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## THEY CAN DO WHAT!? LIMITATIONS ON THE USE OF CHANGE-OF-TERMS CLAUSES

Peter A. Alces\* and Michael M. Greenfield†

### INTRODUCTION

Contract is based on intent, specifically the intent to consent to some adjustment of rights and risk in exchange for a *quid pro quo*. We determine the enforceability of that allocation of rights and risk at the outset of the parties' undertaking. That is, whether a transaction is a contract, an enforceable promise, is determined by reference to the parties' exchange *ab initio*. We could not brook a contract law that accommodated the parties' weaving in and out of a contract as the vicissitudes of their transactional interests and positions changed over time. It is significant that contract *fixes* risk after it first allocates it.

Contract too is a supple device, and therein lies the source of some of its greatest value in the course of exchanges. The certain initial allocation of risk is leavened by the law's ability to accommodate the parties' interests in flexibility. Although there are gains to be realized from certainty, there are also benefits to reserving the ability to adjust the initial allocation of rights and responsibilities in order for both parties to capture as many benefits of exchange as they can. And that vindication of flexibility need not result in a zero-sum game. Even the weaker contracting party *may* benefit from contract doctrine that permits the stronger contracting party to effect adjustments in the initial allocation as changing circumstances warrant. So long as the dominant party is able to extricate itself from an allocation of risk that becomes less attractive, that dominant party is more likely to enter into the contract in the first place, or so the story goes.

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But there is another side to the story. Contracts are relational<sup>1</sup> and give rise to expectations between the parties. During the course of the contractual relationship, the parties may make investments based on those expectations and the initial allocation of rights and risk. If the dominant party then adjusts that allocation, no matter how good the reason, the weaker party may be profoundly prejudiced by the adjustment. That prejudice is not mitigated significantly by the fact that the contract explicitly reserved the dominant party's right to adjust the initial allocation as circumstances, or simply the dominant party's interests, dictate. So the provision of a unilateral right to amend the terms of a contract rests uneasily with fundamental assumptions about the nature of contract liability as well as, perhaps, with contract doctrine. There is a tension for the law to resolve, and the tools—viz., contract doctrine—available to resolve that tension may not be up to the task; they may lack the ability to refine the balance in ways that can resolve the tension between certainty and flexibility that contract law vindicates.

Although the phenomenon of unilateral adjustment of contract terms is not a new one,<sup>2</sup> the uneasy fit between the dominant party's

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1. Ian Macneil defines the relational contract theory:

A relational contract theory may be defined as any theory based on the following four core propositions:

First, every transaction is embedded in complex relations.

Second, understanding any transaction requires understanding all essential elements of its enveloping relations.

Third, effective analysis of any transaction requires recognition and consideration of all essential elements of its enveloping relations that might affect the transaction significantly.

Fourth, combined contextual analysis of relations and transactions is more efficient and produces a more complete and sure final analytical product than does commencing with non-contextual analysis of transactions. For purposes of this Article, relational contract theory means these four propositions, nothing more and nothing less.

Ian R. Macneil, *Relational Contract Theory: Challenges and Queries*, 94 NW. U. L. REV. 877, 881–82 (2000). Ian Macneil is the leading relational contract theory scholar. For elaboration on the relational contract theory, see also Ian R. Macneil, *Contracting Worlds and Essential Contract Theory*, 9 SOC. & LEGAL STUD. 431 (2000); Ian R. Macneil, *Contracts: Adjustment of Long-Term Economic Relations Under Classical, Neoclassical, and Relational Contract Law*, 72 NW. U. L. REV. 854 (1978); Ian R. Macneil, *Economic Analysis of Contractual Relations: Its Shortfalls and the Need for a "Rich Classificatory Apparatus,"* 75 NW. U. L. REV. 1018 (1981).

2. See, e.g., *Bakery & Confectionery Workers' Int'l Union v. Nat'l Biscuit Co.*, 177 F.2d 684, 688 (3d Cir. 1949) (upholding actions taken pursuant to a change-of-terms provision regarding pensions in employment contract); *Badie v. Bank America*, 79 Cal. Rptr. 2d 273, 278 (Cal. Ct. App. 1998) (expert

ability to change terms and the weaker party's interest in the certainty and enforceability of the original terms has come into particularly stark relief as the fabric of consumer transactions is strained during challenging economic times. It is one thing to become upset with your credit card issuer and pay off the card by accessing your equity line; it is quite another when you become upset with your credit card issuer at a time in which the available credit on your equity line is reduced to the point that you cannot pay off and walk away from the credit card issuer. So once you lose the *ability* to walk away from new, less attractive terms, the *right* to do so is illusory.

This article will survey the numerous contexts in which one party reserves the right to unilaterally adjust the terms of a continuing contract, perhaps subject to the other party's right to terminate the contractual relationship.<sup>3</sup> Our focus is on contracts that endeavor to fix the terms of the parties' deal across a series of interactions, rather than discrete but recurring transactions in which one party reserves the right to change terms in succeeding contracts. We have found examples of unilateral change-of-terms provisions in a range of consumer contracting settings including, perhaps most notably, credit cards, the subject of recent federal legislation designed to curb overreaching by card issuers.<sup>4</sup> Not surprisingly, banks also typically

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testified that "including a change-of-terms provision in account agreements ha[s] been the industry practice [in the credit card industry] since bank credit cards first became available in the 1960's"; *Automatic Vending Co. v. Wisdom*, 6 Cal. Rptr. 31, 33 (Cal. Dist. Ct. App. 1960) (finding contract and unilateral rate changes enforceable because of good faith obligation bestowed upon modifying party); *State v. San Francisco Sav. & Loan Soc'y*, 225 P. 309, 311–12 (Cal. Dist. Ct. App. 1924) (holding that depositors that signed an agreement with a bank which allowed the bank to change its bylaws at a later time were not bound to amendments eliminating the payment of interest on dormant accounts); *Krupp v. Franklin Sav. Bank*, 255 A.D. 15, 17 (N.Y. App. Div. 1938) (finding amendments to be binding on the consumer automatically because of "the express agreement between the parties to abide by amended by-laws").

3. The UCC distinguishes between "termination" and "cancellation." "'Termination' occurs when either party pursuant to a power created by agreement or law puts an end to the contract otherwise than for its breach. On 'termination' all obligations which are still executory on both sides are discharged but any right based on prior breach or performance survives." U.C.C. § 2-106(3) (2002). "Cancellation," on the other hand, "occurs when either party puts an end to the contract for breach by the other and its effect is the same as that of 'termination' except that the cancelling party also retains any remedy for breach of the whole contract or any unperformed balance." U.C.C. § 2-106(4) (2002).

4. On May 24, 2009, President Obama signed legislation designed to regulate credit card companies' ability to alter terms of contracts. The Credit Card Accountability Responsibility and Disclosure Act restricts credit card companies' ability to unilaterally increase interest rates. Credit Card

include unilateral change-of-terms provisions in their account agreements, though this is not limited to the consumer setting.<sup>5</sup> Similarly, providers of utility and utility-like services include unilateral change-of-terms provisions in their consumer agreements. We have found them in contracts for telephone service (both land-line<sup>6</sup> and cellular<sup>7</sup>), and television service (both cable<sup>8</sup> and satellite<sup>9</sup>).

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Accountability Responsibility and Disclosure Act of 2009, Pub. L. No. 111-24, 123 Stat. 1734-66 (2009).

5. *E.g.*, Bank of America Online Banking Service Agreement, [http://www.bankofamerica.com/onlinebanking/index.cfm?template=service\\_agreement&statecheck=VA#4h](http://www.bankofamerica.com/onlinebanking/index.cfm?template=service_agreement&statecheck=VA#4h) (last visited Mar. 2, 2010) (“We may change this agreement at any time. For example, we may add, delete or amend terms or services. We will notify you of such changes by mail or electronic message. If you initiate any transfer of funds or bill payment through your Online Banking services or make any Transfers Outside Bank of America after the effective date of a change, you indicate your agreement to the change.”); Schwab Bank Savings Account Application Agreement, [http://www.schwab.com/cms/P-2887295.3/APP44939\\_02\\_WB.pdf?cmsid=P-2887295&cv0](http://www.schwab.com/cms/P-2887295.3/APP44939_02_WB.pdf?cmsid=P-2887295&cv0) (last visited Mar. 2, 2010) (“We may add, delete, or amend terms or services at any time, including fees and charges for the Service. We will notify you of such changes by mail, email, by posting a notice of a change online, or by any other means permitted by law. Use of the Service after the effective date of the change will constitute your acceptance of such amendment.”).

6. *E.g.*, Vonage Terms of Service, <http://www.vonage.com/tos/#CHANGES> (last visited Mar. 2, 2010) (“We may change the terms and conditions of this agreement from time to time. By subscribing to our service, you agree that we may provide to you by use of electronic communications required notices, agreements, and other information concerning Vonage, including changes to this agreement.”).

7. *E.g.*, AT&T Wireless Service Agreement, <http://www.wireless.att.com/learn/articles-resources/wireless-terms.jsp> (last visited Mar. 2, 2010) (“You can accept the Service Agreement in several different ways: (i) by giving us your electronic signature via our website; (ii) by giving us your electronic signature over the phone through our automated phone consent process; (iii) by signing an electronic signature pad; (iv) in certain third party retail locations, by giving us your written signature; or (v) *by using the wireless service after a modification to your service if you have been informed that continued use of the new service will mean you’ve given us your acceptance.*”) (emphasis added); Sprint.com Visitor Agreement and Acceptable Use Policy, <http://www.sprint.com/legal/agreement.html> (last visited Mar. 2, 2010) (“We reserve the right to modify this Policy and Agreement at any time, effective upon its posting, as modified, on [www.sprint.com](http://www.sprint.com). You agree to the Policy and Agreement by accessing or using our Website, products or services, or by sending any electronic transmission through our Network.”); Verizon Wireless Customer Agreement: [http://www.verizonwireless.com/b2c/globalText?textName=CUSTOMER\\_AGREEMENT&jspName=footer/customerAgreement.jsp](http://www.verizonwireless.com/b2c/globalText?textName=CUSTOMER_AGREEMENT&jspName=footer/customerAgreement.jsp) (last visited Mar. 2, 2010) (“We may change prices or any other term of your Service or this agreement at any time, but we’ll send you written notice first. If you use your Service after the change takes effect, that means you’re accepting the change. But if a change to your Plan or this agreement has a material adverse effect on you, you can cancel the line of Service that has been affected within 60 days of receiving the notice with no early termination fee.”).

8. *E.g.*, Comcast Subscriber Agreement, <http://www.comcast.net/terms/subscriber/> (last visited Mar. 2, 2010) (“We may change our prices, fees, the Services and/or the terms and conditions of this Agreement in the future. Unless this Agreement or applicable law specifies otherwise, we will give you thirty (30) days prior Notice of any significant change to this Agreement. If you find the change unacceptable, you have the right to cancel your Service(s). However, if you continue to receive Service(s) after the end of the notice period (the ‘Effective Date’) of the change, we will consider that you have accepted the changes. You may not modify this Agreement by making any typed, handwritten,

Insofar as other utilities are regulated by governmental entities, and the terms of their contracts with consumers not the subject of individual negotiation,<sup>10</sup> there does not seem to be the same recourse to the unilateral change-of-terms provision, which might be telling in itself.<sup>11</sup> Other consumer contexts in which the dominant party retains the right to unilaterally change the terms of the contract include investment services,<sup>12</sup> on-line retailers,<sup>13</sup> customer loyalty reward

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or any other changes to it for any purpose.”); Cox Communications Policies, [https://www.cox.com/policy/#Online\\_Privacy\\_Policy](https://www.cox.com/policy/#Online_Privacy_Policy) (last visited Mar. 2, 2010) (“Cox reserves the right to modify the terms of this Agreement or prices for the Service and may discontinue or revise any or all other aspects of the Service in its sole discretion at any time by posting changes online. Your continued use of the Service after changes are posted constitutes your acceptance of this Agreement as modified by the posted changes. The updated, online version of this Agreement shall supersede any prior version of this Agreement that may have been included in any software or related materials provided by Cox.”); Time Warner Cable Residential Services Subscriber Agreement, [http://help.twcable.com/html/twc\\_sub\\_agreement2.html](http://help.twcable.com/html/twc_sub_agreement2.html) (last visited Mar. 2, 2010) (“TWC has the right to add to, modify, or delete any term of this Agreement, the Terms of Use, the Subscriber Privacy Notice or any applicable Tariff(s) at any time. An online version of this Agreement, the Terms of Use, the Subscriber Privacy Notice and any applicable Tariff(s), as so changed from time to time, will be accessible at <http://help.twcable.com/html/policies.html> or another online location designated by TWC, or can be obtained by calling my local TWC office.”).

9. *E.g.*, Direct TV Customer Agreement, <http://www.directv.com/DTVAPP/global/contentPage.jsp?assetId=P400042> (last visited Mar. 2, 2010) (“We reserve the right to change the terms and conditions on which we offer Service. If we make any such changes, we will send you a copy of your new Customer Agreement containing its effective date. You always have the right to cancel your Service, in whole or in part, at any time, and you may do so if you do not accept any such changed terms or conditions . . . If you elect not to cancel your Service after receiving a new Customer Agreement, your continued receipt of Service constitutes acceptance of the changed terms and conditions.”); Dish Network Residential Customer Agreement, <http://www.dishnetwork.com/downloads/legal/RCA.pdf> (last visited Mar. 2, 2010) (“If you are an existing Dish Network customer, we will notify you of any changes to, or

Replacement of, this agreement, and your continued receipt of Dish Network services or equipment following receipt of such notice shall constitute your acceptance of such changed or replaced agreement. If you are an existing customer and do not wish to accept any changed or replaced agreement, you must notify us immediately and we will, at our option, either cancel your service or allow you to continue to receive your services under the previous version of this agreement”) (text in all caps in original).

