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Unconscionability in California: A Need for Restraint and Consistency

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Unconscionability in California: A Need for Restraint and Consistency

by

HARRY G. PRINCE*

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Introduction

The final recommendation of the Advisory Committee and the decision to delete [Section 2-302 of the Uniform Commercial Code] was based upon the belief that giving courts unqualified power to strike down terms they might consider "unconscionable" could result in the renegotiation of contracts in every case of disagreement with the fairness of provisions the parties had accepted.¹

When the trial judge announced his finding that Paramount Pictures had imposed a contract with unconscionable terms upon noted humorist, author, and syndicated columnist Art Buchwald and that the court would reform the agreement to reach a just result, the lead attorney for Paramount exclaimed, "Never before in the annals of American jurisprudence has a judge taken it upon himself to remake the parties' bargain."² That attorney was wrong. In California and many other states, courts often engage in the practice of reforming contracts based upon a determination that some part of the bargain was unconscionable.³ Such cases, however, usually involve consumers rather than sophisticated business people.⁴ The Buchwald v. Paramount Pictures Corp. decision was shocking because the court found that a party of Mr. Buchwald's stature, who had collaborated in the venture with an experienced Hollywood producer and had been represented by two agents,⁵ had been taken advantage of through a com-

³. See infra notes 129-131 and accompanying text.
⁴. See infra notes 103-117 and accompanying text.
⁵. Buchwald embarked upon his effort to sell his movie idea in collaboration with his friend, Alain Bernheim, a movie producer. Bernheim had worked as an agent before going on to produce a series of Hollywood motion picture films. Buchwald was initially rep-
monly used motion picture industry contract. Equally startling was the court’s stated intention to rewrite the compensation portion of the agreement.

The decision in *Buchwald v. Paramount Pictures* is not an anomaly in California. Indeed, Art Buchwald and the late music promoter Bill Graham have more in common than just the attainment of considerable status in the entertainment world. California state courts have held that both businessmen were victimized by unconscionable bargains that warranted judicial intervention and reformation of the contracts. A critical analysis of these and other significant California cases raises significant doubt about the soundness and consistency of the unconscionability doctrine as applied by California state courts. The lack of consistency is highlighted by the recent decision of another California trial judge, sitting in the same courthouse as the judge in *Buchwald v. Paramount Pictures*, that the very same contract used in virtually identical circumstances was not unconscionable. While differences of opinion among trial judges should be expected, in this case the inconsistent results can be attributed to peculiarities of the unconscionability law in California.

Perhaps capriciousness in the application of the doctrine of unconscionability by some courts should not come as a great surprise. The incorporation of the unconscionability doctrine into the Uniform Commercial Code (U.C.C.) in Section 2-302 generated as much controversy and discussion as any other section of the first Official Text of
the U.C.C.\textsuperscript{11} Although Section 2-302 applies only to contracts for the sale of goods, courts have regularly used the Section to resolve issues in other types of contracts.\textsuperscript{12} Evidence of the broader influence of Section 2-302 is found in Section 208 in the Second Restatement of Contracts, which embodies the language of U.C.C. Section 2-302(1) and proposes that the unconscionability doctrine be generally applied to the law of contracts.\textsuperscript{13}

The commentators on Section 2-302 tend to be divided into two camps. Supporters of Section 2-302 advocate that the Section satisfies the legitimate need for guarding against overreaching and unfair contracts in the modern marketplace where the use of standardized contracts is widespread; detractors of Section 2-302 fear that granting broad police power to courts to strike unfair clauses or contracts will lead to inconsistent and unpredictable interference with contracting parties.\textsuperscript{14}


\textsuperscript{13} Restatement (Second) of Contracts § 208 (1979). The Reporter's Note to § 208 observes that while § 2-302 is literally inapplicable outside of sale of goods contracts, it has proven very influential in non-sales cases. \textit{Id.}

Since the promulgation of Section 2-302, the fears of its detractors have proved to be largely unwarranted. Generally, the courts in most states have shown restraint in examining contracts or clauses for unconscionability.\textsuperscript{15} Notably, the first principal critic of Section 2-302, Professor Arthur Leff, predicted in his early writings that "[t]he courts will most likely adjust, entrusting the irritating aspects of the Section with a smoothing nacre of more or less reasonable applications, or the legislatures may act if things get out of hand."\textsuperscript{16} Thus, while Professor Leff was quite critical of Section 2-302 as drafted, he correctly predicted the tendency of the courts to restrain its application.\textsuperscript{17}

The general comfort of courts and commentators with the application of Section 2-302 over the years is reflected in the preliminary report issued by the study group appointed to consider revising Article 2.\textsuperscript{18} The study group determined that Section 2-302 did not need

conscionability doctrine to police for price fairness when the market fails to do so); Melvin Aron Eisenberg, \textit{The Bargain Principle and Its Limits}, 95 Harv. L. Rev. 741 (1982) (suggesting courts give expansive application to unconscionability); Richard A. Epstein, \textit{Unconscionability: A Critical Reappraisal}, 18 J.L. & Econ. 293 (1975) (speaking in favor of a restrictive use of unconscionability to police the bargaining process, but not as a limit on substantive contract terms); Jane P. Mallor, \textit{Unconscionability in Contracts Between Merchants}, 40 Sw. L.J. 1065 (1986) (arguing that courts should be receptive to claims of unconscionability by merchants). Other writings on unconscionability are cited throughout this Article.


17. Some writers have argued that the courts should be less restrained in applying the unconscionability doctrine. See, e.g., Eisenberg, \textit{supra} note 14, at 800 (suggesting extended use of the unconscionability doctrine to reconstruct old norms and to add new ones that limit the enforceability of bargains); Jeffrey L. Harrison, \textit{Class, Personality, Contract, and Unconscionability}, 35 Wm. & Mary L. Rev. 445, 450 (1994) (suggesting greater use of substantive unconscionability as a limit on "unfair exchanges" to promote a sense of entitlement among the disadvantaged).

18. The work on revision of Article 2 begins with the deliberations of a study group appointed by the Permanent Editorial Board for the Uniform Commercial Code. The study group issued a Preliminary Report in 1990 and thereafter a drafting committee was appointed. The drafting committee submitted an initial draft for consideration in August
revision and went so far as to recommend the elevation of Section 2-302 to Article 1, which would make it applicable to all articles of the U.C.C.\textsuperscript{19} While the preliminary study recommended that the Official Comments to Section 2-302 be revised substantially to sharpen the focus of procedural misconduct to be guarded against,\textsuperscript{20} the study group also found that Section 2-302 had not proven to be the unruly and fearsome creature that critics first anticipated.

A review of the unconscionability decisions in California, however, suggests that the fears of the Section's early detractors may have come to fruition in that state. The course of Section 2-302 in California has veered away from the more general trends at its inception. The California Legislature initially enacted Article 2 in 1962 without adopting Section 2-302—one of only two states to do so.\textsuperscript{21} The decision in California to drop Section 2-302 was based on concern about potentially excessive discretion that could be exercised by judges to strike down entire contracts or clauses based on subjective, indeterminate views of unfairness.\textsuperscript{22}

Seventeen years passed, and other attempts at passage of an unconscionability statute failed, before Section 2-302 was adopted in California in 1979 as part of consumer protection legislation predominately aimed at financial abuses within the home improvement indus-


\bibitem{94-yale} \textit{Preliminary Report}, supra note 19, at 2-3. The Report raises, among other issues to be addressed in § 2-302 comment revisions, three key questions: (1) whether complete disclosure can be outweighed by a lack of meaningful choice; (2) whether the test for unconscionability should be limited to the time of contracting or might include the inducement and enforcement phases; and (3) whether § 2-302 should be more clearly aimed at consumer rather than commercial contracts. \textit{Id.}

\bibitem{94-yale} California and North Carolina were the only two jurisdictions to omit § 2-302 when adopting the U.C.C. Section 2-302 was subsequently adopted in North Carolina in 1971. \textit{Farnsworth}, supra note 11, § 4.28, at 325 n.5.

\bibitem{94-yale} See California State Bar Committee on the U.C.C., supra note 1, at 135-36 (emphasizing the Advisory Committee's concern about the courts' unqualified power to strike down terms of a contract under § 2-302); \textit{infra} notes 154-166.
Section 2-302 was adopted as Section 1670.5 of the California Civil Code rather than as part of the Commercial Code, making the Section applicable to all contracts rather than only to contracts for the sale of goods.

More significant than the unusual history of the adoption of Section 2-302 in California, however, is the fact that California courts have been both less restrained and more inconsistent than courts in other jurisdictions in applying the unconscionability doctrine. As the reported unconscionability cases in California have accumulated since 1979, the courts have exhibited some disturbing, if not alarming, tendencies. First, California courts have displayed an undue sympathy for claims of unconscionability by merchant or merchant-like parties when the thrust of the claim is that the victim-merchant suffered from a lack of meaningful choice resulting from unequal bargaining power. Second, the California courts have also shown an inclination to assess substantive unconscionability on the basis of hindsight despite the explicit provision in Section 2-302 that the terms of the contract should be viewed at the time of formation. Third, the courts have reformed contracts and granted remedies that raise questions about application of the doctrine as a basis for affirmative relief rather than the more generally accepted defensive use to render a clause or contract unenforceable. And lastly, the courts have approached “price-term” unconscionability cases in a manner that not only highlights the inherent difficulties in determining when a price is excessive, but also takes the unorthodox and highly questionable approach of

23. See infra notes 154-171 and accompanying text.
24. For reasons of simplicity, § 1670.5 of the California Civil Code will be referred to as § 2-302 throughout this Article.
25. See A&M Produce v. FMC Corp., 186 Cal. Rptr. 114, 123 n.12 (Ct. App. 1982) (explaining that the unconscionability doctrine, as codified in California Civil Code § 1670.5, is applicable to all types of contracts).
26. A search of Westlaw's California case law data bases for opinions citing California Civil Code § 1670.5 yielded a list of 26 published cases with 13 decided between 1981 and 1989 and 13 decided between 1990 and 1994. The search does not reflect all the California unconscionability cases—for example, Buchwald v. Paramount Pictures is not reflected in the list—but the search results do suggest increasing use of the doctrine in California courts.
27. The term “merchant” will be used herein to identify parties generally possessing experience or sophistication in business dealings rather than meaning sellers of wares, per se. The intent is to draw a distinction between parties who should have substantial business experience and consumers or “little persons” who are much less likely to have a high degree of business experience or sophistication.
28. See infra notes 228-447 and accompanying text.
29. See infra notes 448-494 and accompanying text.
30. See infra notes 495-512 and accompanying text.
judging unfairness based on the cumulative profits from many separate transactions with many different parties.31 Ultimately, the California cases suggest broader, constructive lessons about application of the unconscionability doctrine.

This Article briefly describes the history and general construction of unconscionability found in the United States. The legislative and judicial history of the unconscionability doctrine in California, before the adoption of Section 2-302 as California Civil Code Section 1670.5 in 1979, is reviewed. Then, unconscionability cases decided in California since the adoption of Section 2-302 are analyzed. The Article concludes with suggestions about the lessons to be learned from the application of the unconscionability doctrine in California.

Four principal suggestions are discussed. First, the courts should be extremely conservative in granting relief to merchants on unconscionability grounds when based on lack of meaningful choice because of unequal bargaining power. Second, the courts should be especially careful to base their assessments on the perspective of the parties at the time the contract was formed. Third, the courts should abandon the false distinction between offensive versus defensive use of the doctrine. Finally, the courts should use a carefully circumscribed approach to price-term unconscionability cases that focuses primarily on excessive contract price versus market price disparity in individual cases and not on vague notions of excessive profits.

I. General History and Construction of the Unconscionability Doctrine

The history of unconscionability32 and the general construction of Section 2-30233 have been well documented by other commentators. These topics will be reviewed briefly in this Article for the purpose of identifying issues relevant to the main focus.

A. History of Unconscionability

The lineage of the unconscionability doctrine has been described as obscure in part because the courts did not explain the concept with

31. See infra notes 513-537 and accompanying text.
33. General reviews of unconscionability may be found in the leading contracts textbooks. See Calamari & Perillo, supra note 11, §§ 9-37 to 9-38, at 397-409; Farnsworth, supra note 11, § 4.28, at 323-39; Murray, supra note 12, § 96, at 481-502.
any specificity in its earliest common law usage. Comparisons have been made with the older Roman law concept of *laesio enormis*, which allowed for rescission of contracts because of inadequacy of the price based on a moral precept that there should be fair exchange of values. Notably, the *laesio enormis* concept initially was well defined in that it applied only to land sale contracts and had specific quantitative limits; the price to be paid by the seller was required to be less than half of the land’s value. Thus, the doctrine did not grant broad license to police for fairness.

Unconscionability in courts of equity was not specifically delineated, but instead underscored the broad proposition that courts of equity would not enforce an unfair bargain if it would make the courts a tool in achieving an unjust or unfair result. The initial status of eq-

34. See Spanogle, supra note 14, at 937-38 (discussing applications of unconscionability found in both law and equity, but stating that no explicit rule was formulated); Comment, Unconscionable Contracts: The Uniform Commercial Code, 45 Iowa L. Rev. 843, 846 (1960) (noting that the vagueness of unconscionability in equity was reflective of the flexible application given to such concepts).

35. See generally James Gordley, Equality in Exchange, 69 Cal. L. Rev. 1587 (1981) (discussing concepts of price fairness reflected in *laesio enormis*, related civil code doctrines, and common law unconscionability). See also Angelo & Ellinger, supra note 15, at 474-75 (tracing French civil code concepts similar to unconscionability back to Roman Law *laesio enormis*); Cellini & Wertz, supra note 32, at 193 (1967) (stating that the beginnings of unconscionability go back to *laesio enormis*); Leff, supra note 14, at 539 (noting similarity between equity unconscionability and *laesio enormis* statutes focus on uneven bargains). But see Spanogle, supra note 14, at 951-52 (stating that there is no direct link between *laesio enormis* and the unconscionability doctrine in the U.C.C. or common law).


37. Professor Dawson describes a virtual ebb and flow of the *laesio enormis* and similar civil law concepts coming into the first portion of this century with both France and Germany tending toward restriction of the doctrine’s limitation on freedom of contract while still seeking ways to address the underlying concern with fair exchanges. Dawson, supra note 36, at 370-76. More recent assessments indicate that the “German courts have adopted a conservative approach, motivated by a desire to avoid uncertainty in the law.” Angelo & Ellinger, supra note 15. But see Gordley, supra note 35, at 1626-27 (suggesting a more expansive policing against one-sided contracts in Germany). The French law of *lesion* has been described as reflecting some extensions of the just price concept in recent times. See id. at 1625-26; Arthur Taylor von Mehren, The French Doctrine of Lesion in the Sale of Immovable Property, 49 Tul. L. Rev. 320, 323-27 (1975).

38. See Emily L. Sherwin, Law and Equity in Contract Enforcement, 50 Md. L. Rev. 253, 254-55 (1991) (stating that equity operated on higher moral plane and would not assist one party in taking unfair advantage); Robert A. Hillman, Debunking Some Myths About Unconscionability: A New Framework for U.C.C. Section 2-302, 67 Cornell L. Rev. 1, 26-27 (1981) (equity courts grew because law courts failed to employ fairness principles). It should be noted that the usefulness of equity decisions in interpreting § 2-302 has been questioned because, among other things, the equity cases often involved real property transactions dissimilar to sale of goods and other types of transactions and because equity
uity courts, as exceptional in jurisdiction and manned by ecclesiastics, explains the emphasis on fairness as a prerequisite to the equity court's award of relief to a complaining party. An objectionable result might be unjust for a number of reasons according to an equity court; an example would be when the bargain gave too much benefit to one party at too great an expense or hardship to the other party. In cases in which the exchange was unequal or a bad bargain had been made, such facts were generally not enough to get relief, even in equity; the party seeking relief also had to show an element of unfairness in the contracting process or a gross inequality in the exchange.

Before the promulgation of Section 2-302 and the beginning of its influence, courts in law were largely deemed incapable of denying enforcement based on an absence of fairness in the exchange. The courts of law, when determined to do so, were forced to find an indirect way to deny enforcement to an unconscionable contract or term. The Official Comments to Section 2-302 indicate that the Sec-

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40. The equity courts would refuse to grant an injunction or order specific enforcement if the hardships outweighed the benefits, if the enforcement would be oppressive, or if it would cause disproportionate hardship to the party against whom enforcement was sought. See Murray, supra note 12, § 96, at 482; Note, Section 2-302 of the Uniform Commercial Code: The Consequences of Unconscionability in Sales Contracts, 63 Yale L.J. 560 (1953).

41. See Contract Buyers League v. F&F Inv., 300 F. Supp. 210, 227 (N.D. Ill. 1969) (construing Illinois law noting that mere excessive price is not sufficient for unconscionability in equity); Ryan v. Weiner, 610 A.2d 1377, 1380-81 (Del. Ch. 1992) (inadequacy of price must be coupled with inequitable or oppressive conduct); Smith v. Harrison, 325 N.W.2d 92, 94 (Iowa 1982) (imprudent bargain is not enough for relief in equity); Farnsworth, supra note 11, § 4.27, at 319-21 (stating that although mere inadequacy of consideration was not grounds to withhold equitable relief, a contract that was unconscionable would not be enforced in equity); Cellini & Wertz, supra note 32, at 198 (stating that unless the inequality of consideration was extreme there must also be bargaining misconduct); but see Hillman, supra note 38, at 36-37 (observing that not all equity decisions required both uneven terms and unfair bargaining).

42. See 1 Corbin, Contracts § 128, at 188 (1952) (noting that courts at common law did not create a rule against unconscionable bargains); Farnsworth, supra note 11, § 4.27, at 322-23 (noting that standards for fairness fashioned by courts of equity did not preclude the enforcement of bargains at law); Sherwin, supra note 38, at 254-55 (equity had extra layer of fairness defenses not applicable at law).

43. See Calamari & Perillo, supra note 11, § 9-38, at 401 (courts of law resorted to "imaginative flanking devices" to defeat unfair contracts); Spanogle, supra note 14, at 934 (courts denied enforcement of unfair contracts through "surreptitious" means).
tion was created principally to give courts of law the explicit ability to decline to enforce such contracts.44

Professor Leff’s early writings on unconscionability provide a history of the drafting of Section 2-302 and note that the first appearance of an unconscionability section was in the 1941 proposed draft of the revised Uniform Sales Act.45 This Section concerned contract provisions that varied from the Uniform Sales Act based on an express agreement of the parties.46 Professor Leff underscored that the 1941 proposed section indicated that such bargained-for arrangements should be enforced by the courts.47 The section was quickly withdrawn by the drafting committee because the means of administration were deemed inadequate.48

Between 1941 and 1948, the drafts of proposed Section 2-302 tended to focus on form contracts. Drafters of the Section expressed concerns that standardized terms in form contracts did not reflect the agreement of the parties and left much room for abuse.49 However, by 1948, the Section was no longer limited in application to form contracts; rather, it had expanded to cover the general contours of the

44. U.C.C. § 2-302, Comment 1 begins:
This section is intended to make it possible for the courts to police explicitly against the contracts or clauses which they find to be unconscionable. In the past such policing has been accomplished by adverse construction of language, by manipulation of the rules of offer and acceptance or by determinations that the clause is contrary to public policy or to the dominant purpose of the contract. This section is intended to allow the court to pass directly on the unconscionability of the contract or particular clause therein and to make a conclusion of law as to its unconscionability. The basic test is whether, in 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.


45. Leff, supra note 14, at 489-501.
46. Id. at 489.
47. See id. See also Spanogle, supra note 14, at 942 (noting that the original intent was “to insulate dickered terms whether fair or not”).
49. See id. at 491-95; Cellini & Wertz, supra note 32, at 199-200.
present-day Section 2-302. After 1948 there were no material changes in the scope of the Section.

The primary reason for the creation of Section 2-302 is clearly stated in the first Official Comment of the U.C.C. The drafters were convinced that the courts were policing on grounds of unconscionability and that such policing would achieve greater consistency if done explicitly rather than through indirect means. In most instances, the drafters have largely been proven correct. A majority of courts have been cautious in their application of the unconscionability doctrine and from these decisions one can identify a framework of the doctrine as generally construed.

B. Prevailing Trends in Application of the Unconscionability Doctrine

Assessments of Section 2-302 usually begin with the observation that the Section does not contain a definition of unconscionability. The critics of the Section have cited the lack of a definition as its major failing. On the other hand, supporters of Section 2-302 assert that the lack of a precise definition reflects the wisdom that the unconscionability doctrine defies such a description. Thus, the lack of

50. Leff, supra note 14, at 494 (citing 1948 draft § 2-302):
Section 2-302. Unconscionable Contract or Clause.
(1) If the court finds the contract to be unconscionable, it may refuse to enforce the contract or strike any unconscionable clauses and enforce the rest of the contract or substitute for the stricken clause such provisions as would be implied under this Act if the stricken clause had never existed.
(2) A contract not unconscionable in its entirety but containing an unconscionable clause, whether a form clause or not, may be enforced with any such clause stricken.

51. By the appearance of the 1957 Official Text of the Uniform Commercial Code, § 2-302 was changed to move the remedial options to subsection (1) and to add a new subsection (2) concerning the need for an evidentiary hearing; the requirement that the contract be viewed at the time of contracting was also added. See infra notes 118-121 and accompanying text.

52. See supra note 44 and accompanying text.


54. See Murray, supra note 12, § 96, at 486-89 (§ 2-302 fails to set forth a workable statement of unconscionability); Leff, supra note 14, at 487-88 (describing the text as having "amorphous intelligibility" and the comments as irrelevant).

55. See, e.g., Epstein, supra note 14, at 304 (noting that the strength of the unconscionability doctrine is its flexibility); Gerald T. McLaughlin, Unconscionability and Impracticability: Reflections on Two U.C.C. Indeterminacy Principles, 14 Loy. L.A. Int'l & Comp.
a specific definition arguably gives courts the necessary room to address problems the exact contours of which have yet to be defined.\textsuperscript{56}

Notwithstanding the debate over whether Section 2-302 can or should precisely define unconscionability, there are definitions of the term that are frequently used by the courts to identify the essence of the doctrine. The first Official Comment to Section 2-302 states that the principal purpose of the doctrine is "the prevention of oppression and unfair surprise" and that "[t]he basic test is whether, in the light of the general commercial background and the commercial needs of the particular trade or case, the clauses are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract."\textsuperscript{57} The Official Comment directs the courts to engage in weighing and balancing, which suggests that a contract is not unenforceable merely because of some imbalance in terms or bargaining power, but that the unfairness of the terms must reach an extreme or alarming level.

Definitions of unconscionability created by the courts are consistent with the Official Comment. The phrasing adopted by the United States Supreme Court is often cited: an unconscionable contract is one "such as no man in his senses and not under delusion would make on the one hand, and as no honest and fair man would accept on the other."\textsuperscript{58} To meet the court's definition of unconscionability, the challenged bargain must be distinctly beyond the permissible range of advantage allowed to one of the parties so that the bargain shocks the conscience of the court.

In addition to the definitions going to the essence of unconscionability, a general survey of cases and commentary relating to Section 2-302 yields a consensus on construing the Section: (1) Section 2-302 is generally deemed to require a showing of combined procedural and

\textsuperscript{56} See Ellinghaus, \textit{supra} note 14, at 759-61 (§ 2-302 grants to courts the room for reasoned and creative application of the unconscionability doctrine). The chief drafter of Article 2, Professor Karl Llewellyn, asserted that "an approach by statute [is] dubious, uncertain and likely to be both awkward in manner and deficient and spotty in scope." LLEWELLYN, THE COMMON LAW TRADITION, \textit{supra} note 53, at 370.


\textsuperscript{58} Hume v. United States, 132 U.S. 406, 411 (1889) (quoting Earl of Chesterfield v. Janssen, 28 Eng. Rep. 82, 100 (Ch. 1750)). A revealing discussion of \textit{Earl of Chesterfield v. Janssen} and two notable English cases that preceded it can be found in Davenport, \textit{supra} note 14, at 124-26. Davenport emphasizes that the earlier cases involved not only grossly uneven exchanges, but also one party taking advantage of the other's lack of sophistication. \textit{Id.}
substantive unconscionability;\textsuperscript{59} (2) courts are more receptive to consumer or nonmerchant claims of unconscionability than to claims by merchants;\textsuperscript{60} (3) unconscionability should exist at the time that the contract was made for the doctrine to be applied;\textsuperscript{61} (4) courts generally have taken the position that unconscionability can be used only as a defense against enforcement and not as a basis for affirmative recovery;\textsuperscript{62} and (5) courts have used the doctrine to police price terms, but not without some uneasiness.\textsuperscript{63}

(1) \textit{Procedural and Substantive Unconscionability}

Professor Leff provided the general framework for the construction of Section 2-302 when he analyzed unconscionability as having two separable elements: procedural and substantive.\textsuperscript{64} Substantive unconscionability refers to the actual terms of the agreement, while procedural unconscionability pertains to the bargaining process. Most successful claims involve a combination of procedural and substantive unconscionability,\textsuperscript{65} but it is debatable whether both elements must be present.\textsuperscript{66} Some courts have also indicated that a sliding scale applies:

\begin{itemize}
  \item \textsuperscript{59} See infra notes 64-102 and accompanying text.
  \item \textsuperscript{60} See infra notes 103-117 and accompanying text.
  \item \textsuperscript{61} See infra notes 118-128 and accompanying text.
  \item \textsuperscript{62} See infra notes 129-138 and accompanying text.
  \item \textsuperscript{63} See infra notes 139-153 and accompanying text.
  \item \textsuperscript{65} See Kohl v. Bay Colony Club Condo., Inc., 398 So. 2d 865, 867-69 (Fla. Ct. App. 1981) (observing virtual unanimity among authorities that both procedural and substantive elements must coalesce to establish unconscionability); Hunter, supra note 12, at 169 (stating that § 2-302 cases require both substantive and procedural unconscionability as practical matter); Mallor, supra note 14, at 1073 (noting that almost all findings of unconscionability involve both substantive and procedural unconscionability).
  \item \textsuperscript{66} A number of courts and commentators have recognized that one element of unconscionability standing alone may render a contract unenforceable in rare or exceptional cases. See Gillman v. Chase Manhattan Bank, N.A., 534 N.E.2d 824, 829 (N.Y. Ct. App.
for example, a contract with extraordinarily oppressive substantive terms will require less in the way of procedural unconscionability.\(^6\) The question whether both elements are required is particularly relevant to claims of unconscionability that focus on the price term.\(^7\)

Substantive unconscionability looks to the oppressiveness or one-sided nature of the transaction and simply restates the basic requirement that the substantive terms must be unreasonably favorable to one party or unduly burdensome to the other.\(^8\) The types of contracts or terms most often subjected to the test of unconscionability include excessive price terms, termination-at-will clauses, add-on security clauses, limitations on damages for breach, and limitations on periods for filing claims.\(^9\) In determining whether such terms were unconscionable, one court pointed out that the mere presence of some imbalance was not enough to render the contract unconscionable because contracts do not necessarily grant identical rights to the par-

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\(^7\) See infra notes 146-153 and accompanying text.

\(^8\) See Wilson v. World Omni Leasing, 540 So. 2d 713, 716 (Ala. 1989) (unconscionability requires terms that are unreasonably favorable to one party); Martin Rispens & Son v. Hall Farms, Inc., 621 N.E.2d 1078, 1086-87 (Ind. 1993) (substantive unconscionability refers to oppressively one-sided or harsh terms); Phillips, supra note 64, at 216 (substantive unconscionability involves terms that impose excessive burdens or unfairly benefit).

