Advanced Contracts, Tendering and Public Procurement
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Formation of Contract - Free Consent III
Unconscionable and Standard Form of Contracts

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Unconscionable and Standard forms of Contract

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The doctrine of unconscionability is an important aspect in both Indian contract law and UK contract law, which falls under the common law framework. In common law, the concept of unconscionability plays a significant role in rendering a contract voidable. Similarly, in Indian law, Section 16(3) of the Indian Contract Act addresses unconscionability as a matter that can be addressed by the courts. It is crucial to understand what constitutes an unconscionable bargain or term in a contract. The term 'unconscionable' refers to something that goes against the fairness and societal norms of a given society. It signifies something that is unacceptable and challenges the moral conscience of the society. Consequently, if a contract fails to meet the standards established by a human society, it may be set aside.

The objective test for unconscionability is particularly relevant in the context of modern contracts, such as standard form contracts. To comprehend standard form contracts, it is essential to consider the impact of the modern industrial revolution, where a market condition arises with a dominant producer and numerous consumers. For instance, a notable example of this modern-day industrial revolution market is McDonald's, which supplies standardized food products across various cities, jurisdictions, countries, and continents, catering to many consumers.

The extensive production and provision of services in such scenarios have contributed to the emergence of standard form contracts. These contracts aim to establish uniform terms and conditions across most jurisdictions, unless specific laws require modifications to the contractual provisions. McDonald's, for instance, prefers standardized terms and conditions for selling burgers in the US and India. This concept of standard form contracts entails the standardization of contractual terms and conditions.

Standard form contracts can be effectively understood through the example of insurance contracts, such as those offered by the Life Insurance Corporation of India (LIC). Let us consider the Jeevan Anand policy as an illustration of a life insurance policy.

In the case of insurance contracts, a standard form is developed for a specific policy, like the Jeevan Anand policy. The terms and conditions of this policy are predetermined and standardized for all prospective consumers interested in obtaining life insurance from LIC. This means that multiple individuals enter the same contract, which exemplifies the essence of a standard form contract.

Standardization offers several advantages, the first being time-saving. If individual contracts were to be created for each life insurance consumer, a considerable amount of time would be spent on contract preparation. By using a standard form, this time can be significantly reduced.

Secondly, standardization also saves costs. Printing out separate documents, dedicating time, and involving many executives in negotiations and redrafting would be a costly endeavour. Standard form contracts mitigate these expenses.

Moreover, standardization brings about uniformity within a company like LIC. The company has a clear understanding of the consistent terms and conditions that govern the contract. It eliminates variations based on factors such as location, income, or age, providing the company with peace of mind. With well-defined terms and conditions, LIC can effectively draw up contracts and defend them, if necessary.

Standardization in contracts is increasingly becoming a preferred approach across various industries, including business contracts. This trend is driven by the numerous advantages it offers, such as promoting uniformity, consistency, and cost and time savings.

Standard form contracts are inevitable in today's business landscape. Even industries like automobile manufacturing and the service sector, including hospitals, adopt standard form

contracts. In hospitals, for example, a standard form is used for patient admissions in the outpatient or inpatient departments. While specialized procedures or surgeries may require specific contracts, the initial admission process typically follows a standardized template. Different departments within the hospital may have their own templates for specialized treatments.

Standard form contracts are also prevalent in government-related services. For instance, when the government provides electricity through distribution companies, negotiating and creating separate contracts for each consumer would be impractical. Hence, electricity distribution companies rely on standard form contracts to streamline their operations.

Overall, standard form contracts exist across various industries, both in the product and service sectors. They ensure efficiency, consistency, and clarity in contractual relationships, benefiting businesses, service providers, and even government entities.

One crucial condition in such contracts is that if a consumer fails to pay their electricity bill for three consecutive months, the electricity distribution company has the authority to disconnect their electricity supply. This standard term serves as an advantage for the government in addressing allegations of discrimination or unfair treatment. Standardization helps challenge claims of unfair treatment because it establishes that the same rules, contracts, and terms and conditions apply to everyone.

Standardization proves beneficial in various government services, including public sector banks, where standard forms are used to communicate prepayment charges, processing fees, and other contractual terms to consumers. These standardized terms ensure consistency and mitigate the risk of discrimination.

Standardization is widely practiced and highly advantageous for businesses across industries. However, it is crucial to acknowledge the challenges associated with standard form contracts. One primary challenge is determining what constitutes fair and unfair terms, which can be subjective and dependent on the specific contract and clauses involved.