10. For example, the Federal Power Act regulates the transmission and sale of electric energy to the public. 16 U.S.C. § 824 (2005). In addition the Natural Gas Act regulates natural gas companies. 15 U.S.C.S. § 717 (2005).

11. *E.g.*, *Fed. Power Comm’n v. Sierra Pac. Power Co.*, 350 U.S. 348 (1956) (holding that the Federal Power Act does not authorize unilateral contract changes); *United Gas Pipe Line Co. v. Mobile Gas Serv. Corp.*, 350 U.S. 332, 337 (1956) (“[T]he Natural Gas Act does not give natural gas companies the right to change their rate contracts by their own unilateral action.”).

12. *E.g.*, E\*Trade Account Agreement, <https://us.etrade.com/e/t/prospectestation/help?id=1209021000> (last visited Mar. 2, 2010) (“Change in Terms/Termination of Service. We may change (add to, delete or amend) the terms or terminate your use of our electronic fund transfer services at any time, with or without cause and without affecting your outstanding obligations under this Agreement. We may terminate or suspend your electronic fund transfer service immediately if: any of

programs,<sup>14</sup> and various other providers of computer community services.<sup>15</sup> Such change-of-terms provisions are also found in

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you breach this or any other agreement with us; we have reason to believe that there has been or may be an unauthorized use of your account, Card or PIN; there are conflicting claims to the funds in your account; or any of you requests that we do so. If you ask us to terminate your account or the use of any Card, you will remain liable for subsequent transactions performed by you or any authorized user.”); Schwab One Brokerage Account, <https://investing.schwab.com/public/file?cmsid=P-221707> (last visited Mar. 2, 2010) (“In addition, you may in the future receive from Schwab supplemental terms or disclosures that pertain to certain account types, service features and benefit packages. These supplemental terms and disclosures, this Application Agreement and the Schwab One Account Agreement are collectively referred to as the ‘Agreement and Disclosures.’ You agree to read the Agreement and Disclosures carefully and retain copies for your records.”).

13. *E.g.*, Amazon.com Conditions of Use, [http://www.amazon.com/gp/help/customer/display.html?ref=footer\\_cou?ie=UTF8&nodeId=508088](http://www.amazon.com/gp/help/customer/display.html?ref=footer_cou?ie=UTF8&nodeId=508088) (last visited Mar. 2, 2010) (“We reserve the right to make changes to our site, policies, and these Conditions of Use at any time. If any of these conditions shall be deemed invalid, void, or for any reason unenforceable, that condition shall be deemed severable and shall not affect the validity and enforceability of any remaining condition.”); BarnesandNoble.com Terms and Conditions of Use, [http://www.barnesandnoble.com/include/terms\\_of\\_use.asp](http://www.barnesandnoble.com/include/terms_of_use.asp) (last visited Mar. 2, 2010) (“Barnes & Noble.com reserves the right to make changes to the Barnes & Noble.com Site, posted policies and Terms of Use at any time without notice or liability.”); Blockbuster Online Terms and Conditions, <http://www.blockbuster.com/corporate/termsAndConditions> (last visited Mar. 2, 2010) (“Blockbuster may at any time, and at its sole discretion, modify these Terms and Conditions of Use, including without limitation the Privacy Policy, with or without notice. Such modifications will be effective immediately upon posting. You agree to review these Terms and Condition of Use periodically and your continued use of this Site following such modifications will indicate your acceptance of these modified Terms and Conditions of Use. If you do not agree to any modification of these Terms and Conditions of Use, you must immediately stop using this Site.”); Netflix Terms of Use, <http://www.netflix.com/TermsOfUse> (last visited Mar. 2, 2010) (“Netflix, Inc., reserves the right, from time to time, with or without notice to you, to change these Terms of Use in our sole and absolute discretion. The most current version of these Terms of Use can be reviewed by clicking on the “Terms of Use” located at the bottom of the pages of the Netflix website. The most current version of the Terms of Use will supersede all previous versions. You can see changes from previous versions of the Terms of Use by clicking here.”).

14. *E.g.*, Jet Blue Airlines Contract of Carriage, [http://www.jetblue.com/p/jetblue\\_coc.pdf](http://www.jetblue.com/p/jetblue_coc.pdf) (last visited Mar. 2, 2010) (“Carrier reserves the right, to the extent not prohibited by federal law, to change, delete, or add to any of the terms of this Contract without prior notice. All changes must be in writing and must be available for public inspection at each of the Carrier’s ticket offices. To the extent there is a conflict between the Contract of Carriage and the Itinerary, AskBlue, or other publications, the Contract of Carriage governs.”); Orbitz.com Terms and Conditions, <http://www.orbitz.com/pagedef/content/legal/terms05.jsp?popupsDisabled=false> (last visited Mar. 2, 2010) (“We may modify, revise or update these Terms and/or the Privacy Policy, at any time, by updating this posting. You should visit this page from time to time to review the then-current Terms, because they are binding on you. Your continued use of our site, following the posting of conspicuous notice of any modification, will be subject to the Terms in effect at the time of your use. Certain provisions of these Terms may be superseded by expressly designated legal notices or terms located on particular pages of this Site.”).

15. *E.g.*, Craigslist.com Terms of Use, <http://www.craigslist.org/about/terms.of.use> (last visited Mar. 2, 2010) (“We reserve the right, at our sole discretion, to change, modify or otherwise alter these terms and conditions at any time. Such modifications shall become effective immediately upon the posting thereof. You must review this agreement on a regular basis to keep yourself apprised of any changes. You can find the most recent version of the TOU at: <http://www.craigslist.org/about/terms.of.use.html>.”); Ebay.com User Agreement, <http://pages.ebay.com/help/policies/user->

contracts for the sale of new cars.<sup>16</sup> In the event that the manufacturer

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agreement.html (last visited Mar. 2, 2010) ("We may amend this Agreement at any time by posting the amended terms on this site. Except as stated elsewhere, all amended terms shall automatically be effective 30 days after they are initially posted. Additionally, we will notify you through the eBay Message Center. This Agreement may not be otherwise amended except in a writing hand signed by you and us. For purposes of this provision, a 'writing' does not include an email message and a signature does not include an electronic signature."); Facebook.com Statement of Rights and Responsibilities, <http://www.facebook.com/terms.php?ref=pf> (last visited Mar. 2, 2010) ("We can change this Statement if we provide you notice (by posting the change on the Facebook Site Governance Page) and an opportunity to comment To get notice of any future changes to this Statement, visit our Facebook Site Governance Page and become a fan."); Google.com Terms of Service, <http://www.google.com/accounts/TOS> (last visited Mar. 2, 2010) ("Google may make changes to the Universal Terms or Additional Terms from time to time. When these changes are made, Google will make a new copy of the Universal Terms available at <http://www.google.com/accounts/TOS?hl=en> and any new Additional Terms will be made available to you from within, or through, the affected Services."); MySpace.com Terms of Use Agreement, <http://www.myspace.com/index.cfm?fuseaction=misc.terms> (last visited Mar. 2, 2010) ("MySpace reserves the right to modify this Agreement at any time and from time to time, and each such modification shall be effective upon posting on the MySpace Services. All material modifications will apply prospectively only. Your continued use of the MySpace Services following any such modification constitutes your agreement to be bound by and your acceptance of the Agreement as so modified. It is therefore important that you review this Agreement regularly. If you do not agree to be bound by this Agreement and to abide by all Applicable Law, you must discontinue use of the MySpace Services immediately. You may receive a copy of this Agreement by contacting us at our Help site."); Netflix Terms of Use, <http://www.netflix.com/TermsOfUse> (last visited Mar. 2, 2010) ("Netflix, Inc., reserves the right, from time to time, with or without notice to you, to change these Terms of Use in our sole and absolute discretion. The most current version of these Terms of Use can be reviewed by clicking on the 'Terms of Use' located at the bottom of the pages of the Netflix website. The most current version of the Terms of Use will supersede all previous versions. You can see changes from previous versions of the Terms of Use by clicking here."); PayPal User Agreement, <http://www.paypal.com/cgi-bin/webscr?cmd=xpt/UserAgreement/ua/USUA-outside> (last visited Mar. 2, 2010) ("We may amend this Agreement at any time by posting a revised version on our website. The revised version will be effective at the time we post it. In addition, if the revised version includes a Substantial Change, we will provide you with 30 Days' prior notice of Substantial Change by posting notice on the 'Policy Updates' page of our website."); Twitter Terms of Service, <http://twitter.com/tos> (last visited Mar. 2, 2010) ("We may revise these Terms from time to time, the most current version will always be at [twitter.com/tos](http://twitter.com/tos). If the revision, in our sole discretion, is material we will notify you via an @Twitter update or e-mail to the email associated with your account. By continuing to access or use the Services after those revisions become effective, you agree to be bound by the revised Terms."); Xbox Live and Games for Windows Live Terms of Use, <http://www.xbox.com/en-US/legal/LiveTOU.htm> (last visited Mar. 2, 2010) ("If we change this contract, then we will require you to agree to a new contract that includes such changes if you want to continue to receive the Service. If you do not want to agree to the new contract, you may cancel the Service. Your continued use of the Service will be deemed acceptance of and agreement to the new contract."); YouTube Terms of Service, <http://www.youtube.com/t/terms> (last visited Mar. 2, 2010) ("YouTube reserves the right to amend these Terms of Service at any time and without notice, and it is your responsibility to review these Terms of Service for any changes. Your use of the YouTube Website following any amendment of these Terms of Service will signify your assent to and acceptance of its revised terms.").

16. See, e.g., *Zeno v. Ford Motor Co.*, 238 F.R.D. 173, 182 (W.D. Pa. 2006) (contract terms stated: "Manufacturer has reserved the right to change the design of any new motor vehicle, chassis, accessories or parts thereof previously purchased by or shipped to Dealer or being manufactured or sold in accordance with Dealer's orders. Correspondingly, in the event of any such change by Manufacturer,



raises the price of a car that the consumer has had to order through the retailer, the retailer may pass along any price increase imposed on the retailer by the manufacturer.<sup>17</sup>

Perhaps the context in which the dominant party's reservation of the right to change terms has been most notorious is the employment-at-will setting. Employers' efforts to adjust the terms of the employment "contract" have been subject to judicial review on familiar contract law terms. Such litigation has arisen, for example, when the employer seeks to adjust retirement benefits,<sup>18</sup> bonus plans,<sup>19</sup> or commission rates.<sup>20</sup>

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Dealer shall have no obligation to Buyer to make the same or any similar change in any motor vehicle, chassis, accessories or parts thereof covered by this Order either before or subsequent to delivery thereof to Buyer."); *Samuels v. King Motor Co.*, 782 So. 2d 489, 493 (Fla. Dist. Ct. App. 2001) (buyer order contained the provision: "Manufacturer has reserved the right to change the price to Dealer of new motor vehicles without notice. In the event the price to Dealer of new motor vehicles of the series and body type ordered hereunder is changed by Manufacturer prior to delivery of the new motor vehicle ordered hereunder to Purchaser, Dealer reserves the right to change the price of unit of such motor vehicle to purchaser accordingly.").

17. See, e.g., *Samuels*, 782 So. 2d at 493; GM Special Vehicle Manufacturer Converters Agreement, <http://agreements.realdealdocs.com/Manufacturing-Agreement/SPECIAL-VEHICLE-MANUFACTURER-CONVERTERS-2314980/> (last visited Mar. 2, 2010) ("Prices and other terms of sale applicable to Vehicles are those set forth in GM Pricing.com. Such prices may be changed by GM at any time.").

Unilateral change-of-terms provisions also appear in non-consumer contracts, even beyond the banking context. The legal research services, LexisNexis and Westlaw, reserve the right to unilaterally change the terms of their contracts with subscribers. See LexisNexis Terms and Conditions of Use, <http://www.lexisnexis.com/terms/> (last visited Mar. 2, 2010) ("Modifications to Terms of Use. Provider reserves the right to change these Terms of Use at any time. Updated versions of the Terms of Use will appear on this Web Site and are effective immediately. You are responsible for regularly reviewing the Terms of Use. Continued use of this Web Site after any such changes constitutes your consent to such changes."); Westlaw Terms of Use, <http://west.thomson.com/about/terms-of-use/default.aspx> (last visited Mar. 2, 2010) ("All use of this website, including all content, information, and services provided on this website, is subject to the following terms of use ('Terms'), which constitute a legal agreement between you and West. By accessing, browsing, or using this website, you acknowledge that you have read, understood, and agree to be bound by these Terms. We may update these Terms at any time, without notice to you. Each time you access this website, you agree to be bound by the Terms then in effect.").

18. See, e.g., *Bakery & Confectionery Workers' Int'l Union v. Nat'l Biscuit Co.*, 177 F.2d 684, 688 (3d Cir. 1949) (upholding defendant's actions that were pursuant to contract which included provisions, such as, "The company . . . reserves the right to modify, cancel or terminate [the retirement] plan or any part thereof at any time, which right shall include the right to cancel, terminate or decrease pensions already granted . . .").

19. See, e.g., *Isla Verde Hotel Corp. v. Nat'l Labor Relations Bd.*, 702 F.2d 268, 269 (1st Cir. 1983) (holding unilaterally canceling Christmas bonus violated the National Labor Relations Act); *Nat'l Labor Relations Bd. v. Downtown Bakery Corp.*, 330 F.2d 921 (6th Cir. 1964).

