Consumer contracts in action

Meirav Furth-Matzkin[[1]](#footnote-1)\*

[This piece was prepared for the Browning Symposium on Consumer Law in the 21st Century, hosted by the Montana Law Review in September 25, 2020. This piece was presented in a panel on “Real Problems for Real Consumers.” I thank the Symposium editor, Ms. Kelsey Dayton, for inviting and hosting me, and the moderator, Mr. Chuck Munson, for helpful feedback and comments].

# Introduction

Scholars have long recognized that there are often significant disparities between the law on the books and the law in action. Surprisingly, however, less is known about the gaps between the formal rules and contractual arrangements that govern consumer transactions and their actual, on-the-ground implementation.

In this Essay, I will briefly survey three types of disparities that my work has so far focused on: (1) the disparities between the social reality of contracting and the law that purports to govern it; (2) the disparities between the legal protections accorded to consumers and their perceptions and understandings of these legal rights and remedies; and (3) the disparities between the written terms of consumer agreements and the ways in which they are enforced by sellers in practice.

By elucidating these gaps, I hope to enable a more nuanced understanding of the actual role that contractual language, legal rules, and other (legal and extra-legal) forces play in shaping sellers’ ongoing relations with consumers, and in promoting, or threatening consumer welfare. The primary goal of this Essay (and discussion) is to grapple with one key question: When and how should consumer contracts and markets be regulated? Ultimately, I hope that by elucidating the disparities between “contracts-in-books” and “contracts-in-action,” this research could assist policymakers in devising regulation that will improve consumer welfare in practice, rather than on paper only.

# I. Gaps Between Consumer Contracts and the Law

One of the ways in which my research examines the gap between the social reality of contracting and the law that purports to govern it is by studying the use of legally unenforceable contract terms. Although these terms contravene mandatory regulation, and are unlikely to be upheld by courts, I find that they are routinely included in various types of consumer contracts.

My first article to study unenforceable contract terms examines the prevalence of such terms in residential lease agreements.[[2]](#footnote-2) The article draws on a hand-collected sample of seventy residential lease agreements from Massachusetts. After hand-coding the leases against the mandatory rules governing landlord-tenant relations, I find that these agreements frequently contain unenforceable terms. These include, *inter alia*, overbroad liability waivers, disclaimers of the landlord’s implied warranty of habitability, unenforceable late fees or security deposit provisions (requiring higher deposit than the maximum allowed by law or imposing late fees before the minimum default time has elapsed), and clauses purporting to shift mandatory maintenance and repair duties from the landlord to the tenant.

The article also provides evidence that these unenforceable contract terms play an important role in shaping tenants’ expectations and beliefs. Using a survey of 200 residential tenants, it shows that most tenants read their residential leases, if not *ex ante*, then at the post-contract stage, when experiencing a rental problem. Furthermore, most tenants rely on these agreements as their main source of information about their rights and remedies, and often act in accordance with their signed agreements when rental disputes arise. What this suggests, I argue, is that landlords include these clauses in rental contracts because they are effective in shaping renters’ expectations and behavior, not in convincing courts.

Drawing on these findings, a following article directly tests the effects of unenforceable liability disclaimers on tenants’ behavior through a series of controlled experiments.[[3]](#footnote-3) The results reveal that after reading contracts containing unenforceable liability disclaimers, tenants are about eight times more likely to bear costs that the law imposed on the landlord than are tenants reading contracts with enforceable liability provisions. Notably, the inclusion of unenforceable terms also discourages tenants from searching online for information about their rights as renters; and the terms mislead even the minority of tenants who conduct online searches about their legal rights and remedies.

Taken together, these findings suggest that current efforts to protect consumers are inadequate, as they overly rely on consumers to discipline sellers by taking action against them if they breach the law. Yet, as long as consumers remain uninformed about the legal rules governing their relations with sellers, and rely on their contracts to ascertain their rights and remedies, they are unlikely to challenge sellers who fail to comply with these rules. I therefore discuss possible policy prescriptions, such as the imposition of statutory form contracts, in certain consumer markets (e.g., the residential rental market).