It is important to recognize the power wielded by contract draftsmen when creating standard form contracts. As a contract draftsman employed by McDonald's, for example, the contract you create will be used worldwide, and every consumer will be required to agree to its terms. It is your responsibility to protect the interests of your client and employer, demonstrating loyalty and faithfulness.

Undoubtedly, when creating a contract, the natural inclination is to draft terms and conditions that are advantageous and favourable to one's own company or client. This power of contract drafting is subject to scrutiny because, as the saying goes, "power corrupts, and absolute power corrupts absolutely." The ability to shape the contract can potentially lead to the inclusion of unfair terms, allowing the party to escape liability in case of legal disputes.

In the 1970s and 1980s, the UK recognized the exploitative nature of contracts and enacted the Unfair Terms and Contracts Act in 1977. This legislation aimed to protect consumers from unfair terms in contracts and extended beyond consumer contracts to address unfair terms in a broader context. As a result, significant developments took place, with courts becoming actively involved in scrutinizing and judging the fairness of terms in standard form contracts.

Determining what constitutes fair and unfair terms requires consideration of societal norms and values. Terms that shock the consciousness of society and are deemed unconscionable are considered unfair. For example, let us consider the scenario of giving clothes to a dry cleaner. While receiving a receipt is a standard practice, the terms and conditions specified on the receipt become crucial. These terms serve as a risk assessment document, anticipating potential disputes in case of deficient service. Similarly, when dining at a restaurant, if the food is contaminated or of poor quality, the terms and conditions become relevant to address any grievances.

In instances where a laundry person damages an expensive item like a Kancheepuram saree, beyond raising objections and engaging in arguments, the terms and conditions of the contract become vital. It is important to note that early court cases, such as Thornton v. Shoe Lane Parking Limited, established a distinction between a contract and a receipt. A contract encompasses all terms and conditions agreed upon by both parties, while a receipt merely acknowledges the delivery of goods.

The power to create contract terms and conditions necessitates scrutiny to prevent the inclusion of unfair terms. The enactment of legislation and the intervention of courts have played crucial roles in ensuring fairness in standard form contracts, protecting consumers from exploitative practices.

The court established that a receipt serves as evidence of a contract but is not the contract itself. Contracts can be expressed or implied. For example, when giving clothes for dry

cleaning, there is an implied contract. The receipt acts as evidence of that implied contract, but it does not constitute the contract itself. It is important to distinguish between the two.

Moreover, courts recognized the responsibility of sellers or service providers to bring the terms and conditions to the consumer's attention. If the terms and conditions are printed on the back of the receipt, it is the seller's duty to indicate this by including "P T O" (please turn over) on the first page. This ensures that the consumer is aware that there are terms and conditions on the backside.

Furthermore, the courts addressed the issue of fine print and extensive terms and conditions. In cases like insurance policies, where the standardized terms and conditions are printed in small, fine words on a single sheet of paper, the courts intervened. They required sellers to highlight and bold exclusionary terms or those terms that may adversely affect the buyer's rights. By doing so, even if the rest of the terms and conditions are difficult to read, the buyer can easily identify problematic or objectionable clauses.

When it comes to electronic contracts, such as opening an email account, users are typically required to agree to the terms and conditions before proceeding. Dialog boxes with "I agree" and "I do not agree" buttons are presented, and users must scroll down to click "I agree" to access their email account or upload software or apps. Additionally, apps may request specific permissions, such as accessing contacts or Gmail accounts, highlighting the importance of certain factors.

The courts have emphasized the duty of sellers and service providers to make consumers aware of the terms and conditions in standard form contracts. This includes indicating where the terms and conditions are located and appropriately highlighting critical clauses to ensure transparency and fairness in contractual agreements.

After obtaining our consent, service providers deliver their services based on standardized terms and conditions. This applies to various electronic contracts, such as software installations like MS Office or online marketplaces like Amazon and Flipkart. These contracts are standardized and require agreement from the user before accessing the services. However, the issue arises when determining whether a term is fair, acceptable, or unconscionable, leading to possible court intervention.

Under the Indian Contract Act, unfair terms can render a contract voidable in two ways. First, the entire contract can be held voidable if the unfair term is so fundamental that the entire

contract becomes invalid. Second, the doctrine of severability can be applied, allowing the court to remove the objectionable clause while upholding the rest of the contract. This approach recognizes that contracts can be complex and extensive.

To evaluate unfair terms, courts may adopt the "blue pencil rule" akin to an editor's role. They identify objectionable clauses or words and strike them out while allowing the remaining contract to stand if it is deemed acceptable.

Unconscionability is subjective and can vary based on market conditions and societal values. Judges rely on their moral consciousness and legal reasoning to determine whether a term is unconscionable.