In this article we consider the operation of unilateral change-of-terms provisions in the context of consumer protection legislation, commercial legislation generally, and the common law of contract. There is something about such terms that rankles. It seems as though the mechanics of contract—provision of a term to which the parties ostensibly “agree”—are being manipulated to take advantage of the fact that standard-form contractual documents, pretty much by definition, *are* irrational to read.<sup>21</sup> Typical unilateral change-of-terms clauses are generally buried in the boilerplate of form “agreements” that the weaker contracting party could not understand even if she were disposed to read it and, therefore, it would be irrational for her to read it. Further, the argument that somehow the terms of such forms are policed by the marketplace has been cast into doubt because it is unwise to undermine the consensual nature of contract with fictions that would rely on dubious economic analysis.<sup>22</sup>

So, in response to the apparent acceptance of the now-ubiquitous unilateral change-of-terms clauses, we offer an overview of their use and something of a primer for courts to consider in ruling on the enforceability of the clauses and the changes made pursuant to them.<sup>23</sup> We are not comfortable with their presumptive enforceability

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20. See, e.g., *Schoppert v. CCTC Int'l, Inc.*, 972 F. Supp. 444 (N.D. Ill. 1997); *Hathaway v. General Mills, Inc.*, 711 S.W.2d 227 (Tex. 1986) (holding that company could not unilaterally alter commission rates because they did not notify employee).

21. See JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE § 2-3, at 37 (6th ed. 2010) (“Many sales contracts are not fully bargained, not carefully drafted, and not understandingly signed . . . by both parties.”).

22. Clayton Gillette suggests forms are policed by the marketplace. Clayton P. Gillette, *Rolling Contracts as an Agency Problem*, 2004 WIS. L. REV. 679, 683 [hereinafter Gillette, *Rolling*] (An offeree who does not assent to terms should be considered to have accepted them if “his or her interests are sufficiently, if imperfectly, represented by other parties or institutions that are inextricably involved in the creation of contract terms”). Other scholars disagree with that proposition because of the irrationality of reading forms. See, e.g., Peter A. Alces, *Guerilla Terms*, 56 EMORY L.J. 1511, 1527, 1513 (2007) (“A guerilla term is a provision in a form contract that takes advantage of ‘rational ignorance’—the irrationality of reading terms in forms . . . [and] it is not in rational form drafters’ interest to bring [guerilla terms] to the attention of less sophisticated consumers . . . .”); Yannis Bakos, Florencia Marotta-Wurgler & David R. Trossen, *Does Anyone Read the Fine Print? Testing a Law and Economics Approach to Standard Form Contracts*, NYU CENTER FOR L. ECON. & ORG., Oct. 2009, available at <http://ssrn.com/abstract=1443256>. Cf Charles L. Knapp, *Opting Out or Copping Out? An Argument for Strict Scrutiny of Individual Contracts*, 40 LOY. L.A. L. REV. 95 (2006).

23. For other contemporary treatment of change-of-terms clauses, see Oren Bar-Gill & Kevin Davis, *Empty Promises*, 83 S. Cal. L. Rev. xxx (2010), and two recent student notes. Eric Andrew Horwitz, Note, *An Analysis of Change-of-Terms Provisions as Used in Consumer Services Contracts of Adhesion*,

and, instead, believe there is good reason to presume that they are unenforceable,<sup>24</sup> just as are disparate terms exchanged in the formation of a sales contract under Article 2 of the Uniform Commercial Code (hereinafter UCC or the Code).<sup>25</sup> We understand that the better rule under the Code's "battle of the forms" provision is that disparate terms proffered by each party are "knocked out," with the parties' contract consisting of the terms upon which the writings agree as well as other commercially reasonable supplementary terms provided by commercial context and the Code.

Our analysis, then, will begin in Part I with consideration of how Article 2 jurisprudence might inform our conclusions about the enforceability of unilateral change-of-terms provisions. There are several sections of the sales article that concern the scope of risk adjustment over the course of a contractual relationship and impose limitations on such adjustment in terms that might pertain as well to the enforceability of change-of-terms provisions in contracts not within the scope of Article 2.

Part II will survey apposite "consumer protection" legislation, both federal and state. The state versions of this legislation generally concern credit card agreements, and may perhaps best be appreciated as the product of the "race to the bottom": the competition among states eager to attract lucrative credit card business. The object of this legislation is to permit the banks that issue credit cards to export the law of the enabling states and thereby impose unilateral change-of-terms provisions on residents of all states. The recent federal credit card legislation may best be appreciated as push-back on such efforts.

Finally, Part III will survey apposite common law principles that might shed light on the enforceability of change-of-terms provisions and the enforceability of changes made pursuant to those provisions. The best way to appreciate the potential application and operation of these principles is in relation to the object of contract generally, an

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15 U. MIAMI BUS. L. REV. 75 (2006); Daniel Watkins, Note, *Terms Subject to Change: Assent and Unconscionability in Contracts that Contemplate Amendment*, 31 CARDOZO L. REV. 545 (2009).

24. See Todd D. Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96 HARV. L. REV. 1173 (1983) (terms in standard-form contracts of adhesion should be viewed as presumptively unenforceable).

25. U.C.C. § 2-207 (2002).

object that could be obscured by the mechanics of doctrine that may be too easily manipulated.

### I. THE CODE ANALOGY

The scope of Article 2 of the UCC is limited to sales of goods. Article 2A, governing much of the law of personal property leases, is by its terms limited to certain bailments for hire of the same subject matter. There may be nothing unique about “goods” qua goods so far as the application of particular contract conceptions are concerned; indeed, we may understand the fact that Articles 2 and 2A are limited in their scope by reference to their subject matter as a reflection of political or even economic rather than jurisprudential forces. That is, whatever contract accomplishes, it is not always obvious that the Article 2 or 2A iteration of the rule would not apply well beyond the sale or lease context.<sup>26</sup>

In recognition of that fact, courts have often relied on those two articles of the Code as the source of helpful analogy.<sup>27</sup> The sales and lease articles of the UCC would only apply by analogy to most of the contexts considered in this article because most of the transactions involve the provision of services or contractual relationships within the scope of other state or federal legislation, such as Article 4 of the UCC and complementary federal legislation governing the bank-customer relationship. But Article 2, and by extension those portions of Article 2A based on the sales article, constitutes an important jurisprudential statement concerning contract formation and adjustment dynamics. The analogy to the perspective first offered in

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26. Indeed, the Restatement (Second) of Contracts draws heavily on Article 2 for the Restatement’s articulation of rules generally applicable to all kinds of contracts.

27. See, e.g., 21st Century Props. Co. v. Carpenter Insulation & Coatings Co., 694 F. Supp. 148, 151 n.2 (D. Md. 1988) (stating that “roofs (because of their immovable nature) . . . are not ‘goods’ within the meaning of the Uniform Commercial Code[.]” however, “it is appropriate to use the warranty provisions of the Code . . . by analogy” (emphasis added)); Hoffman v. Horton, 186 S.E.2d 79, 80 (Va. 1972) (holding that the sale of land is not governed by the UCC, “[h]owever, while the Uniform Commercial Code is not controlling here, [the court] think[s] it appropriate to borrow from [the UCC] to establish the rule applicable to the transaction at hand”); Olmstead v. Mulder, 863 P.2d 1355, 1359 (Wash. Ct. App. 1993) (holding that the sale of real estate is not governed by the UCC, but “the reasoning of the UCC on the disclaimer of warranties is persuasive and can be applied by analogy in this case” (emphasis added)).

Article 2, therefore, may be apt. There is not an immediately obvious reason why the formation and adjustment rules should proceed from different jurisprudential premises outside of Article 2 than they would within the uniform sales law.

We must also keep in mind, however, that all analogies are, at least in part, inherently fallacious. The legislature could have chosen to apply the Article 2 rules beyond their scope directly, so that courts need not have relied on arguments by analogy. But by and large, the legislatures have not extended the rules of Article 2 to other contexts, so perhaps we cannot assume identity between the transactional, economic, and policy bases supporting Article 2 and those supporting the more general contract law. There should, though, be good reason for any dissonance.

Six arguably apposite Article 2 rules in particular provide sources of analogy; and each is considered in the subsections that follow: open-price terms,<sup>28</sup> output and requirements contracts,<sup>29</sup> a party's right to specify particular terms,<sup>30</sup> "battle of the forms,"<sup>31</sup> modification,<sup>32</sup> and failure of an exclusive remedy to achieve its essential purpose.<sup>33</sup> Some of those provisions will more obviously and directly pertain to issues such as those that arise in the unilateral change-of-terms setting, but all, we submit, present analyses that respond to the same or sufficiently similar transactional and theoretical tensions.

### *A. Open Price Terms*

Section 2-305 of the Code recognizes that "[t]he parties if they so intend may conclude a contract for sale even if the price is not settled."<sup>34</sup> The object of the provision is to give effect to the *intent* of the contracting parties, not to endorse one party's (i.e., the dominant

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28. U.C.C. § 2-305 (2002).

29. *Id.* § 2-306.

30. *Id.* § 2-311.

31. *Id.* § 2-207.

32. *Id.* § 2-209.

33. *Id.* § 2-719.

34. U.C.C. § 2-305(1) (2002). UCC Article 2A, however, lacks an analogous provision.

party's) imposition of all of the risk of price fluctuation on the other. The comments make clear that whether the parties actually intended a deal notwithstanding their failure to include a certain price is "a question to be determined by the trier of fact."<sup>35</sup> Further, the black letter of the provision contemplates the situation in which the contract provides that one party, seller or buyer, will fix the price: "A price to be fixed by the seller or by the buyer means a price for him to fix in good faith."<sup>36</sup> And in the case of a merchant, "good faith" is measured by reference to objective indicia.<sup>37</sup> There is no reason to assume that there would be any difference between a contract that leaves price open but to be set in the future by one of the contracting parties, and a contract that fixes a price at the outset subject to adjustment at the instance of one or the other contracting parties.

Not all unilateral change-of-terms provisions expressly concern price, but all contract terms concern risk, and risk is just the flip side of price.<sup>38</sup> But § 2-305 is an important statement, even in cases where the price of the contract subject matter is not directly at issue. First, note the context in which the provision would operate: between likely sophisticated contracting parties with the *actual intent* to leave the price term open.<sup>39</sup> The most obvious reason why the parties would choose to leave such risk "unfixed" is that they each have been able to hedge their bets on price, perhaps by entering into offsetting contracts with other contracting counterparties. Alternatively, a party

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35. *Id.* § 2-305 cmt. 2 ("Under some circumstances the postponement of agreement on price will mean that no deal has really been concluded, and this is made express in the preamble of subsection (1) ('The parties *if they so intend*') and in subsection (4). Whether or not this is so is, in most cases, a question to be determined by the trier of fact.") (emphasis in original).

36. *Id.* § 2-305(2).

37. *See id.* § 2-305 cmt. 3 (rejecting the "uncommercial idea" that the seller may subjectively "fix any price he may wish").

38. *See* Hal S. Scott, *The Risk Fixers*, 91 HARV. L. REV. 737 (1978).

39. Under U.C.C. § 2-305(1)(a)–(c) (2002), the parties may intend to leave the price term open if "nothing is said as to price," "the price is left to be agreed by the parties and they fail to agree," or "the price is to be fixed in terms of some agreed market or other standard . . . ." *See, e.g.,* *Arbitron, Inc. v. Tralyn Broad., Inc.*, 400 F.3d 130 (2d Cir. 2005) (radio-listener demographics service/radio broadcaster intended to leave the price open); *Gage Prods Co. v. Henkel Corp.*, 393 F.3d 629 (6th Cir. 2004) (chemical suppliers failed to agree on a price); *Flagler Auto., Inc. v. Exxon Mobil Corp.*, 582 F. Supp. 2d 367 (E.D.N.Y. 2008) (gasoline supplier/retailers intended to leave the price open); *Offices Togolais Des Phosphates v. Mulberry Phosphates, Inc.*, 62 F. Supp. 2d 1316 (M.D. Fla. 1999) (phosphate rock seller/buyer said nothing about price).

might not be concerned about a fixed price because that party is a middleman, confident of the ability to pass on price increases to sub-buyers or to those for whom the contracting party performs services on a cost-plus basis.

Section 2-305 also contemplates that the courts may fix a reasonable price if the party empowered by the contract to do so fails to do so in good faith. In that event, the court will fix a “reasonable” price.<sup>40</sup> Of course, that presumes that the premise of § 2-305 has been satisfied: the parties intended to conclude a contract even though the price was not settled at the time of contracting. Section 2-204 would be the measure of that intent. That section provides that a contract may be formed so long as the parties “intend” to contract *and* the court can ascertain a reasonably certain basis for granting relief in the event one of the contracting parties fails to perform.<sup>41</sup> So a court could always invalidate the operation of a price escalation, or any unilateral change-of-terms provision if the court concludes *either* that the parties did not *intend* to provide the dominant party such unilateral power or that the uncertainty of the “contract” terms obscured any reasonable basis for granting relief. It would depend upon the circumstances of the parties at the time the court invalidated the agreement, but it might well be the case that the court winds up eviscerating what the dominant party thought was a contract, and eviscerating with it what the dominant party thought its contract rights to be. The prospect of this occurrence might have sufficient *in terrorrem* effect to discourage the dominant party from pushing too hard on the unilateral right to change terms.

The § 2-305 recognition of contract when one party has reserved the right to set a term as significant as price is consistent with a conception of contract that would recognize the enforceability of a unilateral change-of-terms provision. The Code’s deference to open-price terms and their completion in a commercially reasonable manner would also support, by analogy, the enforceability of those

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40. WHITE & SUMMERS, *supra* note 21, at 134 (“When there is a gap, 2-305 directs the court to determine ‘a reasonable price,’ provided the parties intended to contract.”).