\(^9\) See FARNSWORTH, supra note 11, § 4.28, at 328-31; Epstein, supra note 14, at 305-15.
ties.\textsuperscript{71} Other courts have noted that relief cannot be had merely because a party has made a bad bargain.\textsuperscript{72} Rather, the level of unfairness must be such that it "affronts the sense of decency."\textsuperscript{73}

Professor Leff also emphasized the fact that the statement in the Official Comments to Section 2-302 that its goal is "prevention of oppression and unfair surprise" suggests that procedural unconscionability may take two different forms: first, "unfair surprise," resulting from misleading bargaining conduct, and second, "oppression" (in the absence of unfair surprise) resulting from inequality of bargaining power.\textsuperscript{74} Some courts have highlighted the difference between the two forms of procedural unconscionability as involving a "lack of knowledge" or a "lack of voluntariness."\textsuperscript{75} Procedural unconscionability characterized by surprise or lack of knowledge focuses on terms that are deceptively hidden in a mass of contract language, the object of other concealment, or imposed in circumstances involving haste or high pressure tactics so that they are not likely to be read or understood.\textsuperscript{76} Surprise may also be found in terms that are so unintelligible that they deny comprehension even by the party who discovers


\textsuperscript{74} Leff, supra note 14, at 499-500. See also Spanogle, supra note 14, at 943 (stating that unfair surprise implies deception and that oppression implies compulsion from lack of opportunity to determine terms).


This form of procedural unconscionability has antecedents in the policing doctrines of duress, misrepresentation, and mistake.77

_Germantown Manufacturing Co. v. Rawlinson_79 offers a compelling example of procedural unconscionability by unfair surprise. Joan Rawlinson challenged a confessed judgment note on the grounds that her signature had been obtained through fraud and duress.80 The judgment note was for an open amount and was one of two presented on behalf of her husband's former employer as a means of the husband avoiding prosecution for embezzlement.81 When the amount of the note was later determined by the employer to be over $200,000, Ms. Rawlinson challenged the validity of her assent.82 The appellate court found, in addition to fraud and duress, that the elements of unconscionability were present in that Ms. Rawlinson was asked to co-sign the confessed judgment without advance notice, she was discouraged from consulting an attorney, her husband and the employer's agent made misleading representations about her potential liability under the notes, and she was in an emotionally unsettled state due to the recent discovery of her husband's crime and loss of employment.83 The meeting in which Ms. Rawlinson learned of the judgment notes and was asked to sign them took a total of thirty to forty-five minutes.84 Because of flaws in the bargaining process, the court concluded that Ms. Rawlinson did not understand her potential liability under the note that she signed.85

77. See Bank of Indiana v. Holyfield, 476 F. Supp. 104, 109-10 (S.D. Miss. 1979) (noting that lack of knowledge may come from use of fine print, complex language, or lack of sophistication); Wille v. Southwestern Bell Tel. Co., 549 P.2d 903, 906-07 (Kan. 1976) (identifying factors that included, _inter alia_, use of preprinted contract with inconspicuous terms, complex phrasing, or deceptive language). See also Spanogle, _supra_ note 14, at 954 (finding unfair surprise in deceptive or unduly technical language).

78. See Ellinghaus, _supra_ note 14, at 763-65; Epstein, _supra_ note 14, at 295.


80. _Id._ at 139-40.

81. _Id._ at 140. The first note was for $160,000, which the husband was able to satisfy immediately. The second note was for any amount above $160,000 that the company might later determine that the husband had taken. _Id._

82. _Id._

83. _Id._ at 147. Ms. Rawlinson had also suffered a recent miscarriage and her husband had raised the possibility of divorce once she learned of his criminal conduct. _Id._ at 139-40.

84. _Id._ at 139-40, 147.

85. _Id._ at 147. Another example is the classic case of _Henningsen v. Bloomfield Motors_, Inc., 161 A.2d 69 (N.J. 1960), which involved a question of manufacturer liability for harm resulting from the sale of a defective automobile. _Id._ at 73. The clause limiting the automobile manufacturer's liability for breach of warranty was placed inconspicuously in the contract so that the buyer was unlikely to find the clause in the ordinary course of a purchase. _Id._ at 92. The limitation on liability was also phrased such that, even if found, it
The other form of procedural misconduct, based on oppression or lack of voluntariness, is a departure from prior policing doctrines and is conceptually more difficult to apply. Application of Section 2-302 to this form of procedural unconscionability is based on the idea that even when the party with less bargaining power is fully cognizable of and understands a term, that party may have no choice but to accept the provision although the circumstances do not prove actual duress. The stronger party's ability to dictate the contract terms may result not only from a gross advantage in financial size, but also from immediate exigencies. A caveat in the Official Comments to Section 2-302 states that the Section is not designed to disturb allocation of risk because of advantage in bargaining power. Thus, the fact that there is some imbalance in bargaining power should not inevitably lead to a finding of procedural unconscionability. The absence of negotiation is also not an absolute indication of unfair advantage by the stronger party. Rather, the bargaining imbalance must reach such an ex-
treme level that it leaves the weaker party virtually without choice and results in oppressive terms.\textsuperscript{91}

The Utah Supreme Court observed in a recent opinion that, in the landmark case of \textit{Williams v. Walker-Thomas Furniture Co.},\textsuperscript{92} the D.C. Circuit "recharacterized" procedural unconscionability as involving an "absence of meaningful choice."\textsuperscript{93} While the \textit{Williams} formulation has gone on to become probably the most often-cited definition of unconscionability,\textsuperscript{94} the \textit{Williams} language has the potential to transform unconscionability standards in a manner that would further obfuscate the already vague concept of procedural unconscionability through oppression. Notably, the facts supporting the claim of unconscionability in \textit{Williams} related in large part to the surprise element of unconscionability. The court deemed the add-on clause in question to be written in such language that the average person probably would have found it unintelligible in the unlikely event that the clause was actually discovered and read.\textsuperscript{95} But the \textit{Williams} opinion also suggests procedural unconscionability based on a lack of meaningful choice, in that the plaintiff's lack of economic resources meant that she had little choice but to purchase household goods from the defendant or some other similar seller who operated in the economically depressed area and sold goods on presumably unfair terms.\textsuperscript{96}

\begin{itemize}

\item \textsuperscript{92} 350 F.2d 445 (D.C. Cir. 1965).


\item \textsuperscript{94} See Murray, supra note 12, at 490.

\item \textsuperscript{95} Williams v. Walker-Thomas Furniture Co., 350 F.2d 445, 449 (D.C. Cir. 1965).

\item \textsuperscript{96} The following is a more complete statement from the majority opinion in \textit{Williams}:

Unconscionability has generally been recognized to include an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party. Whether a meaningful choice is present in a particular case can only be determined by consideration of all the circumstances surrounding the transaction. In many cases the meaningfulness of choice is negated by a gross inequality of bargaining power. The manner in which the contract was entered is also relevant to the consideration. Did each party to the contract, considering his obvious education or lack of it, have a reasonable opportunity to understand the terms of the contract, or were the important terms
A better example of procedural unconscionability through lack of meaningful choice is found in the equally well-known case of *Henningsen v. Bloomfield Motors*, 97 which involved a harsh warranty provision in an automobile purchase contract. On the facts of *Henningsen*, the argument for lack of meaningful choice is quite persuasive because of the practical importance of automobiles in society and the fact that the same unconscionable warranty provisions were used by the automakers association that accounted for most automobile sales in the United States. 98 A small number of other cases can be identified with actual or near monopolies or oligopolies in which one party holds a substantial bargaining advantage and the option of declining the transaction is arguably not reasonable. 99 Although the argument that the buyer in *Williams* had limited choices seems not only to draw on the equities of the case, but also probably reflects the likely reality of the consumer's choices, the case is better viewed as involving unfair surprise. Moreover, extension of the reasoning may prove troublesome because of the difficulties in determining when alternative sources are sufficient and when the party has a meaningful alternative in simply declining the transaction. 100

hidden in a maze of fine print and minimized by deceptive sales practices. . . . But when a party of little bargaining power, and hence little real choice, signs a commercially unreasonable contract with little or no knowledge of its terms, it is hardly likely that his consent, or even an objective manifestation of his consent, was ever given to all the terms.

350 F.2d at 449 (citations omitted).


98. Id. at 87.

99. See *Associated Press v. Southern Arkansas Radio Co.*, 809 S.W.2d 695, 697 (Ark. Ct. App. 1991) (discussing contract between radio and only news service available in geographical area); *Allen v. Michigan Bell Tel. Co.*, 171 N.W.2d 689, 693-94 (Mich. Ct. App. 1969) (finding that customer had no realistic alternative to yellow page advertising in holding clause limiting liability of telephone company unconscionable); *Art's Flower Shop v. Chesapeake & Potomac Tel. Co.*, 413 S.E.2d 670, 675 (W. Va. 1991) (finding that telephone company had a monopoly on yellow pages directory and that no comparable alternative existed in determining that limitation on liability was unconscionable); *but see WXON-TV, Inc. v. A.C. Nielsen Co.*, 740 F. Supp. 1261, 1265 (E.D. Mich. 1990) (limitation on liability in contract was not unconscionable even though there were only two sources of ratings information services available to television station, especially because customer had gone without ratings services in the past); *Wille v. Southeastern Bell Tel. Co.*, 549 P.2d 903, 911 (Kan. 1976) (finding that limitation of liability by telephone company was not unconscionable); *Vasilis v. Bell of Pennsylvania*, 598 A.2d 52, 54 (Pa. Super. Ct. 1991) (denying claim of unconscionability, noting that yellow page advertisements are outside the realm of necessary services and therefore subject to private contract arrangements between commercial parties).

100. See *Phoenix Leasing v. Sure Broadcasting, Inc.*, 843 F. Supp. 1379, 1385 (D. Nev. 1994) (assuming that no other lender was available, borrower of funds to start up company still could have declined loan if terms were not acceptable); *Citizens Ins. Co. of America v.*
The early debate on Section 2-302 focused significant attention on whether a term could be unconscionable even though it was clearly disclosed by the stronger party and understood by the weaker party before assenting. Although a number of courts and commentators have accepted the proposition that oppression or the absence of meaningful choice may provide a basis for procedural unconscionability in exceptional cases even when the objectionable term is fully disclosed, this form of procedural unconscionability remains inherently more suspect than one based on a finding of unfair surprise. When a merchant seeks a determination of unconscionability based on a lack of meaningful choice, the underpinnings for procedural unconscionability are even more dubious.

(2) Protecting Consumers Rather than Merchants

A consensus exists among courts and commentators that Section 2-302 is more likely to be available to consumers than to merchants.
The equitable roots of unconscionability reflect a traditional concern for relatively weaker parties that are more likely to be taken advantage of in the bargaining process.\footnote{104} Although some early drafts of Section 2-302 excluded merchants from its protection,\footnote{105} the text of the Section does not limit its application to nonmerchants, and several cases cited in the Official Comments involve transactions between merchants.\footnote{106} Moreover, U.C.C. provisions other than Section 2-302 contemplate the possible application of the unconscionability doctrine in favor of merchants.\footnote{107}

Despite the ability of courts to apply Section 2-302 to merchants, they have been reluctant to apply the Section in favor of merchants or other sophisticated parties.\footnote{108} The courts occasionally treat some merchants essentially as quasi-consumers based on a lack of business experience, lower educational level, or other similar disadvantage relative to the other party.\footnote{109} The basis for applying the doctrine in favor

\footnote{104} Professor Leff notes that equity cases repeatedly involved parties such as the old, the young, and the sick who might have been taken advantage of in the bargaining process. \cite{Leff, supra note 14, at 528-38.}

\footnote{105} See \cite{Leff, supra note 14, at 492-93} (noting that under the 1943 draft, merchants could not invoke the unconscionability defense if they had the opportunity to read the document).

\footnote{106} In the Preliminary Report on possible revisions of § 2-302, the study group notes that courts have restrained themselves, "particularly in commercial disputes," by avoiding the rewriting of substantive terms. \cite{Preliminary Report, supra note 19, pt. 3, at 2-3.} The study group, however, also disfavored the proposal that a distinction be made in § 2-302 between consumers and merchants. \cite{Id.}

\footnote{107} See, e.g., U.C.C. § 2-205 cmt.4 (1990) (stating that unconscionability doctrine may serve as limit on enforceability of firm offers by merchants); § 2-719(3) (indicating that consequential damage limitations may be unconscionable in nonconsumer transactions).

\footnote{108} See, e.g., Canal Elec. Co. v. Westinghouse Elec. Co., 973 F.2d 988, 996-97 (5th Cir. 1992) (reflecting disinclination to find unconscionability in limitation on liability agreed to by "highly sophisticated business entities"); Geldermann & Co. v. Lane Processing, 527 F.2d 571, 576 (8th Cir. 1975) (holding that liquidation provision was not unconscionable because it was common to the commercial future trading arena); \textit{but see} \cite{Johnson v. Mobil Oil Co., 415 F. Supp. 264, 265-67 (E.D. Mich. 1976)} (reviewing findings of unconscionability in merchant cases); \cite{Farnsworth, supra note 11, § 4.28, at 330-31} (noting that § 2-302 has been used to favor some merchants including franchisees); \cite{Mallor, supra note 14} (asserting that there is a growing trend of applying unconscionability in merchant cases).

\footnote{109} See \cite{Johnson v. Mobil Oil Corp., 415 F. Supp. 264, 265-67 (E.D. Mich. 1976)} (observing that retailer dealer had less than eighth-grade education, was practically illiterate, signed the contract while busily engaged with service station, and did not discuss any term other than amount of rent); \cite{Weaver v. American Oil Co., 276 N.E.2d 144 (Ind. 1971)} (finding that lessee had less than high school education, limited business experience, did not read lease or have it explained, and dealt with much larger lessor which presented a take-it-or-leave-it lease). \textit{See also} \cite{Mallor, supra note 14, at 1080-84} (discussing cases involving unsophisticated merchants).
of such quasi-consumers is that they are more likely to be taken advantage of by either surprise or gross inequality in bargaining power than the sophisticated merchant.\footnote{110} Even when appellate courts uphold trial court findings of unconscionability in the unsophisticated merchant cases, they frequently express reservations.\footnote{111}

While courts on rare occasions grant relief to merchants who are not quasi-consumers, such decisions are inherently suspect with regard to the presence of procedural unconscionability.\footnote{112} The courts have stated that there is a presumption against finding unconscionability in contracts between merchants.\footnote{113} The sophisticated business entity is deemed more likely to guard against hidden terms in a contract and is held responsible for understanding the terms of the contract.\footnote{114} The sophisticated business entity is more likely not only to have the benefit of counsel,\footnote{115} but also to have alternatives and to be able to bargain effectively for balanced terms.\footnote{116} For these reasons, courts have been reluctant to find that a merchant has been taken advantage of through


\footnote{112} See White & Summers, supra note 66, § 4-2, at 184 (presumably few merchants are subject to gross advantage-taking required under § 2-302); Mallor, supra note 14, § 96, at 498-99 (difficult for true merchants to show unfair surprise or inferior bargaining position).


The cases from California discussed below indicate a pattern of decisions that vary from the norm and raise questions about the courts finding unconscionability between merchants.

(3) Unconscionability Judged at the Time Contract Was Made

When Section 2-302 began to take its present shape in 1948, it did not contain the explicit requirement that the contract be examined for unconscionable terms under the circumstances existing at time the contract was formed. A proposal to add the time limitation arose after the first official text was carefully studied. The proposal was included in the 1955 proposals for amendment to the U.C.C. Supporters of the amendment reasoned that the proposed change would emphasize to courts assessing unconscionability that the courts should not apply hindsight, but instead should consider the issue as of the time the contract was formed. Section 2-302, with the new time limitation, took its present form in 1957.

Notable in light of the change to Section 2-302, the equity antecedents to unconscionability might cause denial of enforcement of a contract based on unfairness in formation, performance, or enforcement. Nevertheless, the drafters of Article 2 specifically rejected a proposal arising from the New York study of the U.C.C. that Section 2-302 be altered to allow courts to refuse enforcement based on a

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118. See supra note 43 and accompanying text. The first official text of § 2-302 in 1952 did not contain the language on time perspective. The 1952 version read:
   (1) If the law court finds the contract or any clause of the contract to be unconscionable it may refuse to enforce the contract or may strike any unconscionable clauses and enforce the contract as if the stricken clause had never existed.
   (2) When it is claimed or appears to the court that the contract or any clause thereof may be unconscionable the court may afford the parties an opportunity to present evidence as to its commercial setting, purpose, and effect to aid the court in making the determination.

119. See THE KARL LLEWELLYN PAPERS, supra note 118, § J, Uniform Commercial Code, Part XIV (1)(a) [hereinafter THE KARL LLEWELLYN PAPERS].

120. See id. at § J, Part XIX (1)(a). See also Leff, supra note 14, at 540-41 n.236 (noting that "hindsight" perspective was firmly rejected by the drafters).

121. See THE KARL LLEWELLYN PAPERS, supra note 118, § J, Part XIX(1)(a). See also id. at Part XIV (2)(b).

122. See CALAMARI & PERILLO, supra note 11, at 399-400; Sherwin, supra note 38, at 254-57.
harsh result of contract performance. Consistent with this drafting history, the courts routinely emphasize that, in assessing unconscionability, they must adopt the perspective of the parties at the time the contract was made and that the burden of proof is on the party making the claim of unconscionability.

The requirement that the contract be assessed from the time of making may pose some subtle difficulties. In a classic case involving the price of cotton, the court stated that, in order to find unconscionability, the contract price must be exorbitant based on a price disparity existing at the time of contracting and that there was no need for the court to consider how the price of cotton may have moved after the execution of the contract. When events occurring after the formation of the contract have allegedly made the enforcement of the contract one-sided or unfair, unconscionability is irrelevant and other doctrines, such as impracticability or the implied duty of good faith, may be applicable. On the other hand, if there is a claim that one party possessed information of an impending change in the market at

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123. See The Karl Llewellyn Papers, supra note 118, § I, Part XIV (2)(b).
124. See Boston Helicopter Charter, Inc. v. Augusta Aviation Corp., 767 F. Supp. 363, 375 (D. Mass. 1991) (stating relevant circumstances are those at time of making, not as they later developed); Avildsen v. Prystay, 574 N.Y.S.2d 535, 536 (App. Div. 1991) (stating that other unconscionability cases have looked at fairness from point at which it was formed), appeal dismissed, 588 N.E.2d 91 (N.Y. 1992); Best v. United States Nat'l Bank, 739 P.2d 554, 556 (Or. 1987) (unconscionability is legal issue that must be assessed as of time of formation); Resource Management Co. v. Weston Ranch & Livestock Co., 706 P.2d 1028, 1043-44 (Utah 1985) (observing that judging contracts in hindsight would be inappropriate given that many contracts contain speculative elements that allocate risks based on possibility that circumstances may change in future).
127. See McLaughlin, supra note 55, at 441 nn.9-10; Glopak Corp. v. United States, 851 F.2d 334, 338 (Fed. Cir. 1988) (noting that the price adjustment clause that caused seller's price and profit to be reduced must be judged from the time contract was made and should not be judged by the manner in which the adjustment clause actually applied); Don King Prods., Inc. v. Douglas, 742 F. Supp. 778, 780 (S.D.N.Y. 1990) (stating that subsequent performance under contract may constitute breach of duty of good faith, but has no bearing on unconscionability at time contract was made). See also Margaret N. Kniffin, A Newly Identified Contract Unconscionability: Unconscionability of Remedy, 63 Notre Dame L. Rev. 247 (1988) (discussing the impact of Restatement (Second) of Contracts § 351(3) on the ability to recover disproportionately large contract damages).
the time of formation of the contract, such a claim may appropriately be reviewed under Section 2-302, but only to the extent that it affected the fairness of the contract at the time it was made. The court should properly view the contract from the time of making, with the range of possible eventualities in mind, including the one that came to fruition, and ask whether the provision was so unfair at the time of execution that it would shock the conscience of the court. California courts have shown a tendency to judge contracts in hindsight to determine unconscionability—an approach that is inconsistent with the clear dictates of Section 2-302.

(4) Reformation and Defensive Use of Unconscionability

The text of Section 2-302 provides that where unconscionability is found, the courts may refuse to enforce the entire contract or may strike or limit a particular term. An early draft of Section 2-302 expressly permitted courts to reform contracts for the parties, but the final draft failed to include that provision. The options of striking a clause or limiting its effect, however, necessarily grant the courts, at a minimum, a limited ability to reform the contract. Courts have exercised the power to remake bargains by reducing the price, requiring cause for one party's termination, increasing a duration term, or reducing an interest rate.

Based on an unduly restrictive reading of Section 2-302, some courts have taken the view that the Section can be used only in a defensive posture by a party fending off an action for breach and not as a basis for affirmative recovery. A few courts, however, have recog-

128. See Ellinghaus, supra note 14, at 802-03. The court in Adams v. John Deere Co., 774 P.2d 355 (Kan. Ct. App. 1989) was faced with a claim by a dealer for John Deere products that a provision excluding any claim for lost profits upon termination of the contract was unconscionable. The dealer had been terminated in accordance with a provision in the contract allowing termination with 180 days notice. Id. at 356-57. The court stated emphatically that any claim of breach was independent of the question whether the "no lost profits" clause was unconscionable at the time the contract was made. Id. at 362. Accord Resource Management Co. v. Weston Ranch & Livestock Co., 706 P.2d 1028, 1043-44 (Utah 1985) (finding subsequent conduct relevant to breach, but not to unconscionability).

129. See supra note 4 and accompanying text.

130. See Hunter, supra note 12, at 151-53.

131. See Calamari & Perillo, supra note 11, at 405; Farnsworth, supra note 11, § 4.28, at 327; Hunter, supra note 12, at 151-53 nn.38-42.

132. See Cowin Equip. Co. v. General Motors Corp., 734 F.2d 1581, 1582 (11th Cir. 1984) (holding that damages are not available for an unconscionable contract); Bennett v. Behring Corp., 466 F. Supp. 689, 700 (S.D. Fla 1979) (stating that unconscionability cannot be utilized to obtain affirmative recovery of money damages), appeal dismissed, 629 F.2d
nized that the doctrine may be properly used as a basis for granting affirmative relief to a party either through restitution or by enforcing other provisions of the contract. Indeed, the distinction between defensive use and offensive use of the doctrine often becomes attenuated. When a party attempts to obtain a refund of a deposit paid by seeking to strike the clause prohibiting the refund, the net effect of finding unconscionability is that the party asserting it is allowed to gain an affirmative recovery. Further, when a party sues for damages and faces a barrier in the form of a contract term that is challenged as unconscionable, then the finding that such a term is unconscionable would obviously open the way for an action for damages. The one legitimate concern underlying the approach that bars affirmative use of the doctrine is the fact that the presence of unconscionable terms does not in itself serve as a basis for a remedy.

The distinction between defensive and offensive use is illogical and should be discarded because it may well result in only one of two similarly situated parties being unable to make use of the unconscio-


133. See Langemeier v. National Oats Co., 775 F.2d 975, 978 (8th Cir. 1985) (noting that § 2-302 allows the court to enforce the remainder of agreement without the unconscionable term); Ahern v. Knecht, 563 N.E.2d 787 (Ill. Ct. App. 1990) (affirming lower court decision that awarded plaintiff restitutionary damages). See also WHITE & SUMMERS, supra note 66, § 4-8, at 204 (recognizing possibility of restitutionary recovery).

134. Various commentators have recognized this difference. See FARNSWORTH, supra note 11, § 4.28, at 327 n.21 (noting difference between recognizing a cause of action based on the fact that the contract or term is unconscionable as opposed to striking a clause and enforcing the remainder of the contract in a manner which grants affirmative relief); WHITE & SUMMERS, supra note 66, § 4-8, at 204 (stating that restitutionary recovery is an appropriate remedy when the benefit has been transferred pursuant to a clause later found to be unconscionable).

135. See Langemeier v. National Oats Co., 775 F.2d 975 (8th Cir. 1985) (noting that § 2-302 allows the court to enforce the remainder of the agreement without the unconscionable term); Master Lease Corp. v. Manhattan Limousine, Ltd., 580 N.Y.S.2d 952, 953 (App. Div. 1992) (showing that a successful finding that warranty clause was unconscionable could then enable defendants to recover money damages on their counterclaim for breach of warranty).

136. See WHITE & SUMMERS, supra note 66, § 4-8, at 203-04 (acknowledging that § 2-302 provides no remedy for unconscionability, but arguing that punitive damage should be allowed because of quasi-fraud nature).
nability doctrine. For example, if two parties purchase appliances from door-to-door salespersons for outrageously and indefensibly exorbitant prices as a result of sharp dealing, the party who purchases on credit can refuse to pay and then use the unconscionability doctrine defensively to fend off a claim by the seller for payment. The party who has cash and is able to pay on delivery cannot use unconscionability to obtain a partial refund of the price or to rescind the transaction altogether under the approach that blindly denies affirmative relief on a claim of unconscionability.

(5) Policing the Price Term

Another debated aspect of Section 2-302 focuses on how the Section can be used to police against excessive price terms in contracts. Two related issues arise in the course of this debate. The first question concerns how courts determine when a price is sufficiently excessive to be deemed substantively unconscionable. The second issue is whether a finding of unconscionability can be based on an excessive price term alone when there is no showing of procedural unconscionability.

The price term may be alleged to be substantively unconscionable either because the contract price is much higher than the normal market price for a similar purchase or because the contract price greatly exceeds the seller's cost. The latter approach, which focuses on the seller's profit margin, essentially embraces the idea that the seller may make too much profit or that the price may be too high as measured in an absolute manner. While there are commentators and a few courts who seem to accept this approach, it conflicts with basic eco-

137. See McLaughlin, supra note 55, at 44-43 (citing anomalous results from the no-offensive-use approach and questioning whether the drafters of the Section intended to limit the remedy to defensive use).


139. See Perdue v. Crocker Nat'l Bank, 702 P.2d 503, 512-13 (Cal. 1985) (noting the costs and market price factors in more complex assessment of price fairness); WHITE & SUMMERS, supra note 66, § 4-5, at 191 (noting alternative means of measuring for excessive price); Darr, supra note 14, at 1840 (noting alternative means of assessing fairness).

140. See Zepp v. Mayor & Council of Athens, 348 S.E.2d 673, 678 (Ga. Ct. App. 1986) (excessive high price may constitute unconscionable provision under § 2-302); Eisenberg, supra note 14, at 752-53 (interpreting a number of cases to have held or indicated that excessive price alone may lead to determination of unconscionability); Ellinghaus, supra
nomic assumptions that the marketplace should be sufficient to regulate prices and also assumes that the courts have the capability to regulate prices effectively in those circumstances in which market controls do not work.

The alternative approach of determining excessive price by measuring the contract price against the market price (the "contract price-market price" approach) lends itself to more consistent application as a number of courts have recognized. Under this approach, the reasonableness of the seller's markup may properly serve as a secondary test in situations when either a contract price that exceeds the market price is justified by additional costs or there is no market price with which to make a comparison. The inherent difficulty in either approach of policing for excessive prices is the difficulty of determining at what point the price becomes unconscionable.

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note 14, at 790 (stating that courts' acceptance of a large but imprecise disparity between value and price as a species of unconscionability is a "matter for rejoicing").

141. See Darr, supra note 14, at 1823, 1833-34 (stating traditional view of competitive market is that buyers will set price, but noting that lack of information will cause process to fail).

142. Professor Leff offered an interesting analysis of what was probably the earliest price-term unconscionability case, American Home Improvement, Inc. v. MacIver, 201 A.2d 886 (N.H. 1964), noting that the court miscalculated the seller's cost and failed to evaluate the rate of interest realized by the seller. Leff, supra note 14, at 549-51. See also Ellinghaus, supra note 14, at 793 (agreeing with Professor Leff that the early price cases lacked a sophisticated approach to determining whether a price was unconscionable); Darr, supra note 14, at 1826 (noting that reluctance of courts to judge fairness of exchange stems from both respect for value assigned by parties and inherent difficulty in courts assessing value).

