiarity with the German legal system is now well known.[39] While from New York City, Llewellyn graduated from high school in Germany and he spoke German fluently. In the 1920s and early 1930s, he spent two years in Leipzig as a visiting professor and published one of his most important jurisprudential works there.[40] His knowledge of the pre-War practice of standard terms control is obvious from his review of the first comparative book on the topic in which he stated some of his thoughts on the subject.[41] Just as he may have drawn on German law in drafting section 2-302, Llewellyn may also have drawn inspiration for his idea of blanket assent from German practice in the 1950s.[42]

Section 2-302 on unconscionability is the principal American treatment of standard terms. Even where it is not directly applicable—because a transaction does not involve a sale of goods—its approach is often followed, either explicitly or *sub silentio*.[43] Section 2-302 is not limited to standard

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38. *See* SCHLESINGER ET AL., *supra* note 37, at 21. Riesenfeld reports the counsel that Llewellyn gave him immediately upon his arrival in the United States:

> Another piece of advice impressed me even more. He mentioned the failure of courses in comparative law and told me never to reveal when I relied on an idea coming from continental Europe, because that would be the 'kiss of death,' again reiterating that admonition three times over so that it would sink in as it did.

Stefen A. Riesenfeld, *Reminiscences of Karl Llewellyn, in* RECHTSREALISMUS, MULTIKULTURELLE GESELLSCHAFT UND HANDELSRACHT: KARL N. LLEWELLYN UND SEINE BEDEUTUNG HEUTE 11, 14 (Ulrich Drobnig & Manfred Rehbinder eds., 1994).

39. *See* Michael Ansaldi, *The German Llewellyn*, 58 BROOK. L. REV. 705 (1992); Paul D. Carrington, *Der Einfluß kontinentalen Rechts auf Juristen und Rechtskultur der USA* 1776-1933 JZ [JURISTENZEITUNG] 529, 537; Ulrich Drobnig, *Llewellyn and Germany, in* RECHTSREALISMUS, *supra* note 38, at 17; Shael Herman, *Llewellyn the Civilian: Speculations on the Contribution of Continental Experience to the Uniform Commercial Code*, 56 TUL. L. REV. 1125, 1128 (1982); Riesenfeld, *supra* note 38, at 15 ("Llewellyn was intimately acquainted with German doctrinal developments."); James Whitman, *Commercial Law and the American* Volk: *A Note on Llewellyn's German Sources for the Uniform Commercial Code*, 97 YALE L.J. 156 (1987). A close connection remained to the end of his life. When he died in 1962 Llewellyn was working on a set of lectures to deliver in Germany that were to give a "comprehensive picture of his thought" such as he had never before given. WILLIAM TWINING, KARL LLEWELLYN AND THE REALIST MOVEMENT viii (1973).

40. KARL N. LLEWELLYN, PRÄJUDIZIENRECHT UND RECHTSPRECHUNG IN AMERIKA (1933), *translated as* THE CASE LAW SYSTEM IN AMERICA (M. Ansaldi trans., 1989).

41. Karl N. Llewellyn, Book Review, 52 HARV. L. REV. 700 (1939) (reviewing OTTO PRAUSNITZ, THE STANDARDIZATION OF COMMERCIAL CONTRACTS IN ENGLISH AND CONTINENTAL LAW (1937)). Dawson observed that the "main object" of the book was to describe German practice on standardized form contracts. Dawson, *supra* note 13, at 1117-23.

42. Dawson hints at such an inspiration. *Compare* Dawson, *supra* note 13, at 1108 (noting German Supreme Court Judgment of March 8, 1955) *with id.* at 1118 ("[E]ven a brief summary [of Llewellyn's 1960 argument] should suggest how closely it parallels the basic elements in the thinking of German courts and scholars." Nor did the influence of German law on American treatment of form agreements stop with Llewellyn. Émigré German scholars, particularly Friedrich Kessler and Albert Ehrenzweig, had a substantial influence. *See* GOTTFRIED RAISER, DIE GERICHTLICHE KONTROLLE VON FORMULARBEDINGUNGEN IM AMERIKANISCHEN UND DEUTSCHEN RECHT 12 n.65 (1966); KLAPISCH, *supra* note 37, at 55-110; Jerome Frank, *Civil Law Influences on the Common Law—Some Reflections on "Comparative" and "Contrastive" Law*, 104 U. PA. L. REV. 887, 889 (1956); Rudolf B. Schlesinger, *supra* note 12, at 32 n.54.

43. *See* CALAMARI & PERILLO, *supra* note 30, § 9.39, at 370; FARNSWORTH, *supra* note 17, § 4.28, at 308; WHITE & SUMMERS, *supra* note 17, § 4-2, at 153. *See also* Gillman v. Chase Manhattan Bank, N.A., 534 N.E.2d 824, 828 (N.Y. 1988) (applying § 2-302 unconscionability analysis to non-Article 2 transaction); Gonzalez v. A-1 Self-Storage, Inc. 795 A.2d 885, 888 (N.J. Super. Ct. 2000) (applying § 2-302 unconscionability analysis to non-U.C.C. transaction and commenting on role of 2-302 generally). *Cf.* SLAWSON, *supra* note 17, at 142 (noting that when courts adopted unconscionability,

terms, but applies to all contract terms, including separately negotiated terms. In practice, however, most cases in recent times involve standard terms.[44] Review of standard terms is not limited to any one class of contracting parties, e.g., consumers, but applies generally to all parties. Cases applying section 2-302 in practice often involve businesses,[45] although businesses are said to have little success except in cases of procedural unconscionability.[46]

Section 2-302 is a general clause, essentially authorizing courts to review contract terms. It provides little direction and is not backed up by any list of unconscionable terms. The question is a legal one for the court, but requires taking evidence on the term's "commercial setting, purpose and effect."[47] Unconscionability determinations are "fact-sensitive" and are made on a "case-by-case basis."[48] Although section 2-302 does not distinguish between incorporating standard terms into contracts and controlling the contents of those terms, the Official Comment seems to suggest, when it references oppression and unfair surprise, that the section is concerned with both issues.[49] Notwithstanding the absence of a clear statutory mandate, commentary and case decisions under 2-302 distinguish between "procedural unconscionability" and "substantive unconscionability."[50] That pair of terms corresponds to incorporation control and content control, respectively. Procedural unconscionability is concerned with how the parties reached agreement and which terms are part of it, i.e., the contract documents, their legibility and comprehensibility, etc. Substantive unconscionability relates to the promises actually made in the terms themselves, e.g., liability disclaimers.

Since section 2-302 has no explicit control on incorporation of terms, courts have derived a control from the general prohibition of unconscionability. Perhaps as a result, they are disinclined to invalidate terms

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"they were not changing the common law to be like Article 2—they were making the common law and the law of the article simultaneously").

44. SINAI DEUTCH, UNFAIR CONTRACTS: THE DOCTRINE OF UNCONSCIONABILITY 24 n.1 (1977) (reporting one non-standard term case out of 160); SLAWSON, *supra* note 17, at 142 (reporting "not one" case out of "thousands" involving a non-standard term). In the earliest days of the Section, many cases are said to have involved excessive prices, which obviously are not standard terms. Those cases, however, are said to have dwindled to a "trickle." WHITE & SUMMERS, *supra* note 17, § 4-6, at 163.

45. CALAMARI & PERILLO, *supra* note 30, at 371; SLAWSON, *supra* note 17, at 143 (1996) (reporting "[a]t least 40 percent of the parties seeking the protections of unconscionability in the reported cases have been business consumers since 1990").

46. WHITE & SUMMERS, *supra* note 17, § 4-9, at 176. *But see* SLAWSON, *supra* note 17, at 143 (noting that it is applied to both "without distinction").

47. U.C.C. § 2-302(2).

48. Forsyth v. BancBoston Mortgage Corp., 135 F.3d 1069, 1074 (6th Cir. 1997). *Accord*, WHITE & SUMMERS, *supra* note 17, § 4-3, at 156 ("It is not possible to *define* unconscionability. It is *not a concept, but a determination* to be made in light of a variety of factors not unifiable into a formula."). Dawson also emphasized the general character of the Section 2-302 test. *See* Dawson, *supra* note 13, at 1042 (noting that "[a]ll will agree that by any test Section 2-302 is a general clause").

49. CALAMARI & PERILLO, *supra* note 30, § 9.37, at 366, § 9.40, at 373. The Comment is quoted *supra* note 26.

50. Formative for the American discussion is Leff, *supra* note 27. *See also* Hillman & Rachlinski, *supra* note 1, at 456-58 (discussing unconscionability and the importance of Leff's argument). Views of Leff's article are disparate. According to one view, it is one of the twenty-two most influential law review pieces published between 1965 and 1985. Robert C. Berring & Sally Gunderson, *Preface to* 3 GREAT AMERICAN LAW REVIEWS 1, 1-3 (Robert C. Berring & Sally Gunderson eds.,1990). Dawson thought it, of the many articles on U.C.C. unconscionability, "the silliest of them all." Dawson, *supra* note 13, at 1041 n.1.

on this ground alone, except in cases of essential goods or services and monopoly-like situations.[51] They commonly require that *both* procedural and substantive unconscionability be present, employing what has been called a "sliding scale" that allows taking into account both elements.[52] They are reluctant to invalidate a term based on substantive unconscionability alone.[53] A most peculiar result follows from this: a clever user need only make sure that the other party knows of the term's existence. A party who knows what he or she is agreeing to cannot later complain that it is unconscionable.[54] American law imposes on that party a duty to read which is said to enshrine the writing as "sacrosanct" and make it "impregnable."[55]

The unconscionability standard of section 2-302 conjures up a picture of Simon Legree demanding the debtor's first-born child to guarantee performance.[56] It seems to have been meant to impose a hurdle higher than unfairness.[57] The Official Comment says that Section 2-302 is not designed to adjust for imbalances in bargaining power in order to protect weaker parties. Thus it would seem to be more concerned with the bargain that is struck than with the respective strengths and weaknesses of the parties.[58] Although some

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51. *See* U.C.C. [New] Revised art. 2. Sales § 2-302, Comment 1, at 34-35 (Council Draft No. 1) (Oct. 5, 2000) (noting that courts "should seldom invalidate a contract, or a term of a contract, that is not substantively unconscionable solely on the basis of one party's conduct," but "generally" should require both "procedural" and "substantive" unconscionability); Swanson, *supra* note 22, at 365, 393-95.

52. *E.g.*, Marin Storage & Trucking, Inc. v. Benco Contracting and Engineering, Inc., 107 Cal. Rptr. 645, 656 (2001). *See* SLAWSON, *supra* note 17, at 57; Hillman & Rachlinski, *supra* note 1, at 457; Swanson, *supra* note 22, at 367, 393-95.

53. Swanson, *supra* note 17, at 368. *See also* WHITE & SUMMERS, *supra* note 17, § 4-7, at 169.

54. *See, e.g.*, Eller v. Nationsbank of Texas, 975 S.W.2d 803, 807 (Tex. App. 1998) (upholding a term absolving bank of all liability for loss to safe deposit box content, noting "[h]aving signed it, she is bound by its terms"). *But see* WHITE & SUMMERS, *supra* note 17, § 4-7, at 169 (noting that courts have yet to give an answer to this question). Murray notes that in American contract law, "[t]he overriding reluctance to excuse a party from the terms of a record he has signed continues as a brooding omnipresence." John E. Murray, Jr., *The Emerging Article 2: The Latest Iteration*, 35 DUQ. L. REV. 533, 565 (1997). It is especially strong in a business context, even where the signer cannot read the language of the document. *See, e.g.*, MCC-Marble Ceramic Center, Inc. v. Cermanica Nuova d'Agostino, S.p.A., 144 F.3d 1384, 1386 n.5 (11th Cir. 1998) ("We find it nothing short of astounding that an individual, purportedly experienced in commercial matters, would sign a contract in a foreign language and expect not to be bound simply because he could not comprehend its terms."). But under German law, the contract partner ordinarily will be deemed to have accepted foreign language standard terms only if they are in the language in which contract negotiations took place. Schmidt *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, KOMMENTAR ZUM GESETZ ZUR REGELUNG DES RECHTS DER ALLGEMEINEN GESCHÄFTSBEDINGUNGEN 277 (9th ed. 2001) [hereinafter ULMER/BRANDNER/HENSEN, AGB-GESETZ]. Speidel, long before he became Reporter for Revised Article 2, argued against "writ[ing] off the individual consumer who should have reasonably understood that a risk was allocated to him." Richard E. Speidel, *Unconscionability, Assent and Consumer Protection*, 31 U. PITT. L. REV. 359, 364 (1970). He called for eliminating any requirement of assent for consumers and testing consumer general terms only against "oppression." *Id.* at 374-75. *Cf.* WHITE & SUMMERS, *supra* note 17, § 4-7, at 169 ("Courts probably delude themselves when they assume that the prominence of a printed clause brings it to the buyer's attention and thus gives buyer a more 'meaningful choice.'").

55. CALAMARI & PERILLO, *supra* note 30, § 9.45, at 390.

56. *Cf.* WHITE & SUMMERS, *supra* note 17, § 4-3, at 156 (giving as an example, "I have the right to cut off one of your child's fingers for each day you are in default").

57. *See, e.g.*, Smith v. Professional Claims, Inc., 19 F. Supp. 2d 1276, 1280 (M.D. Al. 1998) (noting that "the doctrine of unconscionability is reserved for egregious cases"). *Cf.* WHITE & SUMMERS, *supra* note 17, § 4-2, at 154 ("gross advantage-taking").

58. *But see* MUNZ, *supra* note 33, at 225-26 (arguing that the goal of American law is to create a fictitious equality of the parties).

courts have attempted to give a more concrete definition to unconscionability, no generally accepted tests have emerged.[59] The cases are said to be too fact specific to lead to a useful body of case precedent.[60]

Two alternative tests have been proposed: that of Restatement section 211[61] and that of "reasonable expectations." Under Restatement section 211(3), "Where the other party has reason to believe that the party manifesting such assent would not do so if he knew that the writing contained a particular term, the term is not part of the agreement." The Restatement test has not been frequently applied. A few years ago one review found only forty-three reported decisions applying this test, of which twenty-five came from Arizona.[62] As this provision has been applied, courts have focused on the expectation of the party manifesting assent rather than the drafter of the terms, notwithstanding that the language suggests a contrary focus.[63] This has resulted in the Restatement test becoming more like the "reasonable expectations" test.[64]

The reasonable expectations test invalidates a term that lies outside what a party might reasonably expect. The reasonable expectations test has been applied mostly to insurance contracts, particularly where the fine print negated the insured's purpose in acquiring the insurance.[65] Both the Restatement and reasonable expectations tests look to the expectations and intentions of the particular parties to the transaction.[66]

In important respects all three approaches are similar as applied. They provide general clauses with somewhat different tests. They do not provide separate regimens for incorporating terms into contracts. They do not give specific types of objectionable terms. Their focus is on the individual parties and is case-specific. They do not develop abstract and generalizing rules. They are all said to follow Llewellyn's concept of "blanket assent" which is said to be "best understood to mean that, although consumers do not read

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59. Swanson, *supra* note 17, at 366.

60. SLAWSON, *supra* note 17, at 57.

61. RESTATEMENT § 211 reads in full:

§ 211 Standardized Agreements

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

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

(3) Where the other party has reason to believe that the party manifesting such assent would not do so if he knew that the writing contained a particular term, the term is not part of the agreement.

62. James J. White, *Form Contracts Under Revised Article 2*, 75 WASH. U. L.Q. 315, 324-25 (1997).

63. Hillman & Rachlinski, *supra* note 1, at 459.

64. *Id.*

65. *Id.*

66. But the Restatement test "seems to be suggesting a new kind of objective approach to standardized agreements. Rather than seeking out true assent on a case by case basis, it places the duty on the courts to consider the essential fairness of the printed terms, both from the viewpoint of surprise and inherent one-sidedness." CALAMARI & PERILLO, *supra* note 30, § 9.45, at 391. Had American contract law gone in that direction, it would be similar to the contract model of German law. *See infra* Part IV.B.

standard terms, so long as their formal presentation and substance are reasonable, consumers comprehend the existence of the terms and agree to be bound to them."[67]

Section 2-302 provides only one mechanism for dealing with unconscionable terms: a court may choose not to enforce them. That mechanism, of course, assumes that the user seeks to enforce the unconscionable term. Section 2-302 makes no provision for damages, injunctive, or declaratory relief. It provides no authorization for proactive action by an administrative or other public law body. It is the same for both the Restatement and the reasonable expectations tests. As a result of the method of enforcement, use of unconscionable terms is practically a no-risk proposition. If one party uses the term and the other party does nothing, one wins. If the other party has the wherewithal to challenge the term, if the challenge is unsuccessful, the party using the term wins. If, on the other hand, the party challenging the term wins, the user is no worse off than if he or she had never used the term at all. He or she can now redraft the term in slightly different language and use it again.[68]

Unconscionability, in any case, has proven to be a hard standard to meet: only a small handful of cases—according to one count, just fourteen in one ten-year period—did.[69] Judge Posner noted some years ago that Indiana was "so unfriendly to the defense of unconscionability" that in more than twenty years there was only one reported case where it was accepted: a clause, untitled, in fine print, whereby a high school drop-out guaranteed a multinational oil company against the consequences of its own negligence.[70]

So how is the American approach of unconscionability judged? A current consumers' guide published by the American Bar Association concludes in typical telegraphic text that the rule's application is "uncommon, uneven, and unpredictable."[71] Most scholarly commentators would probably agree. Standard works on contracts[72] and studies of unconscionability suggest as much.[73] Section 2-302 is extremely difficult to defend as a working rule and hardly anyone does.

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67. Hillman & Rachlinski, *supra* note 1, at 461.

68. SLAWSON, *supra* note 17, at 143. Of course, the careful user in the occasional challenge case will settle that case so as not to risk an adverse decision on the term that might hinder its future use. *See* Swanson, *supra* note 17, at 387. For a discussion of the infirmities of enforcement through litigation, see Bates, *supra* note 15, at 6-7, 18-28.

69. U.C.C. Revised art. 2, § 2-105 (Discussion Draft 1997). The actual number of cases is debated, but the fact that the number is in the tens or hundreds rather than in thousands or higher seems clear.

70. Amoco Oil Co. v. Ashcraft, 791 F.2d 519, 522-23 (7th Cir. 1985).

71. ABA Guide to Consumer Law, Chapter 3, http://www.abanet.org/publiced/practical/books/consumer/home.html (last visited Dec. 15, 2002).

72. *See* CALAMARI & PERILLO, *supra* note 30, § 9.45 (finding inconsistency in which theory should be applied, and a lack of uniformity in the results reached in similar cases); FARNSWORTH, *supra* note 17, § 4.28 ("[That] the term is incapable of precise definition is a source of both strength and weakness."); WHITE & SUMMERS, *supra* note 17, § 4-3, at 155 (noting that the test of unconscionability is "nearly useless").

73. *See, e.g.*, Bates, *supra* note 15, at 14 n.40 ("The case law is full of inconsistencies, contradictions, and lacks any sort of unifying theme."); Swanson, *supra* note 17, at 386 ("Athough the commentary is mixed, most is negative, and the volume of discontent alone signals a desire for change—for improvement. The most common criticisms stem from the amorphous nature of the doctrine. . . ."). *See also* John E. Murray, Jr., *Unconscionability: Unconscionability*, 31 U. PITT. L. REV.

Instead of admiring how well it works, supporters of section 2-302 emphasize that alternatives are likely to be worse. When section 2-302 originated, it was subject to much controversy. There was much fear that it would disrupt the commercial world. Llewellyn surely did not have disruption in mind when he proposed section 2-302, but, just as surely, he did hope that section 2-302 would lead to judicial development of a "machinery for striking down"[74] improper terms that would permit courts to "police explicitly against the contracts or terms which they find to be unconscionable."[75] The feared disruption has not occurred.[76] But the cost has been that the provision is rarely enforced and has little effect on actual business practice.[77]

Advocates of the "alternatives-would-be-worse" approach fall into two basic camps that might be characterized as optimists and pessimists. Optimists like the present law. Some believe that there is no problem[78] or that the market sufficiently discourages opportunism in standard terms.[79] Others feel that section 2-302, with all its warts, works pretty well.[80] Pessimists, on the other hand, concede that section 2-302 does not work well. But they doubt that there is any way to improve on it. They are resigned to a less than satisfactory law. Typically they are inclined to continue with judicial development of unconscionability.[81]

The defenses of section 2-302 are less than satisfying. If oppressive terms are not a problem, then why not simply dispense with the section

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1, 2 (1969) ("The existing case law is not helpful with rare exception—the writers have done little beyond deplore the Delphic nature of the concept or the codification thereof.").

74. LLEWELLYN, *supra* note 32, at 369-70. *Cf.* Murray, *supra* note 37, at 38.

75. U.C.C. § 2-302 (Official Comment 1) (2002).

76. This was already noted in 1970. *See* Robert Braucher, *The Unconscionable Contract or Term*, 31 U. PITT. L. REV. 337, 345 (1970) ("Conservatism in the application of section 2-302, together with refusal to give it punitive or penal effect, have kept it from having any noticeably disruptive effect on the *commercial world*.").

77. *See, e.g.*, SLAWSON, *supra* note 17, at 143; *see also* Eben Colby, Note, *What Did the Doctrine of Unconscionability Do to the Walker Thomas Furniture Company?*, 34 CONN. L. REV. 625 (2002) (reviewing a famous unconscionability case and its impact on the party to it).

78. *See, e.g.*, Letter from Professor Randy E. Barnett, Austin B. Fletcher Professor, Boston University School of Law, to Lawrence J. Bugge, Chairman, Article 2 Drafting Committee (Mar. 9, 1999) at 1, 2, *quoted in* Holly K. Towle, *Mass Market Transactions in the Uniform Computer Information Transactions Act*, 38 DUQ. L. REV. 371, 403 (2000) ("There is no great reservoir of problematic cases in which consumers have been victimized in ways that are not currently redressed by 2-302. I searched hard for such cases to include in my casebook . . . but to no avail. The seas were relatively tranquil. . . .It is an attempt to fix something that is not broken, with the effect of harming both consumers and sellers in the process.").

79. *See, e.g.*, Hillman & Rachlinski, *supra* note 1. *See also* Robert A. Hillman, *Debunking Some Myths About Unconscionability: A New Framework for U.C.C. Section 2-302*, 67 CORNELL L. REV. 1, 25 (1981).

80. *See, e.g.*, Hillman & Rachlinski, *supra* note 1, at 461 ("The current bundle of judicial approaches to policing paper-form contracts reflects Llewellyn's vision and provides a workable solution to the issues raised by paper standard forms."); Swanson, *supra* note 17, at 399 ("As for substantive content, the current Section 2-302 adequately serves its underlying purposes. . . . Despite all the fuss, the more things change, the more they remain the same—and that is not a bad result here."); White, *supra* note 62.

81. *See, e.g.*, John E. Murray, Jr. & Harry M. Flechtner, *The Summer, 1999 Draft of Revised Article 2 of the Uniform Commercial Code: What Hath NCCUSL Rejected?*, 19 J.L. & COM. 1, 40 (1999) ("There is no escape from such a necessarily fluid and vague standard."); Murray, *supra* note 73, at 38 ("any statute is at best dubious, uncertain, awkward, deficient or spotty") (paraphrasing LLEWELLYN, *supra* note 32, at 370); SLAWSON, *supra* note 17, at 144, 174 ; William J. Woodward, Jr., *Neoformalism in a Real World of Forms*, 2001 WIS. L. REV. 971, 1004 (2001).

altogether? Nearly everyone recognizes that application of section 2-302 does not work well. But if standard terms are a problem, then why not do something meaningful about them? There is no apparent reason why one should believe that a law that is rarely applied and that has little sanction when it is applied much affects business behavior. Advocates of the status quo insist upon "hard statistical data" to justify revision.[82] Perhaps they should present data supporting the status quo. One need not look far to see that section 2-302 has invalidated only a tiny number of standard terms. An examination of cases illustrates that even the variety of terms subject to the section is limited. Nevertheless, empirical research into what terms businesses actually use would be welcome.

Mixed judgments of section 2-302 are not limited to the scholarly community. A split in public perception became apparent in the course of the reform of the U.C.C. Then consumer groups largely opposed section 2-302 unconscionability while business interests generally supported it.[83]

C. *The U.C.C. Reform Debacle*[84]

By the late 1980s the U.C.C. seemed middle-aged. Article 2 appeared to need change. Since it had been drafted in the 1940s, it had no provision for software or other forms of computer information. An official study commission created in 1988 recommended that a drafting committee be appointed to propose revisions to Article 2. A committee was appointed and began meeting in 1992.[85]

As originally conceived, Revised Article 2 was to include both the existing law of sales of goods and new law for licensing computer information. It was to accomplish this through an approach known as "hub-and-spoke." Matters common to both types of transactions were to be covered by the "hub," while matters peculiar to one type of transaction were to be covered in their respective "spokes." This approach to drafting is well-known to those familiar with European codes that are divided into "General" and "Special" parts. The approach contributes to consistency and uniformity in the law.[86] In 1995 the leadership of NCCUSL decided to abandon the hub-and-spoke approach in favor of a separate article for software and information, Proposed Article 2B—Licenses. It appointed a separate drafting committee to create a new article.[87]

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82. Swanson, *supra* note 17, at 387.

83. Michael M. Greenfield & Linda J. Rusch, *Limits on Standard-Form Contracting in Revised Article 2*, 32 U.C.C. L.J. 115, 144 (1999).

84. "Debacle" is a term used by the original Reporter for Revised Article 2—Sales, Professor Richard Speidel. *See* Speidel, *supra* note 2, at 612.

85. *See generally* Linda J. Rusch, *A History and Perspective of Revised Article 2: The Never Ending Saga of a Search for Balance*, 52 SMU L. REV. 1683 (1999).