41. U.C.C. § 2-204(3) (2002).

provisions in contracts not within the scope of the Code.<sup>42</sup> What remains, though, is to determine whether the limitations that the Code would impose on the enforcement of such provisions should also pertain in the contemporary contexts in which the party insisting upon the unilateral change-of-terms clause would exercise it, and how the Code limitations might operate in the non-Code contexts. Although § 2-305 relies on conceptions of “good faith,” given the vagueness of that conception, it is worthwhile to track its operation in parallel provisions.

### *B. Output and Requirements Contracts*

The quantity term of a contract may be important,<sup>43</sup> but it is not crucial that the contract specify a precise quantity for the contract to be enforceable. What is indispensable is the quantity measure. If the court has the means to determine how the parties *intended* to fix their performance obligation, in terms of quantity, then the court may well be able to ascertain a reasonably certain basis to grant relief.<sup>44</sup>

Section 2-306 recognizes the enforceability of contracts in which the quantity is measured by reference to either the buyer’s needs (or “requirements”) or the seller’s capacity to produce (or “output”). The Code here formulates a rule recognized as well in the common law<sup>45</sup> and again relies on the parties’ bona fides to determine the extent of enforceability: “A term which measures the quantity by the output of the seller or the requirements of the buyer means such actual output or requirements as may occur in good faith[.]”<sup>46</sup> The comment makes clear that although the precise quantity to be transferred pursuant to the contract is not certain, the measure is certain, and, more pertinent

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42. See RESTATEMENT (SECOND) OF CONTRACTS § 33 cmt. e (1981) (“Similar principles [to those found in UCC § 2-305] apply to contracts for the rendition of service.”).

43. See U.C.C. § 2-201 cmt. 1 (2002) (explaining that, under the statute of frauds, “[t]he only term which must appear [in the record of the transaction] is the quantity term . . .”).

44. See *id.* § 2-204 cmt. 3.

45. WHITE & SUMMERS, *supra* note 21, § 4-9, at 173 (citing *In re United Cigar Stores Co.*, 8 F. Supp. 243 (S.D.N.Y. 1934), *aff’d*, 72 F.2d 673 (2d Cir. 1934); *Harvey v. Fearless Farris Wholesale, Inc.*, 589 F.2d 451 (9th Cir. 1979)).

46. U.C.C. § 2-306(1) (2002).



for present analogical purposes, *not* within the sole control or discretion of either party.

Under this Article, a contract for output or requirements is not too indefinite since it is held to mean the actual good faith output or requirements of the particular party. Nor does such a contract lack mutuality of obligation since, under this section, the party who will determine quantity is required to operate his plant or conduct his business in good faith and according to commercial standards of fair dealing in the trade so that his output or requirements will approximate a reasonably foreseeable figure.<sup>47</sup>

Note that the comment explains why such provisions are not infirm as a matter of common law contract doctrine: because the constraint on the party's performance obligation assures that there is mutuality of obligation. Without mutuality of obligation, there can be no contract.<sup>48</sup> So it is telling that § 2-306, a Code provision that accommodates the parties' filling in a performance term after the fact, relies on "commercial standards of fair dealing" to police completion of the term. There is mutuality because discretion is limited by forces outside of the control of the party who would complete the quantity term.<sup>49</sup>

Unilateral change-of-terms provisions, in contrast, could not identify any similar constraint on the dominant party's discretion, leaving the contract open to the charge that it lacks the mutuality of obligation that is crucial to contract.<sup>50</sup> So a court could rely upon the § 2-306 reference to mutuality and "commercial standards of fair dealing" as a means to police, if not invalidate entirely, the dominant party's imposition of a term that shifts the risk of a contract in a

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47. *Id.* § 2-306 cmt. 2.

48. 1 FARNSWORTH ON CONTRACTS § 3.2 (3d ed. 2004); 25 RICHARD A. LORD, WILLISTON ON CONTRACTS § 67:42 (4th ed. 2009). *Cf.* CALAMARI & PERILLO ON CONTRACTS § 4.12 (6th ed. 2009) ("The doctrine is not one of mutuality of obligation but rather one of mutuality of consideration.").

49. *Accord* RESTATEMENT (SECOND) OF CONTRACTS § 34 cmt. b (1981) ("[L]imits on the power [to select the terms of performance] may be either express or implied. Often the choice must reasonable in the circumstances.").

50. *See Harris v. Blockbuster, Inc.*, 622 F. Supp. 2d 396 (N.D. Tex. 2009).

manner prejudicial to the weaker party's interest. And insofar as the mutuality basis of contract is implicated, it would not seem that prior "agreement" could overcome that analysis, ostensible "intent" notwithstanding.

But if that construction of the impact of § 2-306 on the mutuality calculus is to bear the weight that might matter in the case of unilateral change-of-terms provisions, then the Code would need to be consistent with regard to limitations on one contracting party's reservation of a right to unilaterally change the terms of the agreement. Section 2-311, too, concerns this analysis and may inform our understanding of the Code's disposition toward unilateral changes of terms.

### *C. Party's Right to Specify Particular Terms*

Section 2-311 of the Code recognizes the commercial desirability, if not necessity, of providing the contracting parties with the flexibility to respond to transactional exigencies without compromising the enforceability of their deal. Sometimes the best response to uncertainty is to live with it until some point in time when it *must* be resolved, and then to let one of the contracting parties rather than the other resolve it. So long as the discretion of the party empowered to resolve the uncertainty is constrained in some meaningful way, contract law's interest in certain allocation of risk is not compromised. That is the balance struck by § 2-311, which provides:

1) An agreement for sale which is otherwise sufficiently definite (subsection (3) of 2-204) to be a contract is not made invalid by the fact that it leaves particulars of performance to be specified by one of the parties. Any such specification must be made in good faith and within limits set by commercial reasonableness.<sup>51</sup>

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51. U.C.C. § 2-311(1) (2002).

That subsection imposes three threshold limitations on the parties' ability to reserve to one of them the unilateral power to adjust the terms of the contract. First, only "particulars of performance" may be the subject of post hoc determination. Second, the discretion to specify is constrained by good faith and commercial reasonableness. And third, an implicit limitation: the particulars may be "specified." Such "specification" would seem to be something short of a unilateral power to *change* the terms of the parties' agreement. The section insulates the contract from what would otherwise be the effect of a reservation of right to specify particulars: an unenforceable agreement. Still, though, an agreement that would not be enforceable on account of such a post hoc right to specify is not deemed enforceable just because of the existence of that right to specify.

Further, it would seem that insofar as the other subsections of 2-311, as well as the comments thereto, intimate something about the limits of the right to specify, those limitations may also constrain the provision's scope. Subsection (2) provides a gap filler in the absence of contrary agreement with regard to assortment of goods (at buyer's option) and shipment arrangements (at seller's option). Note that both of those options concern matters that must be resolved in order to determine the scope of the counterparty's performance. The seller cannot tender conforming goods unless someone specifies the assortment; and the buyer cannot acquire the goods unless someone makes arrangements for their shipment to the buyer. Neither option provides the dominant contracting party the unilateral right to change the terms of an existing performance obligation imposed on the other. Indeed, any shifting of risk would seem to be incidental. In fact, were it not, that might constitute a sufficient basis to conclude that the right to specify goes beyond mere particulars.

Subsection (3) further reinforces the conclusion that it is in the interest of one party to leave specification of particulars to the other. The subsection contemplates that the parties have left a specification of particulars to be resolved by one party in order to accommodate the performance of both. So if the party who is to specify fails to do so, the counterparty is excused for any delay in its own performance and may treat the failure to specify as a breach. It should be clear that

the provision contemplates a type of specification wholly unlike a dominant contracting party's imposition of an increased price or a change of the terms of performance on the subordinate contracting party.

The bottom line, then, so far as § 2-311's pertinence to our coming to terms with unilateral change-of-terms provisions is concerned, would seem to be that the Code provision contemplates and provides the guidance to help us work through *gaps* that the parties have intentionally left in their agreements.<sup>52</sup> The provision does not support a *change of terms* as much as it recognizes the parties' ability to leave a gap and not render the "contract" illusory or unenforceable because of indefiniteness.<sup>53</sup>

Although § 2-311 provides guidance when the parties have intentionally left "gaps" in their agreement to be completed by one of them prior to or in the course of performance, perhaps the most familiar (if not most notorious) Code provision enforcing a deal beyond the terms of the parties' explicit agreement is the so-called "battle of the forms" provision, which, like § 2-311, relaxes common law premises of contract formation and goes beyond § 2-311 by providing the means to complete the deal even when the parties did not contemplate that means of completion.

#### *D. "Battle of the Forms"*

Section 2-207 of the Code concerns "forms," and "forms" is certainly a term of art used to designate those writings that are irrational to read. When the parties exchange disparate forms, they may well intend to contract and are more concerned with the fact of contract than they are with the terms that would govern their reciprocal undertakings. This is not the place to reproduce the rich

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52. To similar effect is the Restatement: "The terms of a contract may be reasonably certain even though it empowers one or both parties to make a selection of terms in the course of performance." RESTATEMENT (SECOND) OF CONTRACTS § 34(1) (1981).

53. 1 LINDA J. RUSCH, HAWKLAND UCC SERIES § 2-311:1, at 2-488 (Frederick H. Miller ed., 2002).

scholarly investigations of § 2-207,<sup>54</sup> to which many legal scholars (though not your authors) may well owe their tenure; suffice it to say that the interstices of the provision have been subject to exhaustive analyses and after the dust has settled, and we can have some confidence that it has settled, the better view seems quite straightforward: if two parties exchange forms that include disparate terms, the court will enforce a contract between them on the terms upon which the forms agree as well as supplementary terms fixed by course of performance, course of dealing, usage of trade,<sup>55</sup> and Code “gap fillers.”<sup>56</sup> The Code is not as concerned with the specific terms of the parties’ forms because the parties themselves, by relying on forms, evidence a lack of concern about those specific terms.<sup>57</sup> To permit one party to prevail over the other by operation of some mechanical rule, such as a “last shot rule,”<sup>58</sup> would actually be to frustrate the parties’ true rather than merely formal intention.

For present purposes, § 2-207 is important because of what it *does not* have to say about a dominant party’s unilateral right to change the terms of a contract. At first impression, it might seem that the Code’s treatment of the battle of the forms supports the enforcement of unilateral change-of-terms clauses. If the Code can essentially write a contract for parties who have not been sufficiently scrupulous in completing the terms for themselves, it might seem entirely consistent to recognize that one of the parties can permit the other party to complete the terms of a contract. If there may be sufficient

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54. For a thorough critique of the “battle of the forms” under section 2-207, see Corneill A. Stephens, *Escape from the Battle of the Forms: Keep It Simple, Stupid*, 11 LEWIS & CLARK L. REV. 233 (2007).

55. U.C.C. § 1-303(d) (2003). For definitions of these terms, see *id.* § 1-303(a)–(c). The subsections form a hierarchy, with course of performance preferred to course of dealing, and course of dealing preferred to usage of trade. *Id.* § 1-303(e).

56. See, e.g., *id.* § 2-305 (price); *id.* § 2-306 (quantity); *id.* § 2-307 (manner of delivery).

57. See *Daitom, Inc. v. Pennwalt Corp.*, 741 F.2d 1569, 1580 (10th Cir. 1984) (“The provision seems drafted with a recognition of the reality that merchants seldom review exchanged forms with the scrutiny of lawyers.”); *Titanium Metals Corp. v. Elkem Mgmt., Inc.*, 191 F.R.D. 468 (W.D. Pa. 1998); *Richardson v. Union Carbide Indus. Gases, Inc.*, 790 A.2d 962 (N.J. Super. Ct. App. Div. 2002); *Superior Boiler Works, Inc. v. R.J. Sanders, Inc.*, 711 A.2d 628 (R.I. 1998); see also Stephens, *supra* note 54.

58. Under the common law last shot rule, “the terms of the party who sent the last form, typically the seller, would become the terms of the parties’s [sic] contract.” *Step-Saver Data Sys., Inc. v. Wyse Tech.*, 939 F.2d 91, 99 (3d Cir. 1991).

intent to contract to permit § 2-207 to operate, is there not also sufficient intent when the subordinate party by contract permits the dominant party to unilaterally change terms?

In a word, “no.” It is one thing to recognize the commercial viability, even desirability, of a court’s completing a contract by reference to rules that sophisticated parties or their counsel should be expected to anticipate; it is wholly another to accommodate one sophisticated party’s corruption of contracting principles to impose what may be an unconscientious bargain on the other at the time when that subordinate party is in no position to defend itself. In other words, far from being an elaboration of contract principles recognized by § 2-207, the unilateral change-of-terms provision is a corruption of the very foundations of the Code “battle of the forms” rules. For the reasons § 2-207 makes good sense and is consistent with contract principles, unilateral change-of-terms provisions are a corruption of those same principles. A court construing a unilateral change-of-terms provision, therefore, should not be swayed by arguments by analogy to 2-207. The analogy is fallacious; and argument based on that fallacious analogy should be rejected.