143. See Bradford v. Plain Cotton Coop. Ass'n, 539 F.2d 1249, 1255 (10th Cir. 1976) (holding that amount of profit made by purchaser not relevant to claim of price term unconscionability); Bennett v. Behring Corp., 466 F. Supp. 689, 696-98 (S.D. Fla. 1979) (asserting that price-value disparity is irrelevant and asserting that only contract price-market price disparity serves as a basis for unconscionability); Iamartino v. Avallone, 477 A.2d 124, 125-26 (Conn. App. Ct. 1984) (interest rate of 37% to 45% was high but not unconscionable when measured against relevant market rate); Remco Enters. v. Houston, 677 P.2d 567, 572-73 (Kan. Ct. App. 1984) (holding that comparison to market price and not percentage of seller's mark up was relevant to question of excessive price).

144. WHITE & SUMMERS, supra note 66, § 4-5, at 193-94 (noting seller should have chance to show higher than market prices are justifiable).

145. An excellent example of the difficulty in assessing when a price becomes unconscionable is found in Nelson v. McGoldrick, 871 P.2d 177 (Wash. Ct. App. 1994), in which plaintiff operated an heir location business and contracted with defendant for a finder's fee of 50% of $50,000 inheritance of which she was otherwise unaware. The defendant signed the contract in her home and was advised by her husband-real estate broker and son-attorney before signing. The court deemed that agreeing to pay half of the inheritance was not irrational. The court also was persuaded that she could have declined the contract and sought to uncover inheritance on her own in holding that the contract was not unconscionable. Id. at 770-71. See also Darr, supra note 14, at 1826 (noting difficulty of courts assess-
Assuming that a price is found to be substantively unconscionable through an appropriate method, then the second question is whether procedural unconscionability exists. A finding of procedural unconscionability through unfair surprise is unlikely due to the inherently obvious nature of the price term and its importance to any transaction.146 Unfair surprise is not impossible to find, however, because the price may be presented in a deceptive fashion or the buyer may lack information that reveals the excessive nature of the price at the time of contracting.147 Procedural unconscionability may also be present in excessive price cases through oppression under exceptional circumstances in which a true lack of alternatives can be established.148 The most compelling case for lack of meaningful choice would be in a case of necessity when goods or services were required for the well-being of an individual or the continued existence of a business.149

146. See Farnsworth, supra note 11, at 329; Darr, supra note 14, at 1822, 1833; Spanogle, supra note 14, at 951.

147. See Davis v. Kolb, 563 S.W.2d 438, 438-39 (Ark. 1978) (contract to sell timber with market value of $50,000 for contract price of $20,000 was unconscionable when buyer had misled seller about value of the timber and his knowledge of the subject); Waters v. Min Ltd., 587 N.E.2d 231, 234 (Mass. 1992) (finding agreement to sell annuity for contract price of $50,000 when it had cash value of $189,000 and guaranteed value of $694,000 over 25 years was unconscionable when agent for buyer unduly influenced seller and advised her to sell under contract that would give financial benefit to agent); Lehn v. Astor Art Galleries, Ltd., 380 N.Y.S.2d 532, 541 (Sup. Ct. 1976) (contract to sell art objects for $67,000 that had retail value of approximately $15,000 was unconscionable when sales took place in buyers' home under unusual circumstances and seller misrepresented value to uninformed buyers). See also Darr, supra note 14, at 1848 (noting lack of information as crucial impediment to market policing price fairness); Gordley, supra note 35, at 1619 (observing that a party may not be able to use the market to protect against price unfairness because of ignorance or necessity).

148. See, e.g., Kelly v. Widner, 771 P.2d 142 (Mont. 1989) (finding accident release agreement unconscionable when injured party had only ninth-grade education, was impoverished and unable to work because of accident, and was without counsel, and when multiple insurance agents obtained her signature when nature of injuries were still substantially uncertain and settlement barely covered expenses to date); but see Spanogle, supra note 14, at 951 (observing that "absent a monopoly situation, a refusal to bargain is thought justifiable").

149. See, e.g., Ryan v. Weiner, 610 A.2d 1377, 1381 (Del. Ch. 1992) (transfer of house with $12,000 in equity value by unsophisticated owner in exchange for payment of $1900 to avoid foreclosure amounted to unconscionable contract); Howard v. Diolosa, 574 A.2d 995, 998-1000 (N.J. Super. Ct. App. Div. 1990) (finding that the sale of home with fair market value of $150,000-$200,000 for contract price of $25,000 was unconscionable when sellers had been turned down by four institutional lenders and were in desperate need of cash to pay creditors). See also Dawson, supra note 36, at 369-70 (observing under German law in order for economic necessity to provide a basis for excuse from a contract, the necessity must be so severe as to threaten the economic existence of the weaker party as
Because unfair surprise concerning price is unlikely and oppression through lack of meaningful choice is dubious, the question arises whether excessive price alone is enough to render the contract unconscionable. For years, the courts have found excessive price to be at least a primary ground for unconscionability, and some commentators have found support in the court decisions for the position that unconscionability in the price term alone is enough to reform the contract. A closer examination of those cases reveals that the purchasers were almost certainly unaware of the exorbitant nature of the price even if they were aware of the total dollar amount. Moreover, a finding of unconscionability based solely on an excessive price when the buyer knowingly chose to enter into the contract would be incorrect by almost certainly pushing Section 2-302 beyond the use contemplated by various state legislatures when they adopted Article 2. The question still remains open to debate.


151. See White & Summers, supra note 66, §4-8, at 200 (asserting that excessive price alone should be enough to show unconscionability); Eisenberg, supra note 14, at 753 (interpreting number of cases as holding or indicating that unfair price alone is enough to render contract unconscionable); Spanogle, supra note 14, at 952 (concluding that excessive price alone may be enough based on older equity decisions); but see Darr, supra note 14, at 1840-41 (proposing that price unconscionability be found only when (1) the price is excessive, (2) the contracting process is flawed, and (3) the market is such that it is not subject to self-correction); Gordley, supra note 35, at 1627-37 (suggesting generally that mere price term disparity is enough, but stating that "if courts are not to cause more inequalities than they cure, they should confine relief to cases where the price is clearly disproportionate and the disadvantaged party is badly hurt and less able to protect himself").

152. See Hertz Corp. v. Attorney Gen., 518 N.Y.S.2d 704, 708-09 (App. Div. 1987) (noting that excessive prices have usually been accompanied by fraud, deception, and coercion); Murray, supra note 12, at 498; Darr, supra note 14, at 1843-45 (surveying 44 price unconscionability cases and finding that only 2 of 19 successful claims reflected finding of unconscionability without some additional process flaw).

153. See Epstein, supra note 14, at 294 (advocating that the purpose of unconscionability is not allow to courts to act as roving commissions to set aside agreements on subjective bases); Leff, supra note 14, at 548-49 (expressing doubt that the state legislatures would have knowingly adopted a commercial law statute that authorized courts to engage in ad hoc policing of price terms).
II. The History of the Unconscionability Doctrine in California

A. Legislative History

The adoption of the U.C.C. by a state is always a matter of legislative action and the legislative history is illustrative in guiding courts that are applying a provision such as Section 2-302, enacted in California as Civil Code Section 1670.5. Long before Section 2-302 was adopted as part of a consumer protection bill, the California Legislature declined to adopt the Section as part of the Commercial Code after extensive debate. Advocates of the Section urged its adoption on the grounds that it merely restated or properly extended existing California law giving courts the power to apply equitable remedies. Other groups advocated eliminating the Section altogether or modifying it in a significant way. Ultimately, the Section was omitted from the proposed Commercial Code because of concerns that it would give the courts too much power to second-guess the parties under the guise of policing against "unfair" bargains.

A second reason for declining to adopt Section 2-302 was the view that the common law in California was already well developed enough to guard against unfair contracts. Specifically, the courts were deemed to have the explicit power to refuse enforcement of grossly unfair bargains under equity doctrines and to have achieved similar results at law by construing contract language. Further, California courts also had developed rules concerning adhesion contracts that worked to protect parties from unfair bargains. Arguing along


155. See id. at 340 (detailing Analysis and Interim Report of the State Bar of California).

156. See id. at 455-57 (Report of Professors Harold Marsh, Jr., and William D. Warren). The California Bankers Committee proposed that the Section be amended to substitute the term "good faith" for unconscionability. Professors Marsh and Warren proposed altering the language of § 2-302 to exclude contracts between merchants and to further limit application to parties who had prepared form contracts.

157. See California State Bar Committee on the U.C.C., supra note 1 and accompanying text.

158. See SIXTH PROGRESS REPORT, supra note 154, at 456 (Report of Professors Harold Marsh, Jr., and William D. Warren) (stating that California courts have historically used their equitable powers to avoid the enforcement of harsh bargains).


160. See infra notes 189-217 and accompanying text.
the same lines as the chief drafter of the Uniform Commercial Code, some of the California debaters contended that it would be preferable to allow the courts to engage in open policing of allegedly unconscionable contracts rather than "by indirection, if not subterfuge." Their position was buttressed by the argument that expansion of judicial policing power was justified by the proliferation of form contracts in the marketplace. Ultimately, however, the greater concern was that the novelty in the law would make it difficult to predict how great a change would be made in California law and that the courts might engage in judicial overreaching, such as by refusing to enforce a clause or contract even though it "had been thoroughly negotiated by the parties." Thus, the California Legislature decided in 1962 to omit Section 2-302 the Uniform Commercial Code as adopted.

Additional attempts between 1972 and 1976 to add an unconscionability statute to California law, specifically aimed at consumer protection, also failed. The last unsuccessful legislation provided that the courts might consider a number of factors similar to those found in the Uniform Consumer Credit Code as pertinent to the issue of unconscionability, including taking advantage of the lack of knowledge, ability, experience or capacity of a consumer, knowledge of the inability of the consumer to receive benefits properly anticipated from the goods or services involved, gross disparity between the price of goods or services and their value, or knowledge that there is no reasonable probability of payment in full of the obligation by the consumer.

161. See supra note 53.
163. Id.
164. Id. at 456.
165. Id. at 457.
166. Assembly Bill 4306 was introduced by Assemblyman Sieroty on March 29, 1976. The bill proposed that a § 1663 be added to the Civil Code that would have read:
   (a) With respect to any consumer transaction, if the court as a matter of law finds that any aspect of the transaction, any conduct directed against the consumer by a party to the transaction, or any result of the transaction is unconscionable, the court shall, in addition to any other remedy provided for by law, either refuse to enforce the transaction against the consumer, or so limit application of any unconscionable aspect or conduct to avoid any unconscionable result.
167. A.B. 4306, supra note 166.
The proposed bill was referred to the Committee on the Judiciary where it died without further action.\textsuperscript{168}

After the failed attempts, the California Legislature finally adopted the verbatim language of Section 2-302 in 1979 as part of Assembly Bill 510, a consumer protection bill principally aimed at abuses in the home improvement industry. The bill targeted transactions in which consumers were extended credit secured by a lien on their homes and then suffered foreclosure when they defaulted.\textsuperscript{169} The legislature enacted Section 2-302, not as part of the California Commercial Code, but as Section 1670.5 of the Civil Code, making unconscionability applicable to all contracts in California and not just those for the sale of goods. The legislature subsequently adopted the Official Comments to Section 2-302 as an aid to interpreting California Civil Code Section 1670.5.\textsuperscript{170}

While Assembly Bill 510 clearly emphasized consumer protection from unscrupulous practices in the home improvement industry, proponents acknowledged that the adoption of Section 2-302 would have a broader impact.\textsuperscript{171} The legislative history of Section 2-302 in Cali-

\begin{itemize}
\item \textsuperscript{168} A.B. 4306, Assembly Final History at 2209 (on file with author).
\item \textsuperscript{169} The digest of Assembly Bill 510 (A.B. 510) stated: A.B. 510 is one of several bills in the Senate and the Assembly designed to curb abuses by door-to-door salesmen of home improvement goods or services which have resulted in the non-judicial foreclosure sale of homes when homeowners defaulted on payments. . . . Proponents state that most of the victims in these “equity rip-off” schemes are the elderly and the poor. . . . The contract would be secured by a trust deed and would require payments too large for the homeowner to handle over and above his other obligations. At the first instance of default . . . the trust deed would be sold to another company who would then foreclose on the home . . . .
\item J. Fenton, Digest of A.B. 510, Aug. 30, 1979 (on file with author). The Enrolled Bill Report of the Legal Affairs Secretary indicated that to curb unscrupulous business people from taking advantage of unsophisticated homeowners, A.B. 510: (1) adopts the U.C.C. provision on unconscionable contracts, (2) prohibits financial institutions from misconduct through reassigning loan contracts back to the original lender, and (3) requires more notice and publication of foreclosure sales. Report on Enrolled Bill A.B. 510 from J. Anthony Kline, Legal Affairs Secretary to Edmund G. Brown, Jr., Governor of California (Sept. 10, 1979) (on file with author). The Enrolled Bill Report of the Department of Consumer Affairs also cited the particular emphasis of A.B. 510 on consumer home improvement contracts as well as protecting consumers more broadly. Report on Enrolled Bill A.B. 510 from Department of Consumer Affairs, State & Consumer Services Agency to Edmund G. Brown, Jr., Governor of California (on file with author).
\item \textsuperscript{170} Assembly Journal 9230-31 (Sept. 5, 1979); Senate Journal 7091 (Sept. 4, 1979).
\item \textsuperscript{171} Letter from Assemblyman Jack R. Fenton, Chairman, Assembly Judiciary Committee, to Edmund G. Brown, Jr., Governor of California (Sept. 13, 1979). The letter stated that the bill would resolve the problem because it makes “all unconscionable contracts voidable and also provides that unconscionable provisions in a consumer contract are unlawful. This is designed to protect the uninformed consumer who enters into a pa-
\end{itemize}
fornia clearly evidences that the statutory enactment of the unconsci-
nonability doctrine was aimed primarily at consumers involved in
situations in which they might be victims of unscrupulous merchants.
Although references to the general application of Section 2-302 to all
contracts may also be found in the legislative history, Assembly Bill
510 passed where two other attempts had failed, largely on the basis of
the legislature's imperative to curb abuses in the home improvement
industry. Given the consumer protection impetus behind the bill, the
question is whether the same legislators who voted to adopt Section 2-
302 would have acted differently if they had foreseen the application
of the doctrine to many of the non-consumer cases in California since
1979.

B. California Common Law Predecessors to Section 2-302

A number of cases predating the 1979 adoption of Section 2-302 in
California reveal the willingness of courts to police contracts for
unfairness in two types of situations. The earlier type of cases applied
the general principle of equity that courts, usually in cases involving
consumers, will not enforce contracts that are extremely one-sided or
that suggest bargaining misconduct. 172 The later, second category of
cases primarily involved consumers challenging adhesion contracts re-
lying to necessities. Both categories of cases are illustrative in under-
standing and criticizing the current practices of the California courts
in unconscionability cases.

State Finance Co. v. Smith173 and Jacklich v. Baer174 typify the
early cases in which courts refused to enforce contracts based solely

tently unreasonable contract with an opportunity to void the agreement and seek legal
remedies against the unscrupulous seller." Similarly, the Assembly Hearing Digest of A.B.
510 also identified the broad application of the proposed unconscionability statute while
still emphasizing the consumer protection aspects of the bill. T. Carroll, Digest of A.B.
510, Apr. 18, 1979 (on file with author). The inclusion of the unconscionability doctrine, as
embodied in § 2-302, in legislation aimed at abusive practices in foreclosures on consum-
ers' homes was questionable enough procedurally to draw the attention of the Legislative
Counsel of California. In his letter to the Governor about the bill, the Legislative Counsel
focused on the fact that the title of the bill listed "property" as its subject matter without
reference to the unconscionability provision. After discussing the California constitutional
requirement that every act embrace but one subject expressed in the title, the Legislative
Counsel went on to conclude that § 2-302 was "reasonably germane and promotive" of the
declared purpose of the bill to preserve the rights of homeowners and consumers from
fraudulent and deceptive sales practices and to prevent the unjust forfeiture of homes.
Letter from Bion M. Gregory, Legislative Counsel of California, to Edmund G. Brown, Jr.,
Governor of California (Sept. 14, 1979).

172. See supra notes 38-41 and accompanying text.
on the inequity of the bargain. In *Smith* the unsophisticated defendant sought a $70 loan but received it only after agreeing to purchase a worthless truck for about $300. The transaction took place in January 1937, and the defendant defaulted on the loan about six months later. The plaintiff sued for a deficiency of $250 after repossession and sale of the collateral. The court cited the fundamental precept that mere inadequacy of consideration will not render a contract unenforceable, but that an inequality so gross as to shock the conscience of the court may amount to proof of fraud, oppression, or undue influence. In addition, the court found other evidence that the quality of the truck had been misrepresented by the finance company’s agent. The court refused to enforce the loan agreement because it was “inequitable and unconscionable.”

The decision in *Jacklich v. Baer* was based on similar reasoning, even though the facts were not quite as clear. Professional boxer Max Baer entered into an agreement with the plaintiffs that promised them a share of his winnings for a five-year period in apparent satisfaction of a debt of $13,500 he owed them. The contract also contained an option for the plaintiffs to renew their right to a share of Baer’s earnings for an additional five-year period for $5. The plaintiffs received payments totaling almost $33,000 by the end of the first five-year period and sought to enforce the option to renew for $5. The court offered two reasons for refusing to enforce the option. First, accepting the trial court’s interpretation of the contract, the court construed the contract as allowing for exercise of the option only if the initial debt had not been repaid during the first five-year period. Alternatively, the court reasoned that it would be unconscionable to

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175. 112 P.2d at 902-03. The defendant debtor needed the $70 to pay the fees on his existing truck. The second truck was valuable only as scrap and, in fact, was towed to the defendant’s home. Id.
176. Id. at 902. The defendant gave both his preexisting truck and the newly acquired truck as collateral for the loan. Both trucks were repossessed and sold. Id. at 902.
177. Id. at 903.
178. Id.
179. Id. at 904.
180. 135 P.2d at 180-81. The contract also served as a mutual release of an earlier contract that called for the plaintiffs to act essentially as Baer’s personal managers, but not boxing contests managers, and to pay or loan $15,000 to Baer. In return, the plaintiffs were to receive a share of Baer’s winnings and the right to become his boxing contest managers if the other managers did not continue. Id. at 180.
181. Id. at 180.
182. Id.
183. Id. at 182-84.
enforce the contract granting the plaintiffs the right to continue to receive a share of the defendant's earnings without any reciprocal consideration.\textsuperscript{184}

The motivation of the parties for entering into the apparently one-sided option agreement was not clear. Perhaps the contract was a legitimate business arrangement, or, more likely, it was another one of many cases of agents taking financial advantage of unwitting professional athletes.\textsuperscript{185} The court held that the contract, as characterized by the plaintiffs, would be harsh and oppressive and could not be enforced without an affirmative showing of business justification.\textsuperscript{186} The plaintiffs did not produce a convincing justification, and thus the contract was characterized as grossly one-sided. The court was also probably influenced by the apparent lack of sophistication of the boxer and by the manner in which events unfolded. To the extent that the court considered events that occurred after the contract was formed, the time perspective used was appropriate because the decision was based on principles of equity that existed prior to the adoption of Section 2-302 and that allowed hindsight judgment.\textsuperscript{187} Moreover, the decisions in both Jacklich v. Baer and State Finance Co. v. Smith rested on principles of interpretation or apparent fraud in addition to concerns about imbalance in the exchange. Similar factors are found at play in the early adhesion cases.

\textit{Steven v. Fidelity & Casualty Co.}\textsuperscript{188} was an early case involving an adhesion contract and is often cited as embodying the judicially-developed principle of unconscionability in California. \textit{Steven} involved a

\textsuperscript{184} Id. at 183-84.
\textsuperscript{185} The case held undertones of a battle between two parties competing for the right to manage the one-time heavyweight champion. The original contract between Baer and the plaintiffs provided that the plaintiffs "would use their best efforts to 'secure the faithful performance'" by Baer's preexisting managers. \textit{Id.} at 180. Ancil Hoffman, Baer's manager, who provided key testimony and other evidence for Baer in the \textit{Jacklich} case and prevailed over the plaintiffs in the contest to manage Baer's career, provided well for Baer's future despite the boxer's tendency to waste his earnings. \textit{See} Art Rosenbaum, \textit{Max Baer Was the Reluctant Boxing Champ}, S.F. CHRON., Feb. 17, 1988, at D4. Baer was known to say, "I got an annuity that's going to pay me $2,200 a month. I don't know what an annuity is, but I sure as hell know what $2,200 is." Timothy F. Comstock, \textit{Reminiscence: A Hard Hitter in the Ring, Max Baer Was A Real Softie Around Children}, SPORTS ILLUSTRATED, Oct. 15, 1984, at 116, 124. In addition to being a successful boxing manager, Ancil Hoffman was also a well-regarded Sacramento County supervisor for whom a city park is named. Bill Conlin, \textit{Ancil Hoffman: Gone for 12 Years But Not Forgotten}, SACRAMENTO BEE, Aug. 7, 1988, at C2.
\textsuperscript{186} 135 P.2d at 183-84.
\textsuperscript{187} \textit{See} discussion of equity and unconscionability \textit{supra} note 122 and accompanying text.
\textsuperscript{188} 377 P.2d 284 (Cal. 1962).
consumer in a position where the merchant took advantage of extenuating circumstances. In *Steven* the decedent-insured purchased an airplane life insurance policy from a vending machine shortly before he began a flight and, in accordance with the instructions, mailed the document to his wife, the designated beneficiary, before departing. A flight segment on his return trip was cancelled by the carrier because of unexpected events, and an agent for the planned carrier assisted the decedent in finding an air taxi that he boarded with fellow travelers in an attempt to reach a connecting flight home. The air taxi suffered a fatal crash. The insurance company denied coverage because the policy contained a label across the top of the document and other terms providing that it did not cover “Travel on Other Than Scheduled Air Carriers.” The trial court held in favor of the defendant insurance company, and the decedent’s wife appealed.

The majority of the California Supreme Court was persuaded that the limitation on coverage should not be enforced and that the plaintiff should recover on the policy for two reasons. First, the majority found that the policy was ambiguous as to which flights were covered and that the ambiguity should be resolved against the drafter of the policy. Second, the majority reasoned that the decedent, as a “layman,” could reasonably expect that the flight insurance would cover the entire trip, including the emergency substitute flight, unless such flights were clearly excluded by the standardized contract. In reaching its decision, the majority emphasized the circumstances of obtaining the policy: the contract was adhesive in that it was completely without the possibility for negotiation; the usual time and manner of purchase and the instructions to mail the policy to the beneficiary would effectively prevent the insured from reading the policy; even if the policy had been read by the decedent it would have been difficult for him to understand that the air taxi service was not included because it did not fit squarely into the defined categories of

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189. *Id.* at 286, 294.
190. *Id.* at 286-87.
191. *Id.* at 287.
192. *Id.* at 286-88.
193. *Id.* at 287-88.
194. *Id.* at 288, 297-98. The policy used unclear terms such as “scheduled” and “non-scheduled carriers” and even extended policy coverage to certain types of land transportation substituted for flights but never discussed emergency substitute flights. *Id.* at 289-90.
195. *Id.* at 288-89.
196. *Id.* at 297-98.
197. *Id.* at 294.
flights; and the agent for the scheduled air carrier facilitated the substitute air taxi flight.

In concluding its opinion in *Steven*, the majority quoted *Henning-sen v. Bloomfield Motors, Inc.* for the proposition that among the court's tasks is the obligation "to protect the ordinary man" from being taken advantage of through standardized adhesion contracts imposed by the stronger party regarding "services of a public or quasi-public nature." Further, as in the *Henning-sen* case, the circumstances indicated that the decedent was unlikely to find the objectionable provision or understand it if found. The reasoning used in the *Steven* opinion was also used in cases cited as precursors to the adoption of the unconscionability doctrine. The practices of the California courts even before adoption of Section 2-302, however, were not always well-disciplined, and anomalous decisions can be found, as in the cases discussed below.

Foreshadowing the capriciousness that could occur under the license of Section 2-302 was the decision in yet another insurance case focusing on the reasonable expectations of a consumer, *Smith v. Westland Life Insurance Co.* The consumer applied for a life insurance policy and submitted the first month's premium. The company gave the applicant a conditional receipt, known as a "binder," which under California law created a temporary insurance policy subject to termination upon an unfavorable review of the application by the company. The insurance company could avoid providing temporary coverage under the binder only by using clear and unequivocal...
language to the contrary and by calling that language to the attention of the applicant.\textsuperscript{206} The insurance company responded to the applicant within a month of the application, proposing that the requested policy be issued, but only after increasing the premium and omitting coverage for accidental death benefits based on the hazardous nature of the applicant's work as a railroad laborer.\textsuperscript{207} The applicant refused the modified policy.\textsuperscript{208} A second agent for the insurance company met with the applicant and presented the proposed amended policy for a second time, and the applicant refused again, so the agent informed the applicant that his premium payment would be refunded.\textsuperscript{209} The next day, the insured died in an automobile accident.\textsuperscript{210} The California Supreme Court held that the temporary policy continued to be effective until the insurance company gave unequivocal notice and a refund of any premium paid, based on the view that the applicant would reasonably expect coverage until formally notified of rejection and that it would be unconscionable to allow the insurance company to hold premiums without providing such coverage.\textsuperscript{211}

The case was decided by a 4-3 vote, and the dissent took issue with both the majority's opinion and the new ruling requiring an actual refund of the premium to trigger termination of the implied temporary policy.\textsuperscript{212} The dissent asserted simply, but cogently, that the unequivocal rejection of the application by the agent, along with a promise that the premium would be returned, refuted any reasonable expectation by the applicant that he was covered by the requested policy.\textsuperscript{213} The dissent also noted that earlier cases established that return of the premium was not a prerequisite to cancellation of express insurance coverage and that no public policy concerns required such return before termination of the implied temporary policy.\textsuperscript{214}

The dissent can be interpreted to disagree with the view that holding premiums after cancellation was unconscionable conduct by the insurance company. Even the majority indicated that, as long as clear and unequivocal notice is given, the insurance company could avoid providing temporary coverage despite receiving and holding

\textsuperscript{206} Id. at 441.  
\textsuperscript{207} Id. at 435-36.  
\textsuperscript{208} Id. at 436.  
\textsuperscript{209} Id.  
\textsuperscript{210} Id.  
\textsuperscript{211} Id. at 439-40.  
\textsuperscript{212} Id. at 444-46 (Clark, J., dissenting).  
\textsuperscript{213} Id. at 444 (Clark, J., dissenting).  
\textsuperscript{214} Id.
premium payments pending review of the application.\textsuperscript{215} Temporarily holding a premium while evaluating an application is a fair exchange for the cost of the evaluation and, in cases of rejection of the application, compensates for the expense in refunding the premium. The majority's decision certainly favored the "little person," a widowed insurance beneficiary. It is debatable, however, whether the contract shocked the conscience of the court by its terms, or whether the court was overly influenced by the manner in which events actually unfolded.\textsuperscript{216} A review of California decisions after 1979 reveals similar reasoning in which the explicit grant of authority to police for unconscionability perhaps encouraged the courts to exceed their authority and to disturb the parties' bargains based on the court's hindsight judgment.\textsuperscript{217}

### III. Application of the Unconscionability Doctrine in California After the Enactment of Section 2-302

Despite the state legislature's decision not to adopt the Section in 1962, the California courts have declared that Section 2-302 is comparable to the state's judicially-developed doctrine of unconscionability.\textsuperscript{218} One would expect unconscionability decisions in California since 1979 to be relatively consistent with decisions in other jurisdictions that had already enacted Section 2-302; and, in a number of ways, the California decisions do coincide with the general construction of Section 2-302.\textsuperscript{219} California courts require a showing of both procedural and substantive unconscionability at the time the contract

\textsuperscript{215} See id. at 439, 441-42.

