LEGALFOXES LAW TIMES

Examining the concept of unconscionability as grounds for avoiding an agreement

What is meant by unconscionability under contracts?

Unconscionability in general parlance refers to the 'unequal bargaining power'. In relation to contracts, it deals with those contracts that weigh heavily in favour of one partyso that they are against good conscience.Such contracts are deemed unenforceable by courts due to the fact that no reasonable man would agree or give his consent to a contract which is grossly in favour of the other party and accept substantial injury/damage to himself.Free and wilful consent is one of the hallmarks of any contract to be deemed valid by the courts of law. Consent is said to be free when it is not a result of coercion, undue influence, misrepresentation,fraud or mistake.[1]

Jurisprudence put forth by a court of law is also present in order to give legal backing to the analysis of whether a contract is unconscionable or not. In the case of *Earl of Chesterfield v Janssen*[2]it was observed that *'unconscionability can be seen from the nature and subject of the bargaining itself because no man would ever willingly get into acontract that does not benefit him at all.*'

Tracing the development of the principle of unconscionability under contracts

The first inkling of the birth of this concept of unconscionability under contracts can be traced to the year 1856 in which the Supreme Court of the United States laid the foundation for this concept through the case of *Post v Jones*[3]. The relevant part of the judgment is provided hereunder:

"*The contrivance of an auction sale under such circumstances, where the master of the Richmond was hopeless, helpless, and passive -- where there was no market, no money, no competition -- where one*

[1] Section 14, Indian Contract Act, 1872
[2](1751) 28 Eng Rep 82, 100.
[3]*Post v Jones*, 60 U.S. 150 (1856)

party had absolute power and the other no choice but submission -- where the vendor must take what is offered or get nothing -- is a transaction which has no characteristic of a valid contract."[4]

This concept was then further discussed in 1942 in the case of *United States v Bethlehem Steel Corp.*[5] where the Judge minced no words while dealing with the issue of bargaining power and inequality. The relevant part of the judgment is provided hereunder:

"But is there any principle which is more familiar or more firmly embedded in the history of Anglo-American law than the basic doctrine that the courts will not permit themselves to be used as instruments of inequity and injustice? Does any principle in our law have more universal application than the doctrine that courts will not enforce transactions in which the relative positions of the parties are such that one has unconscionably taken advantage of the necessities of the other?"[6]

However, the roots of this concept were still far from being laid in the Legislative sphere. Another landmark judgment specifically dealing with unconscionability of contract was required to set the wheels in motion for the Legislature to come up with a statute to address this issue. The landmark judgment which brought about this change in Legislative intent was that of *Campbell Soup Co. v Wentz*[7] in which the court opined "*We do think, however, that a party who has offered and succeeded in getting an agreement as tough as this one is, should not come to a chancellor and ask court help in the enforcement of its terms. That equity does not enforce unconscionable bargains is too well established to require elaborate citation.*"[8]

Finally, with the passing of Section 2-302 of the Uniform Commercial Code[9] did this imperative concept of Unconscionable Contract get statutory backing. The relevant clause is reproduced here for convenience:

"2.302. Unconscionable Contract or Clause

[4] Id, p.159.
[5] *United States v Bethlehem Steel Corp.*, 315 U.S 289 (1942)
[6] Id, p.326.
[7] Campbell Soup Co v Wentz, 172 F.2d 80 (3rd Cir. 1948)
[8] Id, p.83.
[9] 2-302, Uniform Commercial Code, (1962), 20-21.

(a) If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

(b) When it is claimed or appears to the court that the contract or any clause thereof may be unconscionable the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose and effect to aid the court in making the determination."[10]

This legislation brought about much needed clarity in the US with regard to unconscionable contracts apart from acting as a guiding light to other jurisdictions such as India which had earlier been flummoxed on how to approach this point of law. A number of cases also came about dealing with this point of law such as *Williams v Walker-Thomas Furniture Co.,*[11] *Maxwell v Fidelity Financial Services, Inc.*[12]and others which also aided the jurisprudence around this concept to develop from a judicial point of view in tandem with the legislative framework which the legislation provided. The Restatement (Second) of Contract Law[13] in 1979 further added to the jurisprudence on this contentious and important issue through Section 208.

India's tryst with Unconscionable Contracts

Moving on to the Indian experience with the concept of unconscionability of contracts, it is imperative to point out the case of *Poosathurai v KannappaChettair*[14] which set out the elements for an unconscionable agreement in the Indian context and has been the guiding light with respect to this principle. It was observed in the afore-mentioned case that *"... both the elements of* ***dominant position and the unconscionable nature of the contract*** *will have to be established, before the contract can be said to be brought about by undue influence."*

However, in the initial years in India, the courts had to rely on English cases or the American standard as mentioned earlier whenever unconscionable contracts came before them. Even existing legislations like

[10] Id, p.20.
[11] *Williams v Walker-Thomas Furniture Co.,* 350 F.2d 445 (D.C. cir.1965)
[12] *Maxwell v Fidelity Financial Services Inc.,* 184 Ariz. 82 (1995)
[13] 208, Restatement (Second) of Contract Law, 1979. 28.
[14] *Poosathurai v KannappaChettair*, (1919) ILR 43 Mad 546 PC.