Indeed, to the extent that reference to 2-207 is helpful in considering the enforceability of unilateral change-of-terms provisions, the better reasoned argument would seem to be that the Code’s “battle of the forms” rules militate in favor of finding such provisions unenforceable for the same reason that disparate terms in exchanged forms are unenforceable. Recall that if the buyer’s and seller’s forms conflict, the better reading of § 2-207 counsels that both parties’ terms should be “knocked out.”<sup>59</sup> That result obtains because the fact of the terms’ dissonance confirms that neither party intended to contract on the terms proffered by its counterparty. Of that we may be certain. Similarly, insofar as the dominant contracting party uses the unilateral change-of-terms provision at a time when the subordinate party is unable to extricate itself from the contract, this should as well intimate that there was no intent to contract on the terms as amended and probably no intent *ab initio* to agree to the

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59. See Stephens, *supra* note 54, at 249.

unilateral change either.<sup>60</sup> Insofar as § 2-207, then, is about enforcing a real rather than formal intent to contract; the correct reading of the provision militates in favor of refusing to enforce a unilateral change-of-terms provision unless there is evidence of real intent to contract by operation of such a term.

The same factual predicate that supports the operation of § 2-207 may also, and this can be a matter of framing or perception, raise contract modification issues. Although § 2-207 tells us what the terms of a contract are, another provision, § 2-209, tells us how those terms may be modified by the parties' communications and behavior subsequent to formation. Professors White and Summers describe how the coincidence may arise:

Suppose buyer sends a purchase order. Seller sends an acknowledgment that includes a warranty and disclaimer. The disclaimer "materially alters" under 2-207(2). Later, with knowledge of the warranty and disclaimer, the buyer acknowledges the disclaimer. Does it then become part of the contract (as a modification) under 2-209(1)? Some courts have said "yes!"<sup>61</sup>

Whether the facts raise a formation or modification issue may be a matter of timing. Whatever the resolution of tension between the two provisions, they should both reflect the same disposition toward the formation calculus.

### *E. Modification*

At least in the first instance, modification of an existing contract depends upon the same formalities as does original formation of the contract. So the rules governing both formation and modification

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60. It is dangerous to infer the subordinate party's intent to agree to unilateral amendments by relying on market forces to correct for consumer mistakes. See Alces, *supra* note 22; Oren Bar-Gill, *The Behavioral Economics of Consumer Contracts*, 92 MINN. L. REV. 749 (2008). *Contra* Gillette, *Rolling*, *supra* note 22; Richard Epstein, *The Neoclassical Economics of Consumer Contracts*, 92 MINN. L. REV. 803 (2008).

61. WHITE & SUMMERS, *supra* note 21, §2-3, at 42-43.

should be parallel. That does not mean that they need to be the same; but it does mean that variation between them should track distinctions that make a difference. Or so the story goes. Section 2-209, though, does not—at least at first blush—seem to remain true to that objective. We might imagine that the drafters of Article 2, particularly Karl Llewellyn, were somewhat impatient with formation formalities that could more often than not frustrate rather than serve transactors' interests and, so, just as § 2-207 relaxes formation rules in the case of communications it is irrational for the parties to read, § 2-209 overcomes similar (and similarly inefficacious) obstacles to commerce.

Section 2-209 does make it easier for the parties to modify their contract and does so principally by eliminating any vestige of the consideration requirement the common law would recognize. In place of consideration, the provision relies on intent and good faith. Although a modification need not be supported by consideration in order to be enforceable, the parties must have intended to modify their agreement and must have acted in good faith. The good faith requirement may be redundant given § 1-304,<sup>62</sup> which imposes a pervasive good faith requirement with regard to the performance and enforcement of every contract or duty within the Code, if modification amounts to “performance or enforcement.” So the principal contribution of § 2-209 is the abrogation of any independent consideration requirement. Although Article 2 still requires that consideration support contracts within its scope—there must be a “sale”<sup>63</sup>—consideration is not required in the case of modifications to that original contract.

A dominant contracting party's use of a unilateral right to change the terms of a contract seems to be at least *akin* to a modification of the underlying contract. Of course, one could argue, and perhaps do so convincingly, that exercise of rights under such a term does not

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62. U.C.C. § 1-304 (2003).

63. A “sale” under Article 2 “consists in the passing of title from the seller to the buyer for a price.” U.C.C. § 2-106(1) (2002). This definition of “sale” satisfies the requirement that a contract be supported by mutuality of consideration. The seller suffers detriment by giving up the title to his goods, and the buyer suffers detriment by paying the seller's price.



modify the contract because provision of the right in the original contract form obviates any need to modify. Indeed, that is just what the unilateral change-of-terms provision is for: it provides the party with the right to exercise the ability to change the terms of the contract without actually “modifying” the contract and having to go through the contract hoops required to effect a modification. It may be, then, that we should not expect symmetry between modification and exercise of a right under a unilateral change-of-terms provision.

From another perspective, though, it may make sense to police the operation of a unilateral change-of-terms provision just as we would police modification of an existing contract. After all, from the perspective of the subordinate party, the effect is the same: the dominant party’s exercise of the unilateral change-of-terms clause effects a modification of (*i.e.*, an increase in) the subordinate party’s performance or payment obligation or a modification of (*i.e.*, reduction in) the dominant party’s obligation.<sup>64</sup> From the perspective of contract doctrine, though, the difference may be significant. Although a party from whom a modification is sought still has the ability to decline, the party against whom a unilateral change-of-terms clause operates has purportedly contracted away that prerogative. So the safeguards that protect a subordinate party from an overreaching or otherwise undesirable bilateral modification are not present when the modification is made by the dominant party pursuant to a unilateral change-of-terms clause. If the risks of dominant-party overreaching are the same in the two settings, it is not clear that the formal distinction should make a real difference.

So the approach of § 2-209 may help here. Recall that in place of new consideration, § 2-209 requires “good faith.” Although it is not necessary that a modification be supported by new consideration to be enforceable, it is necessary that the modification be sought in good faith. So if the dominant party were to use duress, that could invalidate the modification obtained. “The effective use of bad faith to escape performance on the original contract terms is barred, and

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64. Examples of a reduction in the dominant party’s obligation include a reduction in the amount of credit to be extended or a reduction in the services (e.g., cable TV channels) to be provided.

the extortion of a ‘modification’ without legitimate commercial reason is ineffective as a violation of the duty of good faith.”<sup>65</sup>

Professors White and Summers have described the transactional dynamic that could reveal the type of extortion that would render a modification unenforceable:

The extortionist is perhaps most familiar: “Pay me more or I won’t finish making the goods and you won’t be able to open up your new business on the scheduled date.” The seller may thus get the buyer over a barrel and extort a higher price or some other concession. The wrong is aggravated if the extortionist insists on concessions that it sought but did not get in the negotiations leading up to the contract in the first place. . . . Courts can hold that they are in bad faith under 1-203<sup>[66]</sup> or unconscionable under 2-302, or invalid under the common law of duress via 1-103.<sup>67</sup>

White and Summers’ ultimate conclusion is that “[t]here will be plenty of hard cases here; more than most of these depend on *a priori* moral judgments about what is fair and what is not.”<sup>68</sup> That also would seem to resonate with the unilateral change-of-terms calculus as well.

Just as modification may be a fair and appropriate response to a change of circumstances not contemplated by the parties at the time of contract formation, a contract provision included and relied upon by the parties in the course of their performance may lead to results inconsistent with the parties’ best intentions. The Code provides courts with a means to police such “terms gone wrong” and, as with modifications, the Code approach may provide guidance as to the best resolution of analogous problems with the operation of unilateral change-of-terms clauses.

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65. U.C.C. § 2-209 cmt. 2, para. 2 (2002).

66. In Revised Article 1, this provision is now located in U.C.C. § 1-304 (2003).

67. WHITE & SUMMERS, *supra* note 21, § 2-7, at 81.

68. *Id.* at 59–60.

*F. Failure of an Exclusive Remedy to Achieve Its Essential Purpose*

If a seller of goods can fix with some certainty the post-delivery risk to which it is exposed, the seller can more accurately price the goods. Thus the Code recognizes and gives effect to a contract term that stipulates the remedy in the event of the seller's breach, generally a breach of warranty. Section 2-719 explains that:

(1) . . . (a) the agreement may provide for remedies in addition to or in substitution for those provided in this Article and may limit or alter the measure of damages recoverable under this Article, as by limiting the buyer's remedies to return of the goods and repayment of the price or to repair and replacement of non-conforming goods or parts; and

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(2) Where circumstances cause an exclusive or limited remedy to fail of its essential purpose, remedy may be had as provided in this Act.<sup>69</sup>

A large proportion of both consumer and commercial sales contracts contain a provision making repair or replacement the buyer's exclusive remedy for the seller's breach of warranty. This provision effectively limits the buyer's remedies, unless the repair-or-replace remedy fails of its essential purpose.<sup>70</sup> The pertinent part of § 2-719, so far as the enforceability of unilateral change-of-terms clauses should be concerned, is the invalidation of the limited remedy when circumstances cause it to "fail of its essential purpose." If a change-of-terms clause provides that the subordinate party may avoid operation of the change by discharging her outstanding obligations to the dominant party, the situation is analogous to a sales contract with an exclusive remedy for breach of warranty. The subordinate party has a "remedy" for the dominant party's specification of an undesirable term: escape from the transaction upon payment for the

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69. U.C.C. § 2-719 (2002).

70. WHITE & SUMMERS, *supra* note 21, § 13-10, at 604 (citing *Riley v. Ford Motor Co.*, 442 F.2d 670 (5th Cir. 1971)).

performance rendered by the dominant party up to that point. But factors outside the contracted-for performance may make this remedy illusory: the subordinate party may not have the resources to accelerate a performance that the contract contemplates will be performed over an extended period of time, or termination of the contract may entail a forfeiture.<sup>71</sup> To be told that you can resist a price increase by immediately paying all amounts outstanding may effectively constrain you to “agree” to the price increase. So in a very real way, the “essential purpose” of that option has failed.

The power of the unilateral change-of-terms clause in continuing contractual relationships is in the dominant party’s ability to exercise the clause when the subordinate party is impotent to avoid the consequences of its operation. So it is in fact somewhat tautological to acknowledge the prejudice that operation of the clause entails: prejudice is the point. To the extent that the limited “remedy” (recall, this is analogy)—the ability to extricate oneself from the continuing contract—*does not fail* of its essential purpose, the unilateral change-of-terms clause has no leverage. As long as the dominant party maintains leverage, it does so precisely *because* that limited “remedy” is of no practical use to the subordinate party.

A court reviewing the operation of a unilateral change-of-terms provision, then, should be sensitive to the practical ramifications of the subordinate party’s exercising an option available to it in order to avoid the effect of the change of terms. If the subordinate party, as a practical matter, would be impotent to avoid the operation of the clause, then the court should find the dominant party’s exercise of the clause to be no more appropriate than would be a dominant party’s reliance on a limited remedy clause when that exclusive remedy has “failed of its essential purpose.”

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71. *E.g., Powertel, Inc. v. Bexley*, 743 So. 2d 570 (Fla. Dist. Ct. App. 1999) (loss of cell phone and phone number).

## II. STATUTORY REGULATION OF CHANGE-OF-TERMS CLAUSES

Part I explored several provisions in the UCC, applicable to both commercial and consumer contracts, which authorize and constrain the use of contract terms that empower one of the parties to *set* the initial terms of their contract. The next two parts turn more specifically to terms that authorize one of the parties to *change* the initial terms of the contract. This Part addresses the legislative and administrative treatment of change-of-terms provisions, primarily in the context of open-end credit. Part III addresses common law doctrine that applies to all kinds of contracts.

In the context of consumer credit, the Truth in Lending Act<sup>72</sup> (hereinafter sometimes referred to as TILA) recognizes the use of change-of-terms clauses. As a disclosure statute, TILA neither expressly validates the practice nor imposes standards for the exercise of the power granted by change-of-terms clauses. The regulation promulgated by the Federal Reserve Board<sup>73</sup> also does not do so, although it does recognize their use. Section 226.9(c) of Regulation Z provides:

(1) Written notice required. Whenever any term required to be disclosed . . . is changed . . . , the creditor shall mail or deliver written notice of the change to each consumer who may be affected. The notice shall be mailed or delivered at least 15 days prior to the effective date of the change. The 15-day timing requirement does not apply if the change has been agreed to by the consumer, or if a periodic rate or other finance charge is increased because of the consumer's delinquency or default; the

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72. Truth in Lending Act, 15 U.S.C. §§ 1601–1700 (2006).

73. Section 105 provides: "The Board shall prescribe regulations to carry out the purposes of this subchapter." Truth in Lending Act § 105(a), 15 U.S.C. § 1604(a) (2006). The Board has promulgated Regulation Z, 12 C.F.R. §§ 226.1–.48 (2009), and has issued the Official Staff Commentary, *id.* supp. I, which further interprets the Act and Regulation Z.

notice shall be given, however, before the effective date of the change.<sup>74</sup>

The Official Staff Commentary underscores that this is merely a disclosure requirement and not a substantive provision authorizing change-of-terms clauses.<sup>75</sup> The enforceability of such a clause and the enforceability of a change implemented pursuant to such a clause are governed by state law.

The Truth in Lending Act took effect in 1969. Twenty years later Congress amended the Act to require additional disclosures for open-end credit secured by the consumer's residence, so-called home equity loans.<sup>76</sup> In the course of implementing this section, Regulation Z departs from the implicit recognition of the enforceability of change-of-terms clauses. The regulation not only specifies the disclosures that a creditor must make, it provides that "[n]o creditor may, by contract or otherwise . . . [c]hange any term."<sup>77</sup> The Commentary elaborates:

A creditor may not include a general provision in its agreement permitting changes to any or all of the terms of the plan. For example, creditors may not include "boilerplate" language in the agreement stating that they reserve the right to change the fees imposed under the plan. . . .<sup>78</sup>

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74. Regulation Z, 12 C.F.R. § 226.9(c)(1) (2009). Effective February 2010, this language has been revised to reflect the enactment of the credit card legislation discussed below and now appears as § 226.9(c)(2)(i).

