

# A CONTRACTARIAN APPROACH TO UNCONSCIONABILITY

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## INTRODUCTION

Freedom of contract can be defended on the basis of consequentialist and nonconsequentialist views. According to the former, individuals can improve their condition when they are free to exchange goods and services by making contracts. Improvement of condition can occur by affecting both the production and the consumption function. First, free exchanges facilitate division of labor and the efficient allocation of the factors of production. Second, since individuals have different utility functions, there is room for mutually advantageous agreements. Nonconsequentialist views defend freedom of contract on ethical grounds. So liberalism holds that a just society must treat individuals as autonomous beings entitled to choose and do as they see fit provided they don't violate others' rights. One way of treating individuals in this way is to let them free to pursue and accomplish associative endeavors for which freedom of contract is often an indispensable institution.<sup>1</sup>

Given the strong case for freedom of contract, the burden of proof falls on any position that purports to restrain its scope. The doctrine of unconscionability authorizes courts to introduce a variety of restrictions on contractual freedom. Specifically, it allows a court to refuse to enforce unfair private agreements, or to modify the terms of a contract that it deems unfair or unreasonable.<sup>2</sup> Arthur Leff introduced a famous distinction between two kinds of unconscionability: procedural and substantive.<sup>3</sup> Leff called bargaining naughtiness "procedural unconscionability," and he used the name "substantive unconscionability" to refer to "evils" in the resulting contract.<sup>4</sup> Procedural unconscionability refers to the procedures of contract formation and, particularly, to various ways in which proper consent may be absent. It therefore comes close to fraud, mistake, duress, and necessity, which are the classic contract-law defenses. Courts have considered monopoly power, unfair surprise, and absence of bargaining process (v.gr. take-it-or-leave-it contracts, standard forms, etc.)

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<sup>1</sup> Richard A. Epstein, *Unconscionability: a Critical Reappraisal*, 18 J. Law & Econ. 293-311 (1975).

<sup>2</sup> See, for instance: Restatement of Contracts (Second) § 208; U.C.C. § 2-302. In civil law jurisdictions, the doctrine of laesio enormis, which is an expansive construal of a remedy in Roman law, performs basically the same function as the doctrine of unconscionability; see: James Gordley, "Contract, Property, and the Will", in Harry N. Scheiber (ed.), *The State and Freedom of Contract* (1998).

<sup>3</sup> Arthur Allen Leff, *Unconscionability and the Code-The Emperor's New Clause*, 115 U. Pa. L. Rev. 485 (1967).

<sup>4</sup> Op. cit., at 487.

as causes that can invalidate the contracting process.<sup>5</sup> Substantive unconscionability refers to unfair, exploitative, or unreasonable contract terms. It has been taken to include, for instance, add-on and waiver-of-defense clauses, warranty disclaimers, exclusion of liability for consequential damages, abusive interest rates, and biased labor arbitration terms.<sup>6</sup>

The unconscionability doctrine allows courts to deny enforceability of unconscionable contracts or to modify their terms. This fact can be described in terms of the influential distinction between protection of entitlements by a property rule and a liability rule, drawn by Calabresi and Melamed.<sup>7</sup> As is well known, while a property rule protects a given entitlement by means of an injunction remedy, a liability rule authorizes the court to fix monetary compensation when the entitlement has been violated. Richard Craswell has applied this distinction to the entitlements established by the doctrine of unconscionability.<sup>8</sup> Clearly the point of the doctrine is to award contracting parties entitlement against unconscionable advantage-taking. When X tries to take unfair advantage from Y in a contract setting, Y's entitlement can be protected by a property rule or by a liability rule. In the former case, the court will plainly reject the enforceability of the contract; in the latter, the court will award damages by adjusting the price of the contract (e.g., diminishing the interest rate in a loan).

Conjoining the distinction between procedural and substantive unconscionability, and the division between protection by a property rule and by a liability rule, we obtain four non-excludable forms of the doctrine:

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<sup>5</sup> Richard A. Epstein, *Unconscionability: a Critical Reappraisal*, see note 1; Alan Schwartz, *A Reexamination of Nonsubstantive Unconscionability*, 63 Va. L. Rev. 1053 (1977).

<sup>6</sup> Seana Valentine Shiffrin, *Paternalism, Unconscionability Doctrine, and Accommodation*, 29 Phil & Pub Affairs (2000), at 205-6.