86. On the hub-and-spoke approach generally in the proposed revisions to Article 2, see Greenfield & Rusch, *supra* note 83, at 123; Rusch, *supra* note 85, at 1686; Speidel, *supra* note 2, at 612-13. Professor Rusch was Associate Reporter for Revised Article 2.

87. According to the Reporter for the Article 2 Drafting Committee, Professor Richard E. Speidel, the NCCUSL dropped the hub-and-spoke approach because certain strong software producers and others in industry opposed it. These producers viewed the draft then on the table as too oriented toward consumers. They wanted their own law. Speidel, *supra* note 2, at 619.

The two drafting committees went about their work separately, although they tried to coordinate their work as best they could. Both committees held open meetings in which they welcomed anyone who wished to attend, and many observers did. Nevertheless, consumer interests soon identified the Proposed Article 2B—Licenses Drafting Committee with the software industry, while business interests saw the Revised Article 2 Drafting Committee as anti-business. It thus should not have been a total surprise when, in 1999, ALI, which itself was less identified with business interests, rejected Proposed Article 2B—Licenses, and NCCUSL, which was more identified with business interests, rejected Revised Article 2.[88]

Neither NCCUSL nor ALI was ready to discard nearly a decade's worth of work. Both acted swiftly to rescue something out of the ashes. NCCUSL was able to act first because it could act alone. It is the source of uniform laws; only for the Uniform Commercial Code does it share sponsorship with ALI. By the simple expedient of detaching the proposed law from the U.C.C., NCCUSL could and did promulgate Proposed Article 2B—Licenses without ALI's cooperation. It dubbed the new law the Uniform Computer Information Transactions Act, or "UCITA." Transforming Article 2B—Licenses into UCITA did require sacrificing the aura of association with America's leading uniform law, the U.C.C. Losing that aura may have diminished UCITA's chances for enactment. The criticism that had led to ALI's defeat of Proposed Article 2B—Licenses did not abate. More than three years after UCITA's promulgation, only two states—Maryland and Virginia—have enacted it. In summer 2002 NCCUSL amended UCITA to improve chances for adoption by other states.

ALI, on other hand, could not unilaterally save Revised Article 2—Sales. ALI had to have the cooperation of NCCUSL in order to amend Article 2, which is part of the U.C.C. While ALI was able to save the idea of revision, it could not keep the 1999 proposal intact in the manner NCCUSL was able to maintain Proposed Article 2B—Licenses. After Revised Article 2—Sales was rejected in summer 1999, ALI conferred with NCCUSL and together they appointed a new drafting committee to write a new Revised Article 2—Sales. While that new draft retained features of the defeated proposal, it eliminated much that had been controversial, and generally simplified and scaled back the changes originally proposed. That new draft, somewhat modified, is likely to receive final approval in 2003.[89]

The original Reporter for Revised Article 2—Sales, Professor Richard Speidel, has explained the different courses that the two proposed laws have taken by pointing to the economic interests concerned with them. In the case of UCITA, former Proposed Article 2B—Licenses, there were substantial economic interests behind the legislation. In the case of Revised Article 2—Sales, on the other hand, there was no comparable group pushing for adoption.

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88. In both instances, the leadership of the respective organizations declined to present the proposals to their memberships for a vote. *See id.* at 611, 619.

89. The proposal was approved by NCCUSL at its annual meeting in summer 2002 and by the ALI Council in October 2002. It has only to receive the approval of the ALI Membership at the ALI Annual Meeting in May 2003 to be adopted. *See* Report of ALI Council Consideration of U.C.C. Projects, *supra* note 31.

Indeed, Speidel believes quite the contrary was the case. According to Professor Speidel, "strong sellers" are very pleased by current Article 2—Sales: "Limited only by the porous doctrines of unconscionability and good faith, strong sellers are able to shape the contract to fit their interests, particularly where small business and consumers are involved."[90] He charges that they opposed proposed revisions without themselves offering solutions that they would accept. He suggests that consumer interests were underrepresented in both committees' deliberations.[91]

The U.C.C. reform caused latent discontent with section 2-302 and its treatment of unconscionable standard terms to surface. The two drafting committees that set to work in 1995 had very different views of how they should treat standard terms and unconscionability. The Revised Article 2—Sales Drafting Committee sought to develop a new, stronger rule, while the Proposed Article 2B—Licenses Drafting Committee chose to maintain the status quo. Consumer representatives involved in the process lauded the former and condemned the latter while business representatives tended to do just the reverse.[92]

The Associate Reporter for Revised Article 2—Sales, Professor Linda Rusch, has detailed the Revised Article 2—Sales Drafting Committee's efforts to reform the U.C.C.'s treatment of standard terms contracts.[93] Early drafts of Revised Article 2—Sales distinguished between standard terms and negotiated contracts.[94] Use of standard terms invoked rules that, to prevent unfair surprise, encouraged users to disclose the terms and to obtain informed consent. Not long into the drafting process, however, NCCUSL leadership decided to drop rules that turned on whether a contract used standard terms.[95]

None of the drafts of Revised Article 2—Sales would have created a separate incorporation control; all of them would have controlled incorporation and content together in the same provisions. But the Revised Article 2—Sales Drafting Committee sought to strengthen those provisions' control over content using a new general clause. The Committee's drafts left the unconscionability provision essentially intact and added a new section 2-206 of varying texts. That latter provision would have provided additional safeguards applicable to standard terms in consumer contracts.[96] For a time the Committee focused on a reasonable expectations test and attempted to concretize that standard to meet criticism that it created too much uncertainty.[97] In the end, however, the Committee dropped the reasonable expectations test and settled on one based on commercial fair dealing.

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90. Speidel, *supra* note 2, at 617-18.

91. *Id.* at 618.

92. The author, then a representative of business, was somewhat unusual in his views. While not promoting radical change, he did urge that the Proposed Article 2B—Licenses Drafting Committee adopt some broadening of Section 2-302 in order to make the proposed legislation more enactable.

93. Greenfield & Rusch, *supra* note 83.

94. Speidel, *supra* note 2, at 615.

95. *Id.* at 614-16. Industry objected to special rules for consumers and to rules based on standard terms. *See, e.g.*, Letter from William M. Elliott, Senior Vice President, General Counsel and Secretary, Gateway to Lawrence J. Bugge, Chairman, U.C.C. Article 2 Drafting Committee (Mar. 9, 1999) (on file with author).

96. For the earlier part of the § 2-206 story, see Murray, *supra* note 54, at 563-71.

97. Greenfield & Rusch, *supra* note 83, at 125-26.

The final version of Proposed section 2-206 reads, in part:

> (a) In a consumer contract, a court may refuse to enforce a standard term in a record the inclusion of which was materially inconsistent with reasonable commercial standards of fair dealing in contracts of that type, or, subject to section 2-202, conflicts with one or more nonstandard terms to which the parties have agreed.[98]

The Committee's final proposal, however, protected warranty disclaimers and warranty modifications that met Code requirements from being invalidated. It thus would have preserved for business one of the most valuable uses of standard terms.

1. *Proposed Article 2B/UCITA*

As already noted, standard terms are especially important in the computer information industry. Copyright law does not protect all information and does not always provide the protection that computer information providers need. Because of limited legal protections provided by intellectual property laws, computer information providers need contractual protections. For the industry, the license is the product.[99] Securing the validity of those licenses was one of its major goals in seeking adoption of Proposed Article 2B—Licenses.

The opening position of Proposed Article 2B—Licenses on standard terms was not dissimilar from that of Revised Article 2—Sales. Given their common origin, that is not surprising. Both started off distinguishing standard terms and negotiated terms, required full opportunity to review, and adopted a general clause review along the reasonable expectations line.[100] Their ending points, however, were rather different.

Whereas Revised Article 2—Sales dropped a distinction between standard terms and negotiated terms, UCITA maintained one in its definition of standard form.[101] This enables it to extend its protections not only to

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98. U.C.C. Revised art. 2—Sales (Proposed Final Draft) (May 1, 1999).

99. *See* UCITA, Prefatory Note (2000) ("What rights are acquired or withheld depends on what the contract says. This point only is implicit in Article 2 for goods such as books; UCITA makes it explicit for the information economy where, unlike in the case of a book, the contract (license) is the product."); *see also* Robert W. Gomulkiewicz, *The License Is the Product: Comments on the Promise of Article 2B for Software and Information Licensing*, 13 BERKELEY TECH. L.J. 891, 895-99 (1998). In Germany, in discussing standard terms, the point is made of insurance: "insurance as product of law" ("*Versicherung als Rechtsprodukt*"). Joachim Schmidt-Salzer, *EG-Richtlinie über mißbräuchliche Klauseln in Verbraucherverträgen, Inhaltskontrolle von AVB und Deregulierung der Versicherungsaufsicht*, VersR [VersicherungsRecht] 1995, 1261, text and accompanying note. *See also* J.H. Reichman & Jonathan A. Franklin, *Privately Legislated Intellectual Property Rights: Reconciling Freedom of Contract with Public Good Uses of Information*, 147 U. PA. L. REV. 875, 900-03 (1999); *cf.* Arthur Allen Leff, *Contract as Thing*, 19 AM. U. L. REV. 131 (1970); Margaret Jane Radin, *Humans, Computers, and Binding Commitment*, 75 IND. L.J. 1125 (2000).

100. *See* Greenfield & Rusch, *supra* note 83, at 125 (noting that the October 1, 1995 draft of § 2-206 included the reasonable expectations test; *see also* U.C.C. Revised art. 2B (Licenses with Prefatory Note and Comments § 2B-308(b)(1)) (Feb. 2, 1996), *available at* http://www.law.upenn.edu/bll/ulc/ulc_frame.htm ("[T]he term creates an obligation or imposes a limitation that is not consistent with customary industry practices and that a reasonable licensor should know would cause most licensees in transactions of similar type to refuse the contract if the term were brought to the attention of the licensee. . . .").

101. UCITA § 102(a)(60). *See also* Speidel, *supra* note 2, at 619.

consumers, but to all participants in "mass market transactions."[102] Advocates of UCITA cite this as a significant advance and a "dramatic legal shift."[103] Yet critics say that the distinction makes relatively little difference in the law that was adopted.[104]

Unlike Article 2 and Revised Article 2—Sales, UCITA has a provision directed toward incorporation of standard terms. Originally, section 209(b) provided that standard terms could become effective in a mass market license even though "a copy of the license is not available in a manner permitting an opportunity to review by the license before the licensee becomes obligated to pay."[105] To make this result more palatable, the section gave the licensee a generous right to return at the expense of the licensor. This shift was somewhat less dramatic than it might otherwise have been, however, because before UCITA was drafted, the Seventh Circuit seemed to allow the same result under Article 2.[106] The provision met significant resistance. At its 2002 Annual Meeting NCCUSL revised section 209 to provide that a term does not become part of the license if "the licensee does not have an opportunity to review the term before agreeing to it."[107]

The early drafts of Proposed Article 2B—Licenses followed the test of Restatement section 211(3).[108] In 1997 the Drafting Committee dropped the Restatement test in favor of the unconscionability standard of section 2-302. At the suggestion of the NCCUSL 1998 annual meeting in July, the test was broadened to prohibit terms contrary to "public policy."[109] The public policy provision is to make clear that UCITA does not uphold licenses that are invalid under federal copyright law. The public policy exception was regarded as not changing existing law.[110]

As enacted, UCITA provides that terms in mass market licenses are not enforceable if they are unconscionable, preempted by federal law, or contrary

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102. *See* UCITA § 209.

103. *See, e.g.*, Towle, *supra* note 78, at 379-80 (2000) ("Under UCITA, the customer in a 'mass-market transaction' is afforded what amount to consumer protections, even if the customer is a business. As noted, this represents a dramatic legal shift.").

104. *See* Speidel, *supra* note 2, at 619.

105. UCITA § 209(b).

106. *See* Hill v. Gateway 2000, Inc., 105 F.3d 1147 (7th Cir.), *cert. denied*, 522 U.S. 808 (1997) (enforcing an arbitration clause that the consumer did not receive or review until after receiving the product). But it appears that the court believed that the consumer did have an opportunity to review, which the consumer did not exercise. *Id.* at 1150. The Article 2 Drafting Committee also struggled with this issue and in the end ignored it. *See* Speidel, *supra* note 2, at 616. Gateway's General Counsel advised the Article 2 Committee Chairman of facts indicating that there was an opportunity to review. Letter from William M. Elliott, Senior Vice President, General Counsel and Secretary, Gateway, to Lawrence J. Bugge, Chairman, U.C.C. Article 2 Drafting Committee (Feb. 3 1999) (on file with author). Similarly, *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585 (1991), does not uphold enforcing standard terms where there is no opportunity to review. The *Shute* Court specifically noted that the question of opportunity to review had been conceded. *Id.* at 590.

107. The summer 2002 final amendments are available at http://www.law.upenn.edu/bll/ulc/ucita/2002act.htm.

108. U.C.C. art. 2B—Licenses (Discussion Draft Mar. 21, 1997), *available at* http://www.law.upenn.edu/bll/ulc/ucc2/397art2.htm.

109. U.C.C. art. 2B—Licenses (Discussion Draft Aug. 1, 1998), *available at* http://www.law.upenn.edu/bll/ulc/ucc2b/2b898.pdf.

110. U.C.C. art. 2B Software Contracts and Licenses of Information (Council Draft No. 4, Dec. 1, 1998) § 2B-105 Reporter's Notes at 38-39 (1998), *available at* http://www.law.upenn.edu.

to public policy.[111] Its unconscionability provision in section 111 is a virtual clone of U.C.C. section 2-302. Critics find little to cheer about in UCITA's control of standard terms. According to one, "UCITA's approach to form contracts in commercial transactions can be captured in one word (enforced)."[112] Another characterizes it as "anything goes."[113]

When the Proposed Article 2B—Licenses Drafting Committee backed off the reasonable expectations test of the Restatement, it considered proposals for stricter review of license terms than the unconscionability standard of 2-302, including one dubbed "unconscionability lite."[114] But those against a more stringent test had one argument at their ready disposal: Article 2B—Licenses was supposed to codify existing law and not create new law.[115] They had only to point to that law. The Reporter, Professor Ray Nimmer, himself observed: "With very few exceptions, standard form contract terms are enforceable."[116]

The argument that the proposed law tracks existing law was more persuasive with the Proposed Article 2B—Licenses Drafting Committee and with the NCCUSL Annual Meeting than it has been with consumer advocates and others in the public sector.[117] Outside the rarified air of drafting committees and annual meetings, critics continue to attack UCITA as too friendly to software suppliers and too unfriendly to consumer interests. They include library associations who fear that suppliers will use standard terms to

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111. UCITA §§ 105 (preemption by federal law; contracts contrary to public policy); 111 (unconscionability); 209 (same).

112. Leo L. Clarke, *Performance Risk, Form Contracts and UCITA*, 7 MICH. TELECOMM. TECH. L. REV. 1, 33 (2000).

113. Reichman & Franklin, *supra* note 99, at 906. They propose that UCITA include a standard of "public interest unconscionability" which would read: "All mass-market contracts, non-negotiable access contracts, and contracts imposing non-negotiable restrictions on uses of computerized information goods must be made on fair and reasonable terms and conditions, with due regard for the public interest in education, science, research, technological innovation, freedom of speech, and the preservation of competition." *Id.* at 930 (emphasis omitted).

114. *See* Report of the Nov. 13-15, 1998 Drafting Committee meeting, http://www.2bguide.com/nov98rpt.html. At the meeting,

> [a] committee member argued in favor of placing some kind of "reasonableness" restriction around mass market license terms, referring to the Hazard memo. Other committee members disagreed, noting that the refund right in this section was the tradeoff for allowing terms to be made available after acquisition. The Reporter agreed, and noting that 2B built in the right to say no to the terms, stated that the committee should not allow courts to throw out terms that were neither unconscionable nor in violation of a fundamental public policy. . . . A committee member responded by asking whether people were satisfied with the unconscionability doctrine or not. Some seemed to want to reject a "refusal term" in a license with the beneficial part of the bargain still being held to be enforceable. If there were problems in the real world, the unconscionability doctrine would have been expanded in the last 50 years. The lack of controversy around the unconscionability standard did not support the argument that a refusal term standard is necessary. Another committee member disagreed, stating that unconscionability issues were mostly raised in small claims court, so there was no data to say that people were satisfied with the standard. . . . The comment was then made that earlier there seemed to be an intent to have a new standard on unconscionability (unconscionability lite) but it no longer seemed to be included.

115. The Drafting Committee Chair, Carlyle Ring, in several conversations with the author at different drafting sessions emphasized that in his experience, a proposed uniform law is most likely to be accepted if it can be presented as merely a codification of existing law and practice.

116. Raymond T. Nimmer, *Breaking Barriers: The Relation Between Contract And Intellectual Property Law*, 13 BERKELEY TECH. L.J. 827, 847 (1998).

117. Speidel argues that NCCUSL is more concerned with getting a law enacted, while ALI is more interested in getting it right. *See* Speidel, *supra* note 2, at 608.

limit use of materials in ways not presently limited by copyright law.[118] Only some critics recognize that UCITA, in upholding standard terms, is not departing from existing law.[119] Prospects for nationwide enactment of UCITA are uncertain at best.[120]

2. *Absence of Comparative Law Inquiries*

Both the Revised Article 2—Sales and the Proposed Article 2B—License Drafting Committees spent a great deal of time considering alternatives to section 2-302. The Revised Article 2—Sales Drafting Committee in particular discussed possible new solutions to the problem seemingly endlessly. One can hardly help but wonder whether those discussions might have been quicker and ultimately more productive if only the committees had had knowledge of foreign approaches. They would have been able to observe standard terms control systems more extensive than section 2-302 in actual operation; they would not have had to guess whether such a system was even possible. The Committees would have had models for ways to implement such systems; they would not have been limited to considering only general clause approaches. Comparative law inquiries could have helped overcome our limited abilities either to conceive of or to experiment with alternatives.

At no time during the decade long U.C.C. reform project did either of the Drafting Committees (or anyone else at ALI or NCCUSL) study foreign experiences with standard terms laws. Indeed, the Drafting Committees were

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118. *See, e.g.*, Free Software Foundation, *Why We Must Fight UCITA*, http://www.gnu.org/philosophy/ucita.html ("UCITA will allow the publishers to impose the most outrageous restrictions on you."); Americans for Fair Electronic Commerce Transactions, *What's Wrong With UCITA?*, http://www.4cite.org/what_problems.html; Letter from American Library Association and four other library associations, to Gene N. Lebrun, President of the National Conference of Commissioners on Uniform State Laws 3 (July 12, 1999), http://www.arl.org/info/letters/lebrun7.12.html ("[UCITA] legitimiz[es] shrink wrap or click on licenses which may include terms that inappropriately restrict use by the purchaser or user."). For the concerns of libraries, see James R. Maxeiner, *The New Commercial Law And Public Information Policy: The Libraries and UCITA*, 219, 233 *in* UNDERSTANDING ELECTRONIC CONTRACTING: UCITA, E-SIGNATURE, FEDERAL, STATE AND FOREIGN REGULATION (Practising Law Institute, 2001). For opposition generally, see the website on UCITA for Laura N. Gasaway's cyberspace law course at http://www.unc.edu/courses/law357c/cyberprojects/spring01/ucita.htm.

119. *See, e.g.*, Clarke, *supra* note 112, at 4: "[T]he National Conference of Commissioners on Uniform State Laws . . . has promulgated a comprehensive commercial statute that fails to remedy or even modify the law of form contracts in purely commercial transactions." *See also* Cem Kaner, *Why You Should Oppose UCITA*, 17 COMPUTER LAWYER, 20, at 21-22 (May 2000):

> You might try arguing that the term is unconscionable under UCITA Section 111, but courts are rarely receptive to a business' plea for relief from a contract term on grounds of unconscionability. You might try arguing that this term should not be enforced because something about it violates a fundamental public policy, but I'm not sure which one you would cite.

But see Law Library Association of Maryland, Testimony In Opposition To Maryland House Bill 19, Senate Bill 142, Feb. 3, 2000, http://www.ll.georgetown.edu/aallwash/tm020300b.html. ("UCITA's explicit endorsement of shrink-wrap licenses will make many unfair terms enforceable in court, whereas today many such terms are thrown out.").

120. *See* Michael L. Rustad, *Making UCITA More Consumer-Friendly*, 18 J. MARSHALL J. COMPUTER & INFO. L. 547, 550 (1999). For further information on UCITA and standard terms, see Clarke, *supra* note 112. Even if UCITA is not adopted nation-wide, it may still have helped industry obtain validation of use of standard terms in shrink-wrap and clickwrap licenses.

hardly aware of them. Foreign readers who are accustomed to comparative law studies being made when new legislation is under consideration are sure to be surprised. Their surprise is all the more justified when one considers that (1) at least one American comparativist called the Committees' attention to those solutions,[121] (2) existing American law may have had a foreign inspiration, and (3) just as the Committees began their work, the International Institute for the Unification of Private Law (UNIDROIT) adopted *Principles of International Commercial Contracts* that include some special rules for standard terms.[122] The Reporter for the post-1999 version of Revised Article 2—Sales, Professor Henry Gabriel, explained that the lack of interest in foreign approaches is to be attributed to the law revision process itself, which is focused on the existing law: "This focus tends to be inward-looking—always focused on the existing Code itself, and therefore, the comparisons with other codes, such as the United Nations Convention on Contracts for the International Sale of Goods (CISG) and the UNIDROIT principles, tend to be incidental as opposed to deliberate."[123]

Only recently and outside of the U.C.C. reform process has the United States seen approaches to standard terms that do more than provide variations on a familiar melody. In 1998 the New Jersey Law Revision Commission proposed a new statute to govern standard terms.[124] The proposed statute is unlike anything else ever seen in the United States. Its goal is to protect freedom of contract from pernicious standard terms; it is not a consumer protection statute. It is not limited to a general clause,[125] but identifies specific types of contract issues, which it then approves, prohibits or marks for evaluation.[126] The similarities to European laws are unmistakable.[127] Other

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121. *See supra* text accompanying notes 11-14.

122. UNIDROIT, PRINCIPLES OF INTERNATIONAL COMMERCIAL CONTRACTS (1994), deals with what is known in the United States as the "battle of the forms" and is not relevant here. Of the other three, article 2.19 defines standard terms. Articles 2.20 and 2.21 provide limited incorporation controls. The former provides that "(1) No term contained in standard terms which is of such a character that the other party could not reasonably have expected it, is effective unless it has been expressly accepted by that party." *Id.* at 58. The latter merely provides that in case of conflict, a term that is not a standard term prevails over a standard term.

123. Henry D. Gabriel, *The Inapplicability of the United Nations Convention on the International Sale of Goods as a Model for the Revision of Article Two of the Uniform Commercial Code*, 72 TUL. L. REV. 1995, 2001 (1998). *See also* Richard E. Speidel, *The Impact of Internationalization of Transnational Commercial Law: The Revision of UCC Article 2, Sales in Light of the United Nations Convention on Contracts for the International Sale of Goods*, 16 J. INT'L L. & BUS. 165 (1995).

124. NEW JERSEY LAW REVISION COMMISSION, FINAL REPORT RELATING TO STANDARD FORM CONTRACTS § 1 (g), at 2 (1998), *available at* http://www.lawrev.state.nj.us. The Commission's Report concluded that existing law does not provide "uniform and flexible standards" and has neither "protected consumers against the opportunism of certain sellers nor has it provided sellers with legal rules based on the logic of the mass market."

125. *Id.* § 8(a). "[A] term is enforceable unless, at the time of sale, the term would have caused a reasonable buyer to reject the sale."

126. *Id.* § 9-12.

127. For example, the New Jersey Commission's associate counsel, John J.A. Burke, wrote the author:

> In reply to your question, the Commission reviewed the European Directive on Unfair Terms in Consumer Contracts as well as the French and German Codes. The Commission followed the European approach in so far as identifying specific issues for legislative governance. However, unlike the European approach, the Commission's Standard Form Contract Act (SFC) is not consumer protection legislation. Rather, it is an attempt to set

than introducing the proposed Act as a bill, the New Jersey legislature has not acted on it. The Commission itself did not produce a study of European laws and presumably did not have the resources to do so. The balance of this article seeks to make a start in that direction.

III. EUROPEAN UNION LAW

Part III addresses control of standard terms in the law of the European Union. Part IV goes on to consider the law in one Member State, Germany. Part IV is necessary because the E.U. law of unfair terms is not directly applicable. There, as in most areas of law, the European Union has chosen to harmonize national laws rather than to adopt a single E.U. law. The device to accomplish harmonization is the directive. Directives are instructions to Member States to adopt laws with particular content. But directives are binding only as to result, and not as to form and method of implementation.[128] The focus of this Part is on the European Union's Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts. Adopted in 1993, the Unfair Terms Directive is the basis of E.U.-wide control of standard terms. It requires Member States to conform their laws to the directive's model.[129]

A. *Origin in Consumer Protection*

The Unfair Terms Directive is consumer protection legislation. The first Europe-wide efforts to address standard terms accompanied the growth of the consumer movement in the 1970s. Even before the European Union looked at unfair terms, a broader and looser group of European States, the Council of Europe, began looking at the issue in 1973. On November 16, 1976, it adopted Resolution (76) 47 on "Unfair Terms in Consumer Contracts and an Appropriate Method of Control" and issued an explanatory memorandum.[130]

> the limits of "freedom of contract" in an area where one party to the contract is the single author seeking to pass virtually all risk to the other party. The SFC Act makes no distinction between merchants and consumers nor does its application depend on the nature of the product that is the subject of the contract, thus unifying the law of contracts for goods, services and intellectual property.

E-mail from John J.A. Burke, Associate Counsel to the New Jersey Law Review Commission, to author (July 8, 2002) (on file with author). *See also* John J.A. Burke, *Contract as Commodity: A Nonfiction Approach*, 24 SETON HALL LEGIS. J. 285 (2000).