75. It states:

Examples of issues not addressed by § 226.9(c) because they are controlled by state or other applicable law include:

- (1) The types of changes a creditor may make.
- (2) How changed terms affect existing balances, such as when a periodic rate is changed and the consumer does not pay off the entire existing balance before the new rate takes effect.

*Id.* supp. I, cmt. 9(c)-2.

76. Pub. L. No. 100-709, § 2(a), 102 Stat. 4725 (1988), adding § 127A (codified at 15 U.S.C. § 1637a (2006)).

77. Regulation Z, 12 C.F.R. § 226.5b(f)(3) (2009). Paragraph three then lists several exceptions to this prohibition.

78. *Id.* supp. I, cmt. 5b(f)(3)(i)(2).

Hence, in this specific credit context, creditors are denied the power to impose change-of-terms clauses on consumers. The recently enacted Credit Card Accountability Responsibility and Disclosure Act of 2009 (hereinafter Credit CARD Act), however, continues to recognize the creditors' use of change-of-terms clauses in other settings. Section 101 of the Credit CARD Act amends TILA § 127 to require forty-five days advance notice of certain changes in the terms of an open-end credit card account and gives the consumer the right to cancel the account and complete payment pursuant to the pre-change terms of the account.<sup>79</sup>

Federal law thus tolerates change-of-terms clauses in most open-end credit contracts. With the exception of home equity loans, it does not prohibit the use of those clauses. Until enactment of the Credit CARD Act, federal law imposed no constraints on a creditor's exercise of the power conferred by a change-of-terms clause.<sup>80</sup> Regulation of the use of those clauses is thus a matter of state law. It turns out, however, state law—or at least the law of the several most relevant states—has been extremely supportive of a creditor's use of change-of-terms clauses.

In 1978 the United States Supreme Court decided *Marquette National Bank of Minneapolis v. First of Omaha Service Corp.*,<sup>81</sup> holding that a bank located in Nebraska could issue a credit card to a consumer residing in another state and charge that consumer an interest rate prohibited by the consumer's state but permitted by Nebraska. This started a courtship by several states, seeking to attract credit-card issuing banks to locate their credit-card operations in

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79. Credit CARD Act of 2009, Pub. L. No. 111-24, § 101(a)(1), 123 Stat. 1735 (2009) (to be codified as Truth in Lending Act § 127(i), 15 U.S.C. § 1637(i)); see 74 Fed. Reg. 5244, 5248 (Jan. 29, 2009) (adding a sample form for disclosing a change of terms in an open-end credit card account). Regulation Z, 12 C.F.R. app. G-20-G-23 (2009).

80. *But see* Rossman v. Fleet Bank (R.I.) Nat'l Ass'n, 280 F.3d 384, 390–91 (3d Cir. 2002) (power cannot be exercised in such a way as to make the initial disclosures inaccurate) (discussed *infra* text accompanying note 131). For the impact of the Credit CARD Act of 2009, see *infra* text accompanying notes 135 and 136 (changes in certain fees must be reasonable).

81. *Minneapolis v. First of Omaha Serv. Corp.*, 439 U.S. 299 (1978). This holding related to national banks. In 1980 Congress extended this rule to cover state-chartered banks. Depository Institutions Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, § 501(b), 94 Stat. 132 (1980) (codified at 12 U.S.C. § 1735f-7a(b) (2006)).

those states.<sup>82</sup> The courtship succeeded, and as a result of the migration, more than eighty percent of credit-card volume originates from issuers located in Delaware, South Dakota, Utah, Ohio, and Virginia.<sup>83</sup> The legislatures in these states either eliminated or drastically relaxed their usury laws and enacted other provisions that favor credit-card issuers. Foremost among these other provisions are statutes that authorize card issuers to use change-of-terms clauses. For example, the South Dakota law states, “[u]pon written notice, a credit card issuer may change the terms of any credit card agreement, if such right of amendment has been reserved, regardless of whether the card holder can use the card for new purchases.”<sup>84</sup> Delaware goes further by authorizing the issuer to change the terms even if the contract with the consumer does not expressly so provide: “Unless the agreement governing a revolving credit plan otherwise provides, a bank may at any time and from time to time amend such agreement in any respect . . . .”<sup>85</sup> The law in Virginia is similar, permitting the issuer to change terms even if the contract is silent on the matter.<sup>86</sup> The law in Ohio and Utah is similar to the law in South Dakota, validating change-of-terms clauses.<sup>87</sup> All these states thus bless the use of change-of-terms clauses in contracts for open-end credit.

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82. See LYNN LOPUCKI, *COURTING FAILURE* 53–55 (2005).

83. These are, in alphabetical order, American Express, Bank of America, Capital One, Citibank, Discover, GE Money, HSBC, JP Morgan Chase, Target, USAA, US Bank, and Wells Fargo. Ben Woolsey & Matt Schulz, *Credit Card Statistics, Industry Facts, Debt Statistics*, CREDITCARDS.COM, Jan. 15, 2010, <http://www.creditcards.com/credit-card-news/credit-card-industry-facts-personal-debt-statistics-1276.php> (citing NILSON REPORT (April 2009)). The eighty percent figure is for 2008 and is true with respect to both number of cards issued and the dollar amount of outstanding balances.

84. S.D. CODIFIED LAWS § 54-11-10 (2008).

85. DEL. CODE ANN. tit. 5, § 952(a) (1999).

86. VA. CODE ANN. § 6.1-330.63(c) (2005) (“Any contract or plan . . . may be amended in any respect by the bank or savings institution at any time and from time to time to modify or delete terms, or to add new terms . . . .”). In addition, see UNIF. CONSUMER CREDIT CODE § 3.205(1), 7 U.L.A. 88 (1974) (“Whether or not a change is authorized by prior agreement a creditor may change the terms of an open-end credit account applying to any balance incurred before or after the effective date of the change.”).

87. OHIO REV. CODE ANN. § 1109.20(d) (West 1996) (“Subject to any requirements under applicable federal law, a bank and a borrower may specify in their agreement any terms and conditions for modifying or amending the agreement.”); UTAH CODE ANN. § 70C-4-102(2)(a) (2006) (“[A] creditor may change any written term of an open-end consumer credit contract at any time while the open-end consumer credit contract is in effect and apply the new term to the unpaid balance in the account if . . . the open-end consumer credit contract expressly provides that the creditor may change terms of the open-end consumer credit contract from time to time.”).



As described in the introduction to this article, however, change-of-terms clauses are by no means confined to credit card contracts. Rather, they pervade all consumer contracts that contemplate an ongoing relationship in which a merchant provides services to a consumer. With respect to these other kinds of contracts, however, there has been no race to the bottom, and state legislation addressing the enforceability of change-of-terms clauses is rare. To the extent it exists, it is not as favorable to the dominant party as the legislation applicable to open-end credit contracts. We are not aware of any statute of general applicability that addresses change-of-terms clauses. But landlord-tenant legislation sometimes addresses the matter and does so in a manner not so favorable to the dominant party. Thus, a Michigan statute prohibits a landlord from including in a residential lease agreement a provision that permits the landlord to “alter a provision of the rental agreement after its commencement without the written consent of the tenant.”<sup>88</sup>

### III. COMMON LAW LIMITS ON CHANGE-OF-TERMS CLAUSES

Part I examined the common law doctrines and UCC rules that govern assent to the formation and modification of contracts. Part II dealt with several statutory and administrative rules that authorize or constrain the use of change-of-terms clauses. This part examines four aspects of the common law that pertain to change-of-terms provisions: interpretation, liquidated damages clauses, unconscionability, and good faith.

#### *A. Interpretation*

A contract provision that authorizes one party to change the terms of a contract does not necessarily enable the party to add provisions that deal with entirely different subject matter. A provider of cellular

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88. MICH. COMP. LAWS ANN. § 554.633(1)(l) (West 2005). The paragraph goes on to provide exceptions for changes required by law; changes reflecting changes in taxes, insurance, or utility expenses; and changes in rules that are required to protect the physical health, safety, or peaceful enjoyment of tenants or guests.

phone service for example may not—under the authority of a change-of-terms provision—amend the contract to require the subscriber, for an additional sum, to purchase life insurance. Several courts have concluded that a change-of-terms clause is properly understood to authorize changes in the terms that are expressly stated in the contract, and perhaps additional terms that are similar to those terms, but not additions that address extraneous matters not contemplated by the contract. An example of such extraneous matter is dispute resolution.<sup>89</sup> The scope of a change-of-terms clause is not unlimited. An attempted addition of a term beyond the scope of the clause will not be effective.<sup>90</sup>

### *B. Liquidated Damages*

A second limitation on the enforceability of certain changed terms is the law governing penalty clauses. Under traditional contract doctrine, parties to a contract may stipulate in advance what the remedies will be in the event of a breach. But the stipulation must have as its objective the specification of damages in circumstances in which the loss is difficult to ascertain.<sup>91</sup> If the objective is punishment

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89. *Badie v. Bank of America*, 79 Cal. Rptr. 2d 273 (Cal. Ct. App. 1998) (refusing to enforce a provision that would have required disputes to be resolved only by arbitration); *Kortum-Managhan v. Herbergers NBGL*, 204 P.3d 693 (Mont. 2009) (same); *Discover Bank v. Shea*, 827 A.2d 358 (N.J. Super. Ct. Law Div. 2001) (same); *Sears Roebuck & Co. v. Avery*, 593 S.E.2d 424 (N.C. Ct. App. 2003) (same).

90. In response to this restrictive interpretation of the power granted by a change-of-terms provision, the Utah legislature amended its statute by adding: “For purposes of this section, ‘change’ includes to add, delete, or otherwise change a term of an open-end consumer credit contract.” 1999 Utah Laws 180, § 2 (*amending* UTAH CODE ANN. § 70C-4-102 (2001)).

Delaware went even further, demonstrating the extent of its capture by the credit-card industry, when it amended DEL. CODE ANN. tit. 5, § 952(a) (2001) to read:

[a] bank may at any time and from time to time amend such agreement in any respect, whether or not the amendment or the subject of the amendment was originally contemplated or addressed by the parties or was integral to the relationship between the parties. Without limiting the foregoing, such amendment may change terms by the addition of new terms or by the deletion or modification of existing terms, whether relating to [enumerating more than a dozen features of open-end credit] or other matters of any kind whatsoever.

72 Del. Laws 15, § 12 (1999).

Presumably, even the Delaware statute has some limit (e.g., the insurance example in the text). And, of course, these statutes apply only to open-end credit contracts, so restrictive interpretations remain applicable to other kinds of contracts (e.g., telephone, television, and banking services).

91. RESTATEMENT (FIRST) OF CONTRACTS § 339(1) (1932):

of behavior that amounts to breach of the contract, the stipulation is not enforceable.<sup>92</sup> Drawing heavily on Article 2 of the UCC, the Restatement (Second) provides:

Damages for breach by either party may be liquidated in the agreement but only at an amount that is reasonable in the light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss. A term fixing unreasonably large liquidated damages is unenforceable on grounds of public policy as a penalty.<sup>93</sup>

Properly viewed, consumer contracts call for the consumer to perform as agreed, including making payments in a timely fashion and observing other terms of the agreement, such as not exceeding a credit limit. When the contract stipulates amounts that consumers must pay when they breach these parts of the agreement, those amounts must be justified as sound estimates of loss to the other party under circumstances in which it is not feasible for that party to establish the amount of damages caused by the breach. Often this is not the case. Instead, the amounts seem intended to deter or punish the specified behavior (or simply generate revenue). Examples include such things as fees for exceeding a credit limit, failing to make a payment by its due date, and writing a check on an account

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An agreement, made in advance of breach, fixing the damages therefor, is not enforceable as a contract and does not affect the damages recoverable for the breach, unless

(a) the amount so fixed is a reasonable forecast of just compensation for the harm that is caused by the breach, and

(b) the harm that is caused by the breach is one that is incapable or very difficult of accurate estimation.

92. *Id.* cmt. a:

Punishment of a promisor for breach, without regard to the extent of the harm that he has caused, is an unjust and unnecessary remedy. Therefore, the power of parties to make an enforceable contract for the determination of damages in advance is limited as stated in this Section.

93. RESTATEMENT (SECOND) OF CONTRACTS § 356(1) (1981); *cf.* U.C.C. § 2-718(1) (2002):

Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy. A term fixing unreasonably large liquidated damages is void as a penalty.

that has insufficient funds. In the context of setting a fee, a merchant's exercise of the power granted by a change-of-terms clause is limited by the doctrine of liquidated damages.

### C. Unconscionability

Another constraint on the enforceability of such clauses is the doctrine of unconscionability. Prodded by the enactment of the UCC, courts have embraced this historic doctrine and extended its application to contracts outside the scope of the UCC.<sup>94</sup> According to the landmark case, *Williams v. Walker-Thomas Furniture Co.*,<sup>95</sup> unconscionability consists of the "absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party."<sup>96</sup> This has evolved into the idea that there are procedural and substantive elements to unconscionability.<sup>97</sup> Courts have stated variously that both elements must be present;<sup>98</sup> that they comprise a sliding scale, so that the more pronounced one element is, the less necessary is the other;<sup>99</sup> and that

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94. U.C.C. § 2-302 (2002) (applicable to "transactions in goods"). The Restatement (Second), applicable to all contracts, states:

If a contract or term thereof is unconscionable at the time the contract is made a court may refuse to enforce the contract, or may enforce the remainder of the contract without the unconscionable term, or may so limit the application of any unconscionable term as to avoid any unconscionable result.