In India, there has been a longstanding need to moderate contracts, ensuring they align with societal values and prevent unjust enrichment. While profiting from contracts is acceptable, unjust enrichment is discouraged. Unfair terms in contracts have been subject to judicial intervention and scrutiny, with various principles and doctrines developed over time.

In India, the 199th Law Commission Report specifically studied unfair terms in contracts, dividing them into two categories: substantive unfairness and procedural unfairness. These characteristics help identify and address unfair terms in contract law.

The Law Commission report serves as a standard for evaluating unfair terms in contracts. However, despite the recommendations of the report, the Indian government did not take immediate action to amend the Indian Contract Act or enact separate legislation, like the approach taken in the UK. Nonetheless, the Consumer Protection Act of 2019 addresses certain aspects of unfair terms in contracts and unfair trade practices.

There are two types of unfairness in contract formation. The first is procedural unfairness, as identified by the Law Commission. Procedural unfairness occurs during the process of contract formation, where the issue of consent becomes crucial. Examples of procedural unfairness include "take it or leave it" contracts commonly seen in standard forms. In such cases, an insurance company or a hospital presents a contract and insists on immediate acceptance, leaving little or no opportunity for the consumer to thoroughly review the terms before agreeing. For instance, hospitals may require patients to sign forms before commencing treatment. This lack of time for review and absence of dissent options constitutes procedural unfairness, which is prevalent in many situations.

Procedural unfairness relates to the consumer or contractor not having sufficient time to review the contract before agreeing to it and facing limitations on expressing dissent or refusal.

Let us assume you have taken your car to a shopping mall and need to park it. As you enter the parking area, there is an automated system where you press a button to obtain a parking ticket. The procedural unfairness in this scenario arises from the fact that the contract is being formed as soon as you press the button and receive the ticket, without being informed of the terms and conditions that apply. Where can you find the terms and conditions of the shopping mall? Often, they may display a phrase such as "parking at owner's risk," but the adequacy or fairness of such a term is open to question.

Instances of procedural unfairness can be found in various situations, such as "take it or leave it" contracts. For example, when you visit a hospital, they may ask you to fill out forms or sign documents before providing treatment, leaving little opportunity to review the terms or seek alternative options. The absence of choice or room for dissent in such cases constitutes procedural unfairness.

Procedural unfairness is also evident in government contracts, where the contracting process and execution often display elements of dominance and unequal bargaining power. The courts have emphasized the importance of fairness in government contracts, not only in substance but also in appearance. This means that the documentation and procedures surrounding government contracts must reflect fairness to ensure a fair contracting system.

The second aspect, substantive unfairness, focuses on unfair terms within the contract itself. Substantive unfairness occurs when a term in the contract heavily favours one party or provides unilateral rights to terminate without any corresponding rights for the other party. Unfair terms that unilaterally benefit one party at the expense of the other are considered substantively unfair.

Societies seek to establish criteria and parameters to judge what is fair and just in contracts. The goal is to prevent exploitation and exclusion of those who may not be well-versed in their rights or contract negotiation. Unfair terms in contracts warrant intervention to ensure a fair legal system. It is a sign of a robust legal system and contributes to the growth of a society, economy, and market conditions. Fairness should be practiced not only by government agencies but also in government and private contracts.

One common form of substantive unfairness is the exclusion of liability clause. This clause often forms the crux of unfair terms in contracts. For example, an airline like IndiGo, which provides numerous passenger services, may have a standardized form of contract for all its passengers. Within this contract, IndiGo may include an exclusion of liability clause, stating that they will not provide refunds. The controversy surrounding refund clauses is relevant in this context.

In summary, procedural unfairness relates to the process of contract formation, such as limited time for review or lack of choice, while substantive unfairness pertains to terms within the contract that heavily favour one party. Evaluating and addressing unfair terms in contracts is crucial for maintaining fairness in a legal system and ensuring the well-being of all parties involved.

When examining exclusionary clauses in standard forms of contracts, it is important to understand that contracts often aim to reduce liability. The relationship between tort law (which deals with civil wrongs, including negligence) and contract law is significant. If a hospital commits medical negligence, under tort law, the hospital is legally responsible for compensating the patient or consumer for the harm caused.

However, when we transition from tort law to contract law, the same hospitals may draft standard forms of contracts that seek to achieve a different outcome. They may include clauses that exclude their liability, stating that the hospital will not be held responsible for any deaths or incidents that occur within their premises. These clauses are known as exclusion of liability clauses.