In 2002 Professor Larry Bates made an even more radical proposal: standard terms should be presumed invalid; the relationship between user and the other party should be regarded as a "status relationship" subject to regulation; and that an administrative body should approve use of standard terms. Significantly, he drew inspiration from foreign experiences. Bates, *supra* note 15, at 90-105.

128. *Id.* at 326-31, 792-94. Directives contrast with "regulations," which are applicable generally, are binding in all respects and are directly applicable. *Id.* at 324. *See generally* Peter-Christian Müller-Graff, *EC Directives as a Means of Private Law Unification*, *in* TOWARDS A EUROPEAN CIVIL CODE (Arthur Hartkamp et al. eds., 2d rev. ed. 1998).

129. Report from the Commission on the Implementation of Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts, COM (2000) 248 final (noting that Germany, the Netherlands, Portugal, and the Nordic countries had only to amend their laws) [hereinafter E.U. Commission Report].

130. *Unfair Terms in Consumer Contracts and an Appropriate Method of Control, Resolution (76) 47 of the Comm. of Ministers*, Council of Europe, 262d Meet. (1977).

The Resolution noted that consumers were increasingly offered goods and services on terms that prejudice their interests but which they had no power to amend. The resolution's first recommendation was to encourage Council members to adopt legislation to protect consumers "against unfair terms in contracts based on standard texts and in other contracts where the consumer has little, if any, possibility of negotiating or influencing their content." The scope of the resolution was limited to consumers, but with respect to consumers it applied to consumer contracts generally and not just to standard terms. The resolution addressed both incorporation and content.

The accompanying explanatory memorandum found the source of the problem in the essence of standard terms. Suppliers generally have the advantage in drafting standard contract forms. Individual consumers rarely negotiate those terms and, if they do, they seldom have bargaining power sufficient to protect their interests. The principle of freedom of contract permits suppliers through use of standard terms to impose on consumers terms that "satisfy the suppliers' interests but disregard the interests of the consumers."[131] The explanatory memorandum gives a non-exhaustive list of twenty-eight terms considered to be unfair in the majority of member States. It classes those terms into six broad general classes: terms regarding formation, termination, and performance; terms limiting the liability of the supplier; terms limiting the consumer's rights or remedies; terms relating to security; terms relating to disputes; and other terms. The specific terms are familiar. A few examples from the list are given in the margin.[132]

The European Union itself first raised the issue of one-sided standard terms in 1975 when the Commission, the E.U.'s principal governing body, issued its first consumer protection proposals. In the 1970s a number of E.U.

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131. *Id.* at 11.

132. Examples include:

4. Terms whereby a contract will continue in being for an unreasonably long period unless terminated by the consumer by a specified date. . . .

6. Terms whereby the supplier reserves the right to decide unilaterally whether the goods are in conformity with the contract or not. . . .

8. Terms whereby the goods need not correspond with those elements of their description which are essential to the consumer or with the sample or need not be fit for the purpose communicated by the consumer and accepted by the supplier or in default of such communication with their normal use. . . .

9. Terms whereby the supplier can without reasonable grounds withhold the fulfillment of his obligations. . . .

12. Terms whereby the liability of the supplier is either excluded or limited to an unjustified extent. . . .

14. Terms whereby the right of the consumer to repudiate a contract under which the supplier is bound to repair the goods and does not do so within a reasonable time is excluded. . . .

18. Terms whereby the withholding by the consumer of all or part of the payment due, if the supplier does not fulfil his obligations, is prohibited. . . .

21. Terms whereby a consumer is prohibited from claiming a right of set-off against the supplier. . . .

25. Terms which impose a burden of proof on the consumer which normally would lie on the supplier. . . .

26. Terms which impose on the consumer an unreasonably short period of time to make complaints to the supplier. . . .

27. Terms whereby, without good reason, the consumer is required to have goods repaired by the supplier exclusively or to obtain replacement parts only from him.

Id. at 14-16.

Member States adopted national standard terms legislation.[133] Only weeks after the Council of Europe issued its recommendations, the German legislature adopted the Standard Terms Statute.[134] In 1976 the Commission issued a preliminary draft directive of standard clauses in consumer contracts. That proposal died.[135]

Throughout the legislative processes in Europe comparative law played a part. In 1978 the Council of Europe made standard terms the subject of its Eighth Annual Legal Colloquy on European Law. The colloquy included reports on standard terms law in the United Kingdom, Germany, Israel, Sweden, Cyprus, and Ireland.[136] In 1984 the Commission of the European Union returned to the issue of unfair terms and issued a working paper on abusive clauses in consumer contracts.[137] Before issuing a draft directive, it commissioned a comparative study of the law in the Member States of the European Union and elsewhere.[138]

In 1990 the Commission again proposed a draft directive on unfair terms. The Union adopted the final version of the Unfair Terms Directive on April 5, 1993.[139] It required Member States to implement it by December 31, 1994. Adoption of the Unfair Terms Directive was part of a larger initiative in the consumer protection area. In 1992 a new article was added to the E.U. Treaty that specifically directs the Union to address the interests of consumers.[140] Several other directives also provide consumers protection.[141]

B. *The Unfair Terms Directive*

The Unfair Terms Directive is a "minimum" directive, that is, it sets out minimum standards. Article 8 explicitly permits Member States to maintain or

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133. *See* Ewoud H. Hondius, *Unfair Contract Terms: New Control Systems*, 26 AM. J. COMP. L. 525, 525-26 (1978).

134. AGB-Gesetz, *supra* note 10. *See* Otto Sandrock, *The Standard Terms Act 1976 of West Germany*, 26 AM. J. COMP. L. 551 (1978).

135. Ulmer *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 82, margin no. 66.

136. *Standard Terms in Contracts: Proceedings of the Eighth Colloquy on European Law*, Council of Europe, (1979).

137. *See* E.U. Commission Report, *supra* note 129, at 5; Hermann-Josef Bunte, *Zehn Jahre AGB-Gesetz—Rückblick und Ausblick*, NJW [Neue Juristische Wochenschrift] 1987, 921, 921.

138. Note, *Commission of the European Communities Amended Proposal for a Council Directive on Unfair Terms in Consumer Contracts*, 15 J. CONSUMER POL'Y 97 (1992), (*citing* EWOUD HONDIUS, UNFAIR TERMS IN CONSUMER CONTRACTS (1987)). *See also* HONDIUS, STANDAARDVOORWAARDEN: RECHTSVERGELIJENKE BESCHOUWINGEN OVER STANDAARDISERING VAN KONTRAKTSBEDINGEN EN OVERHEIDSTOEZICHT DAAROP (1978) (with summaries in French at 835-44, in English at 845-54, and in German at 855-65).

139. Council Directive 93/13/EEC, 1993 O.J. (L. 95) 29 [hereinafter Unfair Terms Directive]. For a brief recounting of the chronology, see E.U. Commission Report, *supra* note 129, at 5.

140. Now Article 153 of the Treaty Establishing the European Community (incorporating the changes made by the Treaty of Amsterdam amending the Treaty on European Union, the Treaties establishing the European Communities and certain related acts). Its paragraph 1 provides:

> In order to promote the interests of consumers and to ensure a high level of consumer protection, the Community shall contribute to protecting the health, safety and economic interests of consumers, as well as to promoting their right to information, education and to organise themselves in order to safeguard their interests.

141. *See* P.J.G. KAPTEYN & P. VERLOREN VAN THEMAAT, INTRODUCTION TO THE LAW OF THE EUROPEAN COMMUNITIES: FROM MAASTRICHT TO AMSTERDAM 1108 (Lawrence W. Gormley ed., 3d ed. 1998).

to adopt "more stringent provisions" in order to ensure "a maximum degree of protection for the consumer."[142]

The Unfair Terms Directive is limited to contracts with consumers, *i.e.*, natural persons acting for purposes outside their trade, business, or profession.[143] It does not require that Member States control standard terms that are used between non-consumers, although the laws of some Member States do.[144] As originally proposed, it would have applied to all terms in all contracts with consumers. As a result of Member State criticism, the scope of the directive was narrowed. As adopted it does not apply to terms that have been "individually negotiated."[145] "[P]re-formulated standard contracts" are not individually negotiated.[146] It excludes from content review the "main subject matter of the contract" and the "adequacy of the price and remuneration."[147]

The Unfair Terms Directive has no specific provision that governs incorporation into contracts. It is debated whether the "transparency" provision of Article 5—which requires that when in writing "terms must always be drafted in plain, intelligible language"—should be regarded as an incorporation control or a content control."[148] The principal problem with that interpretation is practical: as presently structured, for a term to be invalidated, it must be unfair under the content control of Article 3.[149]

Control of the content of terms is the heart of the Unfair Terms Directive.[150] The control consists of a general clause, essentially in Article 3, and a list of exemplary unfair terms in an Annex. Article 6(1) provides that "unfair terms" as defined in Article 3 shall not be binding on consumers in contracts with sellers or suppliers. Article 3(1) requires that a contract term shall be regarded as unfair "if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer."[151] Although the language of Article 3(1) suggests that two separate criteria must be met, *i.e.*,

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142. Unfair Terms Directive, *supra* note 139, art. 8.

143. *Id.* art. 2(b). The European Court of Justice rejected the idea that "consumers" includes non-natural persons. Joined Cases C-541 & 542/99, Cape Snc v. Idealservice Srl, 2001 E.C.R. I-09049.

144. Germany, for example. *See infra* text accompanying notes 243-44.

145. Unfair Terms Directive, *supra* note 139, art. 3(1). *See infra* text accompanying notes 325-33.

146. Unfair Terms Directive, *supra* note 139, art. 3(2).

147. *Id.* art. 4(2). Terms dealing with those issues must still be "in plain intelligible language."

148. *Workshop 4: Obligation of Clarity and Favourable Interpretation to the Consumer (Art. 5), in* The Integration of Directive 93/13 into the National Legal Systems 158 (1999), *available at* http://europa.eu.int/comm/dgs/health_consumer/events/event29_04.pdf [hereinafter Integration of Directive 93/13]. The same article further provides that when in doubt, terms are to be given the interpretation most favorable to the consumer. In favor of regarding Article 5 as an incorporation control is the twentieth recital of the Preamble of the Unfair Terms Directive, which states: "whereas contracts should be drafted in plain intelligible language, the consumer should actually be given an opportunity to examine all the terms . . . ." Unfair Terms Directive, *supra* note 139, art. 5.

149. *Id.* Item (i) in the Annex to the Unfair Terms Directive, which provides that a term may be found unfair if it precludes an opportunity to review prior to the contract becoming binding, raises the same issue. *See also infra* note 336 (discussing German Code placement of transparency under the content control).

150. *See Workshop 3: The Definition of "Unfairness": The Application of Art. 3(1), 4(1)—and of the Annexes of the Directive, in* Integration of Directive 93/13, *supra* note 148, at 132 [hereinafter *Workshop 3*].

151. Unfair Terms Directive, *supra* note 139, art. 3(1)

significant imbalance and action contrary to good faith, the official position is that any clause that causes a significant imbalance is by definition contrary to the principle of good faith.[152] Perhaps because the Unfair Terms Directive is not directly applicable law, this point has not been as significant an issue as it might otherwise have been. It is in effect resolved by the implementing language that a particular Member State uses. Article 4(1) provides that the unfairness of a term is to take into account "all the circumstances attending the conclusion of the contract." But, as already noted, national law is not to judge whether the contract itself is unfair.[153]

A separate Annex lists seventeen different specific types of terms that may be considered unfair.[154] The list is "indicative" only, that is, a contractual term on the list is not automatically deemed unfair but only subject to evaluation.[155] The terms identified in the list, rather than the language of the general clause itself, are to serve as "the first and the essential reference point in answering the questions: what is unfairness? when are there grounds for considering a clause as unfair?"[156] Since the Unfair Terms Directive is a minimal directive, Member States may completely prohibit terms in the Annex. Some Member States have done so. There have been proposals that the Unfair Terms Directive itself should be amended to consist of both a list of terms subject to evaluation and a prohibited list.[157] A few of the items on the list may be discussed briefly here.

Item (b) of the Annex to the Unfair Terms Directive has been the most frequently litigated class of term.[158] It permits finding a term unfair and thus unenforceable if the term has the object or the effect of inappropriately excluding or limiting the legal rights of the consumer *vis-à-vis* the seller or supplier or another party in the event of total or partial non-performance or inadequate performance by the seller or supplier of any of the contractual obligations, including the option of offsetting a debt owed to the seller or supplier against any claim which the consumer may have against him. Item (b) recently lost significance when the European Union took a still more aggressive approach to the issue of guarantees. In Directive 1999/44/EC of the European Parliament and of the Council of 25 May 1999 on certain aspects of the sale of consumer goods and associated guarantees (the "Guarantees Directive"), it made certain guarantees mandatory. No review of terms for unfairness is necessary where the law makes the terms mandatory.[159]

Item (i) of the Annex to the Unfair Terms Directive is particularly significant in connection with shrink-wrap and click-wrap licenses. It provides that a term may be found unfair if it has the object or effect of "irrevocably binding the consumer to terms with which he had no real opportunity of

152. *See id.* at 141.

153. *See infra* text accompanying note 147.

154. The European Court of Justice has held that it is not necessary that the list itself be enacted into positive law. *See infra* text accompanying note 170.

155. E.U. Commission Report, *supra* note 129, at 16.

156. *Workshop 3*, *supra* note 150, at 137.

157. *Id.* at 138.

158. E.U. Commission Report, *supra* note 129, at 16.

159. For a discussion of the effect of the Guarantees Directive on German law, see *infra* text accompanying notes 357 to 359.

becoming acquainted before the conclusion of the contract." This incorporation control is at odds with the original version of UCITA section 209 that authorized this very type of term.[160]

Item (q) of the Annex to the Unfair Terms Directive calls for evaluating, among other terms, a term "excluding or hindering the consumer's right to take legal action or exercise any other legal remedy, particularly by requiring the consumer to take disputes exclusively to arbitration not covered by legal provisions." The European Court of Justice held that this provision renders invalid forum selection clauses with consumers.[161] The court found that a clause that selected the seller's principal place of business which was far from the consumer's domicile (but in the consumer's home country) "must be regarded as unfair within the meaning of Article 3 of the Directive in so far as it causes, contrary to the requirement of good faith, a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer."[162]

As noted Article 6 provides that unfair terms shall not be enforced. But the Unfair Terms Directive is concerned with more than invalidating objectionable terms. It seeks affirmatively to stamp them out. Article 7(1) requires Member States to ensure that "adequate and effective means exist to prevent the continued use of unfair terms." The Unfair Terms Directive does not limit the means chosen. It does not require a particular form of judicial or administrative proceeding. Leaving aside measures not available throughout the European Union, two procedures that are available in all countries to help stamp out unfair terms might strike American lawyers as unusual. The European Court of Justice held recently that effective protection of consumers requires that national courts of their own motion determine whether a term is unfair.[163] The second measure is the consumer association action required by Article 7. Its Paragraph 2 requires that consumer groups be authorized to bring actions "to prevent the continued use of such terms."[164] It requires further that these actions may be directed against sellers collectively and not just against a single seller.[165] These measures are designed to overcome the infirmities of private litigation where ordinarily the judgment affects only the party before

160. *See supra* text accompanying note 105.

161. Case C-240/98, Océano Grupo Editorial SA v. Rocío Murciano Quintero, 2000 E.C.R. I-4941.

162. *Id.* at I-4973.

163. *Id.* at I-4976. The Court reasoned that "the system of protection introduced by the Directive is based on the idea that the consumer is in a weak position vis-à-vis the seller or supplier, as regards both his bargaining power and his level of knowledge." It noted that "[i]n disputes where the amounts involved are often limited, the lawyers' fees may be higher than the amount at stake, which may deter the consumer from contesting the application of an unfair term." *Id.* at I-4973.

164. Unfair Terms Directive, *supra* note 139, art. 7(2):

> The means referred to in paragraph 1 shall include provisions, whereby persons or organizations, having a legitimate interest under national law in protecting consumers, may take action according to the national law concerned before the courts or before competent administrative bodies for a decision as to whether contractual terms drawn up for general use are unfair, so that they can apply appropriate and effective means to prevent the continued use of such terms."

165. Unfair Terms Directive, *supra* note 139, art. 7(3).

the court, and not the world at large (i.e., inter partes, but not ergo omnes), and only for that one specific term.[166]

Article 6(2) of the Unfair Terms Directive requires that Member States take steps to ensure that the directive's protections are not circumvented by choice of non-European Union law. This requirement, however, applies only if the consumer has a close connection "with the territory of the Member States."

C. *Implementation in the Member States of the Unfair Terms Directive*

Member States must conform their laws to the requirements of directives. Conformity does not mean uniformity; the actual implementation of directives varies significantly from Member State to Member State. Although directives are often quite detailed, a review of their provisions can give only a partial picture of the applicable law. This is the case with the Unfair Terms Directive, which is less specific than some other directives. Part IV of this article discusses the application of the Unfair Terms Directive in Germany and gives a picture of how the directive actually works in practice in one country. This section provides an overview of the steps that have been taken to implement the directive throughout the European Union, but does not address the actual law in each of the Member States.[167]

The Unfair Terms Directive instructed the Commission to report on the directive's implementation after five years. The Commission delivered its report in April 2000 ("Commission Report"). The Commission Report includes a list of the implementing statutes in the Member States.[168] Detailed reports on implementation in the individual Member States were included in the papers of a conference held prefatory to the issuance of the Commission's Report.[169]

The Commission reported that it had brought proceedings before the European Court of Justice against all the Member States for infractions in implementing the directive, but that most of these proceedings had been concluded without the Court having to issue a judgment. Subsequent to the Commission Report, the Court has issued several judgments on implementation. The only judgment of the Court that went against the Commission was the case against Sweden, where the Court held that Sweden did not need to include the Annex of the Unfair Terms Directive verbatim in its positive law, since the Annex was merely exemplary and since Sweden both included the Annex in the legislative history and actually dealt directly with most of the terms contained in the Annex in its law.[170]

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166. *See* E.U. Commission Report, *supra* note 129, at 22-23.

167. For a short survey of the law in all E.U. Member States plus Switzerland, see Ulmer *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 99-120. *See also* Integration of Directive 93/13, *supra* note 148 (with reports in English and French on many Member States).

168. E.U. Commission Report, *supra* note 129, at 38

169. *See* Integration of Directive 93/13, *supra* note 148.

170. Case C-478/99, Commission v. Kingdom of Swed., 2002 E.C.R. I-04147. The Court held for the Commission in C-144/99, Commission v. Kingdom of the Neth., 2001 E.C.R. I-03541 (finding that the Netherlands failed to fulfill its obligations under the Unfair Terms Directive by not transposing Articles 4(2) and 5, concerning transparency, into Dutch law) and in Case C-372/99, Commission v. Italy, 2002 E.C.R. I-00819 (finding that Italy failed to fulfill its obligations under the Unfair Terms

The Commission also reported on its own efforts to implement the directive. These included subsidizing dialogues between consumers and industry at both the national and European levels, subsidizing legal actions for injunctions brought by consumer groups to eliminate unfair terms, conducting information campaigns, sponsoring a conference on implementation of the directive in Member States, and working to develop empirical data on unfair terms.[171] The last mentioned is among the more interesting from an American perspective.

While in the United States a well-represented view holds that the incidence of "unconscionable" terms in contracts is low, there is no comparable position in Europe. Nevertheless, on both sides of the Atlantic participants in discussions of standard terms have lamented the absence of empirical data that might confirm the existence of a problem and disclose its extent.[172] The Commission undertook as part of its mission of implementing the directive a program to fill that gap. There were two basic components to that effort: market studies and a case-law database. Its report summarizes the results of seven different market studies that examined use of unfair terms in contracts in a variety of industries and countries.[173]

In order to monitor implementation of the directive, the Commission set up for an initial five-year period a data base, accessible to the public, to include all known legal decisions regarding unfair terms (the "CLAB" Database). The CLAB database includes files based on specific contractual terms challenged in legal action as unfair. Although the collection focuses on consumer contracts, CLAB also includes decisions regarding terms strictly between non-consumers. In its initial five years of operation the database accumulated 7649 cases.[174] About 3000 of these cases predated the directive. About one third of the Commission Report is devoted to an annex giving statistics from the CLAB database.[175] The Commission has now asked for bids to carry on the CLAB database for five more years.[176]

In its report the Commission left no doubt that it believes that unfair terms in consumer contracts are a real problem. It concluded that "balanced contractual relations are anything but the rule, that unfair terms are widely

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Directive by only prohibiting the actual use of unfair terms, and not the recommendation of the use of unfair terms, as required by Article 7(3)). Looking to the Netherlands case, the German legislature adopted into statutory law a rule that had been applied through judicial interpretation. *See infra* note 337.

171. E.U. Commission Report, *supra* note 129, at 9-12. The conference took place in Brussels July 1-3, 1999. The Papers are collected in Integration of Directive 93/13, *supra* note 148. The proceedings are an exercise in practical comparative law, including both reports on the laws governing unfair terms in most of the Member States as well as special sector reports and comparative overview reports.

172. *See, e.g.*, Kötz, *supra* note 18, at A11-A12; Llewellyn, *supra* note 41, at 700 n.3, 703-04. *See supra* text accompanying notes 82-83.

173. *See* E.U. Commission Report, *supra* note 129, at 9, 39-41.

174. *Consumer Policy: Commission Aims To Update Unfair Terms Data Base*, EUR. REP., section 2583, Apr. 7, 2001.

175. E.U. Commission Report, *supra* note 129, at 43-62.

176. *See Consumer Policy*, *supra* note 174; Allgemeine Ausschreibung Nr. DG SANCO 2001/B3/002 bezüglich der Sammlung und Analyse von "Fallrecht" in den Staaten des EWR betreffend mißbräuchliche Klauseln in Verbraucherverträgen für die Jahre 2001-2005, http://europa.eu.int/comm/dgs/health_consumer/library/tenders/call24_de.pdf.

used, and that new types of unfair terms arise by the day."[177] The market studies demonstrated, it contended, not only "the ubiquity of unfair terms in standard-form contracts but also the enormous difficulty of getting hold of the contractual terms before concluding a contract."[178]

D. *The Future of the Unfair Terms Directive*

The Commission Report is not limited to stating the law at the turn of the century. The Commission in its report also raised questions designed "to trigger the widest and most fruitful possible debate on the subject."[179] The Commission referred its report, including its questions for comments, to the Economic and Social Committee, a formal body of the European Union established under the Treaty of Amsterdam to give non-binding advisory opinions. While the Commission Report on a whole was rather upbeat, the Committee's response was less so. Its first conclusion was: "Rather than merely 'approximating' legislation, the main objective of any future revision of Directive 93/13/EC—which is hopefully not far away—must be to truly harmonise and standardise legislation in the Member States in this area."[180]

The Commission revisited the limitations on the directive's scope. It noted that the implementation laws in some Member States did not include all three exclusions contained in the directive, i.e., of non-consumers, of individually negotiated terms, and of the main subject matter of a contract.[181] It asked whether one or more of these limitations should be eliminated. The Economic and Social Committee answered yes: get rid of all three.[182]

The Commission raised relatively few questions about the future of the content control. It noted that in practice, it had not made much difference whether a member state had chosen to adopt the general clause of Article 3(1) almost verbatim or had rephrased it to a greater or lesser extent. More important in the Commission's view was the way in which Member States had transposed the Annex list of suspect terms into national law. The Commission stated its view that the practical effect of the content control would be greater if all Member States would adopt the list and do so in a way that minimized its vagueness and led to published "black lists" of prohibited terms. It asked whether the contents of the indicative list should be given in greater detail or number and whether its nature should be altered.[183] The Economic and Social Committee answered that the list should not be lengthened, but tightened up

177. E.U. Commission Report, *supra* note 129, at 13.

178. *Id.* at 9.

179. E.U. Commission Report, *supra* note 129, at 2.

180. Opinion of the Economic and Social Committee on the Report from the Commission on the Implementation of Council Directive 93/13/EEC of 5 April 1993 on Unfair Terms in Consumer Contracts, 2001 O.J. (C 116) 116, 124 at 10.1 [hereinafter Opinion of the Economic and Social Committee].

181. E.U. Commission Report, *supra* note 129, at 14-15, 31.

182. Opinion of the Economic and Social Committee, *supra* note 180, at 124 ¶ 10.2 and ¶ 10.3. *See infra* text accompanying notes 252-260.