\textsuperscript{216} Equity did allow courts to consider the results of contract performance, see supra notes 118-120 and accompanying text, but the denial of coverage in this case may well have been outside the realm of the "harsh" results that equity sought to avoid.

\textsuperscript{217} See infra notes 415-466 and accompanying text.

\textsuperscript{218} See Perdue v. Crocker Nat'l Bank, 702 P.2d 503, 511-12, 511 n.10 (Cal. 1985) (stating that adoption of § 2-302 codified established doctrine that courts may refuse enforcement of unconscionable contracts), appeal dismissed, 475 U.S. 1001 (1986). See also Graham v. Scissor-Tail, Inc., 623 P.2d 165, 173 n.19 (Cal. 1981) (stating that "[t]he judicially developed concept of unconscionability has recently become a part of our statutory law").

\textsuperscript{219} See Perdue, 702 P.2d at 511 n.9 (indicating approval of the widely used procedural and substantive unconscionability framework even though the court in Graham had used an alternative approach that asked first whether the contract was adhesive and second whether the terms were unconscionable or inconsistent with the reasonable expectations of the adhering party, stating that either analysis should lead to the same result).
was made and often reject claims when an element of the doctrine is missing, whether the claimant is a consumer or a merchant.

Nevertheless, the California cases have marked a distinctive path in a number of important ways. First, California courts have been unduly indulgent of merchant-like parties claiming unconscionability


221. *See, e.g.*, Coon v. Nicola, 21 Cal. Rptr. 2d 846, 852-54 (Ct. App. 1993) (holding that a medical arbitration agreement was not unconscionable when the patient signed under non-emergency conditions, terms were clearly laid out, there was a subsequent option to rescind, and the arbitral forum was fair); General Motors Corp. v. Superior Court, 15 Cal. Rptr. 2d 622, 628 (Ct. App. 1993) (holding that a comprehensive release agreement was not unconscionable when the signing widower was represented by counsel who cosigned release and the terms of the release were clear and not overly one-sided); Shadoan v. World Sav. & Loan Ass'n, 268 Cal. Rptr. 207, 211 (Ct. App. 1990) (holding that loan agreement containing both a prepayment penalty provision and a unilateral call provision was not unconscionable because consumers failed to establish that other lenders did not offer more favorable terms and because statutory law allowed prepayment penalty provisions); Dean Witter Reynolds v. Superior Court, 259 Cal. Rptr. 789, 797 (Ct. App. 1989) (holding that a termination fee in an investment account agreement was not unconscionable when plaintiff was a sophisticated investor and alternative financial institutions offered competing investment accounts without the termination fee).

222. *See, e.g.*, U.S. Roofing, Inc. v. Credit Alliance Corp., 279 Cal. Rptr. 533, 544-45 (Ct. App. 1991) (holding that a disclaimer of warranty by a finance lessor was not unconscionable when the merchant lessee had a choice of finance lessors, the disclaimer was conspicuous, and a remedy was available from the supplier/manufacturer); West v. Henderson, 278 Cal. Rptr. 570, 572-76 (Ct. App. 1991) (holding that a contractual six-month limitations provision on claims by a commercial lessee was not unconscionable when the lessee had the opportunity to read before signing, the lessee could have leased elsewhere, and the imbalance in the limitations provision could be justified by the lessor's need to avoid long pending claims on property); Markborough California, Inc. v. Superior Court, 277 Cal. Rptr. 919, 926-27 (Ct. App. 1991) (holding that a clause limiting liability of an engineering company to its consulting fee of $67,640 was not unconscionable even when breach caused more than $5 million in damage because the parties were dealing at arms length and the client had an opportunity to accept, reject, or modify the terms of the agreement); Appalachian Ins. Co. v. McDonnell Douglas Corp., 262 Cal. Rptr. 716, 728-31 (Ct. App. 1989) (holding that a mutual waiver of liability in a contract for use of a rocket to lift a communications satellite was not unconscionable when the satellite did not reach its desired orbit, thereby rendering it useless and causing $105 million damages on $6-7 million contract, because both parties were sophisticated businesses, the contract was not a preprinted form but rather a negotiated instrument, the mutual waiver was required by a government agency, the buyer could have purchased a rocket from an alternative supplier, and requiring the buyer to cover risks through insurance was not unreasonable); Central Bank v. Kaiperm Santa Clara Fed. Credit Union, 236 Cal. Rptr. 262, 273-74 (Ct. App. 1987) (holding that an indemnification clause in a money order agency contract was not unconscionable when the merchant plaintiff had alternative sources and the risk allocation was reasonable in light of the circumstances).
based on unequal bargaining power. Second, the courts have shown a tendency to examine contracts with the benefit of hindsight rather than assessing the contract from the parties' perspective at the time the contract was formed. Third, California courts have wavered on the possible offensive use of the doctrine to obtain an affirmative recovery. Fourth, the courts have taken an unrestrained approach to price-term unconscionability by examining cases on the elusive notion of "excessive profits," rather than the more reliable basis of comparison between contract and market prices, and by judging fairness on the cumulative effect of many different transactions rather than assessing individual contracts. The questionable decisions often involve more than one of these issues.

A. Merchants and Unconscionability in California

A particularly troubling aspect of the recent application of the unconscionability doctrine by California courts is their willingness to indulge claims made by merchants. Although merchants are certainly capable of entering into bargains that either initially or eventually appear to be one-sided, merchants generally have greater difficulty than consumers in showing procedural unconscionability based on surprise resulting from hidden or unintelligible terms because they are expected to possess more sophistication or business experience than nonmerchants. Merchants are also less likely to be able to show procedural unconscionability through oppression or the absence of meaningful choice because they possess greater bargaining power or access to alternative sources. Nevertheless, the most notorious California decisions on unconscionability involve merchants who succeeded in convincing the courts that their contracts involved not only substantive unconscionability, but also procedural unconscionability based on lack of meaningful choice. *Graham v. Scissor-Tail, Inc.*, *A&M Produce Co. v. FMC Corp.*, and the recently decided *Buchwald v. Paramount Pictures Corp.* compose a trilogy of alarming California decisions in which the courts misapplied Section 2-302.

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223. *See infra* notes 228-447.
224. *See infra* notes 448-494.
225. *See infra* notes 449-512.
226. *See infra* notes 513-557.
227. *See supra* notes 113-114 and accompanying text.
228. *See supra* note 116 and accompanying text.
230. 186 Cal. Rptr. 114 (Ct. App. 1982).
Graham v. Scissor-Tail, Inc. is the preeminent case applying the unconscionability doctrine in California after the adoption of Section 2-302 in 1979. The Section was adopted after the cause of action arose but before the Graham decision, and the California Supreme Court asserted that the new statute merely enacted the preexisting, judicially developed doctrine of unconscionability that had long been part of California common law. California courts, as well as courts in other states, have subsequently treated Graham as an authoritative construction of Section 2-302. Although the most significant weakness in the reasoning of the Graham decision is its discussion of procedural unconscionability, the court's finding of substantive unconscionability is also questionable.

The Graham case arose out of a series of concert promotion contracts between Bill Graham, a prominent contemporary music promoter, and Leon Russell, a rock musician and sole owner of Scissor-Tail, a corporation through which Russell marketed the serv-

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234. See Richard Harrington, Bill Graham, Lead Act at Last, Wash. Post, Oct. 7, 1992, at B7. Graham's biography is an interesting one. He was born in Germany and made it out of that country during World War II as an orphan. Graham came to New York at ten and grew up in a foster home before eventually obtaining a college degree in business administration. See Bill Graham & Robert Greenfield, Bill Graham Presents: My Life Inside Rock and Out 1-50 (1992) [hereinafter Bill Graham Presents]. Graham served in the Army during the Korean War and received both a court martial for insubordination and a Bronze Star citation for bravery under enemy fire. Id. at 50-61.

After an attempt at acting in New York, Graham moved to the San Francisco area and became involved with a politically active theater group. Id. at 118-19. Graham's first production was a legal defense fundraiser for the theater group in November of 1965. Id. at 121. The success of the fundraiser led Graham to produce musical events as a business. He quickly became a leader in that field. Id. at 122-32.

Graham died in a helicopter crash in October of 1991 and was reported to have left an estate of $50 million. See Philip Elwood, Unauthorized Graham Biography Absorbing, Flawed, S.F. Examiner, Feb. 27, 1994, at D7. Two biographies on Graham have been published: John Glatt, Rage & Roll: Bill Graham and the Selling of Rock (1994), and Bill Graham Presents, supra.
ices of his band. The contracts called for Graham to promote concerts in four cities beginning in July 1973. The contracts for the first two concerts were signed by both parties, but after a dispute arose, Scissor-Tail failed to execute the third and fourth contracts and obtained the services of an alternative promoter for those two concerts. The issue in the contract dispute was whether Scissor-Tail should bear a portion of the loss incurred from promotion of the first concert. The contracts were executed on standardized forms supplied by the American Federation of Musicians (A.F. of M.), the defendant's union, and expressly provided for the manner in which profits would be shared without stating how losses would be treated.

Graham initiated the legal proceedings with a breach of contract suit against Scissor-Tail in the fall of 1973. Scissor-Tail responded with an action to compel arbitration under the terms of the contracts, which expressly provided for arbitration by an executive board of the A.F. of M. The trial court ordered arbitration, and an initial arbitration decision was rendered in favor of Scissor-Tail without a hearing. A joint request for a hearing was made, and the matter was reopened. The arbitrators ruled for Scissor-Tail a second time and held that Graham would have to absorb the full amount of the loss. The trial court affirmed the arbitrator's award, finding again that the

236. Id.
237. Id. at 167-69.
239. Graham, 623 P.2d at 167-68. The contracts called for Russell to receive the greater of "applicable A.F. of M. scale" or 85% of the profits in three of the cities and 90% of the profits in the fourth location after the deduction of appropriate expenses. Id. at 169.
240. Id. at 169.
241. Id. Paragraph 9 of the contracts provided that all disputes would be decided by the local board if all the musicians were members of the same local board or by the international board if the musicians belonged to different locals. Id. at 168 & n.2.
242. Id. at 169.
243. Id.
244. Id. at 169-70. Other issues concerning a challenge to some expenses claimed by Graham and the availability of attorney's fees were decided in favor of Graham, apparently because the hearing officer had no directions on those matters. Id.
agreement to arbitrate was enforceable and there was no basis to overturn the award favoring Scissor-Tail.245

After Graham prevailed on appeal, the case was heard by the California Supreme Court. Graham argued that the form contract was an unenforceable contract of adhesion to the extent that it allowed the union to arbitrate a dispute arising between a union member and a nonmember.246 The court began its analysis by citing the definition of an adhesion contract often used in California: "The term signifies a standardized contract, which, imposed and drafted by the party of superior bargaining strength, relegates to the subscribing party only the opportunity to adhere to the contract or reject it."247

In analyzing the adhesion contract issue, the court noted that A.F. of M.'s constitution and bylaws did not permit members to sign any contract other than the union's standardized contract that included the clause designating the union as the arbitrator.248 The court also found that most musicians of any significance or prominence were union members; thus, the court concluded that Graham was forced to adhere to the form contracts if he wanted to promote the concerts of popular musicians.249 The court reached this conclusion even though some terms of the contract were actually negotiable.250

The court's determination that the contract was adhesive was only the first step in its analysis. It emphasized that even a contract of adhesion would generally be enforceable except in cases in which either the contract contained terms that fell outside of the reasonable expectations of the adhering party or some of the contract's provisions were unconscionable.251 The court quickly dismissed the possibility that the arbitration provision might have fallen outside of Graham's reasonable expectations because he admitted to previously signing

\footnotesize{245. Earlier, in findings of fact and conclusions of law filed with the order compelling arbitration, the trial court specifically found that Graham had not entered into the arbitration agreement under mistake and that no grounds existed to rescind or revoke the arbitration agreement. \textit{Id.} at 169 \\& n.5. The trial court incorporated and affirmed those findings and went on to conclude that (1) there had been no misconduct by Scissor-Tail in the process; (2) there had been no misconduct by the arbitrator in exceeding the limits of power, bias, prejudice, or partiality; and (3) any appearance of arbitrator impartiality was known by Graham at the time he executed the contracts. \textit{Id.} at 170 \\& n.8.}

\footnotesize{246. \textit{Id.} at 170-72.}


\footnotesize{248. \textit{Id.} at 172.}

\footnotesize{249. \textit{Id.}}

\footnotesize{250. \textit{See infra} notes 269-270 and accompanying text.}

\footnotesize{251. \textit{Graham}, 623 P.2d at 172-73.}
thousands of the form contracts, including at least fifteen with Scissor-Tail. Graham also had been a party to previous arbitration proceedings under the contracts and had even threatened Scissor-Tail that he would file a complaint with the A.F. of M. if the dispute in question was not resolved to his satisfaction.

The California Supreme Court then considered whether the contract should be held unconscionable. Although Graham had phrased his challenge in terms of a lack of due process, the California Supreme Court reshaped the argument as being an assertion that the arbitration form was "so inimical to fundamental notions of fairness" as to be unconscionable. The court began by acknowledging that provisions of the California Arbitration Act contemplated that parties should have "complete contractual autonomy" in choosing an arbitrator; the parties could even agree to a nonneutral arbitrator. This analysis of California law could have provided enough support for enforcement of the A.F. of M. clause, but the court did not stop the analysis there.

Going far beyond the state's statutory law and judicial precedent, the California Supreme Court cited a New York appellate court case, In re Cross & Brown Co., for the proposition that a person may not be a judge in his own case—the law presumes that such a party cannot have the "'impartiality necessary to act in a judicial or quasi-judicial capacity.'" As discussed below, use of the Cross & Brown opinion to disqualify the A.F. of M. board as arbitrator was disingenuous for a number of reasons. Nevertheless, the California Supreme Court reasoned that the interests of the union, although not a party to the dispute, were so closely allied with those of its members that the union was subject to the same presumption of non-objectivity. This reasoning was supported with language from United States Supreme Court decisions suggesting that arbitration proceedings should have

252. Id. at 173.
253. Id.
254. Id.
257. Id. at 174.
258. Id. at 174-75.
261. Id. at 177.
"minimum levels of integrity." The California Supreme Court effectively reformed the contract by remanding the case and instructing that the parties be given an opportunity to agree upon a neutral arbitrator and, if unsuccessful in doing so, that the trial court should appoint an arbitrator.

Given the legislative history of Section 2-302 and its common law precedents, the Graham case raises serious doubt about whether a sophisticated party, such as Bill Graham, and a contract term, such as the A.F. of M. arbitration clause, present the circumstances that the California Legislature intended for courts to police with Section 2-302. More specifically, however, the facts of the case simply do not support findings of procedural and substantive unconscionability.

First, Graham could not assert procedural unconscionability based on unfair surprise for the same reason the court found the term was not beyond his reasonable expectations: Graham admitted to being intimately familiar with the A.F. of M. contract, he had been party to a multitude of the same agreements, and he had previously been party to arbitrations thereunder. Graham could not assert that he had been victimized by a contract clause that was either hidden from him or unintelligible to him. Graham's early threat to file a complaint with the A.F. of M., if Scissor-Tail did not accept a proposed compromise, reflects his knowledge and understanding of the clause.

The California Supreme Court found the alternative form of procedural unconscionability: a lack of meaningful choice through gross inequality of bargaining power. A key to the finding was the court's determination that all artists and musicians of any prominence used the same contract. The court refused to entertain the possibility, although asserted by Scissor-Tail and amicus curiae parties, that the objectionable clause could have been subject to negotiation by Graham, in light of his great prominence and success. Graham, who undoubtedly had access to legal counsel, could have challenged the clause on his own or with the support of other promoters. While Gra-

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262. Id. at 176 (quoting Hines v. Anchor Motor Freight, 424 U.S. 554, 571 (1976)).
263. Id. at 180.
264. Id. at 173.
265. The court noted that Graham sent a telegram to Russell on August 7, 1973, shortly after the first two concerts on July 29 and August 5. Id. at 168 n.3. While the details are not spelled out in the opinion, a reasonable guess is that Graham proposed a compromise that would have allowed Graham to promote the last two concerts. In the absence of a compromise, Graham threatened to file charges with the A.F. of M. Id.
266. See id. at 172.
267. Id.
ham enjoyed the reputation of being assertive in his business dealings, it is possible that he did not challenge the provision because he did not object to the A.F. of M. process. The California Supreme Court overlooked the fact that Graham's threat to initiate arbitration against Scissor-Tail probably evidenced his confidence in, rather than his suspicion of, the A.F. of M. arbitration process.

Although the court acknowledged that the profit-sharing percentage and some other terms were obviously subject to negotiation, it also dismissed those items that were negotiable as being of "relatively minor significance." While Graham's ability to negotiate minor terms would not undercut an argument for lack of meaningful choice, the fact that a party was able to negotiate key pricing provisions should have weakened, if not precluded, such a claim. The court construed Scissor-Tail's determination to find a promoter amenable to its desired apportionment of the profits as an indication that the term was not negotiable, supporting its conclusion that the contract was one of adhesion. The court failed to recognize that at the same time, Graham also could have elected to refrain from promoting Scissor-Tail or other groups that would not agree to his terms on price or arbitration. It is reasonable to infer that Graham's services were valuable enough that someone would have paid his price.

A New York court observed in a similar case that the question of meaningful choice or oppression through unequal bargaining power in a transaction may be influenced by whether the contract is a business venture or a contract for life's basic necessities. The court noted

268. See Richard Harrington, Rock's Rough and Ready Promoter; Bill Graham, No-Nonsense Pro in a Psychedelic World, WASH. POST, Oct. 28, 1991, at D1:
[...]
Whether you were a star, a manager or a fan, you never had to guess where you stood with Graham—he'd let you know, right to your face.

See also Jane Scott, Origins of a Star-Maker; Book Chronicles Rock 'N' Roll Pioneer's Life, PLAIN DEALER, Nov. 6, 1992, at 28 (describing Graham as the "world's premier concert producer" and noting that he stood up to everyone "from Hell's Angels to tyrannical, abusive rock group managers").


270. Id. The mere fact that a group was highly desirable and therefore had an advantage in bargaining power does not mean that a contract was not the result of negotiation. Cf. Glopak Corp. v. United States, 851 F.2d 334, 338-39 (Fed. Cir. 1988) (finding that even though the United States government refused to yield and include a price adjustment clause, the agreement was nonetheless the product of negotiation, Glopak having simply failed to succeed in obtaining its desired contract provision).

that music promoters are always free to leave the business. In this regard, the *Graham* case stands in contrast to contracts for medical services, life insurance, and automobiles, which rise to a different level of practical necessity for consumers. California courts have recognized the difference between business ventures and basic necessities in analyzing contracts for unconscionability.

Even if the court was correct in finding procedural unconscionability in the formation of the contract, it still had to find substantive

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272. *Id.* See also *supra* notes 92-100 and accompanying text.

273. Professor Dawson has noted that German courts have been receptive to claims of "economic necessity" relating to bargains entered into by claimants in fear of serious economic loss, but not to claims of necessity by parties attempting to make a profit. Dawson, *supra* note 36, at 62-63. Dawson reported "that [t]he prospect of gain might often produce willingness to incur an immediate sacrifice, through a transaction in which the values exchanges were unequal . . . . free choice of the interested parties should not be interfered with in such cases, in spite of a disproportion of values . . . ." *Id.* See also John P. Dawson, *Unconscionable Coercion: The German Version*, 89 HAY. L. REV. 1041, 1057-59 (1976) (also citing German distinction between necessity based on need to preserve the life of a going business, such as a retail store, as compared with a discrete venture aimed to produce profit); United States v. Bedford Associs., 657 F.2d 1300, 1313 (2d Cir. 1981) (rejecting a claim of unconscionability by a lessor of real property to a federal agency in an arrangement that would have produced millions of dollars of revenues but risked substantial losses as well); Tennessee Imports, Inc. v. Filippi, 745 F. Supp. 1314, 1328 (M.D. Tenn. 1990) (rejecting a claim of unconscionability in an exclusive distributorship contract calling for arbitration in Italy because, although the term may have been nonnegotiable, the distributor was aware of clause and was willing to accept it in the hopes of reaping great profits and arbitration is favored by federal and international law). The *Filippi* court noted that if the distributor thought the term was too unfair it was free to walk away. *Id.*

274. See *Coon v. Nicola*, 21 Cal. Rptr. 2d 846, 852 (Ct. App. 1993) (indicating that even some medical treatment may not be deemed necessary, particularly in non-emergency circumstances); *West v. Henderson*, 278 Cal. Rptr. 570, 575 (Ct. App. 1991) (distinguishing commercial real property lease as a business venture and not in pursuit of life's necessities); Appalachian Ins. Co. v. McDonnell Douglas Corp., 262 Cal. Rptr. 716, 732-33 (Ct. App. 1989) (observing that practical necessity relates to matters "such as medical, legal, housing, transportation or similar services" in rejecting claim that contract for launching of satellite involved essential services); *Yeng Sue Chow v. Levi Strauss & Co.*, 122 Cal. Rptr. 816, 821-22 (Ct. App. 1975) (rejecting claim of a former employee's widow that an employer repurchase clause in a stock option plan was adhesive or unconscionable because the employee's participation in the plan was entirely voluntary). See also *Phoenix Leasing, Inc. v. Sure Broadcasting, Inc.*, 843 F. Supp. 1379, 1385 (D. Nev. 1994) (applying California law and noting that taking out a loan to start up a business venture does not involve a necessity of life that would compel borrower to accept loan); *Bonfield v. AAMCO Transmissions, Inc.*, 717 F. Supp. 589, 596 (E.D. Ill. 1989) (rejecting claim that nonnegotiability of franchise agreement constituted breach of duty of good faith and noting that the franchisee was free to reject the agreement because it did not involve necessities); *Collins v. Click Camera & Video, Inc.*, 621 N.E.2d 1294, 1300 (Ohio Ct. App. 1993) (noting that contract for film processing did not relate to the necessaries of life and therefore customer could have foregone contract if no seller was willing to negotiate limitation of liability).
The Graham court considered the close alignment of interests between the musicians and their union to find that the arbitration provision was substantively unconscionable. The court reasoned that because the union’s mission is to seek favorable wages and improve working conditions for its members, the union’s executive board would presumptively be prevented from acting in a fair and impartial manner in disputes involving its members.

The California Supreme Court cited the Cross & Brown decision for support even though the employment contract in Cross & Brown was distinguishable.

The case involved an employment contract that called for disputes between employer and employee to be arbitrated by the employer’s board of directors. Based on those facts, the New York court characterized the corporate employer and its board of directors as one entity, stating, “We brush aside any metaphysical subtleties about corporate personality and view the agreement as one in which one of the parties is [also] named as arbitrator.” Nevertheless, the New York court cautioned against interpreting its holding too broadly, stating, “By our decision herein we do not intend to limit the power of contracting parties to designate arbitrators who, with the knowledge of the parties, may have an interest in the dispute or who sustain some relationship to a party which would otherwise disqualify the arbitrator from serving.”

The A.F. of M. arbitration clause is readily distinguished from the arbitration clause in Cross & Brown; the musicians and their union do not share the same relationship as the corporation and its board of directors. In Jerry Kravat Entertainment Services, Inc. v. Cobbs, a later New York state court decision involving the same A.F. of M. arbitration clause at issue in Graham, the New York court expressly declined to follow Graham and differentiated the union arbitrators.

275. The California courts have required a finding of both elements of unconscionability, but have suggested application of a sliding scale that requires less substantive unconscionability with greater procedural abuse, and vice versa. Ellis v. McKinnon Broadcasting Co., 23 Cal. Rptr. 2d 80, 83 (Ct. App. 1993) (both procedural and substantive unconscionability required in a sliding scale relationship); Dean Witter Reynolds v. Superior Court, 259 Cal. Rptr. 789, 795 (Ct. App. 1989) (stating that “[a] relatively larger degree of one will compensate for a relatively smaller degree of the other”). This approach is consistent with other jurisdictions. See supra notes 64-66 and accompanying text.


278. Id. at 575-76.

279. Id. at 576.

from the corporate board of directors. In contrast to the rather narrow characterization of the union by the California Supreme Court, the Jerry Kravat decision emphasized that the union does not necessarily share an identity with its members. The union may be at odds with some members on occasion, may not always command the following of its members, or may need to take corrective action against members for the general benefit of the organization.

The Jerry Kravat opinion noted that while the arbitration arrangement might not present complete impartiality, it would nonetheless achieve the goal of speedy resolution by consensual arrangement of the parties. The court also emphasized a number of other points: the parties were sophisticated merchants, not innocent consumers

281. The court stated in part:
Under New York law, an arbitration agreement will rarely be invalidated for partiality because of the relation between the parties and the arbitrators, as long as the relationship is disclosed prior to the making of the agreement, as here . . . . Matter of Cross is distinguishable from the present case. There the employer was a party to the agreement and its board served as arbitrator. Here, however, the Union, whose board is to serve as arbitrator is not a contracting party. Rather, it is the individual musicians who are parties to the agreement.

Id. at 995.

282. While the union may generally gain notoriety from its efforts to obtain better working circumstances for its members, the A.F. of M. serves a broader spectrum of members than other unions might. The A.F. of M. represents orchestras, for example, in collective bargaining as well as a large number of independent contractors, such as Russell and Scissor-Tail whose itinerant schedule prevents such collective action. See House Panel Holds Hearings on Labor Law for Entertainers, BNA WASH. INSIDER, Nov. 15, 1993 (noting that since 1970 live performance entertainers have been deemed independent contractors and therefore not subject to collective bargaining rights under federal law). The bargaining power of the musicians in Graham stands in contrast to the reports of treatment of less famous live performers who are not infrequently subject to having club owners or promoters withhold or reduce pay or otherwise subject them to resolving disputes with the "club bouncer." Id. A.F. of M. clearly has sanctioned members who have crossed picket lines to work. See Conway Twitty . . . , UPI, Oct. 4, 1989, available in LEXIS, Nexis Library, UPI File (indicating sanctions were likely to be leveled against a number of stars and musicians who defied strike of union local to perform); Travis Faces Expulsion from Union, UPI, Sept. 7, 1989, available in LEXIS, Nexis Library, UPI File (reporting that well-known performers Randy Travis, Englebert Humperdink, and David Copperfield had crossed local union picket line). The potential for disputes between the A.F. of M. national board and individual members or union locals was reflected in a mid-1980s battle over control of the national leadership, see Harry Bernstein, Sour Notes Heard in the Musicians Union, L.A. TIMES, July 21, 1987, (Business), at 1, and the decision of the Seattle Symphony to break away from the A.F. of M. and adopt a new bargaining agent, see Judith Michaelson, Music Union Challenged in Seattle, L.A. TIMES, Sept. 13, 1988, (Calendar), at 6. The A.F. of M. has faced severe financial difficulties in more recent years and has lost about one-half of its membership since 1979. See Melinda Newman, AFM Institutes Financial Overhaul, BILLBOARD, June 29, 1991, at 10.

seeking fundamental necessities; the relationship of the union and the members was disclosed prior to the making of the contract; the promoter was free to leave the business and seek other opportunities or join with other promoters to seek a change in the union contract; and the continued work of the promoters was evidence that the arbitration clause was not so unfair as to make the business unprofitable for them. Based on these findings, the Jerry Kravat court deemed it inappropriate to disturb the balance of bargaining power between the parties.

In light of the relative weakness of the claim for procedural unconscionability in Graham, the court should have demanded a strong indication of substantive unconscionability, especially from a merchant. Instead, the California Supreme Court found unfairness in the mere prospect of partiality on the part of the arbitrator and disregarded specific findings that the A.F. of M. procedures would allow the nonunion member to receive a fair hearing. Moreover, the court did not find any flaw in the arbitration that took place and acknowledged that a proceeding that denied a party a fair hearing could have been challenged in the courts. The court’s willingness to

284. Id. at 995-96.
285. Graham v. Scissor-Tail, Inc., 623 P.2d 165, 177 (Cal. 1981). The court stated: Although our review of the record has disclosed nothing which would indicate that A.F. of M. procedures operate to deny any party a fair opportunity to present his position prior to decision [citing A.F. of M. constitution and bylaws], we are of the view that the “minimum levels of integrity” ... are not achieved by an arrangement which designates the union of one of the parties as the arbitrator.