RESTATEMENT (SECOND) OF CONTRACTS § 208 (1981); see CAL. CIV. CODE § 1670.5 (West 1985) (adopting the language of U.C.C. § 2-302 but making it generally applicable to all contracts). For use of the doctrine outside the scope of U.C.C. Article 2, see, for example, *Powertel, Inc. v. Bexley*, 743 So. 2d 570 (Fla. Dist. Ct. App. 1999) (cell phone service); *Best v. U.S. Nat. Bank of Oregon*, 739 P.2d 554 (Or. 1987) (checking account).

95. *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445, 449 (D.C. Cir. 1965) (decided after the enactment but before the effective date of the UCC).

96. Another landmark case, *Henningsen v. Bloomfield Motors, Inc.*, 161 A.2d 69 (N.J. 1960), spoke in terms of public policy, never using the term unconscionability. But its articulation of reasons why an automobile manufacturer's exclusion of liability for personal injuries caused by a defective product emphasized the buyer's lack of choice concerning the contract term, coupled with the unreasonableness of foreclosing compensation for personal injuries. See RESTATEMENT (SECOND) OF CONTRACTS § 208, cmt. a (1981) ("[Unconscionability] overlaps with rules which render particular bargains or terms unenforceable on grounds of public policy.").

97. Arthur Allen Leff, *Unconscionability and the Code—The Emperor's New Clause*, 115 U. PA. L. REV. 485, 487 (1967).

98. *E.g.*, *Garrett v. Janiewski*, 480 So. 2d 1324, 1327 (Fla. Dist. Ct. App. 1985).

99. *E.g.*, *A & M Produce Co. v. FMC Corp.*, 186 Cal. Rptr. 114 (Cal. Ct. App. 1982).

in a contract of adhesion the adhesive nature of the contract per se satisfies the procedural element of unconscionability.<sup>100</sup>

It is often assumed that unconscionability is to be determined as of the inception of the contract. The articulation of UCC § 2-302 supports this belief: “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 . . . .”<sup>101</sup> Other authority, however, supports the view that unconscionability may be determined as of a later point in the contractual relationship. In the context of the sale of goods, UCC § 2-719 permits the seller to displace the remedies ordinarily available under the UCC by limiting the buyer to repair or replacement of goods that do not conform to the contract.<sup>102</sup> It also provides, however, that “[w]here circumstances cause an exclusive or limited remedy to fail of its essential purpose, remedy may be had as provided in this Act.”<sup>103</sup> This provision requires an examination of the situation as of the time of breach, not the inception of the contract. So does the next subsection of § 2-719:

(3) 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 limitation of damages where the loss is commercial is not.<sup>104</sup>

The unconscionability of an exclusion of consequential damages depends on the situation at the time of the injury. The circumstances surrounding the breach are relevant to determining whether an exclusion of consequential damages is unconscionable. For example, if there is a defect in the electrical system of a car and the car is out

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100. *E.g.*, *Flores v. Trans-America HomeFirst, Inc.*, 113 Cal. Rptr. 2d 376, 382 (Cal. Ct. App. 2001); *cf.* *Maxwell v. Fidelity Fin. Servs., Inc.*, 907 P.2d 51, 59 (Ariz. 1995) (either procedural or substantive unconscionability may suffice).

101. To same effect is RESTATEMENT (SECOND) OF CONTRACTS § 208 (1981) (“If a contract or term thereof is unconscionable at the time the contract is made . . .”).

102. *See supra* text accompanying note 69.

103. U.C.C. § 2-719(2) (2002).

104. *Id.* § 2-719(3).

of service for a week for repairs, it may not be unconscionable to exclude recovery of damages for the diminished value of the car and for the cost of a rental during that week. But if the defect in the electrical system causes a fire that destroys the car, it may indeed be unconscionable to foreclose the recovery of the consequential damages for destruction of the car and the cost of a rental during the period it reasonably takes the buyer to purchase a replacement.<sup>105</sup> The point is that the unconscionability of the exclusion of consequential damages cannot be determined until those damages are known.

In the context of a change-of-terms clause, one could examine whether the clause is unconscionable because it confers the power on the dominant party, leaving the other party at the mercy of the dominant one. On its face, this seems to be the view of the Principles of the Law of Software Contracts, recently adopted by the American Law Institute. Section 1.11 tracks UCC § 2-302, referring to unconscionability at the inception of the contract, and Illustration 4 states that “[a] court should hold [a change-of-terms provision] unconscionable because it attempts to bind the transferee to terms of which it is not and cannot be aware at the time of contracting.”<sup>106</sup> The broad sweep of this assertion, if applied to a contract for the sale of goods, would mean that the parties could not agree that the seller would, post-formation, determine the price of the goods. And yet, as we have seen, the UCC specifically permits an open-price contract.<sup>107</sup> Given the constraints of good faith established by statute and the common law,<sup>108</sup> this assertion in the Software Principles is untenable as a matter of general applicability.<sup>109</sup>

One could (as in the goods case) say that the unconscionability of the clause must be determined at the outset and that the clause is

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105. See Roy Ryden Anderson, *Failure of Essential Purpose and Essential Failure of Purpose: A Look at Section 2-719 of the Uniform Commercial Code*, 31 Sw. L.J. 759, 775–76 (1977); Jonathan A. Eddy, *On the “Essential” Purposes of Limited Remedies: The Metaphysics of U.C.C. Section 2-719(2)*, 65 CAL. L. REV. 28, 29 (1977).

106. PRINCIPLES OF THE LAW OF SOFTWARE CONTRACTS § 1.11, illus. 4 (2009).

107. See *supra* note 33 and accompanying text.

108. See *infra* Part I.D.

109. Of course, the Principles do not assert it as a matter of general applicability. In the context of software contracts, it may be a perfectly sound proposition. That is a matter beyond the scope of this article.

unconscionable at the outset to the extent that the merchant later exercises it in a particular way. But this seems to mask that the inquiry is made as of the time the merchant attempts to exercise the power given by the clause. And the review concerns whether that exercise surpasses the appropriate bounds of the authorization to make changes unilaterally.<sup>110</sup> Several courts agree.

Courts have invoked unconscionability as a limit on the enforceability of change-of-terms clauses. An example is *Powertel, Inc. v. Bexley*,<sup>111</sup> in which a cellular phone service provider added a forced-arbitration clause to its existing contracts, by means of a revised agreement included in an envelope containing a monthly bill. Plaintiff sued on behalf of a class of consumers who had allegedly been improperly charged for long-distance calls.<sup>112</sup> Defendant attempted to shunt the proceedings into arbitration, but the court held that the arbitration clause—added by means of a change-of-terms clause—was unconscionable.<sup>113</sup> It rejected defendant's argument that plaintiffs could have avoided the clause by terminating their contracts and finding another telephone service. Doing so would have entailed inconvenience and expense, so plaintiffs did not have a meaningful choice about the matter.<sup>114</sup> Further, the bill stuffer did not call plaintiffs' attention to the fact or substance of the changed agreement.<sup>115</sup> As another court recently put it, "Without notice [of the

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110. Cf. KARL LLEWELLYN, *THE COMMON LAW TRADITION* 362 (1960), speaking of standard-form contracts:

It would be a heart-warming scene, a triumph of private attention to what is essentially private self-government in the lesser transactions of life . . . if only all business men and all their lawyers would be reasonable.

But power, like greed, if it does not always corrupt, goes easily to the head. So that the form agreements tend either at once or over the years, and often by whole lines of trade, into a massive and almost terrifying jug-handled character; the one party lays his head into the mouth of a lion—either, and mostly—without reading the fine print, or occasionally in hope and expectation (not infrequently solid) that it will be a sweet and gentle lion.

111. *Powertel, Inc. v. Bexley*, 743 So. 2d 570 (Fla. Dist. Ct. App. 1999).

112. *Id.*

113. *Id.* at 574.

114. Plaintiffs would have had to purchase new telephones and, at a time before the portability of phone numbers, obtain new numbers. In some contexts, though evidently not in *Powertel*, the consumer may be subject to an early termination charge.

115. *Powertel*, 743 So. 2d at 574.

changed term], an examination would be fairly cumbersome, as [the consumer] would have had to compare every word of the . . . contract with his existing contract in order to detect whether it had changed.”<sup>116</sup> Having concluded that the modification was procedurally unconscionable, the court then concluded that it was substantively unconscionable as well.<sup>117</sup>

Given the prevalence of change-of-terms clauses, a consumer cannot reasonably avoid them. In that sense then, there is an absence of meaningful choice. But the real focus must be on the dominant party’s exercise of the power granted by a change-of-terms provision. Here, too, there often is an absence of meaningful choice: the consumer may reasonably avoid a particular exercise of the power given by a change-of-terms clause only by ending the relationship with the other party. Whether this is sufficient to supply a meaningful choice depends at best on the expense and inconvenience in ending the relationship. If termination entails substantial expense or inconvenience, there is no meaningful choice. Even if there is no expense and little inconvenience, if all (or substantially all) of the other party’s competitors have adopted the new term, there is no meaningful choice.<sup>118</sup> The enforceability of the change then will turn on an evaluation of the reasonableness of the changed term, i.e. whether the term unreasonably favors the merchant.

The consequences of a conclusion of unconscionability bear noting. Under the Restatement formulation, if a court holds a change-of-terms provision, or the party’s exercise of it, to be unconscionable, the court may limit or refuse enforcement. But a consumer protection statute may provide for additional remedies. Known variously as

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116. *Douglas v. U.S. Dist. Court for the Cent. Dist. of Cal.*, 495 F.3d 1062, 1066 n.1 (9th Cir. 2007). Compare the agreements cited in notes 13–15 *supra*, purporting to make changes in their terms effective merely by posting the change on the dominant party’s web site. This presumably requires the adhering party to visit the site periodically (daily?) to read the entire agreement to see if any of the terms has changed.

117. *Powertel*, 743 So. 2d at 576–77 (reaching that conclusion because the arbitration clause cut off the consumer’s right to common law and statutory remedies and foreclosed the possibility of proceeding by class action even though the damages suffered by any one consumer were too small to warrant assertion of rights in either litigation or arbitration).

118. In jurisdictions that treat adhesion contracts as per se procedurally unconscionable, *supra* note 100, it would not matter that the consumer could find a contract elsewhere on other terms.



UDAPs (for Unfair or Deceptive Acts or Practices Acts), consumer fraud acts, deceptive trade practices acts, or little-FTC acts, these statutes often prohibit unconscionable acts or practices.<sup>119</sup> One who violates the prohibition may be liable not only for actual damages, but also minimum damages,<sup>120</sup> multiple damages,<sup>121</sup> and in the event of successful proceedings to establish the violation, costs and attorney's fees.<sup>122</sup>

#### *D. Good Faith*

This brings us to the final constraint on the exercise of the power granted by change-of-terms clauses: the obligation of good faith. Drawing again on the UCC, the Restatement (Second) of Contracts states, "[e]very contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement."<sup>123</sup> Per the UCC, "good faith" means "honesty in fact and the observance of reasonable commercial standards of fair dealing."<sup>124</sup> Citing this definition, the Restatement concurs, stating:

The phrase "good faith" is used in a variety of contexts, and its meaning varies somewhat with the context. Good faith performance or enforcement of a contract emphasizes

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119. See CAROLYN CARTER & JONATHAN SHELDON, UNFAIR AND DECEPTIVE ACTS AND PRACTICES 4.4.1 n.711 (7th ed. 2008) (in 17 states, the consumer protection act proscribes unconscionability).

120. *E.g.*, Kansas Consumer Protection Act § 14(a), KAN. STAT. ANN. § 50-636(a) (2005) (allowing up to \$10,000 for each violation).

121. *E.g.*, New Jersey Consumer Fraud Act, N.J. STAT. ANN. 56:8-19 (West 2001) (requiring courts to award treble damages).

122. *E.g.*, Michigan Consumer Protection Act § 11(b)(2), MICH. COMP. LAWS § 445.911(b)(2) (2002). For a compilation of the remedies available under UDAPs, see CARTER & SHELDON, *supra* note 119, app. A.

123. RESTATEMENT (SECOND) OF CONTRACTS § 205 (1981). Section 1-304 of the Uniform Commercial Code provides, "[e]very contract or duty within the Uniform Commercial Code imposes an obligation of good faith in its performance and enforcement." U.C.C. § 1-304 (2003). Revised Article 1 has been enacted in more than 30 states. In the rest, a substantively identical provision appears in § 1-203.

124. U.C.C. § 1-201(b)(20) (2003). Most of the states that have enacted revised Article 1 have enacted this definition, though a minority have enacted the prior version, which appears in (former) § 1-201(19) ("honesty in fact in the conduct or transaction concerned"). U.C.C. § 1-201(19) (1999) Even in those states, for transactions within the scope of Article 2 (sales of goods), the objective definition applies. U.C.C. § 2-103(1)(b) (2002) (for parties who are merchants).

faithfulness to an agreed common purpose and consistency with the justified expectations of the other party; it excludes a variety of types of conduct characterized as involving “bad faith” because they violate community standards of decency, fairness or reasonableness.<sup>125</sup>

....