 My research on unenforceable terms has so far focused on the residential rental market. Yet, there is evidence to suggest that this drafting pattern crosses markets and borders. For example, insurance policies were found to contain prohibited coverage exclusions or restrictions;[[4]](#footnote-4) and, according to a recent report, companies continue to include provisions in their arbitration agreements that they know their arbitrators refuse to enforce.[[5]](#footnote-5) In the employment context, there is also evidence that employers often use overbroad non-compete clauses in employment contracts.[[6]](#footnote-6) In future work, I seek to investigate whether unenforceable terms are included even in highly regulated industries, in which firms are closely monitored and severely sanctioned for non-compliance with applicable regulation. Such industries include, for example, the credit card, airline, and insurance industries.

In a working paper, I currently investigate whether unenforceable terms are included in airlines’ contracts of carriage. To explore this question, I have collected 150 contracts of carriage used by certified U.S. air carriers. In this project, I intend to explore several questions that my previous work has left unresolved. For example, my work reveals that residential companies are less likely to use contracts containing unenforceable terms than private landlords (“moms and pops”). This lends support to the supposition that unenforceable terms may often be included unknowingly, in view of drafters’ ignorance of the law. Yet, could such terms be included intentionally, even in contracts used by multi-million dollars companies, to mislead consumers about their rights under the law? I hope to shed further light on this question through a series of interviews with the lawyers who draft airlines’ contracts of carriage and the regulators who supervise them.

# II. Gaps between the Law and Consumers’ Perceptions

The research on unenforceable terms illustrates that consumers are contract formalists: They believe that they will be held to whatever it is that the contract says, even when the law determines otherwise.[[7]](#footnote-7) In other words, this research demonstrates that there is often a mismatch between the legal reality governing consumer transactions and consumers’ legal perceptions and intuitions.

To further explore this gap, Michigan Law Professor Roseanna Sommers and I have conducted a series of randomized controlled experiments.[[8]](#footnote-8) We presented lab participants with scenarios in which a seller makes a representation that is later disclaimed or qualified in the contract, and the consumer signs the contract in reliance on the seller’s false representation, without reading the terms or noticing the discrepancy.

Across all experiments, we find that laypeople are contractual formalists, not only because they trust that the representations in the contracts they sign are true, but, more profoundly, because they believe that all contracts, even those induced by fraud, are legally binding.

This common intuition reflects consumers’ somewhat cynical view of the law: Even though most of the respondents in our study believed that it is unfair to hold consumers to terms they had been deceived into signing, they nonetheless assumed that the law would enforce such contractual provisions to the letter. In fact, we found that in many cases, the fact that the contract contradicts what the consumer was promised prior to signing made almost no difference to laypeople’s intuitions about whether the contract would, or should, be enforced as written. These findings hold true regardless of whether the misrepresentation was oral or written in an advertisement, and across all types of transactions.

The results lead to a troubling conclusion: Consumers may be discouraged from challenging contracts induced by fraud, because they might blame themselves for failing to read the fine print.

To mitigate the adverse effects of the interaction between fine print fraud and consumer contract formalism, regulators should consider adopting regulation aimed at educating the public (and especially lower income, less educated customers) about their legal rights and remedies, and alert consumers to the possibility that boilerplate provisions might be unenforceable, fraudulent, or void.

# III. Gaps Between the “Paper Deal” and the “Real Deal”

The third and final gap that this Essay addresses is the gap between consumer contracts on paper and their execution in practice. While researchers and policymakers continue to devote considerable attention to the formal, written terms of consumer contracts, efforts to uncover how these contracts are implemented by sellers in their ongoing interactions with consumers are surprisingly rare.

This dearth of scholarly attention is puzzling, both because of the importance of the “real deal”—the ways in which sellers actually behave in the shadow of their formal agreements—to consumers, and because in the context of business-to-business transactions, there is increasing evidence that the actual implementation of standardized agreements often differs from the “paper deal”—how these contracts appear on paper.[[9]](#footnote-9) For example, legal sociologist Stewart Macaulay already found in the 1960s that lawyers and businesspeople often diverge from their formal agreements in meaningful ways.[[10]](#footnote-10) Since then, considerable scholarly attention has been devoted to how contracting parties behave in the realm of commercial agreements,[[11]](#footnote-11) while little is known about how *consumer* contracts are applied by sellers in their relations with buyers.