For extensive criticism of this reasoning, see Gregory R. Kim, Comment, Graham v. Scissor-Tail, Inc.: Unconscionability of Presumptively Biased Arbitration Clauses Within Adhesion Contracts, 70 Cal. L. Rev. 1014 (1982).

286. Graham, 623 P.2d at 177. The observation that the supreme court never identified a denial of Graham’s rights is consistent with the trial court finding that there was no impropriety in the proceedings. See supra note 243 and accompanying text. Although the contract was not specific about which party would absorb the loss on the concert, it did assure a minimum wage to the musicians, suggesting that the promoter might well be deemed to have accepted the risk of a possible loss. Graham details in his autobiography an occasion when he absorbed a loss in excess of $130,000 because of the cancellation of a Led Zeppelin concert after a member of the band broke his leg. In his own words, Graham stated, “I couldn’t sue them. Because the deal was that when they played they would receive their money. In legalese, they were saying, ‘Why charge us? We didn’t do anything wrong.’ That is the risk that the promoter always takes. Which people may not be aware of.” Bill Graham Presents, supra note 234, at 373-74.

287. The court stated: “If, in the course of arbitration proceedings, the resisting party is actually denied a fair opportunity to present his position, ample means for relief are available through a subsequent petition to vacate the award.” Graham, 623 P.2d at 177 n.23. This factor has been significant for other courts. See Tate v. Saratoga Sav. & Loan Ass’n, 265 Cal. Rptr 440, 444 (Ct. App. 1989) (observing that the Graham court “made
find fault with the arbitration arrangement in *Graham* stands in marked contrast to other cases involving claims in California and other jurisdictions that arbitration arrangements were unconscionable. 288

Relying on these questionable bases, the California Supreme Court rendered its first and still most prominent unconscionability decision following the adoption of Section 2-302. The *Graham* decision set precedent for future, equally problematic unconscionability decisions in California, including *A&M Produce Co. v. FMC Corp.* 289 and *Buchwald v. Paramount Pictures.* 290

little effort to tie its holding to the statutory grounds for challenging an arbitration award*”).

288. See, e.g., Madden v. Kaiser Found. Hosps., 552 P.2d 1178, 1188 (Cal. 1976) (underscoring that “arbitration has become a proper and usual means of resolving civil disputes” and encouraging courts to move away from the “era of hostility toward arbitration” in upholding a contract calling for arbitration of state employee malpractice claims against hospital); Coon v. Nicola, 21 Cal. Rptr. 2d 846, 852-54 (Ct. App. 1993) (medical arbitration agreement was not unconscionable when patient signed under non-emergency conditions, terms were clearly laid out, there was subsequent option to rescind, and arbitral forum was fair); Phoenix Leasing, Inc. v. Sure Broadcasting, Inc. 843 F. Supp. 1379, 1387 (D. Nev. 1994) (applying California law and rejecting argument that provision for waiver of jury trial in loan agreement between two commercial parties was unconscionable because of lender’s strong preference for trial by the court rather than by a jury, when term was clear and conspicuous, and borrower was sophisticated business entity represented by counsel); Meyers v. Univest Home Loan, 1993 U.S. Dist. LEXIS 11333, at *13 (N.D. Cal. Aug. 4, 1993) (refusing to find arbitration agreement unconscionable under federal law even though the lender had option to avoid arbitration and the borrower did not); Broemmer v. Otto, 821 P.2d 204, 209-10 (Ariz. App. 1991) (rejecting patient’s argument that arbitration agreement with abortion clinic requiring that any arbitrators be medical doctors licensed in obstetrics/gynecology was unconscionable because of automatic bias), vacated in part, 840 P.2d 1 (Ariz. 1992); Delaney v. Continental Airlines, 1993 U.S. Dist. LEXIS 9868, at *6 (C.D. Cal. June 22, 1993) (rejecting employee’s argument that arbitration before panel of employee’s divisional supervisor, human resources senior vice president, and corporate officer chosen by employee was unconscionable because of inherent bias in favor of employer); Westinghouse v. New York City Transit Auth., 623 N.E.2d 531, 534-35 (N.Y. 1993) (refusing to find an alternative dispute resolution agreement unconscionable even though it allowed a personally involved employee of one of the contracting parties to render final binding decision when contract allowed for judicial review of whether decision was arbitrary, capricious, or grossly erroneous). Cf. Patterson v. ITT Consumer Fin. Corp., 18 Cal. Rptr. 2d 563, 566 (Ct. App. 1993) (finding unconscionability when the operation of the arbitration clause in a consumer loan agreement executed in California was likely to result in adjudication in Minnesota without opportunity for a hearing).

289. See infra notes 291-350.

290. See infra notes 351-414.
UNCONSCIONABILITY IN CALIFORNIA

(2) A&M Produce Co. v. FMC Corp.

A&M Produce Co. v. FMC Corp.\(^\text{291}\) followed shortly after Graham and is subject to much of the same criticisms, even though the merchant claiming unconscionability did not have the notoriety of Bill Graham. A&M Produce also differs from Graham in that the court based its decision in part on the surprise form of unconscionability, albeit on a doubtful basis. The cases are similar in that both courts found a lack of meaningful choice and substantive unconscionability based on questionable considerations. Together, A&M Produce and Graham established a foundation for the application of Section 2-302 that has fostered a lack of proper restraint and consistency in the California courts.

A&M Produce was a farming corporation owned by C. Alex Abatti, a sole proprietor who had been farming all of his life.\(^\text{292}\) A&M Produce sued the defendant farming equipment corporation for breach of express and implied warranties.\(^\text{293}\) The trial court found a disclaimer of warranties clause and an exclusion of consequential damages clause to be unconscionable and ruled in favor of the plaintiff.\(^\text{294}\) While the disclaimer of warranties presented some interesting issues,\(^\text{295}\) the key provision for the purposes of this discussion was the exclusion of consequential damages.\(^\text{296}\)

\(^{291}\) 186 Cal. Rptr. 114 (Ct. App. 1982).

\(^{292}\) Id. at 117.

\(^{293}\) Id. at 118.

\(^{294}\) Id.

\(^{295}\) FMC made the often heard argument that the disclaimer of warranties met the technical requirements of U.C.C. § 2-316 and therefore could not be subject to a test of unconscionability under § 2-302. The court properly rejected that argument. Id. at 120. See Michael J. Phillips, Unconscionability and Article 2 Implied Warranty Disclaimers, 62 CHI-KENT L. REV. 199, 222-24 (1985) (indicating that both statutory construction and case law support application of § 2-302 to § 2-316 disclaimers). Moreover, the court noted that the attempt by FMC to exclude any express warranties was ineffective under § 2-316(1). A&M Produce, 186 Cal. Rptr. at 121 n.10. Thus, even if one were to find that the implied warranties were effectively disclaimed, an express warranty describing the capacity of the goods would still exist. Consequently, the key question became the validity of the term excluding consequential damages.

\(^{296}\) This case thus implicated § 2-719(3), which applies unconscionability specifically to attempts to limit consequential damages. U.C.C. § 2-719(3) (1990). Consequential damages may be limited or excluded unless the limitation or exclusion is unconscionable. Limitation of consequential damages for injury to the person in the case of consumer goods is prima facie unconscionable, but the limitation of damages when the loss is commercial is not. The plaintiff apparently did not raise "failure of essential purpose" under U.C.C. § 2-719(2) as an alternative challenge to the limitation on remedies under the contract.
The dispute in *A&M Produce* arose from the purchase of a weight-sizer, a piece of farming equipment used in harvesting tomatoes. When the weight-sizer malfunctioned, most of the tomato crop was lost. *A&M Produce* then sued for breach of warranty, seeking to regain the portion of the price paid for the equipment and the value of the lost crops as consequential damages. FMC cross-complained, seeking the balance due on the purchase price of the weight-sizer. In the course of the trial, the court ruled that it would be unconscionable to enforce the limited remedy provision of the agreement and further that the provision as not set out in a conspicuous fashion. The appellate court's review focused on the issue of unconscionability.

The *A&M Produce* court followed *Graham* in concluding that the unconscionability doctrine existed in California prior to the adoption of Section 2-302 and then proceeded to construe the doctrine as requiring procedural and substantive elements. The court also found procedural unconscionability based on surprise, determining that the exclusion clause was not particularly conspicuous because it appeared "in the middle of the back page of a long preprinted form contract" and was never brought to *A&M Produce*'s attention by FMC. Likewise, the court found procedural unconscionability through a lack of meaningful choice because of unequal bargaining power, citing FMC's position as a large business conglomerate versus *A&M Produce*'s position as a relatively small farming corporation with no previous experience in tomato harvesting. In addition, the court held the

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297. *A&M Produce*, 186 Cal. Rptr. at 117.
298. *Id.* at 118.
299. *Id.* at 117-18.
300. *Id.* at 118.
301. *Id.* The cited opinion is from the third trial in the case. A first trial resulted in a hung jury, and a new trial was ordered after the second trial on grounds not specified in the court's opinion. *Id.*
302. In addition to the general application of § 2-302, § 2-719(3) specifically indicates that consequential damages may be excluded in the absence of unconscionability. U.C.C. § 2-719(3) (1990).
303. *A&M Produce*, 186 Cal. Rptr. at 121-22. The court thus varied from the *Graham* approach, which prefaced its unconscionability analysis with a determination that the contract was one of adhesion, but reasoned that the *Graham* approach in fact embodied the search for both procedural and substantive unconscionability. *Id.* at 122-23. In Perdue v. Crocker Nat'l Bank, 702 P.2d 503, 511 n.9 (Cal. 1985), *appeal dismissed*, 475 U.S. 1001 (1986), the California Supreme Court described the analysis in *A&M Produce* as an "alternative analytical framework" to that offered by the supreme court in *Graham* that should lead to the same result.
305. *Id.* at 125.
exclusion of consequential damages substantively unconscionable. The lost crops were easily foreseeable in this context as an element of consequential damages if not for the limited remedy that placed the risk of loss on A&M Produce. Thus, the court found the exclusion of consequential damages to be unconscionable.

The *A&M Produce* findings of procedural unconscionability through surprise and unequal bargaining power are unpersuasive, inconsistent with other decisions involving the failure of a party to read a signed contract, and at odds with the apparent legislative intent behind California’s adoption of Section 2-302. The form contract in *A&M Produce* was a simple one-page, two-sided form. On the front side was a bold, fully-capitalized reference to the terms and conditions on the back of the agreement; the front side reference was located immediately below the typed-in names of the buyer and seller and immediately above the typed-in quantity, description, and price for the goods being sold. It would have been difficult for A&M Produce to review the typed-in terms, such as the price, without seeing the reference to the terms on the reverse side. While the reverse side does contain sixteen somewhat lengthy provisions, the disclaimer stands out conspicuously in fully-capitalized print that is substantially larger than the other terms. The limitation on remedy immediately follows the disclaimer and is also capitalized and in print size that is somewhat larger than all provisions except for the disclaimer. The juxtaposition of the two capitalized, larger-print provisions makes them conspicuous from the other terms. Once identified, the limitation on remedy is explicit.

In addition to the conspicuous nature of the terms, A&M Produce had a significant amount of time in which to review the form agreement before finalizing it. Indeed, the appellate court specifically

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306. *Id.* at 126.
307. The form is reproduced in its entirety as an appendix to the published opinion. *Id.* at 130-31. It is difficult to tell the exact original size of the paper and type, but the typed-in terms indicate the paper was at least 8.5" x 11" and probably closer to 8.5" x 14", suggesting that the print would have been larger than it appears in the reporters.
308. The form read in part: “SELLER hereby agrees to sell to BUYER, UPON AND SUBJECT TO THE TERMS AND CONDITIONS ON THE FACE AND BACK HEREOF, the equipment described below.” *Id.* at 130.
309. *Id.* at 131.
310. *Id.*
311. *Id.* The term reads, in part, “SELLER IN NO EVENT SHALL BE LIABLE FOR CONSEQUENTIAL DAMAGES ARISING OUT OF OR IN CONNECTION WITH THIS AGREEMENT . . . CONSEQUENTIAL DAMAGES FOR PURPOSES HEREOF SHALL INCLUDE, WITHOUT LIMITATION, LOSS OF USE, INCOME OR PROFIT.”

recognized that A&M had the opportunity to read the back of the contract or seek the advice of an attorney.\textsuperscript{312} Even though these were two commercial entities dealing at arms length, the court was persuaded that the obligation was on the seller to take steps to bring the damages limitation clause to the attention of A&M.\textsuperscript{313} Although the overall sentiment of the opinion suggests that A&M was a quasi-consumer, in fact, the court noted that Abatti had been farming all of his life and that A&M "was conceded [to be] a large-scale farming enterprise by Imperial Valley standards, employing five persons on a regular basis and up to fifty seasonal employees at harvest time, and . . . farming some 8,000 acres."\textsuperscript{314} While courts in other jurisdictions have resisted such temptation, the A&M Produce court treated A&M as a nonmerchant just because it was a small operation relative to FMC.\textsuperscript{315} The case is inconsistent with decisions in California and other states that hold parties, even actual consumers, more responsible for reading contracts in non-emergency circumstances.\textsuperscript{316} The situation is also less

\textsuperscript{312} Id. at 124.


\textsuperscript{314} A&M Produce, 186 Cal. Rptr. at 125.

\textsuperscript{315} FMC was cited as grossing $40 million in 1974 in its agriculture machinery division alone. \textit{Id.} Cf. Melso v. Texaco, Inc., 532 F. Supp. 1280, 1296-97 (E.D. Pa. 1982) (noting that the sophistication of an oil company does not disprove the sophistication of dealers, many having been in business for more than 20 years), \textit{aff'd}, 696 F.2d 983 (3d Cir. 1982); Monsanto Agric. Prods. Co. v. Edenfield, 426 So. 2d 574, 577 (Fla. Dist. Ct. App. 1982) (holding that the exclusion of consequential damages in a sale of herbicide from a large manufacturer to an "experienced and knowledgeable farmer" did not involve unconscionability); Cayuga Harvester, Inc. v. Allis-Chalmers Corp., 465 N.Y.S.2d 606, 617-18 (App. Div. 1983) (refusing to find unconscionable a consequential damages limitation in a contract for purchase of a harvester by a large, experienced corn farming operation because the transaction was commercial, the buyer had undoubtedly purchased farm machinery containing similar limitations, alternative sellers were available, and the allocation of risks was not substantively unreasonable); K&C, Inc. v. Westinghouse Elec. Corp., 263 A.2d 390, 393 (Pa. 1970) (although manufacturer of dry cleaning machines was much larger, the purchaser corporation headed by attorney and experienced merchant "was hardly the sheep keeping company with wolves").

\textsuperscript{316} See, e.g., Bolanos v. Shalatian, 283 Cal. Rptr. 209, 211 (Ct. App. 1991) (holding that patient with fifth-grade education would still be bound by medical arbitration agreement she signed without reading); West v. Henderson, 278 Cal. Rptr. 570, 575 (Ct. App. 1991) (rejecting claim of unfair surprise based on fact the lessee did not read lease consisting of 20 single-spaced pages, stating that "[p]arties to commercial contracts fail to read them at their own peril"); Markborough California, Inc. v. Superior Court, 277 Cal. Rptr. 919, 927 (Ct. App. 1991) (holding that failure of developer to read clause limiting liability in standardized agreement would not serve as basis for excuse from terms); Meyers v. Univest Home Loan, 1993 U.S. Dist. LEXIS 11333, at *10 (N.D. Cal. Aug. 4, 1993) (rejecting argument that party dealing at arms length had a duty to explain terms to consumers who had opportunity to read the contracts and noting that while failure to read
compelling than cases where the contracts involved multi-paged documents and terms that were difficult to decipher.\textsuperscript{317}

In addition to the dubious finding of "surprise" in the case, the alternative basis for finding procedural unconscionability is also questionable. The court's finding of a lack of meaningful choice was based on the perceived bargaining advantage of FMC and the nonnegotiability of the warranty terms even though the appellate court recognized that A&M had received an initial bid from another seller.\textsuperscript{318} Because A&M deemed the price presented by the first seller to be too high, it sought a bid from FMC.\textsuperscript{319} The appellate court was most likely correct in concluding that FMC's form contract could not have been negotiated to eliminate the exclusion of consequential damages, but the presence of alternative sources for the equipment suggests that A&M did have some meaningful choice. Unlike at least a few other cases involving an apparent monopoly or oligopoly of the goods contracts may be a common practice, there is nothing unfair about expecting parties to read contracts before signing them); Jones v. Asgrow Seed Co., 749 F. Supp. 836, 838 (N.D. Ohio 1990) (finding that seller of seed had no affirmative duty to point out clause limiting remedies for breach to experienced farmer who purchased tomato seed with latent defect); United Van Lines v. Hertz Penske Truck Leasing, Inc., 710 F. Supp. 283, 288 (W.D. Wash. 1989) (rejecting claim of unconscionability by renter of truck who admitted to not reading the clearly worded reverse-side terms despite a front-side reference to the reverse-side terms); Home Fed. Sav. & Loan Ass'n v. Campney, 357 N.W.2d 613, 619 (Iowa 1984) (refusing to impose upon lender a "quasi-fiduciary duty" to give customer notice of every provision in mortgage that might prove disadvantageous even though contract was adhesive in nature when parties had opportunity to read contract and consult lawyer before closing). But see Johnson v. Mobil Oil Corp., 415 F. Supp. 264, 268-69 (E.D. Mich. 1976) (reasoning that "before a contracting party with the immense bargaining power of the Mobil Oil Corporation may limit its liability vis-a-vis an unadvised, [practically illiterate] layman . . . it has an affirmative duty to obtain the voluntary, knowing assent of the other party").

317. In John Deere Leasing Co. v. Blubaugh, 636 F. Supp. 1569, 1571 (D. Kan. 1986), the court found that the liquidated damages clause and other terms on the back side of a lease were in very light-colored fine print that allowed darker front-side print to show through and rendered the back side nearly illegible. The print was so light that it could not be photocopied, and the original was readable by the court only with the aid of a magnifying glass. Id. The court also found the terms, once read, to be so complex as to suggest that the meaning was intended to be obscure. Id. See also Frank's Maintenance & Eng'g, Inc. v. C.A. Roberts Co., 408 N.E.2d 403, 411 (Ill. App. Ct. 1980) (finding that the sole front-side reference to the back-side terms was stamped over so as to render it illegible and that the instructions otherwise addressed only the need to review the order terms on front side).

318. A&M Produce, 186 Cal. Rptr. at 117. The court disregarded FMC's contention that the contract could be negotiated in special circumstances because A&M Produce was not informed of the option. Id. at 125.

319. The first bidder was Decco Equipment Company, which estimated a price of $60,000 to $68,000 for a weight-sizer and cooler. Id. FMC's ultimate price was about half that amount, but without the cooler. Id. at 117.
or services, A&M Produce involved a plaintiff that could have solicited other bids until it found a transaction that it deemed satisfactory.

One of the best and most thorough discussions of the effect of alternative sources in a California case is found in Dean Witter Reynolds, Inc. v. Superior Court. In Dean Witter the plaintiff was a self-described sophisticated investor and lawyer who challenged the fee charged by the defendant upon termination of an investment account. The evidence established that other financial institutions competed with the defendant and offered investment accounts without the termination fee. After surveying unconscionability decisions from within and outside the state, the court concluded that a showing of alternative sources would not necessarily defeat a claim of unconscionability. A claim of lack of meaningful choice, however, would be defeated by a showing of reasonably available alternative sources with contracts free of the terms claimed to be unconscionable. Given that the burden of proof is on the party claiming uncon-

320. Truta v. Avis Rent A Car Sys., Inc., 238 Cal. Rptr. 806, 809 (Ct. App. 1987) (claim of unconscionability in a collision damage waiver provision survived a summary judgment motion when it was alleged that no alternative existed to purchasing the waiver from the car rental company); Henningsen v. Bloomfield Motors, 161 A.2d 69, 95 (N.J. 1960) (finding no meaningful choice when all car manufacturers used same warranty provisions); Art's Flower Shop v. Chesapeake & Potomac Tel. Co., 413 S.E.2d 670, 675 (W. Va. 1991) (finding that telephone company had monopoly on yellow pages advertising services).

321. Cf. U.S. Roofing, Inc. v. Credit Alliance Corp., 279 Cal. Rptr. 533 (Ct. App. 1991) (stating that because finance lessee had discussed leasing arrangement with at least one other finance lessor and was aware of the warranty disclaimer in contract, no procedural unconscionability was present); Appalachian Ins. Co. v. McDonnell Douglas Corp., 262 Cal. Rptr. 716, 728-31 (Ct. App. 1989) (holding that the presence of one competing supplier to launch satellite into orbit and the decision of customer to select lower price contract indicated meaningful choice; A&M Produce distinguished on ground that it involved mass produced item sold by standardized agreement to relatively small party); Premier Wine & Spirits v. E. & J. Gallo Winery, 644 F. Supp. 1431, 1440 (E.D. Cal. 1986) (applying California law and observing that apparently nonnegotiable, mutual 30-day termination clause was not procedurally unconscionable when distributor had alternative product line choices available and was aware of clause).

323. Id. at 791.
324. Id. at 797.
325. Id.
326. Id. See also Spinello v. Amblin Entertainment, 1994 WL 590304, at *3 (Cal. Ct. App. Sept. 29, 1994) (ability of screenwriter to submit script to 70 other producers and to request changes in submission agreement precluded contract from being unconscionable); Central Bank v. Kaipermt Santa Clara Fed. Credit Union, 236 Cal. Rptr. 262, 274 (Ct. App. 1987) (holding that because the money order agency business was highly competitive and the agent had alternative sources, meaningful choice existed even though the bank would not negotiate its indemnification clause); Denlinger, Inc. v. Dendler, 608 A.2d 1061, 1068
scionability,\textsuperscript{327} the plaintiff in \textit{A\&M Produce} should have been required to show more to establish lack of meaningful choice. The \textit{A\&M Produce} opinion focused entirely on the disparity in size of the parties and the nonnegotiability of terms and never inquired into the possibility of alternative sources. Furthermore, the facts give no indication that the buyer was precluded from shopping for better terms because of a monopoly, oligopoly, or particular circumstances such as limited economic choices,\textsuperscript{328} emergency circumstances,\textsuperscript{329} or overtly misleading conduct.\textsuperscript{330}

(Pa. Super. Ct. 1992) (finding no lack of meaningful choice when goods financed were not rare or much sought after and buyer alleging unconscionability failed to allege that all area lumber yards offered substantially similar terms).

\textsuperscript{327} See, e.g., Westlye v. Look Sports, Inc., 22 Cal. Rptr. 2d 781, 793-94 (Ct. App. 1993) (holding that the burden of proof is on the party asserting unconscionability to prove the elements); Citizens Ins. Co. of Am. v. Proctor & Schwartz, Inc., 802 F. Supp. 133, 144-45 (W.D. Mich. 1992) (holding that burden was on party asserting unconscionability to show absence of alternatives including whether foregoing the transaction was a realistic option).

\textsuperscript{328} In Patterson v. ITT Consumer Fin. Corp., 18 Cal. Rptr. 2d 563, 565-66 (Ct. App. 1993), the court found that the plaintiff borrowers were people of “modest” economic means, some self-employed and others jobless, who responded to advertisements of “guaranteed loans” reasonably believing they would not qualify for conventional loans. The court therefore held that the loan agreements calling for arbitration of disputes to be held in Minnesota were presumptively unconscionable. \textit{Id.} at 567. In Northwest Acceptance Corp. v. Almont Gravel, Inc., 412 N.W.2d 719, 720-21 (Mich. Ct. App. 1987), the lessee was in danger of having paving equipment repossessed after falling behind in payments because of the expense of making repairs on the same equipment that had been delivered in defective condition. The court held a revised lease unconscionable because it was presented under circumstances in which the party could either sign immediately or have the equipment taken away. \textit{Id.}

\textsuperscript{329} In Wheeler v. St. Joseph Hosp., 133 Cal. Rptr. 775, 778-79 (Ct. App. 1976), the patient was presented with a form entitled “Conditions of Admission,” while being admitted to the hospital designated by his doctor. The court noted that in such cases, the patient normally goes to the hospital selected by his doctor without a feeling that he has a choice of institutions. \textit{Id.} at 786. The court also found that hospital admission is likely to be an anxious, stressful, and frequently traumatic experience. \textit{Id. See also} Germantown Mfg. Co. v. Rawlinson, 491 A.2d 138, 140 (Pa. Super. Ct. 1985) (holding that a confession of judgment against embezzler husband was unconscionable when the employer from whom he had embezzled had wife sign the judgment without consulting an attorney, while she was recovering from a miscarriage, and believing her signature was necessary to keep her husband out of jail). \textit{Compare} Madden v. Kaiser Found. Hosps., 552 P.2d 1178, 1185-86 (Cal. 1976), in which the court distinguished other medical arbitration cases in that the plaintiff could have elected in advance of the particular treatment to participate in alternative medical plans that did not include the challenged arbitration provisions. Similarly, the court in Coon v. Nicola, 21 Cal. Rptr. 2d 846, 853-54 (Ct. App. 1993), found no unconscionability when the medical arbitration agreement was signed in a post-surgery visit under non-emergency conditions, with forms that were clearly worded, and the patient could have chosen a different physician for post-operative care.

\textsuperscript{330} See Bank of Indiana v. Holyfield, 476 F. Supp. 104, 105-06 (S.D. Miss. 1979), in which an experienced dairy farmer with an eighth-grade education and his wife with a high school education signed a dairy cow leasing contract. The contract was contained in a nine-
Even assuming a degree of unfair surprise or lack of choice, the question remains whether the provision excluding consequential damages was so one-sided as to run afoul of Section 2-302. If confronted with sellers of farm equipment who were unwilling to accept responsibility for lost crops, A&M would have the options of obtaining crop insurance, if available, taking all possible steps to minimize the risk of crop loss, or foregoing the transaction altogether. The decision to purchase less complex equipment from the lower bidder indicates that A&M was willing to accept some risk. As the court noted, the U.C.C. does allow for exclusion of commercial consequential damages under some circumstances; therefore such an exclusion cannot be considered per se unconscionable. Further, much of contract law involves decisions about allocation of risks, and the risk involved necessarily affects the price that one party will pay and that the other party will demand. When the parties have made a bargain assigning risks, other California courts have been reluctant to alter the agreement.