<sup>7</sup> Guido Calabresi and A. Douglas Melamed, *Property Rules, Liability Rules, and Inalienability: One View of the Cathedral*, 85 Harv. L. Rev. 1089 (1972).

<sup>8</sup> Richard Craswell, *Property Rules and Liability Rules in Unconscionability and Related Doctrines*, 60 U. Chi. L. Rev. 1 (1993).

Unconscionability entitlements	Substantive	Procedural
Protection by property rule	1. Substantive entitlement protected by injunction	3. Procedural entitlement protected by injunction
Protection by liability rule	2. Substantive entitlement protected by damages	4. Procedural entitlement protected by damages

**Fig. 1. Forms of the Unconscionability Doctrine**

Paternalism is the most common defense of the doctrine of unconscionability. Indeed, philosophers who discuss paternalism often give unconscionability as example of paternalistic measures.<sup>9</sup> On this view, the doctrine involves a cluster of paternalistic restraints on freedom of contract. According to Joel Feinberg, “the principle of legal paternalism justifies state coercion to protect individuals from self-inflicted harm or, in its extreme version, to guide them, whether they like it or not, toward their own good.” This definition is not particularly useful to describe paternalism in contract law. While paternalism in criminal law forbids agents to commit self-damaging acts, contract law paternalism characteristically refuses to enforce contracts that are harmful to one of the parties. The former fits very well with Feinberg’s definition, but the latter requires a broader definition. In fact, when the state applies the doctrine of unconscionability it often does not exert coercion but rather refuses to use it to enforce a contract. Specifically, forms (1) and (3) of unconscionability entitlements don’t involve state coercion, but its absence.

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<sup>9</sup> Joel Feinberg, Legal Paternalism, and Gerald Dworkin, Paternalism, in Rolf Sartorius (ed.), Paternalism (1983).

Seana Shiffrin has provided a definition of paternalism that is more adequate to frame the paternalistic account of unconscionability. She understands paternalism by A toward B as

behavior (through action or through omission) (a) aimed to have (or to avoid) an effect on B, (b) that involves the substitution of A's judgement or agency for B's; (c) directed at B's own interests or matters that legitimately lie within B's control and (d) undertaken on the grounds that compared to B's judgement or agency with respect to those interests or other matters, A regards her judgement or agency to be (or as likely to be), in some respect, superior to B's.<sup>10</sup>

This definition has one clear advantage over traditional characterizations. As said before, forms (1) and (3) of the unconscionability doctrine do not involve government's use of coercion, but rather its refusal to use coercion for contract enforcement. Therefore, traditional definitions of paternalism focused on "active" coercive interventions (e.g., Feinberg's definition quoted above) cannot accommodate "passive" forms of intervention typical of contract law. Shiffrin's definition covers such "passive" forms, because it allows paternalist behavior to be committed through inaction.

Paternalistic accounts of the unconscionability doctrine are problematic because liberalism is often associated with anti-paternalism.<sup>11</sup> John Stuart Mill declared that "...the only purpose for which power can be rightfully exercised over any member of a civilized community, against his will, is to prevent harm to others. His own good, either physical or moral, is not a sufficient warrant."<sup>12</sup> Mill's invective against legal paternalism was so powerful that contemporary liberal theorists often reject out of hand a paternalist approach to legal institutions. Thus, Shiffrin says that paternalism "directly expresses insufficient respect for the underlying valuable capacities, powers, and entitlements of the autonomous agent. Those who value equality and autonomy have special reason to resist paternalism toward competent adults."<sup>13</sup> Shiffrin's definition of paternalism makes it true by definition that paternalism is disrespectful of individual autonomy. In effect, condition (d) supra says that a government taking a

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<sup>10</sup> Seana Valentine Shiffrin, *Paternalism, Unconscionability Doctrine, and Accommodation*, at 218.

<sup>11</sup> Robert Nozick, *Anarchy, State, and Utopia* 1974, at 58; Bruce A. Ackerman, *Social Justice in the Liberal State* 1980, at 10-12; Eric Mack, "In Defense of the Jurisdiction Theory of Rights", in Guido Pincione and Horacio Spector (eds.), *Rights, Equality, and Liberty*, Dordrecht, Kluwer, 2000.

<sup>12</sup> J.S. Mill, *Utilitarianism, On Liberty, Essay on Bentham* (Mary Warnock ed.) (1962), at 135.