183. E.U. Commission Report, *supra* note 129, at 16-17. Subsequent to this plea, the Commission lost its case seeking to require Sweden to adopt the Annex. The argument the Commission summarized against adopting the Annex was that then the list might limit enforcement of the general provision. One problem in reaching uniformity throughout Europe is that unfairness is measured based on the law otherwise applicable, which varies from Member State to Member State.

and simplified. A "black list" should be created to stand beside the "gray" list.[184]

The Commission noted deficiencies in the transparency requirement. It asked whether changes were needed and whether consumers should be given the right to review terms before concluding a contract.[185] The Economic and Social Policy Committee replied that "[a]ll necessary steps" should be taken.[186]

Many of the Commission's questions, and its most provocative suggestions, relate to what the Commission termed "positive" enforcement. The problem, the Commission asserted, is that the existing system of "negative" enforcement is not enough. While a particular term in a particular contract is deemed unfair, the system of negative enforcement does not prevent others from using the same term found to be unfair or the user of the unfair term from adopting a similar term. Colorfully the Commission commented: "Unfair terms are like the Hydra: cut off one head and others grow in its place."[187]

The Commission posed a whole series of questions related to improving the existing system of negative enforcement and to adopting a new system of positive enforcement. Among the more provocative: Should penalties be introduced to discourage use of unfair terms?[188] Should a procedure be established to declare court decisions to have an effect against everyone?[189] Should an administrative body be established to analyze and prohibit terms?[190] Should actions be taken at a Europe-wide level to eliminate unfair terms?[191]

The Economic and Social Committee was less receptive to changes in enforcement. It found unjustified the Commission's suggestion that civil penalties be applied.[192] It did encourage the Commission to explore the possibility of establishing procedures to make a finding that a term is unfair binding on everyone.[193] It endorsed creating a Community level administrative arrangement and greater use of administrative mechanisms.[194] It stated, however, that a prior approval system was generally inappropriate because it would be "extremely bureaucratic" and still would not guarantee an absence of unfair terms.[195]

The Economic and Social Committee observed a need to clarify the principle of good faith so that it would not lead to different national provisions. Of its own motion the Committee recommended a comparative law inquiry. It asked the Commission and the member states "to jointly

184. Opinion of the Economic and Social Committee, *supra* note 180, at 121 ¶5 and 124-25 ¶10.6.
185. E.U. Commission Report, *supra* note 129, at 18.
186. Opinion of the Economic and Social Committee, *supra* note 180, at 124 ¶10.4.
187. E.U. Commission Report, *supra* note 129, at 24.
188. *Id.* at 20, 23
189. *Id.* at 23.
190. *Id.* at 23-25.
191. *Id.* at 25-27.
192. Opinion of the Economic and Social Committee, *supra* note 180, at 122 ¶6.4.
193. *Id.* at 123
194. *Id.* at 123
195. *Id.* at 124 ¶8.2.1.

explore the possibility of adopting a new approach to this whole area, drawing on U.S. experience with the drafting of framework or standard laws."[196]

The future of these proposals is uncertain. What is clear, however, is that the European Union has taken a strong position that it will protect consumers against unfair terms. Just how that position is implemented in one country is the subject of the next part of this article.

IV. GERMAN LAW

The Unfair Terms Directive, just as any other directive of the European Union, has force only insofar as the fifteen—soon to be twenty-five—member states implement it. In proceedings before the European Court of Justice, the Commission of the European Union acts vigorously to assure that member states implement directives fully and completely. To see how the Unfair Terms Directive actually applies, one must examine national law.

Because directives leave to each member state the form and methods of its implementation, each implementing law is unique to the country adopting it. Ideally, this article would examine the law in each of the member states of the European Union. But no one author could know all the languages and legal systems involved necessary for an examination of fifteen, let alone twenty-five, member states. A consortium would be necessary. For the purpose of this article, it is sufficient to focus on the law of one Member State. Hopefully, similar studies of the laws of other member states will follow publication of this article.

While the law of any Member State could illustrate the implementation of the Unfair Terms Directive, this article examines the law of Germany. There are several reasons for the choice. An obvious economic reason is that Germany, with over eighty million inhabitants, has the largest population of any country in the European Union. Its law presumably governs the most transactions of any Member State's law. But there are more important intellectual reasons to look at the law of Germany first. The German legal system was among the first European legal systems to identify the issue of standard terms and was the first to address the issue systematically. Its Standard Terms Statute was very influential in the drafting of the European directive. As has been noted, its law also may have had a significant influence on American law in its formative stages.[197]

Part IV examines German law and its development in detail. Section A considers the judge-made law that controlled standard terms through 1976. Section B sets out the contract model for controlling standard terms that was developed by the courts and that became the basis of the Standard Terms

196. *Id.* at 121 ¶4.4. Not everyone in Europe is enthusiastic about comparative law inquiries, at least comparative studies with the United States. By a vote of 46 for to 73 against, with 6 abstentions, the Committee voted down a proposal that would have deleted the recommendation quoted in the text for the reason that "U.S. experience with the drafting of framework or standard laws cannot be transposed directly to the European Union. In contrast to the European Union, the United States share uniform legal concepts." *Id.* at 127.

197. Besides such objective factors, there are also important subjective factors: the author knows German and the German legal system.

Statute of 1976. Section C summarizes the principal provisions of the 1976 Standard Terms Statute as it became part of the German Civil Code in 2002.[198] Section D examines how the initial proposals for the E.U. Unfair Terms Directive challenged the contract model in Germany and how German commentators influenced the final form of the Unfair Terms Directive. Finally, Section E discusses how German law applies to American Internet licenses.

A. *German Judge-Made Law*

The German legal system has long provided some control over the use of standard terms. American jurists are used to thinking of the United States as a country of judge-made law, while they see Germany as a country of legislation, yet for three quarters of the last century, German law controlling standard terms was judge-made.[199] In Germany, as in the United States, form agreements achieved widespread use by the end of the nineteenth century. Already in 1871 a statute that imposed liability on railroads also prohibited agreements excluding that liability.[200] Given German insistence that judges have a basis in statute to act, German judges were not quick to challenge standard terms. In 1883 the German Supreme Court (then known as the *Reichsgericht*) held that freedom of contract—in the absence of any legislation—precluded courts from intervening to control standard terms no matter how offensive the terms might be.[201]

When the German Civil Code came into force in 1900, the courts acquired a statutory basis for intervention. That basis was in the general clauses of the Code, especially in sections 138 and 242. The first paragraph of section 138 provides: "A transaction that offends good morals (*gute Sitten*) is void."[202] One might translate "offend good morals" as "unconscionable."[203] Section 242 provides: "Obligations shall be performed in the manner required by good faith [*Treu und Glauben*], with regard to commercial usage."[204] Using these two general clauses, German courts limited enforcement of standard terms.

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198. Gesetz zur Modernisierung des Schuldrechts, Statute for Modernizing the Law of Obligations, v. 26.11.2001 (BGBl. I s. 3138).

199. ZWEIGERT & KÖTZ, *supra* note 23, at 336 (noting that the German law on standard terms is "judge-made law of the purest kind, and in creating it the German courts have done a remarkable and praiseworthy job without parallel elsewhere"). *Accord* Baudenbacher, *supra* note 10, at 341-42 (noting that the law was codified in the AGB and contributed to the E.U. Unfair Terms Directive: "Essentially, all of Europe (with the exception of Switzerland) lives—or will in the near future live—under a law that originated from freely developed judge-made law of the German Supreme Court").

200. *See* Kötz, *supra* note 18, at A38 (discussing Section 5 of the Imperial Liability Statute [Reichshaftpflichtgesetz] of 1871).

201. Judgment of June 16, 1883, RGZ 11, 100 110 (enforcing English language-English law based exclusions of liability). *See* Kötz, *supra* note 18, at A30; Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 531.

202. Dawson, *supra* note 13, at 1046 (providing a comparison of U.C.C. Section 2-302 unconscionability with the general clauses mentioned here).

203. For a discussion of the difficulty of translating Section 138, particularly in connection with standard terms, see OTTO PRAUSNITZ, THE STANDARDIZATION OF COMMERCIAL CONTRACTS IN ENGLISH AND CONTINENTAL LAW 106-07 (1937) (noting the various translations, ranging from "good morals," "boni mores," "public policy" and "unsocial").

204. Dawson, *supra* note 13, at 1044.

Through the 1930s German courts relied principally on the good morals provision of section 138 to police standard terms.[205] Their focus then tended to be on monopoly situations where the party presented with the terms had no choice but to accept them.[206] In 1935 Ludwig Raiser moved the discussion a major step forward by the publication of his post-doctoral dissertation (*Habilitationsschrift*), *Das Recht der Allgemeinen Geschäftsbedingungen,* which provided a thorough analysis of the problems involved under the then-applicable law.[207] Raiser's book was reprinted in 1961 and to this day is cited as a principal source of inspiration in the field.[208] Raiser asked whether there was a misuse of the freedom of contract not only where the user of standard terms has a monopoly position, but also where the user depends upon the indifference or legal inexperience of the other party.[209]

Soon after the reestablishment of a democratic government following the Nazi dictatorship, the reconstituted German Supreme Court (*Bundesgerichtshof*) addressed the issue of control of standard terms. While building on the work of the old Court, the new Supreme Court put its own stamp on standard-terms control.[210] From a technical viewpoint, it shifted from relying on the good morals provision of section 138 to the good-faith provision of section 242.[211] But in addition to this seemingly technical change, the Court's decisions of the 1950s and 1960s set in motion broader changes in thinking that culminated in the Standard Terms Statute. These changes are discussed below in Section B.

Notwithstanding the active role German courts had taken in controlling form contracts,[212] by the early 1970s there was consensus that it was time for legislation. The consumer movement had gathered strength and parties on both sides of the legislative aisle sought its approval.[213] The Ministry of

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205. *See* LUDWIG RAISER, DAS RECHT DER ALLGEMEINEN GESCHÄFTSBEDINGUNGEN 280-83 (1961) (discussing reliance on both provisions and suggestion made to use Section 242).

206. *See* Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 531.

207. Although Raiser's book appeared in the third year of the Nazi dictatorship, it is based on the law in force before 1933. *Cf.* PRAUSNITZ, *supra* note 203, at 106 (noting the "great change" in German law since 1933, that the law discussed pre-dated that change, and that as of 1937 no definite alternative line of decisions in standard terms had developed). Raiser's crucial point of departure that was followed in the 1950s, but since abandoned, was the similarity of standard terms to legal norms. Raiser, *supra* note 205, at 5; *see also* Schmidt-Salzer, *supra* note 99 and accompanying text.

208. *See, e.g.*, Ulmer *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 37-38 (calling it the "path-breaking investigation"); Hans Erich Brandner, *Wege und Zielvorstellungen auf dem Gebiet der Allgemeinen Geschäftsbedingungen*, JZ 1973, 613 (noting that in his "unsurpassed work" Raiser had recognized all the fundamentals of the issues and often the details); ZWEIGERT & KÖTZ, *supra* note 23, at 336 ("pathbreaking").

209. RAISER, *supra* note 205, at 284. *See also* Kötz, *supra* note 18, at A31; Ludwig Raiser, *Vertragsfreiheit heute*, JZ 1958, 1, 7.

210. *See* ZWEIGERT & KÖTZ, *supra* note 23, at 336.

211. Judgment of Oct. 29, 1956, BGHZ 22, 91. *See* Helmut Heinrichs, *Umsetzung der EG-Richtlinie über mißbräuchliche Klauseln in Verbraucherverträgen durch Auslegung Erweiterung des Anwendungsbereichs der Inhaltskontrolle*, NJW 1995, 153, 156; Manfred Wolf & Thomas Pfeiffer, *Der richtige Standort des AGB-Rechts innerhalb der BGB*, ZRP [Zeitschrift für Rechtspolitik] 2001, 303, 304.

212. *See* Dawson, *supra* note 13, at 1103.

213. *See* ZWEIGERT & KÖTZ, AN INTRODUCTION TO COMPARATIVE LAW 358 (Tony Weir, trans., 2d ed. 1992). For the history of adoption of the law, see MARIANNE SCHATZ-BERGFELD, VERBRAUCHERINTERESSEN IM POLITISCHEN PROZESS: DAS AGB GESETZ 62-119 (1984); Brandner, *supra* note 208; Wolfgang Eith, *Zum Schutzbedürfnis Gegenüber Allgemeinene Geschäftsbedingungen*, NJW 1974, 16; Kötz, *supra* note 18, at A9-A11.

Justice established a working group that proposed legislation, while the opposition Christian Democrats prepared a competing proposal. Both drafts were available when, in September 1974, the German Jurists' Association (*Deutscher Juristentag*) considered the issue of standard terms contracts at its biennial meeting.[214] Professor Hein Kötz, one of Germany's leading comparative-law scholars, was commissioned to write a 100-page review of standard terms for the meeting, which he titled "Which Legislative Measures Recommend Themselves for the Protection of the Consumer Against General Terms and Form Contracts?"[215] The title of Professor Kötz's report—provided to him by the Association—is significant. It is "*which* legislative measures" and not, "*whether* legislative measures" are called for.[216] There was little opposition to having some form of strengthened control. Indeed, the political parties all agreed on the final bill and it passed both houses of the German legislature unanimously.[217]

Dissatisfaction with judge-made law was grounded not in its content but in its efficacy. The problem was one of judge-made law generally and not just of judge-made law of standard terms. Above all, judge-made law is limited in its scope. Courts can act only in cases that are brought to them, so their decisions have a limited effect. Court control of terms often did not take place because of the risks of litigation (in Germany, the losing party pays the costs). Courts could control only the most flagrant abuses; they were not seen as well suited to deal with more subtle abuses. Even parties subject to adverse decisions could readily reformulate their standard terms. Judge-made law was criticized for an absence of concrete provisions and for uneven application by lower courts.[218]

Judge-made law also posed a risk that the German legal system takes particularly seriously: that judges might make political decisions. In German

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214. Rolf Stürner, *Die Verhandlungen der Abteilung Allgemeine Geschäftsbedingungen*, JZ 1974, 720.

215. Kötz, *supra* note 18, at A1.

216. Manfred Wolf, *Gesetz und Richterrecht bei Allgemeinen Geschäftsbedingungen*, JZ 1974, 465 (making the same point).

217. Ulmer *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 43, margin no. 19. Bunte notes that between 1974 and 1977, the conviction that there was a need for legislative action was "firmly anchored" in the public, the political parties, and the scholarly community. Bunte, *supra* note 137, at 921-22. Even a foreign observer noted the consensus months before the statute was passed. *See* Dawson, *supra* note 13, at 1117 ("It seems that all now agree on the need for comprehensive legislation."). *See also* Amtliche Begründung zum Regierungsentwurf eines AGB-Gesetztes, Drucksache 7/3919, Teil A5, at 11, *reprinted in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, KOMMENTAR ZUM GESETZ ZUR REGELUNG DES RECHTS DER ALLGEMEINEN GESCHÄFTSBEDINGUNGEN 22-24 (1st ed. 1977) (discussing the political climate and steps taken toward a law). For a contrary view of the law's adoption, see MANFRED THAMM & GERHARD PILGER, TASCHENKOMMENTAR ZUM AGB-GESETZ 41 (1998) (describing the hearing given business interests as a "pure alibi event").

218. For discussions of the problems of using judge-made law, see THOMAS BECKER, DIE AUSLEGUNG DES § 9 ABS. 2 AGB-GESETZ 19-20 (1986); Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 567, margin no. 63; Bunte, *supra* note 137, at 922; Dawson, *supra* note 13, at 1117; Max Dietlein, *Neues Kontrollverfahren für Allgemeine Geschäftsbedingungen?*, NJW 1974, 1065, at 1065 (calling such an action "a lottery with a very high price"); Kötz, *supra* note 18, at A47-A56 (noting that protection by the courts would be really effective only if the party could bring an action against the use of the terms and that action would be effective against all who use such terms); Manfred Wolf, *Vorschläge für eine gesetzliche Regelung der Allgemeinen Geschäftsbedingungen*, JZ 1974, 41, at 41. *See also* Amtliche Begründung zum Regierungsentwurf eines AGB-Geseztes, *supra* note 217, at 20-21. For a comparable discussion of American law, see Bates, *supra* note 15.

understanding, political decisions are for the legislature and for politically responsible executors and administrators. The application of law should be objective. Categorizing certain types of standard terms as unlawful might constitute political decision-making if the illegality of the terms were not already sufficiently set out, explicitly or implicitly, in a statute.[219]

Legislation offered a remedy for these deficiencies and a way to avoid this risk. Legislation is proactive. It can be systematic and have universal effect.[220] It can bring about a reconsideration of standard terms generally in a way that single court decisions cannot. Legislation can thus bring a breadth of application and reduce the incidence of objectionable standard terms. Legislation can provide increased legal certainty.[221] Legislation is the appropriate place for political decisions that approve or disapprove use of particular provisions. In a democratic state, the affected social groups have an opportunity to participate in these political decisions.[222]

Typically in German and other continental legal systems, comparative law inquiries precede substantial legislation.[223] That was the case with the Standard Terms Statute, where such inquiries had an important role in the movement from judge-made law to legislation.[224] In 1967 the Association for Comparative Law (*Gesellschaft für Rechtsvergleichung*) sponsored a symposium at its biennial convention in which experts presented papers setting out the treatment of standard terms in Germany, France, Great Britain, Italy, Switzerland, Scandinavia, and Israel. Ludwig Raiser himself presented the final overall report.[225] He began his report lamenting that he could not

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219. *See* James R. Maxeiner, *U.S. "Methods Awareness" (Methodenbewußtsein) for German Jurists*, *in* FESTSCHRIFT FÜR WOLFGANG FIKENTSCHER 114, (Bernhard Großfeld et al. eds., 1998); JAMES R. MAXEINER, POLICY AND METHODS IN GERMAN AND AMERICAN ANTITRUST LAW: A COMPARATIVE STUDY (1986).

220. Wolf, *supra* note 216, at 465. *Cf.* Dietlein, *supra* note 218; Kötz, *supra* note 18, at A47.

221. Bunte, *supra* note 137, at 922 (noting ten years later a breadth of effect not possible with judge-made law); Stürner, *supra* note 214.

222. Stürner, *supra* note 214. Robert E. Scott, *Is Article 2 the Best We Can Do?*, 52 HASTINGS L.J. 677, 689 (2001) (explaining the death of Revised Article 2: "I think it's naive to believe that a non-governmental, non-elected, elitist body of insiders can ever get those kind of rules right, whatever we mean by 'right.' Consumer issues raise important value choices and difficult normative questions that are best resolved through the ordinary legislative and judicial process."). *See also* MAXEINER, *supra* note 219.

223. *See* Schlesinger, *supra* note 37, at 14-15.

224. *See* Hans Erich Brandner, *Wege und Zielvorstellungen auf dem Gebiet der Allgemeinen Geschäftsbedingungen*, JZ 1973, 613, 613, 618 (noting the comparative law inquiries as one of the distinguishing characteristics of this as the second "generation" of standard terms law and describing them as "important").

225. Ludwig Raiser, *Die richterliche Kontrolle von Allgemeinen Geschäftsbedingungen*, *in* RICHTERLICHE KONTROLLE VON ALLGEMEINEN GESCHÄFTSBEDINGUNGEN 123 (Ernst Caemmerer ed., 1968). There were many other comparative studies. Raiser's nephew did one devoted to the United States. RAISER, *supra* note 42. For other studies from the 1960s that include the United States, see EUGEN AUER, DIE RICHTERLICHE KORREKTUR VON STANDARDVERTRÄGEN (1964) (comparing judicial review of standard form contracts in Germany, Switzerland and the United States); EIKE VON HIPPEL, DIE KONTROLLE DER VERTRAGSFREIHEIT NACH ANGLO-AMERIKANISCHEM RECHT (1963); Eike von Hippel, *The Control of Exemption Clauses—A Comparative Study*, 16 INT'L & COMP. L.Q. 591 (1967). For book-length studies of English law from that time, see THEO KADE, RICHTERLICHE KONTROLLE VON FORMULARMÄSSIGEN HAFTUNGSFREIZEICHNUNGEN IM ENGLISCHEN RECHT (1970) and STANISLAUS PRINZ ZU SAYN-WITTGENSTEIN-BERLEBURG, ALLGEMEINE GESCHÄFTSBEDINGUNGEN IM ENGLISCHEN RECHT: EINE VERGLEICHENDE UNTERSUCHUNG (1969). The Swiss study concluded that the supposedly flexible common law system was much less flexible than the supposedly formalistic civil law system. AUER, *supra*. The Standard Terms Statute did not put a stop to such comparative studies. For two book-

provide empirical studies of the incidence of standard terms and their abuses. Their ubiquity, however, could not be doubted. And so too, Raiser said, was the need for judicial control of their abuses.[226]

Raiser discussed in particular how the presence or absence of content controls impacted controls on incorporation and interpretation. He observed of the courts of different countries that the less emphasis they placed on incorporation and interpretation, the more they were inclined to control content of standard terms directly; and, the more timid they were in controlling content directly, the more likely they were to scrutinize strictly—perhaps too strictly—incorporation and interpretation.[227] While most countries tended to focus on incorporation and interpretation, Raiser reported that German and American courts, the latter with perhaps some reluctance, were increasingly resorting to direct content control. Responding to criticisms that control under section 242 of the German Civil Code was too indefinite, he pointed to the newly adopted section 2-302 of the U.C.C. as another example of a very broad clause.[228]

The legislative history of the Standard Terms Statute demonstrates the importance of comparative inquiry in the legislation. The official government report on the proposed bill devoted a subsection to foreign experiences. It drew attention to the then relatively few statutes that expressly regulated standard terms, in particular the Israeli Standard Contracts Law. It noted that in Sweden and the United States general prohibitions of inequitable terms applied. It took particular note of U.C.C. section 2-302, which it observed was used principally and increasingly against form contracts. It observed that contrary to fears that section 2-302 would endanger legal certainty, groups of cases and approaches were giving the general clause firm contours.[229]

B. *The Contract Model*

Consensus that action was needed contributed to the adoption of the Standard Terms Statute. Equally helpful was a large measure of consensus as to how the statute should limit unfair standard terms without excessively restricting freedom of contract.

Control of standard terms challenges freedom of contract: how can courts control terms in parties' contracts without throwing freedom of contract overboard?[230] Default provisions in contract law permit parties to agree to

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length studies since that have included the United States, see MUNZ, *supra* note 33; WILFRID SCHLOCHTERMEYER, DAS RECHT DER ALLGEMEINEN GESCHÄFTSBEDINGUNGEN IN KANADA MIT BEZÜGEN ZUM DEUTSCHEN, ENGLISCHEN, FRANZÖSISCHEN UND US-AMERIKANISCHEN RECHT (1985) (discussing Canadian law with references to American, English, French, and German law).

226. Raiser, *supra* note 225, at 141 (noting that control was "essential").

227. *Id.* at 138-39. *Accord* Brandner, *supra* note 224, at 614 (noting with a comparison to Italy, that when there are high demands for knowledge of terms, once knowledge is shown, there is an inclination to treat standard form contracts as negotiated contracts); ZWEIGERT & KÖTZ, *supra* note 23, at 335-36. For a recent, similar comment about drafting in America, see Amelia H. Boss, *Taking UCITA on the Road: What Lessons Have We Learned?*, 7 ROGER WILLIAMS U. L. REV. 167, 192 (2001).

228. RAISER, *supra* note 42, at 127-28.

229. Amtliche Begründung zum Regierungsentwurf eines AGB-Geseztes, *supra* note 217, at 21-22.

230. *See* RAISER, *supra* note 42, at 25-35 (discussing the transition from Section 138 to Section 242 and the problems arising from using Section 242 to set limits on private autonomy).

results different from those prescribed by law. If parties assent to those differing results, they are bound by them. If parties use standard terms, when should they be bound by them? The German answer, which the Supreme Court had already begun to develop in the 1950s, is referred to here as the "contract model."[231]

German standard terms law recognizes that when standard terms are used there is little freedom of contract for the party subject to them.[232] While the user typically consults legal counsel to draft them and takes care that the terms work to his or her benefit, the other party rarely does. Thus, though the terms are typically the focus of the user's daily life, the other party is engaged in many transactions, each different from the other. The cost to the other party of exercising the right of freedom of contract is excessive.

Standard terms problems arise because some users exploit their control over drafting to resolve all issues in their favor in order to override results provided by law. Yet, the parties have never agreed on these points. Instead, parties subject to standard terms take those terms as givens. Parties accepting standard terms negotiate principal issues of price and performance and then allow users to provide appropriate terms. In effect, they delegate to users the responsibility to draft terms. Users take upon themselves the obligation to provide suitable terms in good faith.[233] Good faith requires that those terms be even-handed. As the German Supreme Court explained in an early decision:

> [I]t depends upon how to evaluate the statements as the expression of the intention of judicious and honest parties, who want to give their business dealings a general contractual framework. The circumstance has to be taken into account, that the principal [*Auftraggeber*] need not know in detail the content of the standard terms. Since, on the other hand, it needs his assent to be bound, his agreement can relate only to such terms as he can reasonably and fairly expect to be asserted. [234]

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231. *Cf.* Hermann-Josef Bunte, *Gedanken zur Harmonisierung in der EG auf dem Gebiet der mißbräuchlichen Klauseln in Verbraucherverträgen, in* FESTSCHRIFT FÜR HORST LOCHER ZUM 65. GEBURTSTAG, 325, 331 (Peter Löffelmann & Hermann Korbion, eds., 1990) (referring generally to the *Vertragsmodell* of German private law).

232. KARL LARENZ, LEHRBUCH DES SCHULDRECHTS, ERSTER BAND, ALLGEMEINER TEIL, 68 (10th ed. 1970).

233. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 616 (citing BGHZ 54, 106, (109)).

234. Judgment of Mar. 8, 1955, BGHZ 17, 1 (3) (citations omitted). Dawson hinted that Llewellyn might have drawn on the Court's decisions from the 1950s for his idea of "blanket assent." *See supra* text accompanying note 32. The parallels to this very case are remarkable. Consider that only five years later Llewellyn wrote on "blanket assent":

> There has been accompanying that basic deal another which, if not on any fiduciary basis, at least involves a plain expression of confidence, asked and accepted, with a corresponding limit on the powers granted: the boiler-plate is assented to en bloc, "sight, unseen," on the implicit assumption and to the full extent that (1) it does not alter or impair the fair meaning of the dickered terms when read alone, and (2) that its terms are neither in the particular nor in the net manifestly unreasonable and unfair.