the Indian Contract Act, Specific Relief Act and the Indian Evidence Act did not possess requisite provisions to assist the court in these instances. Admirably this could not deter the Indian courts from passing landmark judgments dealing with this concept. Section 16(3)[15] and 23[16] of the Indian Contract Actwas used by the court for delivering judgments such as *Central Inland Water Transport Corporation Ltd. and Anr. Etc. v Brojo Nath Ganguly and Anr.*,[17]where the following was observed:

"The types of contracts to which the principle formulated in this case applies are not contracts which are tainted with illegality but are contracts which contain terms which are so unfair and unreasonable that they shock the conscience of the Court. They are opposed to public policy and required to be adjudged void."[18]

What is astonishing and commendable in this judgment is that without any established precedent or jurisprudence to rely on, the concept of Public Policy in contractual agreements was brought in. This novel principle in contracts at that point opened an avenue for the court which never existed previously. The Indian courts could now use the object of Public Policy while adjudicating upon matters concerning unconscionability of contracts before them.*"If there is no head of public policy which covers a case, then the court must in consonance with public conscience and in keeping with public good and public interest declares such practice to be opposed to public policy."*[19]

The Cons of this principle of Unconscionability

Progress with regards to the development of this field in visible in both jurisdictions which is appreciable. However, there are always two sides to a coin. Hence, there are some limitations as well as to when can unconscionability in contract can be utilized by courts when matters come up before them.

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[15]*(3) Where a person who is in a position to dominate the will of another, enters into a contract with him, and the transaction appears, on the face of it or on the evidence adduced, to be unconscionable, the burden of proving that such contract was not induced by undue influence shall be upon the person in a position to dominate the will of the other. Nothing in the sub-section shall affect the provisions of section 111 of the Indian Evidence Act, 1872 (1 of 1872).*

[16]*"23. What consideration and objects are lawful,* and *what not.—The consideration or object of an agreement is lawful, unless— —The consideration or object of an agreement is lawful, unless—" it is forbidden by law;* ***or is of such a nature that, if permitted, it would defeat the provisions of any law****; or is fraudulent; or involves or implies, injury to the person or property of another; or the Court regards it as* ***immoral****, or opposed to* ***public policy****.In each of these cases, the consideration or object of an agreement is said to be unlawful. Every agreement of which the object or consideration is unlawful is void."*

[17]*Central Inland Water Transport Corporation Ltd. v Brojo Nath Ganguly and Anr.,* 1986 AIR 1571.

[18] Id, p.65.

[19] Id, p.64.

Looking at a few case laws, a similar pattern emerges wherein courts have held '*that the role of the Courts is limited to the interpretation of the plain meaning of the contract and give effect to it, however it dislikes the result of the said plain meaning.* The cases in which the above-mentioned has been observed are*Indianapolis Morris Plan Co. v Sparks*[20]*, Central Bank of India Ltd. v Hartford Fire Insurance Co. Ltd.*[21]*, S.K. Jain v State of Haryana*[22] and *LIC of India and Anr. v Consumer Education and Research Centre and Ors. Etc.*[23]The case of SK Jain went a step further in this regard by observing"*the concept of unequal bargaining power does not apply to commercial contracts.*"[24] This holding is a massive indicator of the outlook of the courts with regard to commercial contracts which are the cornerstone of most agreements/contracts in this age of increasing globalization.

Unconscionability as means of avoiding agreements: Law Commission's recommendations

The Law Commission of India being one of the primary bodies bestowed with looking into the legal framework of the country and suggesting changes also had a few suggestions/observations pertaining to the concept of unconscionability of contracts through the 103rd[25]and the 199th[26] report. The 103rd report did not look at the issue in great detail. The only relevant outcome was that the Contract Act be amended to include the concept of unconscionability.

The 199th report was the one which gave the concept of unconscionability the kind of attention it deserved owing to the repercussions it entails in an increasingly commercialized economy. Draft Bill (2006) on Unfair Terms (Procedural and Substantive)[27] was proposed to be tabled and passed by Parliament which would serve multiple purposes. Going chronologically is the hallmark for any legislation thus, before legislating or laying down statutory guidelines, it was suggested to lay down a workable definition of 'unconscionable'. While laying down a statute subsequently, it was suggested that a cue be taken from the

[20] *Indianapolis Morris Plan Co. v Sparks,* 132 Ind. App. 145 (1961)
[21] *Central Bank of India Ltd. v Hartford Fire Insurance Co. Ltd.,* AIR 1965 SC 1288.
[22] *S.K Jain v State of Haryana,* arising out of SLP no. 21552 of 2007.
[23] *LIC of India and Anr. v Consumer Education and Research Centre and Ors. Etc.,* 1195 AIR 1811.
[24] Supra Note 26.
[25] Law Commission of India, *103rd Report on Unfair Terms in Contract*. (1984).
[26] Law Commission of India, *199th Report on Unfair (Procedural and Substantive) Terms in Contract.* (2006).
[27] Id, p.193.

United Kingdom[28] keeping in mind its experiences and the fact that most of our laws are based on the common law system laid down by the United Kingdom and spread through their process of colonization.

Conclusion

In conclusion, it would be apt to say that there has been significant and appreciable development around the concept of unconscionability in India. However, the current legislative framework does not provide the courts with the requisite statutory backing to enforce this concept of unconscionability of agreements strictly which is needed in an increasingly commercialized economy which strives to be a world leader in the near future. In this v=backdrop, it is imperative that the recommendations of the Law Commission of India are adopted and implemented to the hilt. This goal is very much achievable as can be seen through the progress which the USA and the UK have achieved in leaps and bounds till date.

[28] Id, p.150.