A&M Produce follows the Graham precedent that licenses courts to go to great length to find unconscionability in merchants’ contracts. The succor given to A&M is out of line with the legislative intent behind Section 2-302 to give primary protection to consumers and the reasoning in even the most liberal of the early California cases that protected consumers in circumstances in which they arguably did not have a meaningful chance to protect themselves. The case also runs counter to the majority of opinions from other jurisdictions enforcing

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332. See Markborough California, Inc. v. Superior Court, 277 Cal. Rptr. 919, 927 (Ct. App. 1991) (holding that when a party agrees to assume the risk of most of the economic loss that might occur, either “knowingly or simply because it failed to read the contract,” no justification exists for shifting the loss to the other party when neither agreed to assume it nor was compensated for such assumption); Appalachian Ins. Co. v. McDonnell Douglas Corp., 262 Cal. Rptr. 716, 731 (Ct. App. 1989) (finding that a mutual release leaving the buyer to obtain private insurance in the event of rocket failure was a reasonable arrangement); Central Bank v. Kaiperm Santa Clara Fed. Credit Union, 236 Cal. Rptr. 262, 274 (Ct. App. 1987) (holding that an indemnification clause in a money order agency agreement placing the risk of stolen money orders on the agent was a reasonable risk allocation in light of the agent’s physical control and ability to obtain insurance against theft).
333. See supra notes 170-172 and accompanying text.
334. See supra notes 173-218 and accompanying text.
limitations on liability for consequential damages caused by breach of warranty, particularly with farm-related products that can be affected by the inherent uncertainties in agricultural endeavors.\(^\text{335}\) Indeed, given the variable nature inherent in farming and many other industries, it would be surprising if parties did not attempt to exclude consequential damages.\(^\text{336}\)

It is also hard to reconcile \textit{A&M Produce} with other California decisions, such as \textit{Nunes Turfgrass, Inc. v. Vaughan-Jacklin Seed Co.}\(^\text{337}\) In \textit{Nunes Turfgrass} the plaintiff was a sod grower who occasionally also packaged and sold a retail line of seed mixes in its seven California stores.\(^\text{338}\) For almost 20 years, the plaintiff purchased seed for resale and for sod production from the defendant, Vaughan-Jacklin Seed Company, one of the largest seed companies in the world.\(^\text{339}\) The plaintiff requested a special seed product from the defendant that would yield a hardier and more drought-resistant type of sod and the

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\(^{335}\) See, e.g., Southland Farms, Inc. v. Ciba-Geigy Corp., 575 So. 2d 1077, 1080-81 (Ala. 1991) (exclusion of consequential damages in sale of herbicide is accepted method of risk allocation and not unconscionable given the numerous factors affecting crop yield that are within the control of the customer and not the manufacturer); Monsanto Agric. Products Co. v. Edenfield, 426 So. 2d 574 (Fla. Dist. Ct. App. 1982) (upholding exclusion of consequential damages for breach of warranty in sale of herbicide); Martin Rispens & Son v. Hall Farms, Inc., 621 N.E.2d 1078, 1087 (Ind. 1993) (exclusion of consequential damages even for latent defects in seed would not be unconscionable if parties were aware of the risk).

\(^{336}\) See, e.g., Lindemann v. Eli Lilly & Co., 816 F.2d 199, 204 (5th Cir. 1987) (finding that decision of herbicide manufacturer to limit damages “would serve, in the absence of other evidence, abundantly to fill the risk-allocation function because the uncertainties inherent in the agricultural business are legion, and many of them, such as planting, cultivating, harvesting, and marketing decisions, are uniquely within the control of the farmer”); Jim Dan, Inc. v. O.M. Scott & Sons Co., 785 F. Supp. 1196, 1200 (W.D. Pa. 1992) (observing that limitations of damages in sale of herbicide was reasonable in light of business uncertainties); Golden Reward Mining Co. v. Jervis B. Webb Co., 772 F. Supp. 1118, 1125 (D.S.D. 1991) (noting that in the sale of a prototypical mining machine, the failure to exclude consequential damages would have been surprising); United Van Lines v. Hertz Penske Truck Leasing, Inc., 710 F. Supp. 283, 287-88 (W.D. Wash. 1989) (accepting that truck rental companies would reasonably exclude liability for damage to property in rental trucks to avoid open ended liability); Fox Elec. Co. v. Tone Guard Security, Inc., 861 S.W.2d 79, 83 (Tex. Ct. App. 1993) (holding that considering the modest monthly service charge, it was reasonable that a burglar alarm contract would limit liability; customer could have obtained insurance from the company or from other sources). \textit{But see} Discount Fabric House of Racine, Inc. v. Wisconsin Tel. Co., 345 N.W.2d 417, 422-26 (Wis. 1984) (rejecting a claim that a telephone company’s limitation of liability for breach of contract was reasonable and not unconscionable because of alleged need to avoid open ended claims for damages; asserting that company could absorb liability for small number of claims from less than 1% of customers whose ads contained errors).

\(^{337}\) 246 Cal. Rptr. 823 (Ct. App. 1988).

\(^{338}\) Id. at 825.

\(^{339}\) Id.
defendant eventually developed and produced a new variety of seed that would supposedly meet the plaintiff's needs. The seed was sold to the plaintiff and was planted for sod but proved to be defective. The court determined that the defendant had breached both an express warranty and an implied warranty of fitness for particular purpose. The critical question was the enforceability of a provision in the contract that limited liability for breach to return of the purchase price of the seed and thereby excluded consequential damages.

The *Nunes Turfgrass* plaintiff sought to have the defendant's disclaimer of warranties declared unconscionable. The trial court determined that the limitation on liability was not unconscionable, relying in large part on the fact that the plaintiff was familiar with the damage limitation and had, in fact, included similar language in its own contracts when selling its retail line of seed. The appellate court underscored the observation that both parties were merchants who should be deemed to have knowingly allocated the risk in the manner the contract stated. The end result was that recovery was limited to the purchase price of the seed.

340. *Id.*
341. *Id.*
342. *Id.* at 835-36.
343. *Id.*
344. *Id.* at 832-33.
345. *Id.* at 836.
346. *Id.* at 825.
347. *Id.* at 837. There are similar cases in which the California courts have been unsympathetic to merchants in the face of large losses because of breach. See U.S. Roofing, Inc. v. Credit Alliance Corp., 279 Cal. Rptr. 533, 535, 544-45 (Ct. App. 1991) ("hell or high water" clause disclaiming all warranties between merchant lessee and financing lessor was not unconscionable provided the lessee had recourse against the manufacturer or supplier for any defect in the equipment); West v. Henderson, 278 Cal. Rptr. 570, 574-76 (Ct. App. 1991) (finding no unconscionability for a commercial lessee when counterclaims were dismissed because of a six-month contractual limitations period on lessee claims because (1) the lessee had the opportunity to read the contract and (2) the imbalance in the limitations period could be justified by lessor's need to keep the property free of pending litigation); Markborough California, Inc. v. Superior Ct., 277 Cal. Rptr. 919, 927 (Ct. App. 1991) (clause limiting an engineering company's liability for breach to the greater of $50,000 or the consulting fee of $67,640 was not unconscionable, despite more than $5 million in damages, when the parties were dealing at arm's length and the client had an opportunity to accept, reject, or modify the terms of the agreement); Appalachian Ins. Co. v. McDonnell Douglas Corp., 262 Cal. Rptr. 716, 728-31 (Ct. App. 1989) (mutual damage waiver clause in a contract for use of a rocket to lift a communications satellite was not unconscionable when satellite did not reach its desired orbit, thereby rendering it useless at a loss of $105 million on a $15 million contract because: (1) both parties were sophisticated businesses; (2) the parties negotiated the contract rather than used a pre-printed form; (3) the parties had previously dealt with each other involving similar clauses; and (4) the buyer could have purchased a rocket from an alternative supplier).
While there are cases in other jurisdictions reaching a different result, \(^{348}\) *Nunes Turfgrass* seems to implement the goals of Section 2-302 by not disturbing the allocation of risk based simply on some inequality of bargaining power. As the court in *Nunes Turfgrass* underscored, the risk that the seeds might be defective was implicitly, if not explicitly, on the bargaining table along with the seller's indication that it did not wish to serve the role of insurer should the seeds prove defective; the case might have been decided differently if the risk of defect had been less apparent. \(^{349}\) The anticipated outcome of the arrangement should have been that the buyer take precautions to guard against consequential financial loss should the seeds prove defective, perhaps by obtaining private insurance or through some other means.

While the *Nunes Turfgrass* court did cite *A&M Produce* as well, it relied on other cases. \(^{350}\) The court could possibly have distinguished *Nunes Turfgrass* from *A&M Produce* on the grounds that the buyer was a "larger player" who had experience with the type of contracts in question. However, the buyer in *A&M Produce* was also an experienced farmer of some size, and it is difficult to imagine that he did not have experience purchasing seed and farm equipment with contracts containing limitations similar to those in the FMC contract. Ultimately, in contrast to *A&M Produce*, the fact that the seller was much larger than the buyer did not induce the *Nunes Turfgrass* court to ignore the fact that the buyer was still a merchant.

The determination of the court in *A&M Produce* to find unconscionability in order to protect the merchant-farmer epitomizes the concerns voiced in 1962 when the California Legislature first declined

\(^{348}\) See, e.g., Schmaltz v. Nissen, 431 N.W.2d 657 (S.D. 1988); Hanson v. Funk Seeds Int'l, 373 N.W.2d 30 (S.D. 1985). In *Hanson* the South Dakota Supreme Court held that a limitation on liability for consequential damages was unconscionable because it left the buyer without a minimum adequate remedy for the seller's breach. *Hanson*, 373 N.W.2d at 35. Subsequent to *Hanson*, the South Dakota Legislature passed a legislative enactment "abrogating" the *Hanson* decision. *Schmaltz*, 431 N.W.2d at 662-63 (citing Chapter 410 of the 1986 Session Laws of the South Dakota Legislature). Despite the prior expression of legislative intent on the issue, the South Dakota Supreme Court in *Schmaltz* held that the exclusion of consequential damages was unconscionable because the cause of action arose prior to the legislative abrogation of *Hanson* and no intent was apparent to apply the law retroactively. *Id.* at 663. In *Hanson* and *Schmaltz* there was, of course, the remedy of return of the seed purchase price. The South Dakota Supreme Court apparently deemed this remedy to be inadequate.

\(^{349}\) Compare Martin v. Joseph Harris Co., 767 F.2d 296, 301 (6th Cir. 1985), in which the seller of seed decided to discontinue a 26-year practice of treating cabbage seed for latent fungus, buyers were unaware of the risk and could not have appreciated what the discontinuance of the treatment would mean.

\(^{350}\) *Nunes Turfgrass*, 246 Cal. Rptr. at 833-35.
to adopt Section 2-302. A&M Produce, in tandem with Graham, sent California courts down an uncertain path with regard to the unconscionability doctrine. Buchwald v. Paramount Pictures built on these two cases as a third and recent illustration of the capricious application of the doctrine.

(3) Buchwald v. Paramount Pictures Corp.

No unconscionability case has generated more interest in the state of California than the recent trial court decision in Buchwald v. Paramount Pictures Corp. The case drew much media attention because of the prominence of the parties involved and because it presented a challenge to accepted Hollywood motion picture industry practices concerning contracts and accounting. The judge, sitting without a jury, ultimately decided that the accounting provisions in the contracts were unconscionable.

While the court effectively addressed several issues in applying the unconscionability doctrine, the court misapplied the doctrine in several significant respects: the court was overprotective of merchants in finding procedural unconscionability based on inequality of bargaining power; the presence of substantive unconscionability was questionable and inadequately addressed; the court improperly used hindsight to assess the contract; and the ultimate remedy granted involved the court's substitution of its own judgment for that of the parties about the value of the exchange.

351. No. C706083 (First Phase), 1990 WL 357611 (Cal. Super. Ct. Jan. 8, 1990) [hereinafter Buchwald (First Phase)]. The trial court issued three Statements of Decision: First Phase on Jan. 8, 1990, which decided that the movie was based on Buchwald's treatment; Second Phase on Dec. 21, 1990, which decided that certain terms in the net profit participation agreement were unconscionable; and Third Phase on March 16, 1992, which decided the amount of damages due to Buchwald and Bernheim under the reformed contract. All the decisions are reprinted in Fatal Subtraction, supra note 2 as appendices. One writer has gone so far as to call Buchwald the case of the decade in Hollywood. Kathleen Neumeyer, The Courtship of Eddie's Money, L.A. Mag., July 1992, at 66. The continued interest in the case is reflected in the number of parties filing amicus briefs in the appeal: the Producers Guild of America, the Screen Actors Guild, the Authors Guild, and the American Federation of Television & Radio Artists on behalf of Buchwald; and the California Chamber of Commerce, the California Merchants Association, the American Book Publishers, and the Alliance of Motion Picture & Television Producers on behalf of Paramount. See Kathleen O'Steen, "Coming" Process Winds Down, Daily Variety, Oct. 5, 1994, at 5.


353. The court correctly rejected the argument that a term, rather than the contract as a whole, could not be found unconscionable, properly concluded that a price term could be unconscionable, and adeptly addressed the issue of whether the doctrine was improperly used in an offensive rather than defensive manner. Id. at *6-10, *13-22.
The lead plaintiff in the case was Art Buchwald, a widely syndicated columnist, author, and Pulitzer Prize winner, who has been described as America’s most popular humorist. Buchwald prepared and eventually submitted to Paramount Pictures in March 1982 a brief proposal for a movie ultimately entitled *King for A Day*. Buchwald had first submitted his proposal to Alain Bernheim, a friend and movie producer, who submitted the story to Paramount executives as a proposed project for Paramount movie star, Eddie Murphy. Buchwald had previously sold stories to Hollywood studios and was represented by his own agent. The producer, Bernheim, retained as counsel an executive vice president of the William Morris Agency.

In early 1983 Paramount and Bernheim entered into an agreement for Bernheim to produce the movie if Paramount acquired Buchwald’s idea. Shortly thereafter, Paramount entered into an agreement directly with Buchwald for an option on the story. After several failed attempts to obtain an acceptable script, Paramount surrendered its option on the story in April 1985, thereby giving Bernheim the right to offer the movie concept to other studios.

354. See *FATAL SUBTRACTION*, supra note 2, at xxi, xxiii.
355. Buchwald’s treatment was inspired by his observation of protests aimed at the Shah of Iran during the tenure of President Jimmy Carter. It began as an eight-page treatment entitled, *It’s a Crude, Crude World*, but Buchwald reduced the treatment to two and one-half pages and changed the principal character to a black man at the recommendation of friends in Hollywood. Paramount changed the title to *King for a Day* when the treatment was put into development by the studio. *See Buchwald* (First Phase), 1990 WL 357611, at *1; *FATAL SUBTRACTION*, supra note 2, at 528-29.
357. *See FATAL SUBTRACTION*, supra note 2, at xxiv. Buchwald had sold a number of story ideas to Hollywood studios that were ultimately not made into movies, and he had sold production rights to a novel he had authored that was made into a movie. *Id.* Buchwald had written about movies and movie stars and knew a good many people in the movie business. *Id.* As his lawyer stated, “Art Buchwald was no stranger to the world of movies.” *Id.*
358. Buchwald was represented formally by the Sterling Lord Agency in New York City in his negotiations first with Bernheim and then with Paramount. *See Petition to Court of Appeal for Writ of Mandate at 4, 11, Buchwald* (Second Phase) (Apr. 11, 1991).
359. Bernheim was represented by Roger Davis, chair of the executive committee at the William Morris Agency and a former entertainment lawyer. *FATAL SUBTRACTION*, supra note 2, at 53-54. Because of the relationship of the Buchwald and Berheim contracts, Davis in effect represented both parties. At the time, the William Morris Agency was reportedly “the most powerful literary and talent agency in the industry.” Douglas Kari, Buchwald v. Paramount: *Minding Hollywood's Business*, ENT. L. REP., May 1991, at 3.
361. *Id.* Buchwald’s initial contract was with Bernheim for the same terms as he later accepted with Paramount, $65,000 plus 1 1/2% net profit. *Petition to Court of Appeal for Writ of Mandate at 13, Buchwald* (Second Phase).
Buchwald and Bernheim succeeded in selling the idea to Warner Brothers in 1986, but Warner Brothers abandoned the project in 1988 after it became known that Paramount and Eddie Murphy were filming a movie with similarities to Buchwald's *King for a Day*. The Paramount movie was filmed and released as *Coming to America* and eventually became one of the top grossing movies of 1988, earning more than $350 million.

Buchwald and Bernheim sued for breach of contract on the theory that the contracts required compensation if Paramount made a movie “based on” Buchwald’s story idea and that *Coming to America* was based on Buchwald’s invention. In the first phase of the proceedings, the court decided that *Coming to America* was indeed based on the Buchwald idea. Thereafter, the focus of the court shifted to the compensation the plaintiffs should receive under the contracts with Paramount. The contracts provided for payment of up-front fees amounting to $265,000 and percentages of net profits in the amount of 1.5% for Buchwald and at least 17.5% for Bernheim. Paramount accountants calculated that the movie lost $18 million.

363. *Id.* at *6.
366. The plaintiffs did not proceed on a theory of copyright infringement because Buchwald's treatment was not sufficiently developed to serve as an adequate basis for an allegation that a "story," as opposed to an "idea," had been stolen by Paramount. *Fatal Subtraction*, supra note 2, at 18-19. Moreover, the attorneys for Buchwald concluded that there were more dissimilarities than similarities between Buchwald's treatment and Murphy's movie. *Id.*
367. *Buchwald* (First Phase), 1990 WL 357611, at *14. The trial court noted that there were substantial differences between *King for a Day* and *Coming to America*, but also found many similarities between the two works, as originally written and as developed by Paramount before abandoning the project. *Id.* at *11-14*. The court also found significance in the access many relevant parties had to Buchwald's idea, including Eddie Murphy and John Landis who was considered as director of *King for a Day* and in fact served as director of *Coming to America*. *Id.* at *8-9*.
368. In the first phase of the case, the trial court rejected claims on various tort theories offered by Buchwald and Bernheim, including bad faith denial of contract, tortious breach of the duty of good faith, and breach of fiduciary duty. *Id.* at *14*. Buchwald and Bernheim apparently hoped to get punitive damages. The court determined that there was no showing of fraud, oppression or malice, or other tortious conduct that would warrant the award of punitive damages. *Id.* Thus, Paramount was granted judgment on the tort claims leaving only the damages for breach of contract to be determined. *Id.*
369. *Fatal Subtraction*, supra note 2, at xxv. Buchwald was to get $65,000, 1 1/2% of the net profits, and a screen credit if Paramount made the movie. *Id.* Bernheim was to receive $200,000 if the film was made and a percentage of the net profits that started at 40%, but was reducible to 17.5% if actors, directors, or writers were later given a share of the net profits. *Fatal Subtraction*, supra note 2, at 557 app. C, n.2.
under the net profits formula even though the movie grossed over $350 million. Accounting experts consulted by the plaintiffs verified that, because of the enormous cost of producing the movie in conjunction with the contract definition of net profits, there were no net profits under the contract. Buchwald and Bernheim then challenged the net profit agreement on a number of grounds, including the theory that its provisions were unconscionable, with the goal of obtaining a share of the profits once the allegedly improper provisions were struck from the contract.

Following the Graham approach, the court first analyzed whether the agreements between Paramount and the plaintiffs were contracts of adhesion. The court noted that the amount of up-front fees and the percentage of net profits had been negotiated by the parties.

370. Petition to Court of Appeal for Writ of Mandate at 11, Buchwald (Second Phase).
371. Fatal Subtraction, supra note 2, at 358-59. The experts consulted by the plaintiffs' attorneys verified that because the general production and distribution costs were extremely high (over $75 million) and because Eddie Murphy and John Landis received relatively large "gross" profit participation agreements as the star and director, the movie was destined to never generate any net profits under the contracts. Id. See also John H. Richardson, Paramount, Buchwald and the Profit Question; Attorneys Trade Gibes over Studio's Figures, WASH. POST, Mar. 26, 1990, at B1 (giving the following breakdown of the allocation of the first $250 million box office receipts made by Coming to America: $125 million to theaters, $42.3 million standard distribution fee for studio, $36.2 million actual deducted distribution fee, $6.4 million in interest charges, $48 million to make movie, and $11 million in gross profit participation for the lead actor, Eddie Murphy, and the director, John Landis, thus producing deficit of about $18 million).
372. Apart from unconscionability, other issues raised in the second phase included allegations that Bernheim and Paramount were co-venturers, that Paramount breached its fiduciary duty to Bernheim, that Paramount breached the implied covenant of good faith and fair dealing, and that Paramount breached an express term requiring consultation with Bernheim before granting profit participation to other parties. Fatal Subtraction, supra note 2, at 541-42 app. B. The co-venturer and fiduciary duty issues were rendered moot by the finding that there was no tortious conduct, except that Paramount was deemed to have a duty under the contract to render an accounting. Id. at 554. After it had found some key contract provisions to be unconscionable, the court deemed it unnecessary to decide whether there was also breach of the implied covenant of good faith and fair dealing or the express consultation clause because such findings would not change the remedies. Id.
373. Id. at 542-43. The contracts consisted of several components: a memorandum agreement reflecting the negotiated agreement for the up-front fees and percentage rate of net profits as well as other standard terms, a "turnaround" agreement setting up terms for the studio to return rights to the producer if the project should be abandoned, a document containing "Additional Terms and Conditions," and a net profit participation agreement. Id. at 542.
374. Id. at 542. In the negotiations, Bernheim's agent started by asking for a fixed fee of $200,000 plus 50% of net profits. Ultimately, the parties agreed to a fixed fee of $150,000 that increased to $200,000 based upon Bernheim receiving credit as producer on another film in the interim plus 40% of net profits, reducible to 17.5% based on shares that...
The court also noted that Paramount was willing to negotiate the manner in which net profits would be calculated with a small number of persons in the industry who possessed the necessary "clout," but deemed any such changes to be "cosmetic rather than substantive."\textsuperscript{375} Ultimately, the court relied on \textit{Graham} for the proposition that a contract can still be adhesive even though some of the terms are negotiable.\textsuperscript{376}

The court noted that, under \textit{Graham}, the finding that the contracts were adhesive was just the beginning of the analysis and considered whether the contracts were also unconscionable.\textsuperscript{377} The court quickly acknowledged that Buchwald and Bernheim could not demonstrate procedural unconscionability through surprise.\textsuperscript{378} The court then raised the possibility of procedural unconscionability through "oppression" or "absence of meaningful choice."\textsuperscript{379} Although never expressly stated, the court apparently concluded that there was a lack of meaningful choice based on the same facts and reasoning used to determine that the contracts were adhesive.\textsuperscript{380}

The court proceeded to consider whether the net profits formula was substantively unconscionable. Paramount argued that the net profits agreement should be viewed in the context of the whole contract as a means of allocating revenues, taking into account the fixed compensation received by the plaintiffs and not evaluated as a separable term.\textsuperscript{381} After asserting, quite correctly, that Section 2-302 allows for a contract to be found unconscionable either in whole or in part, the court chose to examine the separate terms and identified seven
provisions that it deemed unconscionable. The seven provisions each granted Paramount the ability to charge, as an expense against gross profit, items that the court deemed "overly harsh" and "one-sided."

After ruling that the contract terms were unconscionable, the trial court announced that it would use its powers under Section 2-302 to produce an equitable result by determining an award of damages that would be fair and reasonable for Buchwald and Bernheim. In the third phase of the trial, Buchwald and Bernheim offered evidence that the combined award for the plaintiffs should be $6.2 million. Paramount countered with evidence supporting a maximum combined award of approximately $430,000. The court found Paramount’s evidence to be more persuasive, but declined to accept the evidence of either party as conclusive. The court did allow the parties’ estimates to establish the “high and low” range in which an award would be made. The court considered a number of factors in determining the fair amount of compensation, including the inexact stipulation that the movie had made “tens of millions of dollars,” the testimony from Paramount’s witnesses that was most favorable to Buchwald and Bernheim, the uniqueness of Buchwald’s concept and the fact that

382. Paramount initially declined to address the issue of unconscionability of the individual provisions on the ground that the agreement must be considered as a whole. After the trial court’s ruling on unconscionability in the second phase of the trial, Paramount sought to challenge the court’s finding that the seven provisions were unconscionable. Petition to Court of Appeal for Writ of Mandate at 19, Buchwald (Second Phase). The trial court, however, rejected the arguments made by Paramount about the seven provisions, "saying he would not allow himself to be manipulated into reconsidering his earlier ruling that the standard movie studio contract is inherently unfair." Rohter, supra note 365. See also FATAL SUBTRACTION, supra note 2, at 482-83.

383. FATAL SUBTRACTION, supra note 2, at 550 app. B. The seven provisions found to be unconscionable were, briefly stated: 1) charging 15% overhead on operating expense allowances for the lead actor’s production company; 2) a flat 10% charge for advertising overhead without relation to actual expense; 3) a flat 15% charge for overhead without relation to actual expense; 4) charging interest based on expenses on an accrual basis while accounting for income on a cash basis; 5) charging interest on overhead; 6) charging interest on profit participation payments before the payments are actually made; and 7) charging interest rates not in proportion to the actual cost of funds. Id.

384. FATAL SUBTRACTION, supra note 2, at 551 app. B. The court rejected a proposal advanced by counsel for Buchwald and Bernheim that they should be given the stated percentage of net profits after the court made allowance for Paramount’s “actual” costs plus a reasonable rate of return on its investment. Id. The court rejected the proposal because it was likely to lead to a windfall for the plaintiffs of compensation far beyond the contemplation of the parties at the time the contract was made. Id. at 551-52.

385. FATAL SUBTRACTION, supra note 2, at 556 app. C.

386. Id.

387. Id. at 556-58.
Bernheim had control of it, the compensation paid to producers on five comparable films, and the fact that Buchwald was a nationally-known humorist who would have brought additional media attention to the film if he had received credit for the story. The court then decided, with very little elaboration, that the appropriate compensation for the parties was $750,000 for Bernheim and $150,000 for Buchwald. Not only does the court's obscure basis for fixing the amount of compensation cause concern, but the basic determination of unconscionability also is highly questionable.

The Buchwald court followed the reasoning of Graham in finding procedural unconscionability, concluding that the contract terms were adhesive even though critical provisions of the agreement were negotiated by the parties, such as the up-front fee and the percentage of net profit sharing. Notably, the Buchwald court had less basis for its decision than the court in Graham because even the net profit formula and other key terms at issue in Buchwald were subject to negotiation by artists with sufficient "clout," whereas the arbitration clause at issue in Graham was arguably not subject to negotiation by even the most successful popular music promoter of the time. Nevertheless, the Buchwald court decided that because these plaintiffs were not able to negotiate for better terms, this portion of the agreement was procedurally unconscionable because of a lack of meaningful choice. In so doing, the court lost sight of the explicit admonition in the Official Comments to Section 2-302 that the purpose of the doctrine is to prevent "oppression and unfair surprise . . . and not to disturb allocation of risk because of superior bargaining power." This aspect of the Buchwald case exemplifies the danger in neglecting a fundamental principle of the unconscionability doctrine; the mere fact that a con-

388. Id. at 557-60.
389. Id. at 558-60.
390. See Robert A. Seidenberg, More Points to Consider in Film Producer's Agreement, N.Y. L.J., Apr. 9, 1993, at 5. Seidenberg highlights a number of items in a producer's agreement that are negotiable, including gross and net participation agreements, screen and advertising credit, involvement in sequels, and actual level of involvement in the making of the picture. All of these items are subject to a degree of negotiation depending on the producer's stature, experience, and deal-making ability. Seidenberg also notes that the studios differ in their willingness to negotiate these terms. See also Nina J. Easton, Hollywood's Ledger Domain, L.A. TIMES, Jan. 6, 1991, (Calendar), at 5; Shahram Victory, Pierce O'Donnell Pans "Fatal Subtraction," AM. LAW., Mar. 1991, at 43 (noting that Eddie Murphy and John Landis together made $22 million from their gross profit sharing agreements).
tract is more favorable to one side than the other, either as a whole or in part, does not mean that the contract is unconscionable.\textsuperscript{392}

The finding of procedural unconscionability also disregarded the possibility of alternative markets for the script, evidenced by the fact that the plaintiffs approached several studios with their proposal before reaching an agreement with Paramount. Moreover, Warner Brothers purchased the rights to the movie after Paramount abandoned the project. Undoubtedly, studios in Hollywood compete for movie ideas and talent, partly by making different profit sharing agreements with those possessing "clout."\textsuperscript{393} As the court noted in \textit{Dean Witter Reynolds}, the presence of alternative options for the weaker party undercuts an argument for lack of meaningful choice.\textsuperscript{394}

The burden should have been on Buchwald and Bernheim to show not only that they did not possess the clout to obtain concessions from Paramount in the net profit arrangement, but also that other avenues were foreclosed. Considering that the \textit{Buchwald} case falls among those in which the contract was not made out of necessity, but instead involved a profit-making venture, Buchwald and Bernheim could have refrained from entering into the contract and could have continued shopping if they were unhappy with the Paramount offer.\textsuperscript{395}

The finding of substantive unconscionability in \textit{Buchwald} is also dubious. The court essentially found that the contracts undercompensated Buchwald and Bernheim in an unconscionable fashion through a one-sided calculation of net profit.\textsuperscript{396} Given that Buchwald had minimal involvement in the subsequent efforts to turn his idea into a screenplay,\textsuperscript{397} the reasonable value of his two-and-one-half page movie treatment is debatable, even if it had led to the most successful movie of all time.\textsuperscript{398} A Paramount executive testified that, over a ten-year period, the Buchwald "treatment," as opposed to a screenplay or

\textsuperscript{392} See supra note 69-71 and accompanying text.
\textsuperscript{394} See supra note 322-326.
\textsuperscript{395} See Crovitz, supra note 393 (commenting that with the degree of open competition for ideas that exists among film studios "no one at the negotiating table pointed a gun at Mr. Buchwald" to force him to enter into the contract).
\textsuperscript{396} After determining that the net profit participation agreement was unconscionable, the court clearly indicated that its task was to increase the compensation to Buchwald and Bernheim, but without giving them a windfall. \textit{Fatal Subtraction}, supra note 2, at 550-51 app. B.
\textsuperscript{397} See \textit{Fatal Subtraction}, supra note 2, at xxv.
\textsuperscript{398} Compare the outcome in \textit{Croce v. Kurnit}, 565 F. Supp. 884, 893 (S.D.N.Y. 1982), in which the court noted the uncertainty in the popular music industry and the high risk of failure of new performers in finding management contracts not unconscionable, even
story, was the only one optioned by Paramount. Similarly, the value of services of a movie producer are subjective, especially in light of the fact that multiple producers may be involved and their actual contributions to the movie may vary. Bernheim, in fact, was to serve as an executive producer, responsible for “bringing the right people together, but not actually supervising production.”