LLEWELLYN, *supra* note 32, at 370-71. Further, "Any contract with boiler-plate results in *two* separate contracts: the *dickered* deal, and the collateral one of *supplementary* boilerplate." *Id.* at 371. Todd Rakoff, who reviewed only Llewellyn's comments, concluded that "[h]e apparently means that the adherent assents in the sense of reposing confidence, within limits, in the drafting party to fill in the terms of the deal." Todd D. Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96 HARV. L. REV. 1174, 1200 (1983). Rakoff found that assumption "very weak" and recommended abandoning it. *Id.* It is, however, the basis of the German law. *Cf.* John Dawson, *The General Clauses, Viewed from a Distance, in* RABELS ZEITSCHRIFT FÜR INTERNATIONALES UND AUSLÄNDISCHES PRIVATRECHT 41, 441, 452-53 (1977) ("[I]t came to be seen that most of the text on printed forms was not read and, if so, was

Good faith requires that the user of standard terms not subject the other party to an unreasonable disadvantage.[235]

German standard terms law sets limits on the freedom of users to exploit their position as drafters to their sole benefit. It prohibits them from taking inappropriate advantage of other parties. Thus, the issue is not controlling the freedom-of-contract (*Vertragsfreiheit*) of parties, but of preventing abuse by one party, the user, of that party's freedom of contract-drafting (*Vertragsgestaltungsfreiheit*).[236]

In German theory, the contract model does not limit freedom of contract. The parties may agree to the terms they like. What the contract model does is prevent one party from using the drafting device of standard terms to introduce terms that unreasonably disadvantage the other party. The contract model does not ask whether the deal or a particular term between the parties is fair; it asks whether the standard terms provided by the user are a good faith basis for the parties' contractual relationship.

The contract model compares a challenged standard term to two principal measures of validity: the essential basic principles of the statute from which the standard term deviates and the essential rights or duties necessary to achieve the purposes of the contract.[237] Unlike the potentially far-reaching inquiry mandated by American law,[238] the scope of the contract model is largely limited to the standard term challenged, the relevant statutory default rules, and the contract concerned. It requires only review of transactions of the type and classes of participants concerned, but not of the circumstances of the individual parties to the particular transaction.[239] The relevant statute serves a "classifying and guiding function" (*Ordnungs-und Leitbildfunktion*).[240] This approach of the contract model is termed "abstract-universal" (*abstrakt-*

seldom understood by the signers, that this made nonsense of the usual tests of mutual assent, that the draftsmen of such documents were in substance and effect law-makers. So the conclusion took firm hold that there should be cast on them the responsibility of law-makers to distribute even-handed justice.").

235. § 307(1) BÜRGERLICHES GESETZBUCH [Civil Code] [hereinafter BGB].

236. *See* Gesetzesentwurf-Entwurf eines Gesetzes zur Modernisierung des Schuldrechts [Draft Legislation for the Modernization of Contract Law], May 14, 2001, Drucksache 14/6040 at 149 (2001); Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 529, margin no. 1; Hermann Josef Bunte, *Die EG-Richtlinie über mißbräuchliche Klauseln Verbraucherverträgen und ihre Umsetzung durch das Gesetz zur Änderung des AGB-Gesetzes*, DB [DER BETRIEB] 1996, 1389, and text accompanying note 22; Bunte, Zehn Jahre, *supra* note 137, at 923; Reinhard Damm, *Europäisches Verbrauchervertragsrecht und AGB-Recht*, JZ 1994, 161, 166-67; Heinrichs *in* PALANDT, GESETZ ZUR MODERNISIERUNG DES SCHULDRECHTS, ERGÄNZUNGSBAND ZU PALANDT, BÜRGERLICHES GESETZBUCH 101, margin nos. 8-9 (61st ed. 2002) [hereinafter PALANDT, BGB 61st ed. ErgB]; Horst Locher, *Das AGB-Gesetz und VOB Teil B*, *in* VOB-Teile A und B-Kommentar, 506 margin no. 3 (Heinz Ingenstau & Hermann Korbion, eds., 14th ed. 2001); *see also* AUER, *supra* note 225, at 99-100, 102 (making the same point before the statute was adopted).

237. § 307(2) BGB, *supra* note 235; *see* Gesetzesentwurf-Entwurf eines Gesetzes zur Modernisierung des Schuldrechts, *supra* note 236, at 149; Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 617 (noting that deviation from default law is not the basis for the control, but the measure); Eike Schmidt, *Inhaltskontrolle von Schuldverträgen*, DRiZ [Deutsche Richterzeitung] 1991, 81, 83.

238. See *supra* text accompanying note 48.

239. *See* Judgment of Oct. 29, 1956, BGHZ 22, 91 (98); Judgment of Mar. 8, 1955, *supra* note 234 at (3); Kötz, *supra* note 18, at A51; Schmidt-Salzer, *supra* note 99, at 1262 (commenting that to a foreign observer not familiar with the "dogmatic-conceptual" phase of German standard terms law, this appears as "a simply incomprehensible approach to the problem").

240. JOACHIM SCHMIDT-SALZER, ALLGEMEINE GESCHÄFTSBEDINGUNGEN 186-89 (2d ed. 1977).

generellen) rather than "particular-personalized" (*konkret-individuellen*).[241] It has permitted German law, through a combination of statutory rules and judicial decisions, to develop a judicature of specific prohibited terms in each of their multiple manifestations.[242]

The contract model is oriented on general contract law. As a result, although the catalyst for passage of the Standard Terms Statute was the consumer movement, it was not limited, as the Unfair Terms Directive is, to consumer contracts. The German law exists to prevent abuse of the freedom of contract drafting by those controlling the drafting of terms. The German law accordingly protects all parties against misuse of standard terms.[243] The law requires no finding of weakness in the party subjected to the terms or oppression by the user. German standard terms law thus is not a special law protecting consumers against overbearing suppliers. It is a general law that governs a particular contract practice, i.e. standard terms.[244] The legislation is an explicit approval of the use of standard terms and an acknowledgment of the rationalization benefits they bring. It defends the freedom of contract.[245]

C. *German Standard Terms Legislation*

The Standard Terms Statute, *Das Gesetz zur Regelung des Rechts der Allgemeinen Geschäftsbedingungen* (*AGB-Gesetz*), entered into force on April 1, 1977. The law quickly assumed a central role in German contract law.[246] From 1977 to 1999 the German Supreme Court alone, not to speak of the lower courts, decided more than 1500 cases dealing with the Standard Terms Statute.[247] The Standard Terms Statute remained a separate statute until

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241. *See* Judgment of July 4, 1997, V ZR 405/96, CR 1998, 286 (287); Damm, *supra* note 236, at 172-174; Helmut Heinrichs, *Die EG-Richtlinie über mißbräuchliche Klauseln in Verbraucherverträgen*, NJW 1993, 1817, 1820; Joachim Schmidt-Salzer, *Transformation der EG-Richtlinie über mißbräuchliche Klauseln in Verbraucherverträgen in deutsches Recht und AGB-Gesetz*, BB [BETRIEBS-BERATOR] 1995, 734-36.

242. Even before the Standard Terms Statute, Kötz judged the effort a success. *See* Kötz, *supra* note 18, at A51 (noting that the courts did not rely on unchecked control using indefinite general clauses, but developed case groups, clause varieties, and contract types).

243. This legislative decision is consistent with practice prior to the adoption of the law, which policed standard terms without regard to whether a consumer was involved. Most leading cases before the statute was adopted, in fact, involved contracts between merchants. *See* Eith, *supra* note 213, at 17; *accord* Bunte, *supra* note 137, at 925. Eith's article is a contemporary argument against limitation to consumer protection. While in principle it protects all parties equally, as will be discussed, it does allow for treatment of businesspersons that is different from that of consumers. *See infra* text accompanying notes 294-96. The provisions of the Civil Code on standard terms, i.e., Sections 305 to 310, are written in terms of general applicability and refer to the user of the terms and the other party to the contract. Section 310 then provides that certain provisions do not apply to contracts with a businessperson (*Unternehmer*). Businessperson is defined in Section 14 I to be "a natural or legal person or a legally capable association of persons, at the conclusion of a legal transaction, acting in exercise of a commercial or independent professional activity."

244. Schmidt-Salzer, *supra* note 241, at 734-36.

245. Markus Stoffels, *Schranken der Inhaltskontrolle*, JZ 2001, 843, 844 (discussing AGB § 8, the provision that became § 307(3) BGB without change, and noting the limitations of § 307(3) that keep price and performance terms firmly in the hands of the contracting parties).

246. Oliver Remien, *AGB-Gesetz und Richtlinie über mißbräuchliche Verbrauchervertragsklauseln in ihrem europäischen Umfeld*, ZEuP 1994, 34 ("Since the Standard Terms Statute was passed, contract law in Germany is above all the law of the control of standard terms.").

247. The cases are listed at ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 1735-88.

January 1, 2002, when its substantive provisions became part of the Civil Code and its procedural provisions became part of a new procedural statute.[248] No major changes were made in the substantive law as it stood at the end of 2001.[249] During its 25-year life, while certain details were adjusted, the law experienced no major amendments. The most noteworthy event in its life was its harmonization with the E.U. Directive.[250] The law is widely regarded as a success.[251] In some sectors of the economy, use of standard terms increased upon adoption of the law.[252]

This article refers to the standard terms legislation by the new Civil Code section numbers rather than by the section numbers of the Standard Terms Statute. Set out below is a transposition table that identifies those provisions by their section numbers in the Standard Terms Statute. Attached as an Appendix to this article is an English translation of the Civil Code provisions.

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248. The Standard Terms Statute was made part of the Law of Obligations, i.e., Book 2 of the Civil Code. Some commentators argued that it should remain a free-standing law or should be made part of the General Part, i.e., Book 1 of the Civil Code, since its effect is not limited to contracts falling under Book 2, Law of Obligations. *See, e.g.*, Peter Ulmer, *Das AGB-Gesetz—ein eigenständiges Kodifikationswerk*, JZ 2001, 491. Wolf & Pfeiffer, *supra* note 209, at 303, 304. Complete transposition tables are given at Heinrichs in PALANDT, BGB 61st ed. ErgB, *supra* note 236, and in the supplement to ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 3-74. The most important is:

Civil Code	Old AGBG
§ 305	§§ 1 and 2
§ 305a	§ 23 (part)
§ 305b	§ 4
§ 305c	§§ 3 and 5
§ 306	§ 6
§ 306a	§ 7
§ 307	§§ 8 and 9
§ 308	§ 10
§ 309	§ 11
§ 310	§ 23 (part)

249. Heinrichs *in* Palandt, BGB 61st ed. ErgB, *supra* note 236 at 100, margin no. 2. For a comprehensive review of the changes, see Friedrich Graf von Westphalen, *AGB-Recht ins BGB—Eine erste Bestandsaufnahme*, NJW 2002, 12.

250. *See infra* text accompanying notes 332-39.

251. Twice in the last decade there was cause to evaluate the success of the law: first, when it was amended to implement the E.U. Unfair Terms Directive, and second, when it was incorporated into the Civil Code in the obligations law reform. With respect to the former, see, for example, Martin W. Huff, *Kleingedrucktes für Europa*, FRANKFURTER ALLGEMEINE ZEITUNG, May 17, 1993, at 15. Huff's editorial, appearing in the business section of a leading conservative newspaper, argued that the call for narrowing the German law as part of the harmonization with E.U. law was not a good idea, since the German law had proven to be a success. *See also* Gesetzeentwurf der Bundesregierung, Entwurf eines Gesetzes zur Änderung des AGB-Gesetzes [Draft Legislation to Change the Standard Terms Law], Feb. 10, 1995, Drucksache 13/2713 at III; Hans W. Miklitz, *AGB-Gesetz und die EG-Richtlinie über mißbräuchliche Vertragsklauseln in Werbraucherverträgen*, ZEP [Zeitschrift für Europäisches Privatrecht] 1993, 522, 524 (stating so "sounds the canon in unison"). With respect to the latter, see, for example, Horst Locher, *Das AGB-Gesetz und VOB Teil B*, *in* VOB-Teile A und B-Kommentar, 505 margin n.3 (Heinz Ingenstau & Hermann Korbion eds., 14th ed. 2001); *see also* Ulmer, *in* ULMER/BRANDNER/HENSEN, *supra* note 54, at 491 (noting general recognition that it was one of the more successful laws of the last several decades). For one dissonant voice—and that quite so—see THAMM & PILGER, *supra* note 217, at 47 ("overwhelmingly, materially negative"); *id.* at 49 ("a defectively designed statute").

252. Bunte, *supra* note 137, at 922.

The standard terms law consists of two principal parts: an incorporation control in sections 305 to 305c, and a content control in sections 307 to 309.[253] The definition of "standard terms" in section 305(1) largely determines the scope of the law. Standard terms are terms prepared beforehand for a multiple number of contracts and are presented (*stellt*) by the user to the other party at the contract's conclusion.[254] The form in which the terms appear does not matter and they may or may not be separate from the rest of the contract. section 305 provides that terms separately negotiated between the parties are not standard terms and are not subject to control under the standard terms legislation.[255]

1. *Incorporation Controls*

Besides defining standard terms, section 305 provides the general rule for when standard terms become part of a contract as a body. Sections 305a through 305c modify the general rule of section 305. Section 305a provides special rules for the transportation and telecommunication industries; Section 305b provides that individually negotiated terms take priority over standard terms, and section 305c provides incorporation and interpretation rules for individual terms.

Section 305(2) requires that users of standard terms give other parties notice and an opportunity to review the terms. Standard terms do not become part of the contract unless they comply with these formalities and the other party assents to their use. The notice may be oral or in writing. If, for certain types of contracts, an express notice creates disproportionate difficulties, a suitable sign at the place of contracting may suffice. The notice must be apparent to an average customer. Thus, for example, if a reference in a contract to the terms is to be sufficient notice, that reference must be so conspicuous that it could not be overlooked even in a fleeting review of the contract.[256] The reference must be made at the same time as the contract and is not effective if made only once the contract is concluded. Thus, for example, a reference on a ticket of admission to a theatre is insufficient, since the ticket is provided only after the contract is reached.[257] The user of standard terms must provide the other party with an opportunity to review the standard terms, but is not required to provide the terms unsolicited.[258] The critical moment is

253. In the Standard Terms Statute the statutory subdivisions made the separation explicit. The four sections dealing with content control (§§ 8-11) were collected together in a separate second subdivision, "Invalid Terms"; the first section in the subdivision, Section 8, had the caption "Limits of the Content Control." Sections relating to definition, incorporation, interpretation, and legal effect of invalidity were collected together in a first subdivision, "General Provisions."

254. This is the general rule, but to comply with the Unfair Terms Directive, the law has been revised to ease these requirements in consumer transactions. *See infra* text accompanying note 266.

255. Although they are still subject to the general clauses of the Civil Code. *See* MUNZ, *supra* note 33, at 240-41.

256. Heinrichs *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, § 305, at 106, margin no. 29 (with case citation); Ulmer *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 2, at 207, margin no. 27.

257. Heinrichs *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, § 305, at 106, margin no. 30 (with case citations).

258. The legislature did not adopt a proposal to require furnishing a copy of the terms without awaiting a request. *See* Ulmer *in* ULMER/BRANDNER/HENSEN, *supra* note 54, § 2, at 220, margin no. 46.

when the customer makes the contractual commitment; sending the terms after the commitment is made will ordinarily not suffice.[259]

Section 310(1) provides that neither the notice nor the opportunity to review requirements apply directly to contracts between businesspersons.[260] They are subject to the general rules of the Civil Code for contracts generally. Often in contracts between businesspersons both parties use standard terms, which leads to the problem known in the United States as the "battle of the forms" and governed by section 2-207 of the U.C.C.[261]

Section 305c(1)(1) provides that surprising terms do not become part of the contract. A term is surprising if, under the circumstances, in particular in view of the external appearance of the contract, it is so unusual that the other party would not expect it. Decisive is not a term's unfairness, but its unusualness.[262] A classic example of a clause prohibited as surprising is one that requires a buyer of a product to obtain necessary service for the product from the seller.[263] Businesspersons receive the full protection of this provision.[264] Section 305c(2) provides that any doubts in construction of a standard term are to be resolved against the user. Section 305b provides that individually negotiated terms take priority over standard terms. Thus, for example, if the parties agree on a delivery date, that agreement is not superseded by a standard term allowing delay.[265]

2. *Content Control*

The heart of German standard terms legislation is its control of the content of standard terms.[266] The content control consists of three parts: a general clause (section 307); a list of terms that *may* be prohibited (section 308, sometimes called the "gray list"); and a list of terms that *are* prohibited (section 309, sometimes called the "black list").

A court reviewing challenged terms is first to confirm that the challenged terms have become part of the contract under sections 305 through 305c. It is then to test them against the content controls, looking first to the prohibited list, then to the suspect list, and only finally to the general clause.[267]

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259. *See id.* § 2 at 222-23, margin no. 48.

260. § 310(1) BGB, *supra* note 235.

261. *See* KARL LARENZ, ALLGEMEINER TEIL DES DEUTSCHEN BÜRGERLICHEN RECHTS 489 (4th ed. 1977); Ulmer *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 2, at 245-63 (discussing when standard terms become part of agreements between businesspersons).

262. Ulmer *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 3, at 302, margin no. 1 308, margin no. 12; Heinrichs *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236 § 305c at 112, margin no. 3 (with case citation). The test for unusualness is with respect to contracts of that type. Ulmer *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 3, at 310, margin no. 14; Schmidt *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 12, at 1453, margin no. 11.

263. Ulmer *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 3, at 319, margin no. 26.

264. *Id.*, § 3, at 345, margin no. 54.

265. *Id.*, § 4, at 363, margin no. 22 (with case citations).

266. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54 at 490 ("*das Kernstuck*"); Heinrichs *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, § 307, at 119, margin no. 2.

267. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 539, margin no. 15.

Section 307(3) explicitly limits the content control to standard terms that provide for changes and additions to default law. It thereby excludes from the content control the fundamental terms of the bargain, namely performances and price.[268] The limitation of the content control to standard terms is designed to insure that the control does not itself interfere with the free market and private autonomy.[269]

The question of validity is a question of law. Fact questions and the burden of proof play a subordinate role. The facts necessary to decide whether a term improperly creates a material disadvantage are usually undisputed. The determination that the disadvantage is unreasonable is purely a matter of law and allows for no taking of proof.[270] To a substantial extent, the evaluation can be abstract and objective.

Sections 308 and 309 list prohibited and suspect terms. The two sections are considered to be applications of the general clause of section 307.[271] Section 309 lists eight types of prohibited terms.[272] It voids without evaluation terms on the list. Thus, for example, section 309(7) voids a term that excludes or limits liability for personal injury ("life, body, health") or for gross negligence.[273] Section 308 lists thirteen types of suspect terms. It does not presume that terms of the types listed are invalid but requires an evaluation of the particular term.[274] For example, section 308(1) requires determination of whether a period of time reserved to accept or reject an offer or to perform is "inappropriately long or not sufficiently definite."

Sections 308 and 309 are intended to increase legal certainty. While few would doubt they have made a positive contribution, the extent to which they have done so may be debatable. Their catalogues provide fixed points of departure. If a term falls under section 309, no further examination is necessary. If a term that falls under section 308, it is tested under specified measures.

Section 310(1) removes standard terms used with businesspersons from the direct controls of sections 308 and 309. However, it leaves those terms subject to testing under the general clause of section 307. Its practical effect is to let courts decide whether section 308 and 309 controls make sense in business contexts. [275] In practice, courts tend to apply them anyway to

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268. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 8, at 495, margin no. 1; Heinrichs *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, § 307 at 125, margin no. 54. However, this does not exclude from the content control terms that relate to price. *Id.* at 125, margin no. 60; *cf.* E.U. Unfair Terms Directive art. 4(2).

269. Stoffels, *supra* note 245, at 844.

270. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 635, margin no. 162; LARENZ, *supra* note 261, at 501. *See* Decision of Oct. 24, 2001, VIII ARZ 1/01, BGHZ 8, 1(01), *available at* http://www.bgh-free.de.

271. Heinrichs *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, § 307, at 119, margin no. 2.

272. The introduction to the list alerts readers that the list assumes that the term in question is not already prohibited by some other provision of law.

273. The entire list is in the Appendix.

274. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 538, margin no. 12.

275. The extent to which the courts, in applying the general clause to agreements between businesspersons, should look to Sections 308 and 309 is controversial. *See* Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 538, margin no. 13. For a book devoted solely to the question, see REINHARD LUTZ, AGB-KONTROLLE IM HANDELSVERKEHR UNTER

standard terms with businesspersons, by analogy.[276] In some areas, that application is nearly automatic.[277]

The general clause, section 307, tests standard terms not caught by sections 308 and 309. The first sentence of subsection (1) of section 307 makes invalid (*unwirksam*) certain standard terms "if, contrary to the requirement of good faith, they place the contractual partner of the user at an unreasonable (*unangemessene*) disadvantage."

Application of section 307(1) to a particular standard term looks to what the legal positions of the parties would be if there were no such term.[278] Courts determine whether the user of the term has one-sidedly exploited control over drafting. Courts focus on the default solution and on the change in legal result. They are not supposed to be concerned with the situation of individual parties.[279] Courts find users have not complied with the good faith requirement when terms are entirely one-sided and take no account of the other parties. They require that obligations imposed by standard terms be reasonable in relation both to the user's own interests and the burden imposed on the other party. In making these determinations, courts rely on other fundamental principles of German law such as necessity (*Erforderlichkeit*) and proportionality (*Verhältnismäßigkeit*).[280] They do not void terms simply because the terms impose burdens. For example, they do not find that a party subject to a standard term is unreasonably disadvantaged if the term is not very burdensome[281] or if it imposes an obligation that would be expected of the party in good faith anyway.[282]

Section 307 does not consist solely of the general clause prohibition in its first sentence. The balance of the section guides application of the general clause. The second sentence of the first paragraph provides that an unreasonable disadvantage may be found in contract language that is not clear

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BERÜCKSICHTIGUNG DER KLAUSELVERBOTE (1991).

276. Gerald Spindler, *Haftungsklauseln in Provider-Verträgen: Probleme der Inhaltskontrolle,* CR 1999, 626, 627.

277. Christian Schubel, *Schuldrechtsreform: Perspektivenwechsel im Bürgerlichen Recht und AGB-Kontrolle für den Handelskauf,* JZ 2001, 1113, 1115. *See also* Hans Erich Brandner & Peter Ulmer, *EG-Richtlinie über mißbräuchliche Klauseln in Verbraucherverttägen: Kritische Bemerkungen zum Vorschlag der EG-Kommission,* BB 1991, 703 (finding extensive uniformity).

278. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 571 margin no. 70 (with case citations); Heinrichs *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, § 307, at 120 margin no. 8 (with case citations). Presumably this process is regarded simply as construction of the statute and not as law-making itself. While German courts routinely rely on judge-made law, it is not for the judges to make policy decisions. *See* MAXEINER, POLICY AND METHODS IN GERMAN AND AMERICAN ANTITRUST LAW, *supra* note 219, at 39-44.

279. Judgment of July 4, 1997, *supra* note 241 at 287 (requiring instead an "überindividuell-generalisierende, typisierende, von den konkreten Umständen des Einzelfalls absehende Betrachtungsweise"). *See* Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 571 margin no. 70.

280. Bunte, *Die EG-Richtlinie, supra* note 236, at text accompanying note 13. Regarding necessity and proportionality and their general importance, see James R. Maxeiner, *Constitutionalizing Forfeiture Law—The German Example,* 27 AM. J. COMP. L. 635, 649 (1979). For proportionality, see generally HANS KUTSCHER ET AL., DER GRUNDSATZ DER VERHÄLTNISMÄSSIGKEIT IN EUROPÄISCHEN RECHTSORDNUNGEN (1985).

281. Schubel, *supra* note 277, at 1114-15 (discussing the tendency to avoid *any* departure from dispositive law).

282. For this paragraph generally, see Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 571-74, margin nos. 70-74.

and comprehensible. The second paragraph provides for two situations when an unreasonable disadvantage is to be presumed. Section 307(2)(1) presumes an unreasonable disadvantage when a standard term makes a material departure from a fundamental principle of otherwise applicable law. Section 307(2)(2) presumes an unreasonable disadvantage if the term takes away or limits a material benefit that the contract is designed to provide.[283] Sections 307(2)(1) and 307(2)(2) complement each other. In practice a clear distinction is not always made between them.[284] Section 307(2)(1), which focuses on the law, is considered clearer and more predictable than section 307(2)(2), which focuses on the contract itself.[285] Section 307(2)(1)does not presume an unreasonable disadvantage merely because the standard term changes the outcome provided by law.[286] It requires that the change be fundamental; that the standard term displace a material interest of the other party or of the society at large protected by the law.[287] Section 307(2)(2) typically is used to test liability limitations and warranty exclusions that are not otherwise prohibited by sections 308 and 309—for example, a liability limitation for ordinary negligence.[288]

In the United States there is a certain resignation that a trade-off between "certainty of contract and fairness of terms" is necessary in the control of standard terms.[289] In Germany, there is no such resignation. There the control of standard terms has come a long way from its beginnings in a couple of general clauses. Under German law there now exists what might be termed a matrix of content control. It provides numerous orientation points for those

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283. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 619, margin no. 142. Larenz notes that nos. 1 and 2 substantially cover each other. LARENZ, *supra* note 261, at 501.

284. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 609-10, margin nos. 131-32.

285. Friedrich Graf von Westphalen, *Der Software-Entwicklungsvertrag—Vertragstyp—Risikobegrenzung*, CR 2000, 73, 76.

286. Heinrichs *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, § 307, at 123, margin no. 28.

287. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 611, margin no. 133; LARENZ, *supra* note 261, at 500 (discussing when legal provisions incorporate material values and when they only have an ordering role). Where statutory guidance is absent, there are increased difficulties in applying the control. Locher, *supra* note 251, 505, margin no. 2 (Heinz Ingenstau & Hermann Korbion eds., 14th ed. 2001).

288. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 625 margin no. 150. How does such a review work in practice? The decision of the German Supreme Court of Oct. 24, 2001, VIII ARZ 1/01, JZ 2002, 1001, *available at* http://www.bverfg.de, can serve as an example. At issue was the validity of a term that disclaimed the landlord's liability to a tenant for ordinary negligence. A leaky roof damaged the tenant's furniture. The court considered whether such a contractual limitation of liability would eviscerate one of the main duties (a so-called cardinal duty) of the lease agreement, the fulfillment of which the tenant could justly rely on. The court turned to the lessor's obligations under the Civil Code, which provides that lessors are responsible for maintaining the premises in a suitable condition. Excluding liability that the lessor is responsible for, the court continued, limits the obligation of the lessor to maintain the premises and works to the material disadvantage of the tenant. The court held that the purpose of a lease of living quarters is to provide a place for the tenant to live and that a tenant cannot be expected to guard against defects in house construction. The court further found that no insurance was available to tenants to guard against the risk of defective construction, while such insurance was available to the lessor as the owner of the building. The court therefore held that the standard term was invalid. It impermissibly disadvantaged tenants contrary to the requirement of good faith. The court did not concern itself with whether the party subject to the term had read it, knew what it meant, or had sought to obtain insurance against the risk of a leaky roof.

289. *See, e.g.*, Greenfield & Rusch, *supra* note 83, at 144, 148.

who would judge the validity of standard terms. Sections 308 and 309 provide relatively fixed points. Section 307 guides its own application, which has passed from general abstract statements to the dominance of "case law" in concrete, specific situations.[290] Precedents and commentary can now fill in the spaces.

The number of precedents and publications in the area is enormous. The German Supreme Court alone has decided more than 1500 cases.[291] Not a month goes by without an article on standard terms. Books devoted to standard terms appear frequently. These books have different approaches to coverage. Some are detailed commentaries on the law. Some are practical; others are theoretical. Dissertations examine particular legal aspects or effects in particular sectors of the economy. Practical guides profile particular industries: a 395-page tome for the construction trade is now in its ninth edition.[292] And the construction trade is just one of many industries to have its own volume. There are even guides for the general public. One, a widely-distributed, 450-page popular paperback, now in its fifth edition, promises to help the general public in "drafting and controlling of the 'fine print.'"[293] These guides could not be produced if the law did not provide predictability.

Professional commentaries adopt a matrix approach to their discussions of content control. First, they give explanations of each of the three principal statutory controls, now sections 307-309. That is the usual approach of a German statutory commentary. But then, deviating from the usual, they catalogue specific terms across all three controls categorizing the terms either by their legal nature (e.g., choice-of-law clauses, mandatory writing clauses) or by the business sector in which they are used (e.g., construction contracts, hospital contracts).[294] This matrix permits precision in identifying when terms are likely to be valid and when they are not.

3. *Enforcement*

As does its American counterpart, German standard terms law provides that impermissible terms are unenforceable.[295] That remedy recently received

290. Friedrich Graf von Westphalen, *Die Entwicklung des AGB-Rechts im Jahr 2001*, NJW 2002, 1688, 1695-96. German judges and scholars already had experience in developing such case groups under the "good faith" provisions of Section 242 of the Civil Code. The process even has a name: "concretisation." Simon Whittaker & Reinhard Zimmermann, *Good Faith in European Contract Law: Surveying the Legal Landscape*, *in* GOOD FAITH IN EUROPEAN CONTRACT LAW 7, 23 (Reinhard Zimmermann & Simon Whittaker eds., 2000).

291. *See supra* note 247.

292. LUDWIG GLATZEL, OLAF HOFMANN & ECKHARD FRIKELL, UNWIRKSAME BAUVERTRAGSKLAUSELN NACH DEM AGB-GESETZ: RECHTSPRECHUNG - SCHNELLÜBERSICHT, MUSTERBAUVERTRAG, GESETZESTEXT (9th ed. 2000).

293. JÜRGEN NIEBLING, GESCHÄFTSBEDINGUNGEN (AGB) VON A - Z: NEUES SCHULDRECHT - NEUE AGB (5th ed. 2002)

294. One commentary gives nearly five hundred pages to this review and treats it in a separate section designated appendix to §§ 9-11. ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 957-1446. A "pocket" commentary to the law devotes nearly half of its 478 pages to its § 9 appendix. THAMM & PILGER, *supra* note 217, at 90-319. The leading "short" commentary to the entire civil code devotes more than a dozen pages and one hundred margin numbers to this aspect of the catalogue under the discussion of Section 307. Heinrichs *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, § 307, at 127-41, margin nos. 68-169.

295. §§ 305, 306 BGB. Section 306(1) provides that in those cases the contract remains

new teeth when the European Court of Justice held that national courts of the European Union must of their own motion examine whether material contract terms are unfair in actions against consumers.[296]

Unlike American law, however, German standard terms law, ever since the legislature first took up the issue in the 1970s, has been concerned with what the European Commission later called "positive enforcement," i.e., measures designed to prevent the use of unfair terms. When the legislature first took up a standard terms law, it considered several alternative approaches to enforcement. One widely discussed proposal called for a "preventive administrative control." Parties who wished to use standard terms would file terms for review and approval with a new administrative agency.[297] In the end, however, the legislature rejected every form of administrative oversight.[298]

Instead of adopting an administrative oversight, at the last moment, the legislature introduced a novel procedural solution: the institutional action, i.e., the *Verbandsklage*.[299] Consumer groups and trade associations have the right to bring suit against those who use or recommend use of unlawful standard terms.[300] These institutional suits exist not to protect individual customers or users of impermissible standard terms, but the contracting public generally from application of impermissible terms.[301] Originally a part of the Standard Terms Statute, since January 1, 2002 that right of action is now governed by the new Law of Actions for Injunctions for Violations of Consumer and Other Law (*Gesetz über Unterlassungsklagen bei Verbraucherrechts-und anderen*

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otherwise effective. It protects the other party to the contract by reversing the usual presumption that the entire contact is void. Schmidt, *in* ULMER/BRANDNER/HENSEN, AGB-Gesetz *supra* note 54, § 6 at 427, margin no. 1. Unlike American law, German law theoretically allows for damages for intentional or negligent use of invalid terms. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 565, margin no. 57.

296. Case C-240/98, *supra* note 161. In the German legal system, the holding affects more than just private litigation. It also requires that notaries—who have an important role in many contracts—examine contract term unfairness. It may also impose similar obligations on the land registry office. Brandner *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 9, at 563-64, margin nos. 54-55.

297. Brandner, *supra* note 224, at 617. The most extreme of these would have made administrative approval a necessary prerequisite to use of any standard terms. Somewhat less extreme proposals included suggestions for registering terms and creation of a special administrative body similar to the Federal Cartel Office to enforce the new law. The Israeli Standard Contracts Law, 1964, 13. L.S.I. 152, (1964-65), served as a model for an administrative approach, but also as a warning, since it did not seem to work too well. *See* Hensen *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 1457, margin no. 4; Uri Yadin, *Legislative Control of Standard Contracts*, *in* RICHTERLICHE KONTROLLE VON ALLGEMEINEN GESCHÄFTSBEDINGUNGEN 143, 154 (1968) (noting only one opinion under the law—a decision denying Dun & Bradstreet's request for approval of a liability exclusion). The original Israeli statute, which can be considered the world's first standard terms statute, is printed in RICHTERLICHE KONTROLLE VON ALLEGEMEINEN GESCHÄFTSBEDINGUNGEN 175. *See also* Ewoud H. Hondius, *Unfair Contract Terms: New Control Systems*, 26 AM. J. COMP. L. 525, 529-32 (1978).

298. Hensen *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 1457-58, margin nos. 5-7.

299. *Id.* at 1457-58, margin no. 9.

300. Bunte, *supra* note 137, at 922. The *Verbandsklage* was understood as a substitute for a farther-reaching administrative control. Eike Schmidt, *Verbraucherschützende Verbandsklagen*, NJW 2002, 25, 28. The original German provisions for a collection action apparently served as inspiration for Article 7 of the E.U. Unfair Terms Directive. Hensen *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 13, at 1482, margin no. 23.

301. Bassenge *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, UklaG at 413; Hensen *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 13, at 1482, margin no. 23 (citing half a dozen Supreme Court decisions).

Verstößen [UklaG]), hereafter referred to as the "Injunctions Act." The institutional action is Germany's closest analogue to an American class action.[302]

Section 1 of the Injunctions Act provides that whoever uses or recommends the use in commerce of standard terms that are invalid under Civil Code sections 307 to 309 is subject to an injunctive action to cease and desist. Sections 2 and 3 of the Injunctions Act provide that qualifying consumer groups, trade associations and chambers of commerce officially recognized by the European Union or by the German federal government are authorized to bring suit. Trial courts, however, spend no time in determining whether a particular association is qualified. Section 4 provides that administrative authorities are to maintain lists of qualified organizations and update them regularly.

Most institutional legal complaints do not require judicial involvement. They follow the "warning" (*Abmahnung*) procedure of German competition law. Under this procedure a potential plaintiff sends a formal letter demanding that the user of the terms cease-and-desist. The demand letter must include the terms claimed to be invalid and the basis for the claim of invalidity. If the user accepts the demand, the user makes a legally binding declaration that it is ceasing and desisting from use of the terms (*Unterlassungserklärung*). Typically in such a declaration the user commits to treat such terms in its contracts with third parties as invalid and agrees to pay a penalty for each later use of a prohibited or comparable term (in cases known to the author, about € 1,000 per term, with a maximum of about € 2,500 to € 9,000 per contract). If the recipient of the demand letter rejects the demand, the plaintiff may then sue and, if the plaintiff wins, recover the costs of the suit.[303] The cost shifting provisions of section 5 of the Injunction Act have the effect of making use of the warning procedure practically if not legally required.

Section 6 of the Injunctions Act provides that plaintiffs ordinarily must sue in the defendant's home jurisdiction. Of importance for American companies, however, section 6 provides further that if the defendant is not located in Germany, the plaintiff may sue in any district where the defendant uses the invalid terms. Section 7 provides as an additional sanction that an eventual judgment is to be published.[304]

Sections 9 and 11 of the Injunctions Act give the institutional action its real teeth. Section 9 requires that a judgment against the defendant must recite the invalid term, identify the type of transaction in which its use by the defendant is prohibited, and prohibit the use of terms having the same content. In ordinary civil litigation, a judgment has effect only for the parties to the suit. But section 11 of the Injunctions Act changes the normal rule and gives

302. *See generally* Harald Koch, *Non-Class Group Litigation Under E.U. and German Law*, 11 DUKE J. COMP. & INT'L L. 355 (2001).

303. Bassenge *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, UklaG § 5, at 421, margin no. 7; Hensen *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ., *supra* note 54, § 13 at 1496-1502, margin nos. 49-66. For a description in English of the *Abmahnung* procedure generally, see Georg Jennes & Peter Schotthöfer, *Germany*, *in* ADVERTISING LAW IN EUROPE AND NORTH AMERICA 203, at § 26, 228-30 (James R. Maxeiner & Peter Schotthöfer eds., 2d ed. 1999).

304. This is a meaningful sanction in Germany where legal proceedings are not as public as in the United States.

the judgment a broader effect. Terms found invalid in such an action are invalid with respect to all of the users' customers.[305] Those customers may rely on the judgment. Defendants who continue to use terms held invalid are subject under section 890 of the Code of Civil Procedure to fines of up to € 250,000 and imprisonment for up to two years.[306]

Consumer associations initiate many actions against standard terms. In Berlin and Stuttgart, two consumer organizations are reported each to give several hundred warnings each year.[307] Not counting cases resolved at the warning stage, in a little more than twenty-four years, consumer associations brought 3523 suits.[308] Consumer associations account for more than half of all reported cases applying the Standard Terms Statute.[309] Their suits can have a broad impact. In one recent case, a consumer association successfully challenged thirteen terms in a standard form recommended by the automobile industry to new car dealers.[310]

Consumer associations might bring even more injunction actions were it not for the costs of such actions and their litigation risks.[311] To help associations bring more actions, the European Union provides the associations with funds.[312] The normal rule of German civil procedure—that the loser pays—helps defray costs when associations win, but exposes them to risks when they lose. To reduce the discouraging effect of the rule, it has been modified for association actions. The law limits the maximum nominal amount in dispute in such cases to € 250,000. In practice, the usual amount is much lower: it ranges from € 1500 to € 2500 per clause in dispute.[313]

Critics of the institutional action believe it to be only a transition measure. They observe that it serves not a private institutional interest, but a public interest. Civil procedure, however, is designed for settlement of private disputes. For example, it gives parties complete right to continue or abandon their lawsuits at will. According to this view, the kind of public interest litigation that the Injunctions Act permits would be better conducted in an administrative proceeding.[314]

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305. Bassenge *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, UklaG § 11, at 426.

306. Hensen *in* ULMER/BRANDNER/HENSEN, *supra* note 54, at 1564, margin no. 14 (stating that someone who uses the terms contrary to a judgment is subject to the sanction of ZPO § 890).

307. Ulmer *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 77, margin no. 62.

308. *Id.*

309. *See* Hans-W. Micklitz, *Rapport sur l'application pratique de la Directive 93/13/CEE dans la République Fédérale d'Allemagne*, *in* The Integration of Directive 93/13 into the National Legal Systems 238, 239, 242 (1999) (noting that from 1976 to 1993, individual actions accounted for one-third of all actions brought, while group actions accounted for two-thirds, and from 1993 to date, the share of individual actions increased to 43% (therefore implying that group actions accounted for 57%)). On the other hand, suits by trade associations have proven to be unusual.

310. Judgment of Sept. 27, 2000, VIII ZR 155/99, BGHZ 145 (203).

311. Hensen *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 13, at 1503, margin no. 69.

312. E.U. Commission Report, *supra* note 129, at 9.

313. Bassenge *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, UklaG § 5, at 422, margin no. 14; Hensen *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ., *supra* note 54, § 15, at 1524, margin no. 31.

314. Schmidt, *supra* note 300, at 25.

D. *The E.U. Directive: The Contract Model Meets the Consumer Model*

The German Standard Terms Statute by all accounts had a profound influence on the Unfair Terms Directive.[315] In popular perception the directive was considered to be narrower, since it applied only to consumer contracts, while the German statute applied to contracts generally.[316] Yet for all the similarities between the two laws,[317] the directive as originally proposed turned out to be something of a challenge to the German contract model.[318]

Alongside the contract model of German law, there is another approach that presses for favor in Europe. This approach was fully realized, or nearly so, in the initial draft of the Unfair Terms Directive, but only partially, if at all, in the text actually adopted. The alternative approach might be called the "consumer protection model." The contract model applies to contracts generally without limitation as to personal characteristics of the contracting parties. The content controls it imposes are abstract and generalizing. The consumer protection model, on the other hand, is limited to consumer contracts. Its content controls are personalized and particularized.[319] The contract model protects freedom of contract; the consumer protection model protects consumers.[320] The Unfair Terms Directive as finally adopted is a compromise between the two models.[321]

The Commission's first draft of the Unfair Terms Directive anticipated a comprehensive control of all consumer contracts without regard to whether the terms appeared in standard forms whether they were individually negotiated, or whether they concerned the fundamental substance of the contract. The draft was anathema to German scholars. They contended nothing less than that the proposal would cause a "considerable dilution of the principle of a free market economy, which is safeguarded by the EEC Treaty."[322] It would bring about a "drastic restriction" in private autonomy

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315. *See supra* note 10.

316. *See, e.g.*, Huff, *supra* note 251, at 15. *See also supra* note 10.

317. While here we focus on differences, the basic similarities are substantial. That the Member States could agree on a general clause was a triumph in itself. *See* Miklitz, *supra* note 251, at 525. The two laws are considered "closely-related," and that is one reason why no separate law was considered necessary. Remien, *supra* note 246, at 65. *See also* Peter Ulmer, *Zur Anpassung des AGB-Gesetzes an die EG-Richtlinie über mißbräuchliche Klauseln in Verbraucher verträgen*, EuZW [Europäische Zeitschrift für Wirtschaftsrecht] 1993, 337, 337-38 (listing similarities and differences).

318. One long-time expert on standard terms law observed that the very similarity of the directive and German law "concealed nothing less than a fundamental difference in institutional conceptions." Schmidt-Salzer, *supra* note 241, at 734. *But see* Ulmer, *supra* note 317, at 341 (noting the differences in purposes of the two laws, but observing that a law's purpose does not always expressly appear in the statute).

319. Damm, *supra* note 241, at 172.

320. Within one legal system, both models theoretically could co-exist. According to one view, however, they might lead to "schizophrenia" if included within one and the same statute. *See* Schmidt-Salzer, *supra* note 241, at 740.

321. Hans Schulte-Nölke, *Fünf Jahre AGB-Richtlinie 93/13/EWG - Weitere Rechtsetzungspläne der Kommission?*, NJW 1999, 3176 [report of the 1999 conference of the Commission on the Directive].

322. Hans Erich Brandner & Peter Ulmer, *The Community Directive on Unfair Terms in Consumer Contracts: Some Critical Remarks on the Proposal Submitted by the EC Commission*, 28 COMMON MKT. L. REV. 647, 652-53 (1991) [hereinafter Brandner & Ulmer, *The Community Directive on Unfair Terms*]. This is an English version, although not an exact translation, of Hans Erich Brandner & Peter Ulmer, *EG-Richtlinie über mißbräuchliche Klauseln in Verbraucherverttägen: Kritische*

and would wholly upset freedom of contract.[323] The German standard terms law did not threaten private autonomy, they argued, but honored it. The predicate for invoking the German content control was the absence of agreement between the parties as to the content of the terms. When standard terms are presented unilaterally and are not negotiated, the legitimacy of their claim to be enforced is slight. The principle of freedom of contract counsels not their free application, but close scrutiny. Where the parties actually negotiate a term, then the principle of private autonomy demands recognizing their choice.[324]

German scholars criticized the draft directive for its control of individual contracts. They argued that the directive should not apply to "individually negotiated terms;" the parties' own negotiations should be recognized to safeguard freedom of contract. Similarly, they urged that the directive not apply to the "principal obligations" of the contract; in a free market economy, the market should determine the price-performance relationship. German scholars stressed that control of standard terms is different from control of individually negotiated terms. Above all, control of standard terms can be "abstract," that is, it does not examine the particular circumstances of the individual contract. [325] Control of individually negotiated terms, on the other hand, requires consideration not only of the specific term in question, but of the entire contract and of all the circumstances of its conclusion. Standard terms thus are suitable for abstract control procedures involving third parties such as consumer groups, whereas individually negotiated terms can be reviewed only in the course of a concrete legal action between the parties.[326]

At first the Commission was reluctant to embrace the German scholars' proposals. But the scholars persisted. Practically on the eve of adoption, in the

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Bemerkungen zum Vorschlag der EG-Kommission, BB [Betriebs-Berater] 1991, 701, 703-04 [hereinafter Brandner & Ulmer, *EG-Richtlinie*]. *See also* Bunte, *supra* note 231, at 331 (considering a July 1989 proposal of the Commission and noting that the E.U. proposal is based on a model of "contractual justice" (*Vertragsgerechtigkeit*)); Peter Hommelhoff, *Zivilrecht unter dem Einfluß europäischer Rechtsangleichung*, AcP [Archiv für die civilistische Praxis] 1992, 71, 90-91 (noting that control of individual contracts encountered sharp opposition because it "buries" private autonomy and disturbs the ordering function of the free market). The Brandner & Ulmer article is regarded as the most influential of German contributions and covers all the core questions. Christian Jorges, *Die Europäisierung des Privatrechts als Rationalisierungsprozeß und als Streit der Disziplinen*, ZeuP 1995, 181, 193.

Brandner and Ulmer grouped their criticisms into four categories: (1) the fact that the draft created a special law for consumers; (2) the scope of the directive; (3) the standard of control; and (4) control procedures. Only their second criticism is addressed here. The first is an issue much broader than the Unfair Terms Directive itself. *See* Miklitz, *supra* note 251, 532 n.74 (noting that the discussion "fills volumes" and with citations thereto).

323. Brandner & Ulmer, *The Community Directive on Unfair Terms*, *supra* note 322, at 652-54.

324. Edgar Zoller, *Dogmatik, Anwendungsprobleme und die ungewisse Zukunft des Vorrangs individueller Vertragsvereinbarungen von Allgemeinen Geschäftsbedingungen (§ 4 AGBG)*, JZ 1991, 850, 853, 855.

325. These criticisms were made by, *inter alia*, Brandner & Ulmer, *The Community Directive on Unfair Terms*, *supra* note 322, at 651-54; Brandner & Ulmer, *EG-Richtlinie*, *supra* note 322, at 703-04; Bunte, *Gedanken zur Harmonisierung*, *supra* note 231, at 329, 331, 333; Hommelhoff, *supra* note 322, at 90-93 (with further citation).

326. Brandner & Ulmer, *The Community Directive on Unfair Terms*, *supra* note 322, at 654. They contended that any control of individually negotiated terms should be permitted only if an "urgent real necessity" is shown and only if the control is subject to different rules. Brandner & Ulmer, *EG-Richtlinie*, *supra* note 332, at 704.

fall of 1992, the Commission largely gave in and changed the text of the Unfair Terms Directive.[327] As adopted, paragraph 1 of Article 3 excludes from the directive's application terms that have been "individually negotiated."[328] Paragraph 2 provides that "pre-formulated standard contracts" are not individually negotiated.[329] Article 4, paragraph 2, provides that findings of unfairness shall "relate neither to the definition of the main subject matter of the contract nor to the adequacy of the price and remuneration."[330] With these revisions, German scholars pronounced that the directive preserved the principle of party autonomy as the "Basic Institution of all European legal systems."[331]

Even with the changes, German scholars recognized that differences in outlook remained. The directive's orientation remains consumer protection; the German law's orientation is general contract law.[332] Germany had no choice but to implement the directive. The question was how to do it. German scholars considered two possibilities: amending the old law or adopting a new one to exist parallel to the old.[333] The legislature looked only at the former possiblility and considered no draft legislation that would have created a new law.[334] The close similarity between the Unfair Terms Directive and the Standard Terms Statute counseled against implementing the directive through a statute separate from the Standard Terms Statute.[335] Restricting the scope of the Standard Terms Statute also did not make sense, since the directive itself set only a minimum standard and explicitly allows Member States to provide protection that reaches further. In Germany, that additional protection consists of the incorporation control and the protection of non-consumers.

The German legislature held fast to the German law and took a minimalist solution that the existing law "should be retained so far as possible," since, in its view, the German Standard Terms Statute was largely in compliance even without revision.[336] The legislature passed relatively minor changes. It modified the conflicts of law rule and added a new section

327. Heinrichs, *supra* note 241, at 1817 (discussing the history of the adoption of the directive). *See* Miklitz, *supra* note 251, at 523 (noting how the German side managed to get individual contracts removed even after the last draft).

328. Council Directive 93/13/EEC, art. 3(1), 1993 O.J. (L 95/29).

329. *Id.* art. 3(2).

330. *Id.* art. 4(2).

331. Heinrichs, *supra* note 241, at 1817.

332. *See* Schmidt-Salzer, *supra* note 241, at 733.

333. This choice is presented explicitly by Heinrichs, *supra* note 211, at 153. *See also* Schmidt-Salzer, *supra* note *241,* at 735; Miklitz, *supra* note 249, at 532-34 (noting that this directive, more than any others before it, posed the issue of a separate law for consumers).

334. *Cf.* Heinrich, *Die Entwicklung des Rechts der Allgemeinen Geschäftsbedingungen im Jahre 1995*, NJW 1996, 1381, at 1381; *Umsetzung der Richtlinie des Rates vom 5.4.1993 über mißbräuchliche Klauseln in Verbraucherverträgen: Referentenentwurf eines Gesetzes zur Änderung des AGB-Gesetzes*, BB 1995, 111.

335. Heinrichs, *supra* note 241, at 1818.

336. Gesetz Entwurf der Bundesregierung, Entwurf eines Gesetzes zur Änderung des AGB-Gesetzes [Draft of a Statute to Amend the Standard Terms Statute], Oct. 20, 1995, Drucksache 13/2713 at points B, *available at* http://www.bundestag.de. When Germany delayed past the deadline for implementing the Unfair Terms Directive, one leading expert in the Standard Terms Statute proposed that almost all required measures could be implemented simply by construing existing law in conformity with the Directive. Heinrichs, *supra* note 211, at 153. Supporting the view of minimal changes, see Remien, *supra* note 246, at 65-66; Ulmer *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, at 346-47 (warning against using the implementation as an opportunity to narrow the law).

for consumer contracts. That section, now Civil Code section 310(3), applies the content control to certain consumer contracts that otherwise exceptionally would not be covered.[337]

Section 310(3) makes yet another change that may seem minor to an outside observer, but illuminates the differences in concepts at stake. It now requires that in consumer contracts, "[w]hen deciding whether there has been unreasonable detriment under sections 307(1) and 307(2) the circumstances surrounding the conclusion of the contract must also be taken into account." German scholars vary in how significant they view the change,[338] but all recognize what this provision means. No longer is the standard terms law exclusively a shield against imposition of improper contract terms, but now it is also a protection of consumers in their typical position of inferiority.[339]

The Unfair Terms Directive and the German standard terms law are both subject to broader European law developments. Further E.U. action in the consumer area is likely and might result either in changes in the directive itself or in adopting legislation that would prevail over the directive. The latter has already occurred in the Guarantees Directive, which obviated any need for control of consumer warranties under Unfair Terms law by substituting mandatory legislative terms.[340]

Whether the Unfair Terms Directive will be revised to reverse the compromises of fall 1992 and introduce the consumer protection model is unclear at the time of this writing. At the July 1999 conference sponsored by the Commission there was interest in extending the directive to principal obligations as some Member States had already done.[341] While the Commission in its April 2000 Report did not formally endorse such a step, it raised the possibility and observed that no problems in practice had arisen in those Member States that had taken this step.[342] The Economic and Social Committee was not so restrained. It recommended that the directive be

337. The exceptional situations arise when a form contract is used only once or originates with a third person. The new section also applied section 305c(2) to consumers. That section construes standard terms against the user. The new section did not subject these consumer contracts to the incorporation control. Subsequent to the adoption of the implementing legislation, the European Court of Justice rejected the argument of the Netherlands that it need not adopt a statutory transparency requirement to implement Article 5 of the directive, because judicial interpretation of the general clause reached the same result. Germany had done the same thing. As part of the obligation reform law, Section 307(1) was added to meet the decision of the court. Beschlussempfehlung und Bericht des Rechtsauschusses: Entwurf eines Gesetzes zur Modernisierung des Schuldrechts, Oct. 8, 2001, Drucksache 14/7052 at 188; Heinrichs *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236 § 307 at 121, margin no. 16.