[B]ad faith may be overt or may consist of inaction, and fair dealing may require more than honesty. A complete catalogue of types of bad faith is impossible, but the following types are among those which have been recognized in judicial decisions:  
... abuse of a power to specify terms . . . .<sup>126</sup>

A change-of-terms provision empowers the merchant to fix or change a term of the contract. In exercising this power, however, the merchant must act in good faith, which the foregoing authorities posit includes the observance of reasonable commercial standards of fair dealing and consistency with the reasonable expectations of the consumer. More than twenty years ago the Supreme Court of Oregon properly applied the obligation of good faith to police a merchant’s exercise of the power to change terms of a consumer contract. In *Best v. United States National Bank*,<sup>127</sup> defendant bank imposed a fee on depositors who wrote checks on accounts that had insufficient funds for the checks to clear (NSF fees). The depositors brought a class action alleging, *inter alia*, that the bank breached its obligation to set the fee in good faith.<sup>128</sup> The trial court granted the bank’s motion for

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125. RESTATEMENT (SECOND) OF CONTRACTS § 205 cmt. a (1979).

126. *Id.* cmt. d. See generally Steven Burton, *Good Faith Performance of a Contract Within Article 2 of the Uniform Commercial Code*, 67 IOWA L. REV. 1 (1981) [hereinafter Burton, *Good Faith*]; Steven Burton, *Breach of Contract and the Common Law Duty To Perform in Good Faith*, 94 HARV. L. REV. 369 (1980) [hereinafter Burton, *Breach of Contract*]; Clayton Gillette, *Limitations on the Obligation of Good Faith*, 1981 DUKE L.J. 619; Robert Summers, *The General Duty of Good Faith—Its Recognition and Conceptualization*, 67 CORNELL L. REV. 810 (1982). For a recent survey of cases discussing the obligation of good faith, see Edward J. Imwinkelried, *The Implied Obligation of Good Faith in Contract Law: Is It Time to Write Its Obituary?* 42 TEX. TECH L. REV. 1 (2009).

127. *Best v. U.S. Nat’l Bank*, 739 P.2d 554 (Or. 1987).

128. *Id.* at 555.

summary judgment, but the Supreme Court of Oregon reversed, stating:

When one party to a contract is given discretion in the performance of some aspect of the contract, the parties ordinarily contemplate that that discretion will be exercised for particular purposes. If the discretion is exercised for purposes not contemplated by the parties, the party exercising discretion has performed in bad faith.

....

In this case the Bank had the contractual discretion to set its NSF fees. . . . [T]hat discretion had to be exercised within the confines of the reasonable expectations of the depositors. . . .<sup>129</sup>

According to the court, those reasonable expectations were that charges for ancillary “services” would be set on the same basis as the charges for maintaining a checking account, viz., in an amount sufficient to cover the bank’s cost of providing the services plus its ordinary profit on those costs. When the bank’s internal communications revealed that the fees were far in excess of those costs (and profit), a fact finder could conclude that the fees were set to “reap the large profits to be made from the apparently inelastic ‘demand’ for the processing of NSF checks and in order to discourage its depositors from carelessly writing NSF checks.”<sup>130</sup>

A few years later the Oregon court had occasion to apply this limitation again. In *Tolbert v. First National Bank of Oregon*,<sup>131</sup> a class of consumers again challenged a bank’s exercise of the power to change terms when it increased its NSF fees. The facts differed from those in *Best*, however, because the consumers in *Tolbert* were informed of the amount of the NSF fee when they opened their

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129. *Id.* at 558.

130. *Id.* at 559.

131. *Tolbert v. First Nat’l Bank of Or.*, 823 P.2d 965 (Or. 1991).

checking accounts, and they were informed of subsequent changes in the fee.<sup>132</sup> The consumers in *Best* were not informed of either.<sup>133</sup> To the Oregon Supreme Court, these differences were critical. Since there was no evidence that the consumers in *Tolbert* were aware of the pricing mechanism for the bank's services, they had no reasonable expectation of the pricing mechanism for resetting the NSF fee.<sup>134</sup> The consumers were aware of the initial NSF fee, the contract empowered the bank to change the fee, the bank notified them before the changes became effective, and the consumers continued to maintain their accounts. The court held that summary judgment for the bank was appropriate.<sup>135</sup>

This reasoning severely limits, perhaps even abrogates, the obligation to perform in good faith. It permits the party with the power to set the terms to set them in any way it wishes. Under this reasoning, the bank could set its NSF fee at, say, \$1,000 per check, so long as it gave notice of the change, even if the change is not commercially reasonable and not consistent with the consumer's reasonable expectations. But this is not the law. The obligation to perform in good faith constitutes a substantive limit on the terms the dominant party may adopt under the authority of a change-of terms provision.

The reasonable expectations of a consumer include the expectation that the other party's specification of a term will not upset the allocation of risk fixed by the contract and will not subject the consumer to punitive sanctions for minor breaches of the contract.<sup>136</sup> To put the extreme case, retroactive changes are beyond reasonable expectations: the purchaser of a computer pursuant to an installment sales contract with a change-of-terms clause does not reasonably expect that the seller may increase the price after the computer has

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132. *Id.* at 966.

133. *Id.* at 967.

134. *Id.* at 970.

135. See *Grasso v. First USA Bank*, 713 A.2d 304, 311 (Del. Super. Ct. 1998) (holding there can be no breach of good faith when the contract expressly permits modification of the interest rate).

136. See *Burton, Breach of Contract*, *supra* note 126, at 372–73. See generally Robert Dugan, *Standardized Forms: Unconscionability and Good Faith*, 14 NEW ENG. L. REV. 711 (1979); Summers, *supra* note 126.

been delivered and put into use. Such an exercise of the power to change terms would not be in good faith, and would be unenforceable. Similarly, a change-of-terms clause in a contract for an automobile and an extended warranty cannot properly empower the seller to increase the price of the warranty if the car requires more than a specified number of repairs. These risks are allocated to the seller, and any change in the price reallocates the risk in an unexpected way.

The same, we would say, is true of increasing the interest rate on a fixed-rate credit card. If a creditor issues a consumer a fixed-rate card, any change in the rate pursuant to a change-of-terms provision should be effective only as to charges incurred after the change. The change should not be effective as to existing balances.<sup>137</sup> As to existing balances, the card issuer assumes the credit risk and should no more be able to change the interest rate than a creditor can hike the interest in a fixed-rate, closed-end auto loan or home mortgage loan. Absent a failure to pay, deterioration in the consumer's credit rating should not enable the creditor to increase the interest rate. Application of the changed rate to existing balances is an attempt to retake an opportunity that the card issuer gave up under the original contract. This is a prime example of the lack of good faith.<sup>138</sup>

Good faith also serves as a limit on the creditor's ability to make prospective changes in the interest rate. In terms of the amount of the increase, the sky is not the limit. And in terms of the timing of the change, the creditor must act reasonably. To illustrate, in *Rossman v. Fleet Bank (RI) National Association*,<sup>139</sup> the bank issued a no-annual-fee card that included a change-of-terms provision empowering it to change the features of the account at any time.<sup>140</sup> Approximately six months later the bank attempted to institute an annual fee.<sup>141</sup> The court held, however, that if the change-of-terms provision permitted

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137. *But see* *Barrer v. Chase Bank*, 566 F.3d 883, 889 (9th Cir. 2009) ("We agree with Chase that it must be able to adjust the price of credit according to how risky it is to lend to a given cardholder."); *Grasso*, 713 A.2d 304.

138. *E.g.*, *Burton, Breach of Contract*, *supra* note 126, at 372.

139. *Rossman v. Fleet Bank (RI) Nat'l Ass'n*, 280 F.3d 384 (3d Cir. 2002).

140. *Id.* at 388.

141. *Id.*

the bank to change the no-annual-fee feature whenever it wanted, the card was not properly described as “no-annual fee.”<sup>142</sup> The court decided the case under the Truth in Lending Act,<sup>143</sup> but the decision could just have easily been grounded on the bank’s obligation to perform in good faith.<sup>144</sup> The Credit CARD Act confirms that there is a substantive limitation on the timing of the bank’s power under the change-of-terms clause in *Rossman*: the Act amends the Truth-in-Lending Act by adding a prohibition against increasing the interest rate during the first year of an account. Notably, it does not characterize the increase as a violation of a disclosure provision of the statute.<sup>145</sup> Instead, the prohibition represents Congress’s judgment that it is not appropriate for a card issuer to use its authority under a change-of-terms clause to increase the interest on a fixed-rate card shortly after issuing the card.

Other provisions in the Credit CARD Act confirm this view that there are substantive limits on the power conferred by a change-of-terms provision. The Act requires that late fees, over-the-limit fees, and other fees be reasonable in amount.<sup>146</sup> It prohibits retroactive

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142. *Id.* at 395.

143. Regulation Z, 12 C.F.R. § 226.5(c) (2009) (“Disclosures shall reflect the terms of the legal obligation between the parties.”); see Official Staff Commentary, Regulation Z, 12 C.F.R. pt. 226, supp. I, cmt. 5(c)(1) (2009) (“The disclosures should reflect the credit terms to which the parties are legally bound at the time of giving the disclosures.”).

144. Indeed, the complaint in *Rossman* also alleged breach of contract, but that allegation was not before the court.

145. Credit CARD Act of 2009 § 101(d), Pub. L. No. 111-24, 123 Stat. 1737 (2009) (to be codified as Truth in Lending Act § 172(a), 15 U.S.C. § 1666k(a)).

146. Credit CARD Act of 2009 § 102(b), Pub. L. No. 111-24, 123 Stat. 1740 (2009) (to be codified as Truth in Lending Act § 149, 15 U.S.C. § 1665d):

(a) In General—The amount of any penalty fee or charge that a card issuer may impose with respect to a credit card account under an open end consumer credit plan in connection with any omission with respect to, or violation of, the cardholder agreement, including any late payment fee, over-the-limit fee, or any other penalty fee or charge, shall be reasonable and proportional to such omission or violation.

Unfortunately, the legislation refers to “penalty” fees and charges. Although it subjects them to the requirement of reasonableness, it would be better to characterize them simply as “other” fees and not support the notion that (reasonable) penalties are enforceable. Note, however, that it requires the penalty fee to be “reasonable and proportional to such omission or violation,” a standard that may be similar to the common-law standards for liquidated damages. The next subsection of § 149 directs the Federal Reserve Board to promulgate a rule establishing “standards for assessing whether the amount of any penalty fee or charge described under subsection (a) is reasonable and proportional to the omission or violation to which the charge relates.” In developing the rule, the Board is to consider the conduct of the

changes in the annual percentage rate, though it gives the creditor limited permission to increase the rate applicable to existing balances if the consumer defaults to the extent of being at least sixty days late in paying.<sup>147</sup> These provisions recognize the proposition that a change in the terms of an existing consumer contract must be reasonable. Although the Credit CARD Act applies only to open-end credit contracts, the proposition that good faith (and reasonableness) serve as limits on the exercise of authority granted by a change-of-terms clause applies to all consumer contracts. Given the expansive view of assent embodied by the objective theory of the mutual assent necessary for formation of contract, a substantive limitation on the power conferred by that assent is especially appropriate when it is given in the context of a contract of adhesion that is not read, not expected to be read, and not desired to be read.

Support for this view that there are limits on the power conferred by a change-of-terms provision may be found in the law governing other transactions. One example is the sale of goods, governed by the provisions of Article 2 of the UCC and discussed in Part I of this article. Another is rental of residential real estate. The Uniform Residential Landlord and Tenant Act permits a landlord to adopt regulations during the term of a lease, even in the absence of

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cardholder; the cost of that conduct to the creditor; the deterrence of that conduct; and any other factors that the Board deems appropriate. *Id.*

147. Credit CARD Act of 2009 § 101(b)(2), Pub. L. No. 111-24, 123 Stat. 1735 (2009) (adding new Truth in Lending Act §§ 171(a), 171(b)(4), to be codified at 15 U.S.C. § 1666j). Although the Act permits retroactive adjustment to this limited extent, it requires the card issuer to roll the rate back to its prior level if the consumer makes the minimum required payments for the six months following the effective date of the increase:

(a) **IN GENERAL**—In the case of any credit card account under an open end consumer credit plan, no creditor may increase any annual percentage rate, fee, or finance charge applicable to any outstanding balance, except as permitted under subsection (b).

(b) **EXCEPTIONS**—The prohibitions under subsection (a) shall not apply to—

....

(4) an increase due solely to the fact that a minimum payment by the obligor has not been received by the creditor within 60 days after the due date for such payment, provided that the creditor shall—

....

(B) terminate such increase not later than 6 months after the date on which it is imposed, if the creditor receives the required minimum payments on time during that period.

authorization in the lease.<sup>148</sup> But any such regulation is enforceable only if it is not for the purpose of evading the landlord's obligations, does not make a substantial modification of the bargain, and is reasonably related to the purpose for which it is adopted.<sup>149</sup>

### CONCLUSION

Contracts of adhesion abound. In the context of consumer transactions, especially, they are nearly universal. The drafting party does not want the consumer to read the contract document, and it is not rational for a consumer to read the document, except perhaps for the few dickered terms. The other terms are not subject to negotiation and are likely to be difficult to understand and unlikely ever to be invoked. Use of contract provisions that authorize the dominant party to change the terms of the contract at will are omnipresent in a wide range of contracts for credit and services. Taken literally, these provisions authorize the dominant party to make any change it desires, adding whatever term it desires. In this article we have shown that there is ample authority for imposing limits on the exercise of this power. This authority originates in federal and state legislation and administrative regulation, the UCC, and the common law. We call on the dominant party in consumer transactions to exercise its power with restraint, in a manner consistent with the adhering party's reasonable expectations, and we call on the courts to draw on their legal authority, especially the obligation of good faith, to rein in a party that would use its power under a change-of-terms provision in a manner inconsistent with the reasonable expectations of the consumer.

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148. UNIF. RESIDENTIAL LANDLORD & TENANT ACT § 3.102(a) (1972).

149. *Id.* § 3.102(a)–(b). For several interpretive challenges under the language of this section, see Horwitz, *supra* note 23, at 96.