Consistent with these observations, one Hollywood dealmaker has suggested that the up-front fees received by Bernheim and Buchwald were lucrative at the time the option was formed, indicating that those parties had advantages over many others attempting to sell relatively meager movie proposals in Hollywood.

Ultimately, Paramount and other major studios have limited the price paid for services of writers, producers, and other artists through a skewed definition of net profits that makes such profits unlikely in most cases. An arrangement to share net profits has never meant the same thing in Hollywood that it has meant in general usage, and participants in the motion picture industry have long been aware that few movies yield net profits under the scheme. The lack of profit-generating movies led Eddie Murphy to describe net profits though they were deemed by the court to be “hard bargains,” reflecting the fact that new artists had little bargaining power over fairly standard industry terms.

399. Buchwald (First Phase), 1990 WL 357611, at *3.
400. See Seidenberg, supra note 390, at 5.
401. Petition to Court of Appeal for Writ of Mandate at 13-14, Buchwald (Second Phase) (citing deposition of Roger Davis, agent for Bernheim).
402. Kari, supra note 359, at 6 n.61 (citing Peter Dekom, a longtime movie dealmaker).
403. The Buchwald court found that practically all movie studios used the very same net profit definition agreement. Fatal Subtraction, supra note 2, at 543. But cf. Seidenberg, supra note 390. Seidenberg specifically disagrees with the Buchwald opinion by noting that the studios differ in their willingness to negotiate net participation terms although substantial changes “are unusual.” Id.
404. See Fatal Subtraction, supra note 2, at 411 (quoting Mel Sattler, Hollywood studio lawyer for more than 40 years, in explaining the development of “Hollywood accounting” as a means of studios protecting themselves against losing movies in the face of proliferating profit participation demands by actors, writers, directors, etc.); Kari, supra note 359.
405. Mel Sattler explained at trial that the seminal profit participation agreement was between the actor James Stewart and Universal Pictures. Even under that agreement, however, Stewart’s 50% of net profit began only after Universal had recouped twice the movie’s production costs. Fatal Subtraction, supra note 2, at 411. See also Richardson, supra note 371 (quoting Brian Walton, executive director of the Screen Writers Guild, as observing that “net profits” is a misleading term that “does not mean, in the movie business, what it may mean in everyday usage”).
406. See Fatal Subtraction, supra, note 2, at 53 (quoting Helene Hahn, the attorney who represented Paramount in negotiating the Bernheim and Buchwald contracts: “[T]he problem is the gross points. . . . They gobble up the net. Everyone knows that. It’s hardly a secret.”); Kari, supra note 359. See also Crovitz, supra note 393.
participation as "monkey points" because of the widespread view that they were seldom paid. At the same time, Paramount offered evidence to refute the view that net profit participation was entirely worthless; Paramount itself had paid more than $150 million of net profits to eighty-four participants on twenty-nine movies over the preceding fifteen years.

Buchwald and Bernheim were astute about the movie industry and were represented by experienced talent agents. The plaintiffs were not unrepresented novices who were surprised about the net profit participation agreement. Thus, Buchwald and Bernheim should have understood that the compensation for their contributions under the contract might well be "only" $265,000 if the movie were made. Moreover, there is no evidence that, at the time the contracts were made, Buchwald and Bernheim were dissatisfied with the fixed monetary compensation, the gain in stature that would have come from a successful project or the uncertain prospect of a share in net profits.

Another weakness in the Buchwald decision is the court's use of hindsight to evaluate the agreement; the court seemed influenced by the eventual production and success of the movie as it affected the net profit participation agreement. A number of uncertainties were present at the time Buchwald and Bernheim signed their contracts, including the possibility that the movie would be unsuccessful, even with Eddie Murphy as the lead actor. The parties also could not predict

407. Easton, supra note 390, at 5.
408. See Fatal Subtraction, supra note 2, at 548 app. B. For a list of the movies and profits generated, see id. at 410.
409. See Kari, supra note 359, at 3-4.
410. In his deposition, Roger Davis, the William Morris agent for Bernheim, stated that if he had thought the deal was unreasonable, he would not have let his client make it. He further explained why the deal seemed reasonable:

Mr. Bernheim was coming off two unsuccessful pictures which he had produced or co-produced. He had nothing but a three-page outline by Mr. Buchwald, who was a personal friend of his, and I had no credentials to go on. . . . The most important thing was to make a development deal to get him some up-front money and to get the project developed into a form where it could be made the basis of a motion picture.

Petition to Court of Appeal for Writ of Mandate at 15-16, Buchwald (Second Phase). The deposition is also partially reprinted in Fatal Subtraction, supra note 2, at 405.

411. A number of Eddie Murphy's movies have been considered financial flops in recent years. See John Hartl, "Batman" Was No. 1, But "Chocolat" Stayed Here Longer, Seattle Times, Jan. 28, 1990, at L1 (noting lack of profit on Murphy movie Harlem Nights during first year of release); John Lyttle, Film/On Cinema, The Independent, June 27, 1994, at 8 (attributing lack of financial success of Murphy movies Another 48 Hours, Boomerang, and The Distinguished Gentleman to the high cost of producing his films); Candice Russell, Dimming Stars Need Retooling; Eddie Murphy and Macaulay Culkin Ca-
the total production cost or the eventual profit participation agreements for the star and the director. The court's decision, almost ten years after a contract was made, that the price was too low for a product with such a subjective value as a movie concept is a capricious application of the unconscionability doctrine. Paramount presented evidence that studios spend millions of dollars annually in development of movie ideas that are never produced and that it had, in fact, spent more than $10 million in 1978 alone on such uncompleted projects. Paramount spent over $500,000 on the King for a Day development before apparently abandoning the project. Because the eventual success of a project is difficult to predict, the risk of incomplete development factors into the value of a movie idea at the time of formation of the contract. Despite the various factors listed by the court, the damage awards seem rather randomly determined from within the broad high and low range established by the parties. The indeterminate nature of the court's calculation causes further concern about the appropriate role of the courts in reforming agreements.

Moreover, the Buchwald decision possesses only limited potential for impact because the studios may well avoid the profit-sharing arrangements altogether or change the contract language to make it more explicit that "net profit participation" is a contingent form of additional compensation beyond any flat fees paid. Presumably,

412. The lack of net profits for Buchwald and Bernheim was due not only to the terms of the net profit agreement, but also to the fact that the movie was costly to make and Murphy and Landis were to receive a share of the gross profits. See Fatal Subtraction, supra note 2, at 358-59. See also Richardson, supra note 371 (observing that net profits will generally not be available in a movie when there are big stars who get gross profit participation and that in Coming to America the star and director shared a full 25% gross participation).

413. Petition to Court of Appeal for Writ of Mandate at 33, Buchwald (Second Phase).

414. See Fatal Subtraction, supra note 2, at 8-9. Warner Brothers spent $250,000 before it abandoned the project in the face of Murphy's Coming to America. Id. at 9.

415. Cf. Croce v. Kurnit, 565 F. Supp. 884, 893 (S.D.N.Y. 1982) (observing that because of great uncertainties in music business and high risk of failure by new performers, "hard bargain" contracts distinctly favoring music publishers were not unfair or unconscionable).

416. See Crovitz, supra note 393, at A10 (predicting that the Buchwald ruling will hurt "little people" because studios will stop offering to them any profit sharing agreements); Easton, supra note 390, at 5 (citing Mike Simpson, co-chair of William Morris Agency's motion picture department for the proposition that the studios, at worst, may stop giving net profit participation on top of fixed fees); Robert A. Welkos & Terry Pristin, Buchwald, Partner Win $900,000 From Studio, L.A. Times, Mar. 17, 1992, at B1 (at one studio, language referring to gross and net participants was eliminated; instead, the agreements refer to "contractually defined participation points"; at other studios, net profits have been
the courts will enforce such contracts if the parties explicitly agree to fixed compensation only or agree to a form of profit participation that clearly reveals the unlikelihood of receiving the additional pay.

The wisdom and significance of the decision in Buchwald has been put in question by the more recent, but less publicized decision of another California trial court contradicting the key holding in Buchwald. The court in Batfilm Productions v. Warner Brothers, Inc., sitting in the same courthouse as the judge in Buchwald, decided that the same net profit participation agreement was not unconscionable in a lawsuit involving similar circumstances. While it is not unusual for trial courts to disagree, in this instance the conflicting results reflect the basic difference between the unconventional approach to merchant claims of unconscionability found in Graham, A&M Produce, and Buchwald and the more restrained approach found in most jurisdictions.

The plaintiffs in Batfilm Productions were two producers who purchased the exclusive motion picture rights to the Batman comic book character in 1979 and then began efforts to produce a movie. Unable to sell the idea to major studios, the plaintiffs entered into a contract with Casablanca Filmworks Ltd., an influential production company, in an effort to have the movie made. Subsequently, Casablanca entered into an agreement with Warner Brothers to make the Batman movie, which in turn led to the 1988 contract between the plaintiffs and Warner Brothers. The contract provided that the plaintiffs would receive a fixed fee as well as thirteen percent of the


418. See supra notes 103-117 and accompanying text.

419. See Kim Masters, Holy Lawsuit, 'Batman', WASH. POST, Mar. 27, 1992, at B1 (reporting that the plaintiffs purchased the movie rights to Batman for $50,000 and formed Batfilm Productions).

420. See id. (reporting that Casablanca was operated by Peter Guber, a major figure in the motion picture industry who eventually produced Batman with his partner Jon Peters); Dan Cox, 'Batman' Suit Riddled with Jokers, VARIETY, Jan. 17, 1994, at 28 (reporting that Batfilm was unsuccessful in convincing a major studio to make the movie and thus sought the assistance of Casablanca and Peter Guber).

421. See David Robb, Warners: 'Bat' Suit 'Frivolous', HOLLYWOOD REP., May 5, 1992 (reporting that the contract between the plaintiffs and Warner Brothers was required as condition to making the movie); Masters, supra note 419, at B1.
While the parties disagreed about the total amount of income, the Batman movie indisputably generated revenues in excess of $285 million, more than any other movie ever made by Warner Brothers and one of the biggest box office sellers of all times. Warner Brothers paid the plaintiffs a total of $400,000 in fixed-fee compensation under the contract, but paid no fees to the plaintiffs under the net profit participation agreement because the movie had generated a deficit.

In the first of several similarities with the Buchwald case, the lack of net profits was caused by high production costs, including gross profit participation agreements with a number of parties, and by the unique method of accounting built into the net profit participation agreement. Another parallel with the Buchwald case was the fact that the contract with Warner Brothers was negotiated for the plaintiffs by a sophisticated party—a former general counsel and senior executive of a major motion picture studio who was intimately familiar with the nature of net profit participation agreements. Yet another similarity was the fact that one of the plaintiffs had written a memorandum that first proposed the general theme of the movie as well as

422. See Batfilm Productions, reprinted in ENT. L. REP., Sept. 1994, at 3 (the Warner agreement provided that the plaintiffs would receive an initial fixed fee of $300,000 for any Batman movie made and another fee of $100,000 once the movie reached a certain level of receipts).

423. See Dennis McDougal, A Blockbuster Deficit, L.A. TIMES, Mar. 21, 1991, at F1 (ranking Batman as the fifth-highest grossing motion picture in history and the biggest hit for Warner Brothers of all time); Michael Miller, Warner Sued over 'Batman' Losses, REUTERS LTD., (Fin. Rep.), Nov. 30, 1993 (Batman was alleged by plaintiffs to have made a total of $1.2 billion in profits from ticket sales, home video sales, and global merchandising); Pair Wants of Batman's Profits, NAT'L L.J., Apr. 13, 1992, at 63 (indicating that Warner Brothers reported $285 million in revenues while the plaintiffs alleged that receipts were closer to $425 million).

424. Batfilm Productions, reprinted in ENT. L. REP., Sept. 1994 (the plaintiffs received $400,000 in fixed fees for the first Batman movie covered by the agreement and an additional $700,000 for two subsequent Batman movies made by Warner Brothers that were not involved in the lawsuit). In addition to suing Warner Brothers, the plaintiffs also sued PolyGram, the successor corporation to Casablanca, and its executive officers. See David Robb, Warner Wins 'Total Victory' in Batman Suit, HOLLYWOOD REP., Jan. 25, 1994.

425. See McDougal, supra note 423 (reporting that because of large actual production cost and gross profit participation granted to actors Jack Nicholson and Michael Keaton, producers Jon Peters and Peter Guber, and director Tim Burton, the chances of the movie ever generating net profits were "almost nil" regardless of the gross revenues realized; the gross profit participation fees for the other parties was estimated to be $60 million of the first $253.4 million box office sales).

426. Batfilm Productions, reprinted in ENT. L. REP., Sept. 1994 (plaintiff Benjamin Melniker was an attorney who had worked for sometime at MGM (Metro-Goldwyn-Mayer) and was described by the court as knowing "all the tricks of the trade" and knowing "inside and out how these contracts work").
the casting of a principal character. The most important similarity, however, was the allegation by the plaintiffs in *Batfilm* that the net profit participation agreement was unconscionable.427

Despite the many analogous facts and issues, the court in *Batfilm* reached a different conclusion about the unconscionability of the net profit participation agreement and revealed a basic philosophical difference with the court in *Buchwald*. Observing that the plaintiffs had received the proper fixed compensation under the contract and emphasizing that the plaintiffs should presumably have understood the net profit participation agreement because of their negotiator’s experience, the court went on to observe that for four centuries common-law courts had neither reformed nor refused enforcement to contracts merely because the exchange might be perceived to be unfair.429 The court emphasized that for a contract to be unconscionable under Section 2-302, it must be "shock the conscience" or be "harsh, oppressive, and unduly one-sided."430 Thus, the court first ruled that viewing the contract as a whole, which the *Buchwald* court declined to do,431 the plaintiffs had failed to prove that the contract was unconscionable.432 The court’s conclusion embodied its view that while the plaintiffs might be entitled to additional compensation to achieve a perfectly “fair exchange,” the unconscionability doctrine does not mandate that all contracts be fair.433 The price of $400,000, not much more than the fixed compensation of $265,000 for the two plaintiffs in *Buchwald*, was not deemed unconscionable.

As the *Buchwald* court had done, the *Batfilm* court then proceeded to examine the individual terms of the net profit participation agreement.
agreement for unconscionability,434 but reached a contrary result. The court held that the plaintiffs failed to prove that any of the terms were unconscionable, with the exception of the method used to compute interest.435 The court determined that the plaintiffs had "presented enough evidence to require Warner Brothers to defend its method of computing interest under the contract."436 Nevertheless, the court ultimately decided that Warner Brothers demonstrated that the calculation of interest was the same as in the plaintiffs’ original contract with Casablanca, was equivalent to arrangements generally available from competitors, and was not questioned during the contract negotiations.437 The court emphasized that its role was to determine what the parties meant by the contract language and that in this case both plaintiffs were experienced enough to understand how the interest computation worked.438 Thus, the court concluded that the contract was performed in accordance with the reasonable expectations of the parties and was not unconscionable.439

The Batfilm court did not allow its decision to be driven by sympathy with the plaintiffs, who apparently conceived the film and struggled unsuccessfully for some time to make it only to see others reap millions of dollars while they settled for $400,000.440 In doing so, the court also refrained from using the hindsight judgment evident in the Buchwald decision,441 remarking that it would not be good for the motion picture industry to allow parties to come into court after a movie had proven successful and have the court remake the bargain.442

Paramount has appealed the Buchwald decision, challenging the trial court finding of unconscionability as well as the ruling that the

434. The accounting provisions challenged were essentially the same as those in Buchwald, see supra notes 368-372 and accompanying text, plus additional terms relating to foreign tax credits, the royalties on videocassette sales, and costs related to reusing the studio lot for future movies. Batfilm Productions, reprinted in Ent. L. Rep., Sept. 1994.
435. Id.
436. Id.
437. Id.
438. Id. The court again emphasized that plaintiff Melniker was an "old hand" at this type of agreement and had once negotiated them on the other side of the table.
439. Id. The judge ultimately dismissed the case. See Robb, supra note 424.
441. See supra notes 411-415 and accompanying text.
movie was "based on" Buchwald’s treatment. An appeal is also likely in the Batfilm case. While the decision in Batfilm is more consistent with the popular construction and legislative history of Section 2-302, the Graham and A&M Produce decisions make the prospects for reversal of the Buchwald doubtful.

B. Hindsight Judgment in California Unconscionability Cases

The text of Section 2-302 and the California case law require that a contract be judged for unconscionability at the time of its making. Nevertheless, the decision in Buchwald was strongly influenced by the way variable factors unfolded after the contract was formed. While similar hindsight judgment can be found in the early adhesion cases, the use of hindsight must be considered a misapplication of Section 2-302. Apart from Buchwald, the California case best demonstrating the impropriety of hindsight judgment is Ellis v. McKinnon Broadcasting Co.

The plaintiff in Ellis entered into an employment contract to work as an advertising salesperson for the defendant television station. The initial and subsequent written contracts contained a clause providing for termination by either party with two-weeks notice. The terms also provided that the plaintiff would receive a twenty-percent commission on sales, but was guaranteed a minimum

443. See Dan Cox, Paramount Finally Files Buchwald Appeal, VARIETY, Apr. 11, 1994, at 32. Paramount originally filed notice of appeal in August 1992, but completion of the appeal was delayed for nearly two years while the trial judge assembled the 37,000 page trial record. Id.

444. See Robb, supra note 424 (quoting plaintiffs' attorney Tom Girardi stating that the judge's decision to dismiss the plaintiffs' case was "outrageous" and would be appealed).

445. See supra notes 118-125 and accompanying text.

446. See, e.g., California Growers Ass'n v. Bank of America, 27 Cal. Rptr. 2d 396, 403 (Ct. App. 1994) (noting that if the contract is fair when made, it does not become unconscionable because of subsequent events); Chretian v. Donald L. Bren Co., 198 Cal. Rptr. 523, 525 (Ct. App. 1984) (emphasizing that the contract should be examined prospectively from the time it was made); Yeng Sue Chow v. Levi Strauss & Co., 122 Cal. Rptr. 816, 822 (Ct. App. 1975) ("It is blackletter law that whether a contract is fair or works unconscionable hardship is determined with reference to the time when the contract was made and cannot be resolved by hindsight by considering circumstances of which the contracting parties were unaware.").

447. See supra notes 411-415 and accompanying text.

448. See supra notes 175-218 and accompanying text.

449. 23 Cal. Rptr. 2d 80 (Ct. App. 1993).

450. Id. at 81.

451. Id. The initial contract was signed when the plaintiff began his employment in December 1986, and a second contract was signed six months later in June 1987. Both contracts were identical in the key provisions. Id.
monthly salary of $2,166 for at least the first three months without regard to actual sales. The key provision in the dispute, however, was one providing that the salesperson would collect commissions only on advertising fees actually received by the station prior to termination of the salesperson's employment.

The plaintiff worked for the defendant for more than two years before voluntarily deciding to leave. The employer collected nearly $100,000 in advertising fees from the plaintiff's sales after he left, which meant that the plaintiff would have been entitled to approximately $20,000 in commissions had he continued his employment. Although the plaintiff indicated in his resignation letter that he understood the consequences of the clause providing that commissions would not be paid for fees collected after his termination date, he subsequently challenged the provision. The appellate court's assessment of unconscionability is presaged by its classification of the clause as a "forfeiture provision." The court proceeded to find elements of procedural unconscionability, unfair surprise, and oppression, as well as substantive unconscionability. While the court's reasoning on procedural unconscionability is subject to challenge, it is the court's assessment of substantive unconscionability that best illustrates hindsight judgment.

452. While the court's opinion indicates the minimum payment was for only the first three months, the employer's brief indicates that the plaintiff was further guaranteed a minimum monthly income of at least $2166 throughout the length of his employment. Respondent's Brief at 5, Ellis v. McKinnon Broadcasting Co.
453. The relevant provision read in part: "The Station will pay Employee commissions only on advertising fees billed and collected.... No commissions will be paid to the Employee on advertising fees received by the Station after the Employee's final date of actual employment." Ellis, 23 Cal. Rptr. 2d at 82.
454. Id. at 81-82.
455. Id. at 82, 85. The case was first heard by the Labor Commission, which found for the plaintiff employee and awarded him damages. The superior court granted a trial de novo and found in favor of the employer, leading to the plaintiff's appeal to the California Court of Appeal.
456. Id. at 82. The plaintiff's termination notice read in relevant part: "I am giving you my two weeks notice of my last working date at KUSI-TV. My last actual date of employment will be March 17, 1989. Therefore, I expect to be commissioned on all monies collected through the close of business on March 17, 1989." Respondent's Brief at 2, Ellis.
457. Ellis, 23 Cal. Rptr. 2d at 82. In addition to arguing unconscionability, the plaintiff also sought to establish ambiguity based on an alleged conflict between a provision for payments only on fees collected and another provision that provided the employee would be entitled to commissions "earned" through the date of termination. Id. The court of appeal decided, however, that no ambiguity existed between the terms "collected" and "earned" and that the written agreement intended to deny the employee commissions on fees received by the employer after the date of termination. Id. at 83.
458. Id. at 82.
The appellate court closely followed the *A&M Produce* analytical structure in considering whether the commissions provision was unconscionable. The court accepted as true the plaintiff's contention that the initial contract was not presented to him until a few weeks after he had relocated and had begun work for the defendant.\(^{459}\) The court also accepted the plaintiff's representation that the contract was presented to him without warning and as a mere formality, thus inducing him to scan the documents only for the commission percentage and minimum draw.\(^{460}\) The plaintiff testified that he did not read the provision at issue until immediately prior to his resignation.\(^{461}\) On this basis the court found procedural unconscionability through "unfair surprise," concluding that the plaintiff's failure to read the contract was "hardly surprising."\(^{462}\)

The court's willingness to excuse the plaintiff from reading the contract is startling and stands at odds with other California cases in which the courts were unsympathetic to parties, even consumers, who failed to read their contracts when they had the opportunity to do so.\(^{463}\) In this regard the case is dissimilar to cases in which the courts have found it reasonable that the consumer did not read all papers

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459. *Id.* at 84. Although the employee's signature was not dated, the document was dated the day the plaintiff began work, and the defendant argued that he had signed it on that date. Additionally, the plaintiff did sign other personnel documents that bore the date of December 1, 1986. Defendant's Trial Brief at 3 n.1, *Ellis v. McKinnon Broadcasting Co.*, No. 638913 (Cal. Super. Ct. Jan. 6, 1991).

460. *Ellis*, 23 Cal. Rptr. 2d at 84-85. During the trial, the court found that the parties had entered into three successive agreements, an initial oral agreement and the subsequent written agreements, all binding on the parties. Respondent's Brief at 2-3, *Ellis*.

461. *Ellis*, 23 Cal. Rptr. 2d at 84.

462. *Id.* at 83-84.

463. See, e.g., Coon v. Nicola, 21 Cal. Rptr. 2d 846, 854-55 (Ct. App. 1993) (failure of patient to read medical arbitration agreement did not render it unenforceable when patient signed under non-emergency conditions, terms were clearly laid out, and defendant had no notice that patient might have been disoriented because of medication); Bolanos v. Khalatian, 283 Cal. Rptr. 209, 211 (Ct. App. 1991) (failure of patient to read medical arbitration agreement did not render it unenforceable when the agreement was signed on non-emergency prenatal visit despite allegation that patient had only fifth-grade education and received no explanation of the form); West v. Henderson, 278 Cal. Rptr. 570, 575 (Ct. App. 1991) (commercial lessee who was presented with initial draft and final lease that she took home before signing was not excused because she failed to read provisions; the court noting that parties to commercial contracts fail to read them at their peril); Markborough California, Inc. v. Superior Court, 277 Cal. Rptr. 919, 927 (Ct. App. 1991) (failure of developer to read clause limiting liability in standardized agreement of engineering company to consulting fee of $67,640 when breach caused more than $5 million in damage did not prove lack of bargaining power when cover letter indicated proposals for different terms would be considered).
signed because of emergency or similar circumstances.\textsuperscript{464} It is difficult to imagine that the plaintiff in \textit{Ellis} could not have availed himself of the opportunity to read the written contract; the court expressly acknowledged that he could have done so.\textsuperscript{465} Nevertheless, the court excused him from doing so, apparently giving little or no weight to the additional factor that the plaintiff was an experienced salesperson who should have appreciated the significance of a signed contract.\textsuperscript{466}

The appellate court buttressed its finding of surprise with the highly questionable reasoning from \textit{A&M Produce} that a party presenting a standard form agreement has the burden of showing that the other party had knowledge of any unusual or unconscionable term.\textsuperscript{467} The court, however, gave only negligible consideration to whether the post-termination provision was "unusual" in the context, summarily stating that any provision leading to the forfeiture of $20,000 must be considered unusual.\textsuperscript{468} The employer argued that the provision for post-termination fees was common not only in the broadcasting industry, but also in comparable commission agreements.\textsuperscript{469} The court, however, quickly dismissed as inapposite a case involving an automobile sales contract that upheld a denial of commissions after termination.\textsuperscript{470} The opinion does not reflect any inquiry at all into broadcasting industry practices. In light of the fact that the plaintiff had worked for a number of years in the broadcasting industry, an inquiry into common practices would have been appropriate to the issue of unfair surprise.

\textsuperscript{464} See Wheeler v. St. Joseph Hospital, 133 Cal. Rptr. 775, 786 (Ct. App. 1976) (understandable that patient did not read form entitled "Conditions of Admission" while being admitted because in such cases the patient normally goes to the hospital selected by his doctor without feeling that he has a choice of institutions, and the experience is likely to be anxious, stressful, and frequently traumatic).

\textsuperscript{465} The court stated, "It is true Ellis could have read the contract more closely when it was presented to him for signature." \textit{Ellis}, 23 Cal. Rptr. 2d at 84.