338. *See* Miklitz, *supra* note 251, at 528 (discussing different views); Remien, *supra* note 246, at 52-57 (arguing that the Unfair Terms Directive did not adopt a "particular-personalized," *i.e.*, *konkret-individuellen*, approach).

339. LOCHER, *supra* note 287, at 506, margin no. 3; Bunte, *supra* note 137, at 1389; Reinhard Damm, *Privatautonomie und Verbraucherschutz—Legalstruktur und Realstruktur von Autonomiekonzepten*, VersR 1999, 129 n.91.

340. For example, the Guarantees Directive displaces the Unfair Terms Directive and provides mandatory law for consumer guarantees. *See infra* text accompanying notes 357-59.

341. Hans Schulte-Nölke, *Fünf Jahre AGB-Richtlinie 93/13/EWG - Weitere Rechtsetzungspläne der Kommission?*, NJW 1999, 3176.

342. E.U. Commission Report, *supra* note 129, at 14-15, 31.

amended to include individually negotiated terms and the main subject matter of the contract.[343]

E. *The American License in Germany*

American standard terms are no strangers to Germany. It used to be that American businesses operating in Germany simply translated their U.S. terms into German and handed them over to their German customers unchanged. Today that still happens more frequently than one would like to think.[344] But such foolishness requires a near reckless lack of attention to businesses located in Germany. However, with ever more American companies doing business worldwide on the Internet, it is understandable that licensors located in the United States and accustomed to doing business at home offer products and services without thinking about foreign law.[345]

Nor are American standard terms strangers to German controls. Not long after the Internet became available in Germany, German consumer groups challenged the Internet terms of major U.S. service providers America Online and CompuServe. The former agreed to a cease-and-desist declaration; the latter suffered a default judgment. In its declaration, America Online agreed to stop using nineteen terms in its standard agreement and promised to pay DM 2,000 (now about € 1,000) each time it uses one of the same terms or a term having comparable content, with a maximum of DM 19,000 (now about € 10,000) per contract. CompuServe, if it uses again any of twenty-three terms in its former standard agreement, is subject to a civil fine of up to DM 500,000 (now about € 250,000) and its Chief Executive Officer to civil commitment for contempt of court for up to six months. The same association of consumer groups also took on Microsoft Corporation's license for its Windows 2000 operating system. Microsoft also agreed to a binding cease-and-desist declaration. As a result these three American firms are committed not to use in Germany many terms that are similar to terms that they continue to use in the United States. These terms govern such matters as: liability

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343. Opinion of the Economic and Social Committee, *supra* note 180, at 124, conclusion 10.3. The Committee also recommended that the Unfair Terms Directive be extended to professionals, i.e., non-consumers. *Id.* at 124, conclusion 10.2.

344. *See* Thomas Hoeren & Dirk Schuhmacher, *Verwendungsbeschränkungen im Softwarevertrag*, CR 2000, 137. It even happens that German companies copy the terms of U.S. market leaders.

345. That model—a mass market software license delivered from an American owner over the Internet directly to the end user—is the only one considered here. Use of shrink-wrap licenses or third party distributors raises additional questions. In the case of shrink-wrap, is the act of opening the software a sufficient manifestation of assent? In German law it is, if the attention of the customer is called to the fact that the software package contains a notice that the license terms are contained within *and* the license terms are made available to the customer *before* opening the package. In the case of third party distribution there is an issue as to whether there is an agreement between the computer information producer and the customer or only between the customer and the distributor. The former is now generally accepted, provided, possibly, that a reference to the relationship with the supplier is noted to avoid that relationship being regarded as surprising. *See* Jürgen Weyers, Die Wirksamkeit von Schutzhüllenverträgen bei Standardsoftware in Deutschland und den USA 19-84 (2000) (unpublished dissertation, Universität Köln) http://www.ub.uni-koeln.de/ediss/archiv/2000/11v3852.pdf. This discussion is also limited to software; German law has not yet followed the UCITA model of referring to "computer information" to include both software and information. The next paragraph in the text, however, shows that the law applies to online services as well.

limitations, warranty disclaimers, licensee obligation to indemnify licensor, unlimited licensee obligation, acceptance of incorporation of other terms, choice-of-law and forum, retention of unilateral right to change terms accepted by subsequent use, agreement that additional terms be incorporated, restriction on right of licensee to terminate, retention of payment on termination, and legal characterization of relationship.[346]

Other American licensors likewise are in for unpleasant surprises if they fail to pay attention to German law. If a licensee is a consumer, almost certainly the license is subject to German standard terms law.[347] If the licensee is a businessperson, a more complicaeted conflicts of law analysis is necessary to determine which controls apply.[348] Yet, in the case of a license to a

346. The author did not attempt to determine the extent to which American companies have already been subjected to standard terms control in Europe. The information in this paragraph comes from a single inquiry of an association of German consumer groups, the Verbraucherzentral Bundesverband e.V. ("VzBv"), about proceedings that it was aware of in Germany against American Internet companies. In a letter to the author dated November 4, 2002, it provided copies of the relevant papers from its actions against America Online, CompuServe and Microsoft. The documents consist of: (1) for America Online, Inc., a demand letter from VzBv dated May 21, 1997, and a "Cease-and-Desist Declaration with Promise to Pay Contract Penalties" (*Unterlassungserklärung mit Vertragsetrafsverspreche*) from America Online dated February 18, 1998 (on file with *The Yale Journal of International Law*); (2) for CompuServe, Inc., a Default Judgment (*Versäumnisurteil*) dated June 2, 1998, Landgericht Berlin, File No. 26.O.364/97 (same); (3) for Microsoft Corporation, a demand letter from VzBv dated April 17, 2000, and a Cease-and-Desist Declaration (*Unterlassungserklärung*) from Microsoft dated October 9, 2000 (same).

347. CISG does not apply to transactions in goods bought for personal, family, or household uses. German conflicts law has special rules for consumers that make it unlikely that an American licensor could avoid the standard terms law even by a choice of law provision. Notwithstanding choice of law, under Article 29(2) No. 1, German standard terms law applies to transactions where a contract follows "an express offer or advertisement" in Germany and the consumer completes the contract in Germany. That will be the case in an Internet transaction where the user has in any sense targeted the German market, e.g., through a presence separate from the Internet or through tailoring its Internet site for German customers. It might even be the case for Internet sites in the United States that make no effort to service the German market. Georg Borges, *Geschäfte per Internet und deutscher Verbraucherschutz*, Zeitschrift für Wirtschaftsrecht 1999, Issue 14, http://www.rws-verlag.de/volltext/borges.htm, at 2.2.

348. Whether CISG applies to software licenses is disputed and depends upon whether software should be characterized as "goods." *See* Boss, *supra* note 227, at 180-82. German law treats mass market licenses as sales of goods under domestic law. Judgment of Nov. 4, 1987, VIII ZR 314/86, CR 1988, 124, 125-26. *See infra* text accompanying notes 355-56. Accordingly German courts have treated transactions in software as sales of goods under CISG. *See, e.g.*, Judgment of Feb. 8, 1995, Landgericht München I, 8 HKO 24667/93, *available at* http://www.jura.uni-freiburg.de/ipr1/cisg/urteile/text/203.htm. Whether they would do so for software delivered over the Internet rather than in a tangible medium is uncertain but considered by some as probable. *Grenzüberschreitende Softwareüberlassung und E-Mängelrüge nach dem CISG*, at B.1.2. (1999), RAUSCHHOFER ONLINE, *at* http://www.rechtsanwalt.de/cisg.html. If CISG does apply, its contract formation rules, Articles 14 *et seq.*, apply. *See* Judgment of Oct. 31, 2001, VIII ZR 60/01, *available at* http://www.bgh-free.de, where the German Supreme Court held that CISG provides the rules regarding incorporation and implied from CISG formation rules an opportunity to review obligations comparable to that required by German law. Article 4 of CISG leaves to local law "[t]he validity of the contract or any of its provisions;" national law provides the rules regarding content control. Schmidt *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, app. § 2 at 276, margin no. 12.

If CISG does not apply, in the absence of an effective choice of a law, a German court would probably apply American law to contracts with non-consumers. Article 28 of the German conflicts law, Einführungsgesetz zum Bürgerlichen Gesetzbuch (EGBGB), provides that in the absence of an agreement, the law of the state having the closest connection to the contract applies. The law with the closest connection is presumed to be the law of the party who has to provide the "characteristic performance" of the contract. That means the law of a foreign supplier ordinarily applies. Schmidt *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, app. § 2, at 269, margin no. 2. One might argue that even if CISG applies, this rule directs application of American content law.

businessperson, an attentive licensor can make an effective choice of American law, probably even in a standard term license.[349]

1. *Incorporation*

A "mass-market license" under UCITA[350] ordinarily constitutes standard terms in the sense of Civil Code section 305(1).[351] If the licensee is not a businessperson, under section 305(2) the license's standard terms become part of the contract only if the licensee is expressly advised of them and is given the opportunity to review them. That review must be at or before the conclusion of the license.[352] If the licensee is a businessperson, then the stringent requirements of section 305(2) do not apply and the laxer rules of the Civil Code governing conclusion of contracts generally govern. Under those rules the reference to the standard terms might be implied by conduct.[353] A procedure whereby the licensee is given access to the terms before committing to the license by clicking ("click-wrap") should be sufficient, at least if the average customer cannot click through without having noticed and decided whether to take the opportunity to review the terms.[354] "Browse-wrap," i.e., a notice given by a site that by using it, the user agrees to certain license terms, is said not to comply with the law's requirements.[355] The individual terms are subject to the other incorporation controls, i.e., individually negotiated terms take priority (section 305b), surprising terms are invalid (section 305c(1)), and ambiguous terms are construed against the licensor (section 305c(2)). Use restrictions are not ordinarily surprising.

2. *Content Control*

With the exception of licenses between businesspersons that include an effective choice of non-German law, UCITA licenses between American

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349. Party autonomy is the basic rule of German conflicts law, i.e., the parties are free to choose the law they wish to apply to their agreement. It is laid down in EGBGB Article 27 and requires that the choice of law either be express or follow with reasonable certainty from the terms of the contract or the circumstances of the transaction. That choice of law could be made in a standard form. Under Articles 27(4) and 31(1) its validity would be determined by the law chosen (e.g., New York law). German Standard Terms law would not apply. Schmidt *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, app. § 9-11, 1124, at 1227-29. Under Article 31(2), however, a party may challenge whether there was an agreement on the point. *Id.* at 1226-28, margin nos. 576-77.

350. UCITA § 102(a)(43) & (44).

351. *See* Schmidt *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, app. §§ 9-11, at 1051-52, margin no. 269. It would not constitute standard terms if it were uniquely used with a party that is not a consumer.

352. Dirk Schuhmacher, *Wirksamkeit von typischen Klauseln in Softwareüberlassungsverträgen*, CR 2000, 641, 644 (noting that this requirement is "essential" and is not satisfied if the terms are contained only in a sealed box). Thus the approach sanctioned by UCITA Section 209(b) would not work. *Cf. id.* at 643 n.16 (expressing skepticism regarding software producer practice of providing for licensee to return product). *See also* Ulmer *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 2, at 230-31, margin no. 55.

353. Ulmer, *supra* note 54, § 2, at 246, margin no. 80.

354. *See* Weyers, *supra* note 345, at 85-91. The author observed that a leading German antiquarian book exchange Internet site in summer 2002 altered its procedures to require a "click-wrap" acceptance of each individual bookseller's standard terms. *See* Zentrales Verzeichnis Antiquarischer Bucher, http://www.zvab.com.

355. Schuhmacher, *supra* note 352, at 643.

licensors and German licensees are subject to German content controls. Application of those controls depends upon the nature of the software license involved, i.e., how it is classified under German law and whether it is with a businessperson or not.

Software can fall into any one of three different classes of contract under German law. A software license where the license term is unlimited is known as a *Standardlizenz* ("standard license") and is treated as a sales contract (*Kaufvertrag*). If the license term is for a limited time period (and typically, although not necessarily, there are recurring payments), then the license is known as a *Dauerlizenz* ("duration license") and is treated as a lease (*Mietvertrag*). Finally, if the software is developed as part of the agreement, then the license is treated as part of a service contract (*Werkvertrag*).[356] UCITA mass market licenses are usually standard licenses in the German sense, and that is the only variety treated here.

Except for separately negotiated terms under section 305b and terms respecting fundamental performances under section 307(3), licenses with consumers are subject to testing first under the prohibited list of Section 309, then under the list of suspect terms under section 308, then finally under the general clause of section 307. In the case of licenses with businesspersons, sections 308 and 309 have no formal applicability, but in practice, application of the general clause of Section 307 usually follows the application of sections 308 and 309.[357]

The introductory language to the prohibited list of section 309 makes explicit that it assumes that a contract term reviewed is one about which the parties might agree otherwise, at least in negotiated terms. The legislature added this language when it integrated the Standard Terms Statute into the Civil Code. It was necessary to take account of the changes in the civil law made to comply with the E.U. Guarantees Directive, which requires that many aspects of consumer contracts—among them warranties—be made mandatory and not subject to modification by agreement.

3. *Warranty Disclaimers and Limitations of Remedy*

Pursuant to the E.U. Guarantees Directive, most issues of consumer warranties and remedies are now mandatory law. Review under standard terms law is foreclosed.[358] American standard licenses with German consumers must comply with this mandatory law.[359]

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356. Bettina Goldmann & Rebecca Redecke, *Gewährleistung bei Softwarelizenzverträgen nach dem Schuldrechtsmodernisierungsgesetz*, MMR [Multimedia und Recht] 2002, 3 (noting that the new legislation had significant changes for *Kaufvertrag* but not for the *Mietvertrag*). Schmidt *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, app. §§ 9-11 at 1051-52, 1057 margin nos. 269, 272. The idea of treating software licenses as *sui generis* was rejected. *Id. See also* Hoeren & Schuhmacher, *supra* note 344, at 137-38.

357. *See supra* text accompanying notes 294-96.

358. *See* Goldmann & Redecke, *supra* note 356, at 6. Civil Code Section 475 invalidates agreements made prior to notification of a defect that limit the consumer's rights under Sections 433-35, 437, and 439-43. Section 475 leaves only a few points open for deviation through standard terms and thus for review under the content controls. For example, a standard term may reduce the warranty period from two years to one. This was no great victory for business, since before the new law came into effect the mandatory warranty period was six months. A standard term might also require that the dissatisfied

Warranties and limitations of remedy in licenses with businesspersons remain subject to testing under standard terms law. Formally, this is only through the general clause of section 307.[360] Practically, the extensive provisions in section 309(8)(b) (reprinted in the Appendix) governing warranties are likely—but not necessarily—to find application.[361] Subdivision (aa) provides a general rule that a term which excludes warranty claims completely or for relevant parts of defective products is invalid.[362] Subdivisions (bb) through (dd) govern terms that limit remedies to repair or replacement: (bb) invalidates such terms unless they expressly reserve the right, should repair or replacement fail, to cancel the contract or to reduce the contract price; Subdivision (cc) precludes a user from imposing costs of repair or replacement on the other party; Subdivision (dd) prevents the user from setting certain pre-conditions on repair or replacement. Subdivisions (ee) and (ff) restrict use of terms imposing deadlines on claims limitation: subdivision (ee) provides that notice requirements for non-obvious defects may not be shorter than the applicable statute of limitations for claims. Subdivision (ff) provides that the legally required statute of limitation may not be reduced to less than one year.[363]

4. *Damage Exclusions and Limitations*

The same provision of the Civil Code that makes warranty provisions in consumer contracts mandatory and withdraws them from disposition by the parties explicitly excludes from its coverage damage exclusions and limitations. The provision provides that they shall continue to be reviewed

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recipient of a defective product accept damages in lieu of performance. Westphalen, *supra* note 249, at 24.

359. The mandatory provisions are the following: Section 433 requires the seller to provide the buyer with the product free of physical or legal defects. Sections 434 and 435 respectively define those defects. Section 437 defines the rights of the buyer in the case of defects. Sections 439-41 govern the parties' rights respecting repair or replacement, rescission and contract price reduction. Section 442 governs the buyer's knowledge of defects. Section 443 governs express warranties. Restructuring standard licenses as duration licenses probably would not help the licensor. Not only are duration licenses generally more demanding, the attempted re-characterization of standard licenses as duration licenses would run up against the probation on circumvention in the second sentence of Civil Code Section 475(1).

360. Now that businessperson to consumer contracts are subject to mandatory law, No. 8b has lost most of its significance. It applies directly only to construction contracts and contracts between consumers. Heinrichs *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236, § 309, at 152, margin no. 53. Practically the only purpose for keeping it in the law was for its effect on contracts between businesspersons. Schubel, *supra* note 277, at 1117.

361. Björn Gaul, *Standardsoftware: Veränderung von Gewährleistungsansprüchen durch AGB*, CR 2000, 570, 571 (noting the "radiant" effect of the two sections on application of the general clause and citing a Supreme Court decision for the proposition that even between merchants a standard term would be invalid if it led to loss of warranty claims); Goldmann & Redecke, *supra* note 356, at 6, 7 (noting uncertainties brought by the modernization law but concluding that the new consumer rules will act as *Leitbild* for application of Section 307 to contracts among businesspersons).

362. Hensen *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, § 11 (10)(a), at 855, margin no. 9; Heinrichs *in* PALANDT, BGB 61st ed. ErgB, *supra* note 236 § 309, at 152-53, margin nos. 53, 56. The law, as recently amended, explicitly provides that those characteristics may include representations made in advertising. § 434(1) BGB.

363. Westphalen, *supra* note 249, at 25. For an extensive discussion of product and inspection requirements in the context of standard software licenses, see Gaul, *supra* note 361, at 571-76.

under the standard terms law.[364] The prohibited list of section 309 governs two types of damage exclusions and limitations. Section 309(7)(a) invalidates standard terms that exclude or limit liability for negligent injury to "life, person or health." Section 309(7)(b) invalidates standard terms that exclude or limit liability for gross negligence or intentional violation of contractual obligations. These same restrictions apply to licenses with businesspersons through application of the general clause.[365] Neither section 309 nor section 308 governs limitations and exclusions of liability for simple negligence. That does not, however, permit the conclusion that they are always permissible.

Standard terms that exclude or limit liability for simple negligence, or for other grounds not covered in section 309(7), are subject to review under the general clause of section 307(2). This principally occurs under section 307(2)(2) which can lead to invalidation of a term that "restricts essential rights or duties resulting from the nature of the contract in such a manner that there is a risk that the purpose of the contract will not be achieved." As the decision of the German Supreme Court of October 24, 2001 holds, the test is "whether the exclusion of liability leads to evisceration of those contractual duties (so-called cardinal duties), which originally made possible the performance of the contract and on the fulfillment of which the contract partner trusted and may rely."[366] It is debated whether an exclusion of liability for damages for typical computer software problems, such as data loss, or the reduction of disk capacity or processing speed, would fulfill that test.[367] Rather than try to identify which duties a court may later determine to be "cardinal," typical disclaimers accept liability for intention, gross negligence, and negligence affecting cardinal duties, excluding all other liability.[368] Alternatively, or additionally, licenses may limit liability. Limitations on the amounts of damages for ordinary negligence are generally permissible. In the case of ordinary negligence affecting cardinal duties, however, the amount of the limitation provided must correspond to the foreseeable amount of damages. Limitations on damages may also restrict liability to direct damage and exclude indirect damage or untypical consequential damages.[369] In either

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364. § 475(3) BGB.

365. Gerald Spindler, *Haftungsklauseln in Provider-Verträgen: Probleme der Inhaltskontrolle*, CR 1999, 626, 631 (referring to AGB § 11, the predecessor of Section 309); Goldmann & Redecke, *supra* note 356, at 7.

366. Judgment of Oct. 24, 2001, *supra* note 288.

367. Schmidt *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, app. § 9, at 1060-61, margin no. 66.

368. Spindler, *supra* note 276, at 631.

369. Hensen *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54,§ 11(7), at 819-20, margin no. 27. One model clause is:

> Schadenersatzansprüche können Sie gegen uns nur dann geltend machen, wenn der Schaden von uns, unseren gesetzlichen Vertretern oder Erfüllungsgehilfen vorsätzlich oder grob fahrlässig verursacht wurde, oder wenn wir einen Schaden dadurch verursacht haben, daß wir eine für die Vertragsdurchführung wesentliche Pflicht vorsätzlich oder grob fahrlässig verletzt haben. [You can validly assert claims for damages against us only if the damage was caused by us, our legal representatives or our fulfillment partners intentionally or with gross negligence, or we caused damages through an intentionally or grossly negligent violation of an obligation material to fulfilling the contract.].

Marcus Werner, *CD-Rom Nutzungsbebedingungen*, CR 1998, 391, 392.

case, such a term is invalid if it includes damages caused by intent or gross negligence.[370]

5. *Copy, Use, and Transfer Restrictions*

The Copyright Statute (*Gesetz über Urheberrecht und Verwandte Schurtzrechte*), in particular sections 69a to 69g governing software, impose certain mandatory requirements affecting standard terms limiting copying or use. Section 69d(2) permits licensees to make back-up copies necessary for future use. A standard term that required the licensee not to make an archival copy, but to rely on such a copy held by the licensor, was held invalid as not recognizing the licensee's interest in having available an archival copy even if the licensor should go out of business. Section 69d(3) permits licensees to observe and test the functioning of software. Section 69e permits licensees to de-compile software when such de-compiling is "indispensable to obtain the information necessary to achieve the interoperability of an independently created computer program with other programs," provided that certain conditions are met. Section 69g(2) provides that contract terms that contradict any of these three sections are invalid.

Other copy, use, and transfer restrictions are subject to the general clause of section 307. The Copyright Statute provides the measure against which departures from the statutory scheme are judged.[371] Section 69d provides that unless the parties provide otherwise, copying and translating programs do not require authorization "where they are necessary for the use of the computer program by any person entitled to use a copy of the program in accordance with its intended purpose, including for error correction."[372] So-called CPU clauses that restrict use to a single computer constitute an unreasonable disadvantage, since they prevent licensees from updating their hardware without having to pay additional charges.[373] Restrictions that limit licensees of standard licenses from sub-licensing the software are effective. Restrictions that prohibit such licensees from transferring such software and all their rights to a third party, however, are not.[374] As a result of the close supervision of terms, it is said that strict license terms in practice often have only minimal effectiveness.[375]

6. *Enforcement*

An American licensor is likely to discover that it has violated German standard terms law when a consumer association sends it a warning letter

370. Spindler, *supra* note 276, at 632.

371. Schmidt *in* ULMER/BRANDNER/HENSEN, *supra* note 54, app. § 9, at 1062-64, margin no. 278; Schuhmacher, *supra* note 352, at 645-46 (addressing particularly copyright law).

372. Translations from the Copyright Statute are from the translation of the World Intellectual Property Organization, http://www.iuscomp.org/gla/. For the scope of permissible restrictions, see Hoeren & Schuhmacher, *supra* note 344, at 139 (noting that Section 69(d) can be departed from only within certain bounds).

373. Schuhmacher, *supra* note 352, at 646-47.

374. Schmidt *in* ULMER/BRANDNER/HENSEN, AGB-GESETZ, *supra* note 54, app. § 9, at 1062-64, margin no. 278.

375. Schuhmacher, *supra* note 352, at 650.

demanding that it cease using unlawful terms or face penalties. The American licensor will then scurry to its American attorney, who hopefully will be well-versed enough to contact a German attorney to confirm that, yes, indeed, a lawsuit and penalties could follow a failure to comply. The German attorney will point out that section 6 of the Injunctions Act permits a German plaintiff to sue a defendant not domiciled in Germany in any district where the defendant uses the unlawful terms. The cease-and-desist declaration a defendant must sign not only will subject it to penalties for using these terms again, but will also prohibit use of similar terms and invalidate all such existing terms. Thus an American licensor cannot blithely assume that it can use prohibited terms free of risk. Should that licensor nevertheless use the terms, it runs the risk that in seeking expansive exclusions of liability, it may fail to take advantage of those limitations on liability that would have been available to it.

V. CONCLUSIONS

National laws that implement the Unfair Terms Directive are a reality throughout Europe. Americans—especially those doing business on the Internet—should take account of them. With the impending enlargement of the European Union, American standard terms will be subject to scrutiny from Ireland to Poland and from Malta to Finland. Failure to revise American standard terms accordingly could have serious consequences. There is every reason to believe that many standard terms that are common in the United States are unlawful in Europe.[376] While this article has not attempted a comparative catalogue of such invalid terms, a future work that does so would be useful.

Functioning systems for control of unfair standard terms exist in Europe. These systems are more ambitious than the present-day American system.[377] Their very existence challenges complacency with current American law. Their existence undermines the two principal arguments raised to support American law: there is no problem, and no system could better balance the competing interests of certainty of contract and fairness of terms. Obviously, our European colleagues think that there is a problem, and they have taken action to deal with it. The apparent success of the German contract model

376. For an example of choice of forum clauses, compare *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585 (1991) (enforcing a choice of Florida forum for Washington state consumer) with *Oceano Grupo Editorial SA v. Rocio Murciano Quintero*, 2000 ECJ CELEX LEXIS 2894 (decision of the European Court of Justice invalidating choice of Spanish forum for Spanish consumer); to see the diverging standards for warranty exclusions and remedy limitations, compare U.C.C. Sections 2-316 and 2-791 (validating such terms) with German Civil Code Section 309(7), (8), and (11) (controlling such clauses) and the E.U. Guarantees Directive (mandating minimum warranties); for the differences in integrated writing and no oral modification requirements, compare U.C.C. Sections 9-202 and 9-209(2) (validating such terms) with Brandner in ULMER/BRANDNER/HENSEN, ABG-GESETZ, *supra* note 54, app. § 9-11, at 1266-1273 (discussing German law's controls on such terms).