Commentators have recently begun calling for “studies of consumer contracts” to shift “from looking almost exclusively at the terms of the *paper deal* to looking at the terms of the *real deal*,”[[12]](#footnote-12) suggesting that the distinction between contracts on paper and their actual implementation may also be relevant to contracts that businesses enter into with consumers.[[13]](#footnote-13) Nonetheless, to date, far too little is known about whether, when, and why sellers depart from their contracts in meaningful ways.

 My working paper on *Selective Enforcement* *of Consumer Contracts* explores the discrepancies between how consumer contracts appear on paper and how they operate on the ground through a large-scale field study of product returns.

The study uses an audit technique in which testers were sent to return non-defective goods to stores with different return policies and reported their return outcomes. The study’s main goal is to test whether sellers accept returns in circumstances in which they are not obligated to do so according to their formal policies.[[14]](#footnote-14)

I find that sellers’ enforcement of supposedly rigid, bright-line contractual provisions is, in practice, considerably more lenient and flexible than their contracts formally require. Across a wide variety of stores—both chain and local, high-end and casual—a significant percentage of sellers (22%) departed from their formal contractual requirements in favor of consumers by accepting their returns upon consumers’ initial requests, and more than one-third of the sellers (36%) relaxed their requirements once consumers complained.

These findings present a puzzle. Why would sellers often include terms in their contracts that they did not intend to enforce? Relying on interviews with store clerks, this research provides an explanation. Sellers prefer to complement rigid terms on paper with a concurrent internal policy of allowing concessions not required by the contract, rather than writing all of the contingencies into the contract and abiding by it. This approach is preferable for sellers because the existence of clear and unconditional terms on paper allows them to fend off opportunistic buyers, who would exploit more detailed (or flexible) contractual language to extract gains that the seller did not intend to offer.[[15]](#footnote-15)

The strategy of adopting a non-customer-facing policy allowing employees discretion to deviate from the “paper deal” can be seen as an attempt to meet the expectations of most good faith consumers, while preventing opportunistic buyers from taking advantage of more lenient terms on paper to extract gains that the seller did not intend to offer.

What are the implications of these “paper deal”—“real deal” disparities for consumers? On one hand, selective enforcement of consumer contracts enables good faith buyers to enjoy better treatment than that for which they originally contracted, while sellers are able to keep prices low by screening out the “bad apples” who would take advantage of a more lenient or flexible term in writing. On the other hand, consumers, to the extent that they are uninformed about sellers’ selective enforcement practices, might refrain from bringing even a just claim to the seller, because they might not realize that they may receive more than what the contract allows.

As illustrated above, consumers tend to be contract formalists, with most believing that whatever the contract says is the final word. They are thus unlikely to reach out to the seller if they erroneously believe that the seller will strictly adhere to the letter of the contract. They are even less likely to complain once the seller refers them to the contract’s clear and unconditional language. While sellers may use complaint-based segmentation benevolently in order to identify the high- value consumers, consumers might be discouraged from complaining even if they have a meritorious claim, and possibly even when their benefits from the seller’s more lenient accommodation exceed the costs to the seller of granting it.

# IV. Distributional Implications

In an ongoing work, I explore the distributional consequences of the “paper deal—real deal” gap. My hypothesis is that while the gaps between the paper deal and the real deal may not be detrimental (and in fact may prove beneficial) to certain consumers, they might adversely affect members of minority groups, as well as lower income, less educated consumers.

First, lower income, less educated consumers (or those belonging to minority groups) might have stronger formalistic intuitions about the written agreement. They might be more demoralized by the contractual fine print, and less willing to challenge it through legal or extra-legal channels. Second, marketing and social psychology research suggests that lower income consumers and minority group members typically feel less entitled and are less likely to complain than are higher income consumers or those belonging to majority groups.[[16]](#footnote-16) The former might consequently cross-subsidize higher income buyers who insist and complain. Finally, sellers themselves might use their discretion to deviate from the formal agreement in a discriminatory manner.

I have already begun collecting data to test the latter prediction. African-American and white male and female testers were sent to make non-receipted returns in 60 retail stores in Chicago. The preliminary findings suggest that there is a significant racial gap in return outcomes: African-American male testers obtain significantly worse outcomes than white males and white females, both before and after complaining to management. If these results are corroborated in future research, they might indicate that the disparities between consumer contracts on paper and in action disproportionately benefit those who are already better off.