\textsuperscript{466} The plaintiff had apparently worked at another television station in Salinas, California for two years before joining the defendant's station, Defendant's Trial Brief at 1, and before that had worked for two years with a television station in Madison, Wisconsin, Respondent's Brief at 3-4.

\textsuperscript{467} \textit{Ellis}, 23 Cal Rptr. 2d at 84.

\textsuperscript{468} \textit{Id}.

\textsuperscript{469} Respondent's Brief at 20-21, \textit{Ellis}.

\textsuperscript{470} \textit{Ellis}, 23 Cal. Rptr. 2d at 85. The court distinguished Division of Labor Standards Enforcement v. Dick Bullis, Inc., 140 Cal. Rptr. 267 (Ct. App. 1977), on the ground that it involved automobile sales commissions and in the automobile industry a "sale" was not deemed made until the vehicle was delivered, while in present case, the "sale" was not viewed as contingent on collection from the customer. \textit{Id}. The distinction rings rather hollow given that under the contract in \textit{Ellis}, payment would never be due the salesperson unless the customer paid. \textit{See supra} note 456 for the relevant contract provision.
The combination of the plaintiff's business experience plus his ample opportunity to read the agreement should have precluded the court from finding procedural unconscionability through unfair surprise. Perhaps an underlying uneasiness with its conclusion in this area explains why the court proceeded to look for procedural unconscionability through oppression.

The court also found procedural unconscionability through "'oppression' based on unequal bargaining power." The court concluded that because the plaintiff was a single employee who had moved across the state to work for the defendant and had no other job offers at the time, he had no choice other than to accept the contract. Similar to the reasoning in Graham and Buchwald, the Ellis court was unpersuaded by the fact that a number of terms, including the starting date, commission rate, and amount of monthly pay had in fact been negotiated by the parties. The court also discounted the fact that in certain instances, presumably when the employee was highly desired, the employer did enter into general negotiations of contracts because the court observed that the plaintiff "was never made aware of that option."

Having concluded that the Ellis contract was procedurally unconscionable, the court also found substantive unconscionability by determining that the denial of commissions after termination was commercially unreasonable. The court acknowledged that ten to fifteen percent of the work on accounts occurred after the initial sale, possibly after a salesperson had left the company, and there was no indication in the record that the post-sales servicing was optional or incidental. In fact, the employer argued that customers who did not receive post-sales servicing often became reluctant to pay their fees. The employment agreement thus was structured to give incentive to salespersons to follow through on all sales. Nevertheless, the court did not consider the provision justified by the employer's concern.

471. Ellis, 23 Cal Rptr. 2d at 84.
472. Id.
473. Id. See discussion of Graham, supra notes 272-273, and Buchwald, supra notes 376-379.
474. Ellis, 23 Cal. Rptr. 2d at 84.
475. Id. at 85.
476. The plaintiff estimated that the post-sales servicing occupied 10-20% of his time. Petitioner's Brief at 5, Ellis. The post-sales servicing apparently included copy changes, scheduling changes, and assisting in the collection process. Respondent's Brief at 4, Ellis.
477. Defendant's Trial Brief at 9, Ellis.
The court also disregarded the employer's argument that it had agreed to pay the plaintiff a minimum of more than $6,000 through the three-month guaranteed draw without assurance that the plaintiff would succeed in selling any advertisements. Ellis might well have left the company with all fees collected, or an amount of less than $6,000 due, if his sales had slowed before he left. Indeed, the employer represented that the plaintiff spent his last two weeks primarily on post-sales collection. Moreover, there was evidence that one reason for the relatively large amount of lost commissions was that the plaintiff left during the middle of the month rather than delaying until shortly after the billing and payment cycle. One can only presume that the timing of departure was the free choice of the plaintiff, probably made in conjunction with his new employer and made with knowledge of the potential impact on his commissions. The avoidance of lost commissions appears to have been largely within the control of the plaintiff under the terms of the contract. Nonetheless, the court viewed the contract not from the range of possibilities that existed at the time of formation, but only from the specific circumstances that had come to pass, largely as a result of the plaintiff's conduct. The court was obviously disturbed at the commission that the plaintiff lost upon termination. Presumably, if the lost fees had been insubstantial, there would not have been a finding of unconscionability. Thus, in a blatant exercise of hindsight evaluation, the court decided the post-termination commissions clause was substantively unconscionable.

The Ellis case is also troubling because it is difficult to reconcile with the earlier California decisions in Neal v. State Farm Insurance Co. and Chretian v. Donald L. Bren Co. In Neal an insurance agent executed a contract that provided for payment of commissions based on sales in the "sixth preceding month." For the first six months of employment, the agent would be compensated based on the

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478. Ellis, 23 Cal. Rptr. 2d at 85.
479. Respondent's Brief at 6, Ellis.
480. Id.
481. The Ellis court also suggested possible reformations of the contract although it refrained from implementing them. First, the court suggested that unearned portions of the guaranteed salary could have been charged against sums due after employment. Ellis, 23 Cal Rptr. 2d at 85. The court further suggested that the employer might have charged a deduction of 15% or less against any post-termination commissions to account for the fact that post-termination servicing of accounts was necessary. Id. at 85 n.4. In essence, the court suggested that the parties could have written a better contract.
482. 10 Cal. Rptr. 781 (Ct. App. 1961).
484. Neal, 10 Cal. Rptr. at 783.
sales by his predecessor agent in the locale, but upon termination, the
gerent agent’s successor would receive the commissions for the departing
agent’s last six months.\textsuperscript{485} The plaintiff brought suit against the insur-
ance company, alleging that the provision resulted in forfeiture of his
commission on premiums sold during his last six months.\textsuperscript{486} The court
agreed that the contract was adhesive, but expressly found that the
arrangement did not amount to a forfeiture and implicitly found that
the arrangement was a reasonable one, noting that courts in other
states had reached a similar conclusion.\textsuperscript{487}

Similarly, in the more recent case of \textit{Chretian v. Donald L. Bren
Co.}, a contract between a real estate salesman and employer provided
that a portion of commissions would not be paid if the salesman left
before escrow closed.\textsuperscript{488} The salesman lost a partial commission of
approximately $17,000, an amount similar to that in \textit{Ellis}, by leaving
before escrow closed.\textsuperscript{489} However, the court found the commission
arrangement to be reasonable in light of the employer’s great interest
not just in obtaining the sale, but also in having it completed to the
customer’s satisfaction.\textsuperscript{490} Although the employers in \textit{Neal} and \textit{Chre-
tian} could have structured the fee arrangements to address more pre-
cisely the economic consequences of a salesperson terminating
employment before a particular sale was completed, the test of uncon-
scionability is not whether the parties could have written a better or
more reasonable contract. The proper test in these cases is whether
the bargain is so one-sided as to shock the conscience and whether
there was some bargaining impropriety resulting from surprise or op-
pression. The \textit{Neal} and \textit{Chretian} courts, unlike the court in \textit{Ellis}, dis-
played the proper restraint and deference to agreements that were not
egregiously one-sided in the allocation of risks.

\textbf{C. Affirmative Use of the Unconscionability Doctrine}

As discussed earlier in this Article,\textsuperscript{491} a fallacious view exists
among many courts that the unconscionability doctrine can never be
used to obtain an affirmative recovery. For the most part the Califor-
nia courts have erred in this regard, but the \textit{Buchwald} court realized

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\begin{itemize}
\item \textsuperscript{485} \textit{Id.} at 785.
\item \textsuperscript{486} \textit{Id.}
\item \textsuperscript{487} \textit{Id.} at 784-86.
\item \textsuperscript{488} \textit{Chretian}, 198 Cal. Rptr. at 524-25.
\item \textsuperscript{489} \textit{Id.} at 525.
\item \textsuperscript{490} \textit{Id.} at 526.
\item \textsuperscript{491} \textit{See supra} notes 132-138 and accompanying text.
\end{itemize}
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that the doctrine may properly pave the way for affirmative relief by eliminating an unconscionable provision in a contract.

The first California case to address the potential use of the unconscionability doctrine to obtain affirmative relief was *Truta v. Avis Rent A Car System, Inc.* The plaintiff asserted, *inter alia*, that the collision-damage waiver fees charged by major car rental companies were unconscionable and sought an injunction and restitution. The trial court granted a demurrer filed by the defendants that asserted unconscionability could be used only as a defense and not as a ground for affirmative relief. The appellate court found that a cause of action based on unconscionability was sufficiently stated to survive a demurrer and that the interaction of Section 2-302 and other state law concerning unfair business practices could give rise to an affirmative relief. While the recognition in *Truta* that the operation of an unconscionable provision could lead to affirmative recovery was a significant development, the opinion rather clearly indicates that Section 2-302 would not be an independent basis for such recovery.

A similar reading of Section 2-302 was given by the court in *California Grocers Ass’n v. Bank of America.* The appellate court overturned the trial court’s issuance of an injunction against a bank charging an allegedly excessive fee for returned deposited checks. The court’s decision was partly based on the grounds that unconscionability has only a defensive use under Section 2-302 and that while separate statutory authority exists for affirmative relief for consumers, no express statute exists to grant such relief to nonconsumers. The court explicitly construed the language of Section 2-302 to mean that the Section may be used only in a defensive manner. Given the type of transaction at issue in the case, the logical consequence of the ruling would be that Section 2-302 could be invoked by the plaintiffs

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492. 238 Cal. Rptr. 806 (Ct. App. 1987).
493. *Id.* at 809.
494. *Id.*
495. The court of appeal found sufficient allegations of excessive price as substantive unconscionability and lack of meaningful choice as procedural unconscionability. *Id.* at 817-18.
496. *Id.* at 815-16. The court cited California Civil Code § 1770, which makes unlawful the insertion of “an unconscionable provision in [a] contract.” *Id.* at 815. Section 1780 provides that a consumer harmed under § 1770 may obtain actual damages, injunctive relief, punitive damages, and other relief deemed proper by the court. *Id.*
497. 27 Cal. Rptr. 2d 396, 403-04 (Ct. App. 1994).
498. *Id.* at 405.
499. *Id.* The court recognized that in *Truta* there was additional statutory authority that served as a basis for affirmative recovery, but indicated that the statutes were inapplicable to the case at hand. *Id.* at 404.
only by allowing fees to become due to the bank and then having the
agility to bring a lawsuit before the fees were collected.

Yet another example of the defensive use approach is the case of
_Shadoan v. World Savings & Loan Ass'n_. This case focused on the
enforceability of a prepayment penalty in a loan agreement. The
plaintiff borrowers paid the penalty and then brought suit charging
that the penalty was unconscionable. Following the general rule re-
lected in _Truta_, the court assumed that Section 2-302 could be used
only to defend against enforcement of the penalty clause and not to
recover the payment already paid. As in _Truta_, the court espoused
the view that other statutory provisions would be necessary to estab-
lish a right to affirmative recovery, assuming the clause was uncon-
scionable. Thus, the plaintiffs in _Shadoan_ would have been barred
from using Section 2-302 because they had taken the cautious ap-
proach of paying the penalty before challenging the contract. While
the _Shadoan_ court ultimately decided that the penalty clause was not
unconscionable, the reasoning dramatizes the inequity of the view that
unconscionability can be used only to fend off a claim for compensa-
tion and not to recover an amount already paid under an unconscion-
ble contract or term.

The _Buchwald_ case is the one recent California case in which the
affirmative use issue was better addressed. As discussed above, Buch-
wald and Bernheim raised unconscionability as part of their claim for
a share of the profits from the movie _Coming to America_. Paramount asserted that the plaintiffs were attempting to make an
improper use of Section 2-302 to obtain an affirmative recovery. The
court in _Buchwald_ observed that an offensive use of the doctrine was
not allowed, but described the posture of the case as one in which
Buchwald and Bernheim brought the lawsuit for breach of contract
and then used unconscionability to prevent Paramount from defend-

501. Id. at 208. The plaintiffs also challenged a clause that allowed the lender to “uni-
laterally call” the loan by demanding payment in full with six months notice. No prepay-
ment penalty could be asserted, however, if “unilateral call” was made by the lender. Id. at
210. The court rejected the plaintiffs’ argument that the two terms combined to make the
contract unconscionable. Id. at 211.
502. Id. at 208.
503. Id. at 208-09. _See also_ Beasley v. Wells Fargo Bank, 1 Cal. Rptr. 2d 446, 454 (Ct.
App. 1991) (stating in dictum that § 2-302 can only be used defensively and not to obtain
restitution).
504. Id.
505. _See supra_ notes 369-386 and accompanying text.
506. Fatal Subtraction, _supra_ note 2, at 543 app. B.
ing on the basis of certain contract provisions. The decision highlights the superficiality of the distinction between defensive and offensive use of the doctrine.

The broader question raised by Buchwald, Truta, and the other California cases addressing the issue of offensive use is whether the generally recognized distinction is meaningful and worth maintaining. A careful analysis of the cases suggests that it is not. The "defensive use only" rule is artificial, is based on a simplistic reading of Section 2-302, and does not effectively administer the policy underlying the unconscionability concept. The mere presence of an unconscionable clause in a contract is not, by itself, a sufficient basis for an affirmative recovery. An affirmative recovery should be allowed, however, in at least two situations: when the operation of the unconscionable clause has already caused a loss to the offended party at the time of trial and justifies restitution and when striking an unconscionable provision gives the party an avenue for recovery based on the remainder of the contract.

D. Price-Term Unconscionability

Early California equity cases recognized that the price term may be an element of unconscionability. In State Finance Co. v. Smith, the unsophisticated buyer agreed in January 1937 to pay the then-substantial amount of $300 for truck that was valuable only as scrap, relying in part on erroneous representations about the quality of the truck. In Jacklich v. Baer, the unsophisticated professional boxer ostensibly obligated himself to pay an amount substantially in excess of $33,000 in repayment of a loan in the amount of $13,500, without any identifiable justification for the exceptional price. These early California cases are consistent with the generally accepted view that a combination of a contract price greatly in excess of an identifiable market price, together with actual or presumed bargaining misconduct, will render the contract unenforceable. Regarding the two more difficult price-term unconscionability issues identified above, there is little California law on whether procedural unconscionability

507. Id. at 544-45.
508. See supra notes 126-135 and accompanying text.
509. See supra notes 174-188 and accompanying text.
510. See supra notes 176-177 and accompanying text.
511. See supra notes 181-183 and accompanying text.
512. See supra notes 139-145 and accompanying text.
513. See supra notes 139-153 and accompanying text.
must always be present in addition to an excessive price, but there are significant and conflicting decisions addressing whether excessive price may be determined by measuring the seller's profit on the transaction.

*Perdue v. Crocker National Bank* was the first California case decided after the adoption of Section 2-302 to focus on an allegation that the contract price included too large an amount or percentage of profits, as opposed to an allegation that the contract price unconscionably exceeded the general market price. In *Perdue* the plaintiff argued that the $6 fee assessed for processing "insufficient funds" checks was excessively high because the actual cost to the bank was no more than a dollar. Reviewing the trial court's decision to dismiss the case on demurrer, the California Supreme Court concluded that the allegation of profit equal to 600 percent or more raised a triable issue of substantive unconscionability. Although acknowledging that a price set by a competitive market was unlikely to be unconscionable, the court reasoned that even the market price might be excessive in light of the seller's cost, the seller's inconvenience in doing business, and the true value of the product or service.

The appellate court in *Perdue* had accepted the argument that the $6 fee was sufficiently small in an absolute sense to preclude a claim of unconscionability, but the supreme court took the position that a

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514. The court in Carboni v. Arrospide, 2 Cal. Rptr. 2d 845 (Ct. App. 1991), *rev. den.*, 1992 Cal. LEXIS 1338 (Cal. Mar. 19, 1992), essentially held that a 200% interest rate on a loan was an excessive price that was sufficient in itself to establish unconscionability. *Carboni* involved a loan of $4000 under a fourth deed of trust with the understanding that the loan would be repaid in a single lump sum of $6000 three months later upon the sale of the property. *Carboni*, 2 Cal. Rptr. 2d at 846. The parties disputed whether the purpose of the loan was to renovate the property or pay medical bills. *Id.* The property was not sold, defendant borrowed additional funds totaling $99,000 before defaulting, and by the time of the trial two years later the total owed was $390,000. *Id.* The debtor had agreed to pay interest at the rate of 200% that was clearly revealed in a disclosure statement. *Id.* at 850. While the existence of reasonable alternatives to this loan was debatable, the court seemed inclined to find the terms too harsh to enforce even in the absence of bargaining misconduct. *Id.* at 848. See Darr, *supra* note 14, at 1843, 1854 (citing *Carboni* as a rare case finding unconscionability based on the substantive term alone).


516. *Perdue*, 702 P.2d at 508, 513. The complaint asserted that the actual cost of processing the checks was only $0.30 per check. *Id.* at 513.

517. *Id.* at 508.

518. *Id.* at 513. The court also noted the possible presence of procedural unconscionability both through unfair surprise because the contract was contained on a "signature card" with extremely small print and through lack of meaningful choice because the terms were nonnegotiable. *Id.* at 513-14.

519. *Id.* at 512.
small fee applied to a large volume of transactions might lead to a “sizeable sum” that would raise a colorable issue of unconscionability.\textsuperscript{520} Because the case involved the appeal of an order to dismiss, the \textit{Perdue} court did not need to resolve the perplexing question of what percentage of profits is excessive.\textsuperscript{521} The opinion, however, clearly endorses both the view that a price may be unconscionable because it gives a party too much profit and the novel concept that the cumulative profits from many separate transactions are relevant to an individual plaintiff’s claim.\textsuperscript{522} Subsequently, the appellate court in \textit{Truta} also endorsed both these concepts in ruling that a $6 per day charge by rental car companies for “collision damage waiver” protection raised a triable issue of unconscionability.\textsuperscript{523} The \textit{Truta} court held that the charging of $6 per day for collision damage waiver protection by car rental companies raised “a colorable claim of substantive unconscionability” based on allegations that the cumulative effect was that the companies received fees that were more than double what they should earn in light of the protection actually provided to customers.\textsuperscript{524}

The same issues recently surfaced again but were treated differently in \textit{California Grocers Ass’n v. Bank of America}.\textsuperscript{525} The plaintiff challenged an alleged 100 percent markup reflected in a $3 bank charge to depositors when the drawer of the check had insufficient funds.\textsuperscript{526} The trial court concluded that the 100 percent markup was too much and ordered that the bank charge no more than 15 percent over its actual costs.\textsuperscript{527} The appellate court emphatically disagreed and reversed, first finding that the $3 charge by the defendant was in

\begin{itemize}
\item \textsuperscript{520} \textit{Id.} at 513. \textit{See Perdue v. Crocker Nat’l Bank}, 190 Cal. Rptr. 204, 209-11 (Ct. App. 1983) (rejecting claim that $6 charge was unreasonable and holding as a matter of law that the disparity between bank’s alleged cost of 30 cents and $6 fee did not rise to level of substantive unconscionability), \textit{vacated}, 702 P.2d 503 (Cal. 1985).
\item \textsuperscript{521} \textit{Cf. Beasley v. Wells Fargo Bank}, 1 Cal. Rptr. 2d 446, 447 (Ct. App. 1991) (affirming decision that bank customers were entitled to restitution of “late payment” and “over limit” fees charged on credit card accounts under state law concerning invalid liquidated damage clauses).
\item \textsuperscript{522} \textit{Perdue}, 702 P.2d at 513. The litigation was settled before the courts resolved the questions. \textit{See Dwight Golann, Developments in Consumer Financial Services Litigation, 43 Bus. Law. 1081, 1082 (1988) (explaining that the settlement was approved in a companion case, Rebney v. Wells Fargo Bank, No. 720307 (Cal. Super. Ct. 1987)).}
\item \textsuperscript{523} \textit{Truta v. Avis Rent A Car Sys., Inc.}, 238 Cal. Rptr. 806, 817 (Ct. App. 1987) (reversing trial court’s grant of dismissal on a general demurrer).
\item \textsuperscript{524} \textit{Id.}
\item \textsuperscript{525} 27 Cal. Rptr. 2d 396 (Ct. App. 1994).
\item \textsuperscript{526} \textit{Id.} at 403.
\item \textsuperscript{527} \textit{Id.} at 400.
\end{itemize}
the low range of market prices charged by competing banks and then emphatically stating that "[t]he huge volume of [fees]—and the consequent cumulative profit to [the bank]—is inconsequential. 'A contract, fair when entered into, does not thereafter become unconscionable simply because a great many other persons enter into identical contracts with defendant thereby increasing defendants' profits.'"

Thus, the California Grocers court directly disagreed with the reasoning in Perdue and Truta that the cumulative effect of many separate contracts may be relevant to a question of unconscionability. Given that the Perdue and Truta courts' cumulative effect approach has no identifiable basis in the language of Section 2-302 or the early equity cases, the position of the California Grocers court is easily more persuasive.

The California Grocers opinion also disagreed with Perdue and Truta on the question whether a large profit margin in small price tag transactions can support a determination of unconscionability. Notably, the California Grocers court expressly distinguished its facts from the Perdue case on the grounds that there was a competitive market among banks with regard to the fee in question and the defendant's fee was at "the low end" of the market. The court also distinguished Perdue on the ground that the markup in that case was in the 600 percent to 2000 percent range, whereas in California Grocers the markup was only 100 percent and still "within the range of commonly accepted notions of fair profitability." Notwithstanding these factual distinctions, the California Grocers opinion gives the unmistakable impression that the appellate court simply did not find the $3 fee to be shocking as an absolute matter.

The ultimate difficulty with the application of the unconscionability doctrine to price term cases such as Perdue, Truta, and California Grocers is the absence of any reliable basis for determining when profits become so large as to be unconscionable. The inherent subjec-

528. Id. at 403 (quoting Bennett v. Behring Corp., 466 F. Supp. 689, 698 (S.D. Fla. 1979)).

529. California Grocers, 27 Cal. Rptr. at 402-03.

530. Id. at 403. In addition to distinguishing Perdue, the court also distinguished the findings of unconscionability in Carboni as involving a 1000% markup and Jones v. Star Credit, 298 N.Y.S.2d 264 (App. Div. 1969), as involving a 300% profit margin. Id. The California Grocers court did not indicate at what point between 100% and 300% a markup might become unconscionable.

531. After referring to many of the classic definitions of unconscionability as involving terms that shock the conscience or confound common sense, the court stated that "more fundamentally, the $3 fee simply is not so exorbitant as to shock the conscience." Id. at 403.
tivity of the doctrine when applied in this manner is almost certainly what the California legislators had in mind in initially omitting Section 2-302 from the California Commercial Code. The subjectivity of such decisions is also reflected in the likelihood that trial and appellate courts in *Perdue*, *Truta*, and *California Grocers* reached differing conclusions about whether the fees charged in the particular case reached the point of being unconscionable. Moreover, if one were to accept the *Perdue* approach that relatively small fees with large profit margins become unconscionable when many people enter into similar transactions, then the possibilities for unconscionability litigation would be endless.\(^{532}\) Other jurisdictions have generally resisted such opportunities to regulate prices under Section 2-302 based on measures of profitability.\(^{533}\)

532. In *Hertz Corp. v. Attorney Gen.*, 518 N.Y.S.2d 704 (Sup. Ct. 1987), the court observed that if unconscionability could be found anytime there is great disparity between price and value as measured by the seller’s cost, then even the “local seller of fruit” could be made to answer claims of excessive prices. *Id.* at 709. A general browse through recent news reports yield many other possibilities for claims that a seller is making excessive profits in what otherwise are small price transactions. *See*, e.g., Lesley Alderman, *Shopping Around for Contact Lenses Can Be an Eye-opening Experience*, *Denver Post*, Sept. 18, 1994, at H12 (discussing common practice of optometrists and ophthalmologists to mark up contact lenses at double the price charged by discount sellers); *Consumer Reports*, Vol. 59, No. 8, Aug. 1994, at 490 (indicating that manufacturers of contact lenses may markup some lenses in excess of 400% based solely on the brand name); *Fintech Elec. Office*, Feb. 17, 1993 (discussing large profit margins made in sale of computer software generally and in European sales); Tony Kornheiser, *Mini & the Moocher*, *Wash. Post*, Sept. 25, 1994, at F1 (discussing hotel practice of imposing excessive markups on the prices of items included in in-room mini-refrigerators).

533. *See* *Merrel v. Research & Data Inc.*, 589 P.2d 120, 123 (Kan. 1979) (holding that fee charged by merchants for returned checks might be so large as to be unconscionable, but that $5 fee was modest and “not even arguably unconscionable” in light of inconvenience to merchant in handling bad checks); *Jacobs v. Citibank*, 462 N.E.2d 1182, 1183 (N.Y. 1984) (summarily rejecting claim that bank’s overdraft charges were unconscionable in the absence of any proof of a lack of meaningful choice or that the charges were “unreasonably favorable” to bank); *Hertz*, 518 N.Y.S.2d at 709-10 (rejecting claim that attorney general had authority to investigate $2.50 per day collision damage waiver charge as possibly unconscionable solely on allegation that charge greatly exceeded the cost to seller); *Best v. United States Nat’l Bank*, 739 P.2d 554, 556-57 (Or. 1987) (rejecting claim of unconscionability for insufficient funds fee of $5 on grounds, *inter alia*, that the fees were relatively small, the fees were similar to those charged by other banks, and the contract did not include a specific fee, but merely a duty to set the fee in good faith). *Cf.* *Wallace v. National Commerce Bancorporation*, 1993 WL 44600, at *3 (Tenn. Ct. App. Feb. 23, 1993) (dismissing claim of unconscionability for insufficient funds fee on ground that the doctrine may not be used to obtain affirmative relief, but refusing to dismiss claim that the fees were set in breach of duty of good faith).
Conclusion

Ultimately, the California cases present four lessons to be learned about unconscionability. First, the California decisions point to the difficulties encountered when courts lose sight of the origins of the unconscionability doctrine and become too solicitous of merchants who claim lack of bargaining power. Second, the cases warn against losing sight of the statutory dictates of Section 2-302 and second-guessing the parties on the basis of hindsight. Third, the cases suggest the general view that unconscionability can be used in only a defensive posture should be discarded. While it is true that the mere presence of unconscionability is not in itself a basis for relief, recovery in restitution or through enforcement of the remainder of the contract may be appropriate. And finally, the California decisions also warn of the problems that arise when courts become so expansive in policing for price term unconscionability that they begin to weigh when a party is making an excessive percentage of profit on a contract, or, worse yet, on many separate contracts. Ideally, the lessons from California would be instructive to its own courts, to the courts in other jurisdictions, and to those who would consider the future of Section 2-302 and the unconscionability doctrine.

The Iowa Supreme Court has stated its view of the proper application of the unconscionability doctrine:

People should be entitled to contract on their own terms without the indulgence of paternalism by courts in the alleviation of one side or another from the effects of a bad bargain. Also, they should be permitted to enter into contracts that actually may be unreasonable or which lead to hardship on one side. It is only where it turns out that one side or the other is to be penalized by the enforcement of the terms of a contract so unconscionable that no decent, fair-minded person would view the ensuing result without being possessed by a profound sense of injustice, that equity will deny the use of its good offices in the enforcement of such unconscionability. . . .

We now recognize the doctrine in law as well as equity but have accepted its limitations.534

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Similarly, Judge Posner has noted in construing Indiana law that its courts do "not conceive it to be a proper judicial function to rewrite commercial contracts entered into by fully adult, fully consenting, fully competent business people" and that the state courts have "resisted thus far the tug to a more paternalistic conception of the judicial role in enforcing contracts." The California courts have not consistently adhered to this guiding principle that unconscionability is a doctrine that should be applied sparingly. The lessons to be learned from its past unconscionability decisions hopefully will steer California to the mainstream in exercising the unconscionability doctrine, and will provide constructive insights to other courts as well.

535. Amoco Oil Co. v. Ashcraft, 791 F.2d 519, 523-24 (7th Cir. 1986).