The question arises: Can contracts waive or diminish the liability that stems from a public element such as negligence? This issue is subject to public policy debates. On one hand, there are exclusion of liability clauses, while on the other hand, there are limitations of liability provisions to consider.

In summary, contracts drafted by hospitals and other entities may attempt to exclude or limit their liability through contractual clauses. This raises discussions about the extent to which contracts can diminish the liability associated with public elements like negligence, creating a public policy debate.

An interesting distinction between contracts and tort law is that contracts offer advantages in terms of evidentiary documentation and the ability to determine rights and liabilities. In tort

law, judgments are based on the discretion of judges who determine the quantum of liability, the principles of law, and whether liability exists in the first place. There is no specific statute guiding judges in tort law, although some modern statutes like the Consumer Protection Act have codified aspects of it.

When relationships are framed within a contract, the contract itself becomes the basis for determining the parties' rights and liabilities. This provides a document that judges must interpret, thereby limiting their discretion. This raises the question of whether limitation of liability is possible in contracts, particularly in standard form contracts.

Regarding the "LOL" clause (Limitation of Liability clause), judicial verdicts indicate that excluding liability is deemed unacceptable and against public policy. Contracts cannot be misused or abused to exclude liability under tort law. However, the possibility of limiting liability is recognized by judges in various jurisdictions, including India, the UK, and the US. The courts have stated that limitation of liability is permissible if the quantum of limitation is reasonable and fair. The test of reasonability becomes the test of fairness, ensuring that parties have the freedom to contract while maintaining a reasonable and acceptable limit on liability.

The advantage of limitation of liability in standard form contracts lies in providing certainty and managing risk for companies and entities involved in numerous contracts. The sheer volume of contracts can create challenges in determining liability for each individual case. Limiting liability helps these entities assess and prepare for their potential liability structure. However, it is important to note that limitations of liability must meet the requirements of reasonableness and fairness.

The fairness rule plays a crucial role in determining liability. Consider the scenario of purchasing Microsoft Office. If the contract states that Microsoft will not be liable if the software fails to work, it would be unacceptable and contrary to societal norms. Companies like Microsoft, being large entities, are expected to take responsibility for their products. Exclusion of liability is generally considered unconscionable, while limitation of liability may be acceptable if it is reasonable.

The acceptability of limitation of liability depends on the type of contract involved. In business-to-business (B2B) contracts, limitation of liability is generally accepted as a fair bargaining practice. In business-to-consumer (B2C) contracts, the reasonableness of

limitation of liability is the determining factor. Business-to-government (B2G) contracts often incorporate limitation of liability to ensure contract performance.

Standard form contracts often include challenging clauses, such as refund policies. Transportation service providers, like airlines or bus companies, anticipate circumstances like flight cancellations or delays due to technical issues. Standardized contracts specify the rights and obligations in such situations, including whether refunds or partial refunds will be provided. Excluding refunds entirely is considered highly unreasonable, but a partial refund may be deemed fair, considering the incurred costs and efforts to accommodate the situation.

Similar considerations apply to other industries, such as cricket matches organized by the Indian Premier League (IPL). Contracts governing fan attendance must be fair, preventing exploitation of consumer interest. Judges and courts play a crucial role in moderating and balancing the interests of all parties involved to avoid unconscionable contract terms.

The doctrine of fundamental breach is a fundamental principle in standard form contracts. It implies that regardless of the terms and conditions, if a contract experiences a core breach, it can be repudiated. For instance, if a bus fails to reach its destination or a product fails to perform its basic function, the contract cannot evade liability. Fundamental breach is also associated with safety concerns. In such cases, the terms and conditions of the contract are deemed irrelevant, and the affected party has the right to repudiate the contract and claim damages.

The rule of contra proferentem places the burden of proof on the drafter of the contract. The drafter, such as Life Insurance Corporation of India (LIC), Indigo Airlines, or the manufacturer of an iron box, must justify the fairness and validity of the contract in court. Standard form contracts, often referred to as boilerplate contracts, are subject to this rule. The burden lies with the drafter to demonstrate that the contract is conscionable and complies with the principles of fairness. If the drafter fails to justify the contract, it may be deemed unconscionable by the court.

These principles also apply to government contracts and the provision of government services, such as those offered by Indian Oil in the form of LPG, electricity, or water supply. The rule of contra proferentem is beneficial as it relieves the exploited party from the burden of proving the unfairness of the contract. If the drafter fails to satisfy the court regarding the reasonableness and enforceability of the contract, it may be invalidated or set aside.

It is important to note that the statements made above reflect general principles and may vary depending on the jurisdiction and specific circumstances involved.