# Conclusion

As this Essay reveals, there is still much to be discovered about the disparities between consumer contracts on paper, in action, and in the law. There is even more to be learned about the implications of these disparities for consumers and for social welfare. This Essay calls scholars and policymakers to move from focusing almost entirely on the terms of the “paper deal” to looking more critically at the contract in action.

1. \* Associate Professor of Law, University of California Los-Angeles School of Law. This Essay draws on the results of my recent and forthcoming work. The studies reported in this Essay were presented in the following publications: Meirav Furth-Matzkin, *On the Unexpected Use of Unenforceable Contract Terms: Evidence from the Residential Rental Market*, 9 J. Legal Anal. 1 (2017); Meirav Furth-Matzkin, *The Harmful Effects of Unenforceable Contract Terms: Experimental Evidence*, 4 Ala. L. Rev. 1032 (2019); and Meirav Furth-Matzkin & Roseanna Sommers, *Consumer Psychology and the Problem of Fine-Print Fraud*, 72 Stan. L. Rev. 503 (2020). I am especially thankful to Ms. Kelsey Dayton for overseeing Symposium and this Essay’s publication in the Montana Law Review, and to the moderator, Mr. Chuck Munson, for engaging with this piece. [↑](#footnote-ref-1)
2. Meirav Furth-Matzkin, *On the Unexpected Use of Unenforceable Contract Terms: Evidence from the Residential Rental Market*, 9 J. Legal Anal. 1 (2017). [↑](#footnote-ref-2)
3. Meirav Furth-Matzkin, *The Harmful Effects of Unenforceable Contract Terms: Experimental Evidence*, 4 Ala. L. Rev. 1032 (2019). [↑](#footnote-ref-3)
4. *See, e.g.,* Robert L. Tucker, *Disappearing Ink: The Emerging Duty to Remove Invalid Policy Provisions*, 42 Akron L. Rev. 519, 523-24 (2009). [↑](#footnote-ref-4)
5. *See* Jeff Sovern, *Report that Companies Include Provisions in Arbitration Clause that They Know the Arbitrator Won’t Enforce—But that Might Suppress Claims Even More*, PUBLIC CITIZEN: CONSUMER LAW & POLICYBLOG (Mar. 8, 2018), http://pubcit.typepad.com/clpblog/2018/03/report-that-companies-include-provisions-in-arbitration-clause-that-they-know-the-arbitrator-wont-en.html. [↑](#footnote-ref-5)
6. *See, e.g.,* Evan Starr, J.J. Prescott & Norman Bishara, *Noncompetes in the U.S. Labor Force* (Univ. of Mich. Law & Econ., Research Paper No. 18–013, 2019), https://papers.ssrn.com/sol3/papers.cfm?abstract\_id=2625714 (finding that noncompetition clauses are surprisingly common even in states that do not enforce them). [↑](#footnote-ref-6)
7. Previous research has also documented consumers’ formalistic intuitions about contracts. *See, e.g.*, Tess Wilkinson-Ryan, *Intuitive Formalism in Contract*, 163 U. Pa. L. Rev. 2109 (2015); Tess Wilkinson-Ryan & David A. Hoffman, *The Common Sense of Contract Formation*, 67 Stan. L. Rev. 1269, 1281–98 (2015) (finding that laypeople put excessive weight on written terms compared to oral agreements, believe that contracts are formed primarily through formalities such as signature and payment, even though contract law does not require such formalities for a contract to be formed, and feel generally obligated to abide by terms that follow formalized assent processes); Yuval Feldman & Doron Teichman, *Are All Contractual Obligations Created Equal?*, 100 Geo. L.J. 5, 5 (2012) (showing that laypeople feel they are bound to the signed contract). [↑](#footnote-ref-7)
8. The results of these experiments are reported in our article. See Meirav Furth-Matzkin & Roseanna Sommers, *Consumer Psychology and the Problem of Fine-Print Fraud*, 72 Stan. L. Rev. 503 (2020). [↑](#footnote-ref-8)