377. One attorney with Baker & McKenzie who is admitted to the bar in both California and Germany reports to German readers that, as a rule, American courts do not undertake content control similar to that under the German standard terms law or the E.U. Unfair Terms Directive. Lothar Determann, *Electronic Business in den USA*, *in* ELECTRONIC BUSINESS, ANBAHNUNG, GESTALTUNG, PRAXIS, 9, margin no. 13 (Georgios Gounalakis, ed. 2002).

suggests that there may not be a necessary trade-off between control of unfair terms and predictable contracting.

If the American system is less ambitious than its European counterparts and is largely limited to striking down terms that "shock the conscience,"[378] it has not been by design. When American legislatures enacted U.C.C. section 2-302, they adopted a provision that its drafters hoped would allow American courts to develop "machinery"[379] for "policing"[380] contract terms. The German Supreme Court's development of such machinery from essentially the same starting point largely confirms the vision of the drafters of the U.C.C.[381] In the United States there has been no national debate about whether the present restrained application of U.C.C. section 2-302 is preferred. The closest that the United States has come to such a debate is the ongoing struggle over reform of the U.C.C. That is a toss-up so far. Business interests blocked the original revision of U.C.C. Revised Article 2—Sales, while consumer groups blocked U.C.C. Proposed Article 2B—Licenses and are threatening UCITA.

How did the German legal system—beginning from a very similar starting point—develop a considerably more ambitious review of standard terms than did the American legal system? A number of explanations come to mind. Surely larger social and political factors were at work. As has been shown, in Germany there was a national consensus to limit oppressive terms.[382] That consensus was rooted in views about society, the individual, and the role of government in society. Where an American might see control of standard terms as government meddling in relations between private parties and as a limitation on freedom of contract, a German might see the choice *not* to intervene as government toleration of exploitation of one private party by another, and government complicity in that exploitation—by providing contract law upholding, and a legal system enforcing, form contracts.

But there are other, more strictly legal explanations for how the German legal system, from a similar starting point, was able to develop an ambitious program of standard terms control and the American legal system was not. In the area of standard terms, the German legal system has limited authoritative sources of the law, has furnished abstract definitions of unlawful terms, and has provided for proactive enforcement of controls. In contrast, the American legal system has multiplied the sources of the law, has individualized the inquiry, and has limited enforcement to retrospective invalidation of challenged terms.

In both the German and the American legal systems the starting point for development of control of unfair terms was application of general clauses by judges. Yet the German legal system had an advantage from the start: it has one Supreme Court that could and did develop and direct evolution of judge-

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378. *See, e.g.*, Ferguson v. Countrywide Credit Industries, Inc., 298 F.3d 778, 784 (9th Cir. 2002).

379. *See supra* note 74.

380. *Supra* note 26 (U.C.C. quoting Section 2-302, Official Comment 1).

381. One cannot read the section on boilerplate in THE COMMON LAW TRADITION—Llewellyn's last word on the subject—and reasonably believe that he would have found the anemic application of Section 2-302 a sufficient response to a problem he found so serious and pervasive. *See* LLEWELLYN, *supra* note 32, at 362.

382. *See supra* text accompanying notes 213 to 217.

made law. German standard terms law is federal law. The pronouncements of its single federal Supreme Court are authoritative.[383] In the American legal system, on the other hand, although the Uniform Commercial Code provides one uniform rule in the general clause in section 2-302, fifty different courts are the sources for interpretation and application of it. It is no wonder that there is no authoritative statement of unconscionability.[384]

Moreover, already more than a quarter of a century ago, while the United States was struggling with judges applying that single general clause, the German legislature chose to build a statutory structure on that judge-made law foundation. That new structure provided additional authoritative points for application of unfair terms control, while maintaining a general clause to respond to the need for flexibility. In contrast, American scholars, including Llewellyn, have mostly assumed that control of unfair terms is necessarily a task for judge-made law with little room for statute law.[385] Obviously the apparent success of the German Standard Terms Statute challenges that assumption. It demonstrates that statute law can facilitate control of unfair terms.

Another reason that German control of unfair terms has been able to develop to be more robust than its American counterpart is that it is abstract rather than personalized. The German system of control was purposely limited to control of standard terms so that it could provide standard solutions to standard problems. Inquiry into all the individual circumstances of particular parties is not necessary or desired. In this way the work of courts in finding facts is reduced. But still more important is that abstract application "concretizes" the general prohibitions into groups of cases and types of terms. It facilitates a universal application of the resulting control. Accordingly, the German legal system rejects the less concrete consumer model. The German legal system avoids control of the main subject of the contract and of individually negotiated terms for fear of infringing on the parties' freedom of contract and interfering with their presumptively sound economic decisions.

What the European Commission calls "positive enforcement"[386] explains how the German legal system has been more successful than its American counterpart in deterring use of unfair terms. An American court's decision finding a term unconscionable cannot do more than invalidate the use of the specific term in a particular contract. It thus has little effect beyond that individual case.[387] A German court's decision, on the other hand, can not only

383. The Court's constitution helps it provide authoritative decisions to develop and direct law creation. It has about one hundred judges, but is spared the burden of deciding constitutional cases, which are the province of the Constitutional Court (*Bundesverfassungsgericht*). Its judges decide most cases in panels of five judges ("Senates") specialized by area of law. As a result the Court is able to provide numerous and consistent decisions.

384. *Accord* Dawson, *supra* note 13, at 1126.

385. *See, e.g.*, LLEWELLYN, *supra* note 32, at 370 ("[I]n our system an approach by statute seems to me dubious, uncertain, and likely to be both awkward in manner and deficient or spotty in scope."); SLAWSON, *supra* note 17, at 174 ("The history of the reforms demonstrates the superiority of judicial law-making over legislation for contract law."); Woodward, *supra* note 81, at 1004 ("Any effort formally to classify the enormous range of commercial contracts subject to article 2 will be labor intensive, incomplete, temporary, and very contentious.").

386. *See supra* text accompanying notes 163-66.

387. *Cf.* Klock, *supra* note 6, at 332 (quoting HUGH COLLINS, REGULATING CONTRACTS 233

invalidate specific terms in a particular contract, it can compel users to cease using those terms and comparable terms in all similar contracts. Further, German law simplifies these procedures so that consumer groups can achieve these results without having to go to court.[388]

Even if the German and American legal systems have gone their separate ways in controlling unfair terms following similar beginnings, there is still much for American jurists to learn from European experiences as they contemplate how to make American law the best it can be for American conditions. This article has discussed two models for control of unfair terms in Europe: the contract model of German law and the consumer protection model of the first draft of the Unfair Terms Directive. It has shown the German contract model in practice as one example of standard terms laws at work in the European Union. Future studies of the law in the other fourteen Member States would disclose variations on these models and possibly different models. Consideration of those models by American jurists could inform the American debate over unfair terms both with respect to whether a farther-reaching control is desirable and, if desirable, how best to implement it.

Even without change in American law, application of present U.C.C. section 2-302 would benefit from attention to European experiences and particularly to the conceptual clarity of the German contract model. The essential discovery of the German contract model—that when standard terms are involved there are two transactions, the dickered deal and the supplementary standard terms—has long been known in America. According to Llewellyn, "Rooted in sense, history, and simplicity, it is an answer which could occur to anyone."[389] The German contract model distinguishes separately negotiated terms from standard terms. In the former, it defers to the parties' choice and the principle of party autonomy. In the latter, it finds little exercise of party autonomy and intervenes to protect freedom of contract. It also provides a rationale, i.e., preventing abuse of the freedom of contract-drafting, for that control.[390]

The German contract model disentangles rather than confounds incorporation and content controls. It recognizes the two as separate issues and imposes separate expectations of each. In the case of incorporation control, it insists that users provide other parties with an opportunity to review the terms. In the case of content control, it rejects the idea, common in the United States, that an opportunity to review can substitute for deficient terms. German parties do *not* have to read the standard terms to be safeguarded from overreaching.

The German contract model is not content to place confidence in a single general clause to control content. American attempts to write a suitable general clause for Revised Article 2—Sales suggest that such a task is virtually unachievable. Instead, the German contract model guides the content

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(1999)). *See also supra* text accompanying note 68.

388. *See supra* text accompanying notes 305 and 346.

389. LLEWELLYN, *supra* note 32, at 371.

390. *Cf.* MUNZ, *supra* note 33, at 225 ("American law controls the basis for unjust contract rules, namely disparate bargaining power; German law [controls] the consequences, the unjust contract rules.").

control of the general clause with presumptions and supplements it with "gray" and "black" lists that treat explicitly specific types of terms. Thus it has successfully concretized control in a way that has eluded American courts.

American law already has concepts similar to those found in German law. For example, it distinguishes "procedural unconscionability" from "substantive unconscionability," and negotiated contracts from standard terms (or adhesion) contracts. The German experience suggests a benefit in courts using those concepts more consistently. American courts, even without legislative action, could do that in their application of existing U.C.C. 2-302. Other important aspects of the German contract model might require legislation. For example, legislation would probably be necessary to add "black" and "gray" lists or to a create a more proactive, deterring control along the lines of the E.U.'s "positive" enforcement.[391] Where legislation is required, American experiences in revising the U.C.C. caution against underestimating the difficulties of reaching a solution capable of enactment.[392] Yet the work of the New Jersey Law Revision Commission shows that the possibility of standard terms legislation is not beyond conception.[393]

Reform begins with the conception that things can be otherwise. Comparative inquiry is one of the best ways there is to broaden the scope of the possible. Reform of existing law is limited by one's ability to conceive of alternatives. Through examination of how other legal systems treat similar problems, one can not only conceive of new alternatives, one can see how they work. One need not adopt or even adapt foreign models to learn from them; comparative examination puts one's own law in a critical light.

For more than forty years the United States has denied itself the benefit of foreign experiences with standard terms. For the last dozen years two of the most influential organizations in American law and legions of lawyers have looked at the controversial issue of unfair terms in standard form contracts with no one systematically studying—indeed, with hardly anyone even noting—that a trading bloc comparable in size to the United States and a major trading partner is itself addressing the very same issues and is applying its laws to Americans. This Article shows that in Europe the scholarly and legislative discussion of standard terms has always had a comparative component to it and is better for it.[394] The attempted reforms of the Uniform Commercial Code undertaken to date could have benefited from the European experiences had only those reforms paid attention to those experiences. Today, thanks to global electronic commerce, European and other foreign standard terms law are on American laptops. And American licenses are on

391. *See supra* text accompanying note 187.

392. There are opportunities here for research into comparative law reform. *Compare* Speidel, *supra* note 2, and Greenfield & Rusch, *supra* note 83 (discussing the difficulties of finding political compromise in the uniform laws process) *with* SCHATZ-BERGFELD, *supra* note 213 (discussing finding a political compromise in Germany).

393. *See supra* text accompanying notes 124-27.

394. Micklitz, *supra* note 251, at 534 n.83 ("[T]here is hardly an area of the law, in which such thorough comparative law inquiries have been produced."). For the general attitude in Europe, see Abbo Junker, *Rechtsvergleichung als Grundlagenfach*, JZ 1994, 921, 921 ("Whoever today advocates turning one's view across borders—'to substitute a global for a national horizon'—can be sure of broad approval. He is riding a mighty wave of the *Zeitgeist*.").

European laptops. The United States can afford to ignore foreign law no longer.[395]

395. *Cf.* Ernst C. Stiefel & James R. Maxeiner, *Why Are U.S. Lawyers Not Learning from Comparative Law?*, *in* THE INTERNATIONAL PRACTICE OF LAW 213 (Nedim Vogt et al. eds., 1997); Ernst C. Stiefel & James R. Maxeiner, *Civil Justice Reform in the United States—Opportunity for Learning from Civilized European Procedure Instead of Continued Isolation?*, 42 AM. J. COMP. L. 164 (1994); James R. Maxeiner, *1992: High Time for American Lawyers to Learn from Europe, or Roscoe Pound's 1906 Address Revisited*, 15 FORDHAM INT'L L.J. 1 (1991).

APPENDIX

Standard terms provisions of the German Civil Code effective January 1, 2002, as translated by Geoffrey Thomas and Gerhard Dannemann.[396]

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Section 2: Shaping contractual obligations by means of standard terms

§ 305 Incorporation of standard terms[397] into the contract

(1) Standard terms are all contractual terms pre-established for a multitude of contracts which one party to the contract (the user) presents to the other party upon the conclusion of the contract. It is irrelevant whether the provisions appear as a separate part of a contract or are included in the contractual document itself, how extensive they are, what script is used for them, or what form the contract takes. Contractual terms do not constitute standard terms where they have been individually negotiated between the parties.

(2) Standard terms are incorporated into the contract only if, during the conclusion of the contract, the user

> 1. expressly draws the other party's attention to them, or if, on account of the way in which the contract is concluded, an express reference to them is unreasonably difficult, he draws his attention to them by means of a clearly visible sign at the place where the contract is concluded and
>
> 2. gives the other party, in a reasonable manner that also appropriately takes account of any physical handicap of the other party discernible by the user, the possibility of gaining knowledge of their content, and if the other party agrees that they are to apply.

(3) Subject to observance of the requirements set out in subsection (2) above, the parties may agree in advance that particular standard terms will apply to a particular type of legal transaction.

§ 305a Incorporation in special cases

Even if the requirements set out in § 305(2) Nos 1 and 2 are not observed, if the other party agrees to their application:

> 1. railway tariffs and regulations adopted with the approval of the competent transport authority or on the basis of international conventions and terms of transport, authorised in accordance with the Passenger Transport Act, of trams, trolley buses and motor vehicles in scheduled services are incorporated into the transport contract;
>
> 2. standard terms published in the official journal of the regulatory authority for Post and Telecommunications and kept available in the user's business premises are incorporated
>
> > (a) into contracts of carriage concluded away from business premises by the posting of items in post boxes,
> >
> > (b) into contracts for telecommunications, information and other services that are provided directly and in one go by means of remote communication and during the provision of a telecommunications service, if it is unreasonably difficult to make the standard terms available to the other party before conclusion of the contract.

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396. German Law Archive (2002), *at* http://www.iuscomp.org/gla/statutes/BGB.htm#b2.

397. The original of the translation into British English translates *Allgemeine Geschäftsdedingungen* as "standard business terms." This article prefers "standard terms" as the more idiomatic American usage.

§ 305b Precedence of individually negotiated terms

Individually negotiated terms take precedence over standard terms.

§ 305c Surprising and ambiguous clauses

(1) Provisions in standard terms which in the circumstances, in particular in view of the outward appearance of the contract, are so unusual that the contractual partner of the user could not be expected to have reckoned with them, do not form part of the contract.

(2) In case of doubt, standard terms are interpreted against the user.

§ 306 Legal consequences of non-incorporation and invalidity

(1) If all or some standard terms have not become part of the contract or are invalid, the remainder of the contract continues to be valid.

(2) Where provisions have not become part of the contract or are invalid, the content of the contract is determined by the statutory rules.

(3) The contract is invalid if one party would suffer unreasonable hardship if he were bound by the contract even after the amendment provided for in subsection (2) above.

§ 306a No circumvention

The rules in this section apply even if they are circumvented by other arrangements.

§ 307 Content Control[398]

(1) Provisions in standard terms are invalid if, contrary to the requirement of good faith, they place the contractual partner of the user at an unreasonable disadvantage. An unreasonable disadvantage may also result from the fact that the provision is not clear and comprehensible.

(2) In case of doubt, an unreasonable disadvantage is assumed if a provision

> 1. can not be reconciled with essential basic principles of the statutory rule from which it deviates, or
>
> 2. restricts essential rights or duties resulting from the nature of the contract in such a manner that there is a risk that the purpose of the contract will not be achieved.

(3) Subsections (1) and (2) above, and §§ 308 and 309 apply only to provisions in standard terms by means of which provisions derogating from legal rules or provisions supplementing those rules are agreed. Other provisions may be invalid under subsection (1), sentence 2, above, in conjunction with subsection (1), sentence 1, above.

§ 308 Clauses whose validity depends on an evaluation[399]

In standard terms the following terms, in particular, are invalid:

> 1. (period for acceptance or performance)
> a provision by which the user reserves the right to an unreasonably long or inadequately specified period for acceptance or rejection of an offer or for performance; this does not include

398. The original of the translation translates *Inhaltskontrolle* as "Review of subject-matter."
399. The original of the translation translates *Wertung* as "appraisal."

reservation of the right to perform only after expiry of the period for revocation or return under §§ 355(1) and (2) and 356;

2. (additional period for performance)
a provision by which the user, in derogation from legislative provisions, reserves the right to an unreasonably long or inadequately specified additional period within which to perform;

3. (right of termination)
the stipulation of a right for the user to free himself, without an objectively justified reason specified in the contract, of his duty to perform; this does not apply to a contract for the performance of a recurring obligation;

4. (right of amendment)
the stipulation of the user's right to alter or depart from the promised performance, unless, taking into account the user's interests, the stipulation to alter or depart from performance is reasonable for the other party;

5. (fictitious declarations)
a provision whereby a declaration of the user's contractual partner is deemed or not deemed to have been made by him if he does or fails to do a particular act, unless

a) he is allowed a reasonable period within which to make an express declaration and

b) the user undertakes to draw to his attention at the beginning of the period the particular significance of his conduct; this does not apply to contracts in which the whole of Part B of the contracting rules for award of public works contracts is incorporated;

6. (fictional receipt)
a provision which provides that a declaration by the user of particular importance is deemed to have been received by the other party;

7. (winding-up of contracts)
a provision by which, in the event that one of the parties to the contract terminates the contract or gives notice to terminate it, the user can demand

a) unreasonably high remuneration for the utilisation or use of a thing or a right or for performance made, or

b) unreasonably high reimbursement of expenditure;

8. (unavailability of the object of performance)
a stipulation permitted under 3. above of the user's right to free himself of his obligation to perform the contract if the object of the performance is not available, unless the user agrees

a) to inform the other party immediately of the unavailability, and

b) immediately to refund counter-performance by that party.

§ 309 Clauses whose invalidity is not subject to any evaluation

Even where derogation from the statutory provisions is permissible, the following are invalid in standard terms:

1. (price increases at short notice)
a provision which provides for an increase in the remuneration for goods or services that are to be supplied within four months of the conclusion of the contract; this does not apply to goods or services supplied in the course of a recurring obligation;

2. (right to refuse to perform)
a provision by which

a) the right under § 320 of the contractual partner of the user to refuse to perform is excluded or restricted, or

b) a right of retention of the contractual partner of the user, in so far as it arises from the same contractual relationship, is excluded or restricted, in particular by making it subject to recognition by the user of the existence of defects;

3. (prohibition of set-off)
a provision by which the contractual partner of the user is deprived of the right to set off a claim which is undisputed or has been declared final and absolute;

4. (notice, period for performance)
a provision by which the user is relieved of the statutory requirement to give notice to the other party to perform or to fix a period for performance or supplementary performance by him;

5. (lump-sum claims for damages)
stipulation of a lump-sum claim by the user for damages or for compensation for reduction in value, if

a) the lump sum in the cases in question exceeds the damage expected in the normal course of events or the reduction in value which normally occurs, or

b) the other party is not given the express right to prove that damage or reduction in value has not occurred or is materially lower than the lump sum agreed;

6. (penalty)
a provision by which the user is entitled to receive payment of a penalty in the event of non-acceptance or late acceptance of performance, delay in payment or in the event that the other party withdraws from the contract;

7. (exclusion of liability for death,[400] injury to body and health and for gross fault)

a) (death and injury to body and health)
exclusion or limitation of liability for losses arising out of death, injury to body or health caused by negligent breach of duty by the user or a deliberate or negligent breach of duty by his statutory agent or a person employed by him to perform the contract;

b) (gross fault)
exclusion or limitation of liability for other losses caused by a grossly negligent breach of duty by the user or a deliberate or grossly negligent breach of duty by a statutory agent of the user or by a person employed by him to perform the contract;

a) and b) above do not apply to restrictions of liability in the terms of transport, authorised in accordance with the Passenger Transport Act, of trams, trolley buses and motor vehicles in scheduled services, in so far as they do not derogate, to the detriment of passengers, from the Regulation concerning the terms of transport by tram and trolley bus and by motor vehicles in scheduled services of 27 February 1970; b) above does not apply to restrictions of liability for State-approved lottery or raffle contracts.

8. (other exclusions of liability in the event of breach of duty)

a) (exclusion of the right to withdraw from the contract)
a provision which, upon a breach of duty for which the user is responsible and which does not consist in a defect of the thing sold or the work, excludes or restricts the other party's right to withdraw from the contract; this does not apply to the terms of contract and tariff rules referred to in No. 7 on the conditions set out therein;

b) (defects)
a provision by which, in contracts for the supply of new, manufactured things or of work,

aa) (exclusion and reference of claims to third parties)

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[400] Literally, "injury to life."

claims against the user on account of a defect as a whole or with regard to individual elements of it are excluded entirely, restricted to the assignment of claims against third parties, or which make the pursuit of legal proceedings against third parties a condition precedent;

bb) (restriction to supplementary performance)
claims against the user are restricted, entirely or with regard to individual elements, to a right to supplementary performance, unless the other party is given an express right to claim a price reduction if supplementary performance is unsuccessful or, except where the defects liability is in respect of building work, to choose to terminate the contract;

cc) (expenditure incurred in the course of supplementary performance)
the user's obligation to bear the expenditure necessary for supplementary performance, in particular the costs of carriage, transport, labour and materials, is excluded or restricted;

dd) (withholding of supplementary performance)
the user makes supplementary performance conditional on the prior payment of the entire price or, having regard to the defect, an unreasonably high proportion thereof;

ee) (time-limit for notice of defects)
the user fixes a period within which the other party must give notice of non-obvious defects which is shorter than the period permitted under ff) below;

ff) (facilitation of limitation)
facilitates the limitation of claims on account of defects in the cases set out in § 438(1), No. 2 and § 634a(1), No. 2, or, in other cases, results in a limitation period of less than one year from the date on which the statutory period of limitation begins; this does not apply to contracts in which the whole of Part B of the contracting rules for award of public works contracts is incorporated;

9. (period of recurring obligations)
in a contractual relationship concerning the periodic delivery of goods or the periodic supply of services or work by the user,

a) a contract duration which binds the other party for more than two years,

b) a tacit extension of the contractual relationship which binds the other party for a period of more than one year in each particular case, or

c) to the detriment of the other party, a period of notice to terminate the contract which is more than three months prior to the expiration of the initial or tacitly extended period of the contract;
this does not apply to contracts for the supply of things sold as a unit, to insurance contracts or contracts between the owners of copyrights and of claims and copyright collecting societies within the meaning of the Protection of Copyrights and Related Rights Act;

10. (change of contract partner)
a provision whereby in sales contracts, contracts for the supply of services or contracts for work a third party assumes or may assume the rights and obligations of the user under the contract, unless the provision

a) specifies the third party by name, or

b) gives the other party the right to withdraw from the contract;

11. (liability of an agent on conclusion of the contract)
a provision by which the user imposes on an agent who concludes the contract for the other party,

a) the agent's own liability or duty to perform the contractual obligation without having made an express and separate declaration in that regard, or

b) where the agent lacks authority, liability which exceeds that under § 179;

12. (burden of proof)
a provision by which the user alters the burden of proof to the detriment of the other party in particular by

a) imposing the burden in respect of circumstances which fall within the scope of the user's responsibility, or

b) requiring the other party to acknowledge particular facts;
Subsection b) above does not apply to acknowledgments of receipt which are separately signed or bear a separate, qualified electronic signature;

13. (form of notices and declarations)
a provision by which notices or declarations to be given to the user or third parties are subject to a stricter requirement than the need for writing or to special requirements with regard to receipt.

§ 310 Scope of application

(1) § 305(2) and (3) and §§ 308 and 309 do not apply to standard terms which are proffered to a businessperson, a legal person governed by public law or a special fund governed by public law. In those cases § 307(1) and (2) nevertheless applies to the extent that this results in the invalidity of the contractual provisions referred to in §§ 308 and 309; due regard must be had to the customs and practices applying in business transactions.

(2) §§ 308 and 309 do not apply to contracts of electricity, gas, district heating or water supply undertakings for the supply to special customers of electricity, gas, district heating or water from the supply grid unless the conditions of supply derogate, to the detriment of the customer, from Regulations on general conditions for the supply of tariff customers with electricity, gas, district heating or water. The first sentence applies mutatis mutandis to contracts for the disposal of sewage.

(3) In the case of contracts between a businessperson and a consumer (consumer contracts) the rules in this section apply subject to the following provisions:

1. Standard terms are deemed to have been proffered by the businessperson, unless the consumer introduced them into the contract;

2. §§ 305c(2) and §§ 306, 307 to 309 of the present Act and Article 29a of the Introductory Act to the Civil Code apply to pre-established conditions of contract even if they are intended for use only once and in so far as, because they are pre-established, the consumer could not influence their content.

3. When deciding whether there has been unreasonable detriment under § 307(1) and (2) the circumstances surrounding the conclusion of the contract must also be taken into account.

(4) This section does not apply to contracts in the field of the law of succession, family law and company law or to collective agreements and private- or public-sector works agreements. When it is applied to labour contracts, appropriate regard must be had to the special features of labour law; § 305 (2) and (3) is not to be applied. Collective agreements and public and private sector works agreements are equivalent to legal rules within the meaning of § 307(3).