9. I borrow the terms “paper deal” and “real deal” from Stewart Macaulay, who used these terms in his work on divergences between formal agreements and their actual implementation in business-to-business transactions. *See, e.g.*,Stewart Macaulay, *The Real and the Paper Deal: Empirical Pictures of Relationships, Complexity and the Urge for Transparent Simple Rules*, 66 Mod. L. Rev. 44, 79 (2003); Stewart Macaulay & William Whitford, *The Development of Contracts: Law in Action*, 87 Temple L. Rev. 793 (2014). [↑](#footnote-ref-9)
10. Stewart Macaulay, *Non-Contractual Relations in Business: A Preliminary Study*, 28 Am. Soc. Rev. 55 (1963). [↑](#footnote-ref-10)
11. *See e.g.*,Charles J. Goetz & Robert E. Scott, *Principles of Relational Contracts*, 67 Va. L. Rev. 1089 (1981); Lisa Bernstein, *Merchant Law in a Merchant Court: Rethinking the Code’s Search for Immanent Business Norms*, 144 U. Pa. L. Rev. 1765, 1787–88 (1996) (showing that “sophisticated merchant-transactors” often depart from official terms of agreements because of social norms, commercial custom, trust, or fear of non-legal sanctions, such as reputational damages); Lisa Bernstein, *Private Commercial Law in the Cotton Industry: Creating Cooperation Through Rules, Norms, and Institutions*, 99 Mich. L. Rev. 1724 (2001); Robert C. Ellickson, Order Without Law (1994) (studying how disputes are resolved in the cattle industry). [↑](#footnote-ref-11)
12. *See* Lisa Bernstein & Hagay Volvovsky, *Not What You Wanted to Know: The Real Deal and the Paper Deal in Consumer Contracts: Comment on the Work of Florencia Marotta-Wurgler*, 12 Jrsl. Rev. Legal Stud. 128, 129 (2015). [↑](#footnote-ref-12)
13. *See e.g.*,Lucian A. Bebchuk & Richard A. Posner, *One-Sided Contracts in Competitive Consumer Markets*, 104 Mich. L. Rev. 827, 828 (2006). [↑](#footnote-ref-13)
14. A preliminary question is whether return policies are legally binding contracts, given that they are typically presented on the back of the receipt, or on the store’s “terms and conditions” webpage, and are not always displayed on an in-store sign that the consumer can review prior to purchase. “Pay-now-terms-later” or “shrink wrap” agreements are generally recognized as legally binding contracts, as long as the consumer had a reasonable opportunity to cancel the transaction after the terms were made available for review. *See, e.g.*, ProCD, Inc. v. Zeidenberg 86 F. 3d 1447 (7th Cir. 1996); Bischoff v. DirectTV, Inc., 180 F. Supp. 2d 1097, 1101 (C.D. Cal. 2002); Brower v. Gateway 2000, Inc., 676 N.Y.S.2d 569, 572 (N.Y. App. Div. 1998); M.A. Mortenson Co. v. Timberline Software Corp., 998 P.2d 305, 308 (Wash. 2000). [↑](#footnote-ref-14)
15. Similar predictions were made by few scholars in the past, without any meaningful empirical investigation. *See, e.g.*, Bebchuk & Posner, at 827–28 (“A seller concerned about its reputation can be expected to treat consumers better than is required by the letter of the contract.”); Clayton P. Gillette, *Rolling Contracts as an Agency Problem*, 2004 Wis. L. Rev. 679, 704–12 (2004) (suggesting that sellers may use a “contract clause that assigns an entitlement to the seller” to protect themselves from consumer misbehavior); Jason Scott Johnston, *The Return of Bargain: An Economic Theory of How Standard-Form Contracts Enable Cooperative Negotiation between Businesses and Consumers*, 104 Mich. L. Rev. 857, 858 (2006); Shmuel I. Becher & Tal Z. Zarsky, *Minding the Gap*, 51 Conn. L. Rev. 69 (2019). [↑](#footnote-ref-15)
16. *See, e.g.,* Vincent C. S. Heung & Terry Lam*, Customer complaint behavior towards hotel restaurant services*, 14 Int’l J. of Contemporary Hospitality management 283 (2003); Paul K. Piff, *Wealth and the Inflated Self: Class, Entitlement and Narcissism*, 40 Personality & Soc. Psych. Bulletin 34 (2014) (demonstrating that higher socioeconomic class status is associated with higher levels of entitlement). [↑](#footnote-ref-16)