<sup>13</sup> Shiffrin, *op. cit.*, at 220.

paternalistic measure must regard its judgement as superior to citizens' judgements. This is per se insulting and humiliating to autonomous individuals.

My purpose in this paper is to discuss two nonpaternalistic defenses of the unconscionability doctrine. In the first section, I will discuss Shiffrin's view, which is premised on self-regarding reasons to refrain from collaborating with people who try to obtain an unfair advantage via a contractual transaction. I will argue that this view has two main shortcomings. First, it is irrelevant to procedural unconscionability and to substantive unconscionability protected by a liability rule (forms 2, 3, and 4). Second, though it is certainly relevant to form 1 (substantive unconscionability protected by a property rule), it is in the end defective because, except under special conditions, informed and free consent justifiably removes transactional unfairness.<sup>14</sup> In the second section, I will propose a contractarian approach to unconscionability. I will argue that this approach provides a defense for procedural unconscionability (forms 3 and 4). It can also bolster some forms of substantive unconscionability (forms 1 and 2). Specifically, it admits "impure substantive unconscionability," which takes inequitable contract terms as evidence of procedural unconscionability, but rejects "pure substantive unconscionability," which is independent of any procedural flaw.<sup>15</sup>

## **I. THE SELF-REGARDING APPROACH.**

Shiffrin proposes a "self-regarding" theory of unconscionability.<sup>16</sup> According to this view, the state, via the courts, should not enforce private agreements whereby one party exploits or takes unfair advantage of the other.<sup>17</sup> While the state can legitimately facilitate private agreements by enforcing contracts, thus deterring contractual breach or remedying its harmful effects, the state may not assist contracting parties to benefit

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<sup>14</sup> It might be also argued (1) that substantive unconscionability relies on the theory of the "just price", and (2) that this theory is inconsistent with contemporary economics. I believe this is a weak argument. It is true that the former claim is plausible. In fact, substantive unconscionability requires some standard of equality in exchange or bargaining equity. But contemporary economics may allow some of these standards; for instance, equality in exchange could be associated with competitive market prices. Some historians of economic thought argue that this was the real meaning of "just price", so the latter claim is controversial. See: James Gordley, *Equality in Exchange*, 69 Cal. L. Rev. 1587 (1981).

<sup>15</sup> Shiffrin uses the label "pure substantive unconscionability" in the same sense; *op. cit.*, at 209.

<sup>16</sup> Shiffrin, *op. cit.*, at 227.

<sup>17</sup> The view had been insinuated as a theoretical possibility by Joel Feinberg (*Legal Paternalism*, in Rolf Sartorius (ed.), *Paternalism* (1983), at 13): "One might argue that what is odious in 'harsh and unconscionable' contracts, even when they are voluntary on both sides, is not that people should suffer the harm they freely risk, but rather that another party should 'exploit' or take advantage of them'.

from unfair or exploitative transactions. Shiffrin claims that “refusal to enforce would only make sense when the content and outcome of the contract were morally objectionable in such a way as to implicate the judge’s and the state’s moral stature”.<sup>18</sup> When the state fulfills a moral duty not to get involved in immorality via the doctrine of unconscionability, it does not take a paternalist stance. It is worth quoting Shiffrin’s clear prose in this respect:

The refusal to enforce need not represent an effort to supplant the judgment or action of the contracting parties or an intention to stop them from engaging in (solely) mutually regarding immoral action. (Such efforts would be paternalist, on my account). Instead, the motive may reasonably be a self-regarding concern not to facilitate or assist harmful, exploitative, or immoral action.<sup>19</sup>

Shiffrin treats the moral duty not to assist evil transactions as a “side constraint.”<sup>20</sup> Thus, she claims that I could refuse—in a nonpaternalist way—to buy cigarettes for you (a smoker) because “I think that I should not perform substantial actions that contribute to your addiction.”<sup>21</sup> It is a “side constraint” because it holds even if I can predict that, as a result from my abstention, someone else will buy more cigarettes for you, or more pernicious ones. By the same token, the state should withhold its coercive power to assist parties to enforce unfair agreements even if it could predict that, as a result from its inaction, more citizens will be victims of unfair actions (perhaps because the state’s refusal causes a decline in economic growth).<sup>22</sup> Indeed, Shiffrin endorses a possibly counterproductive policy proposal on nonconsequentialist grounds:

The state has at least a permission and perhaps a deontological commitment not to assist grossly unfair treatment of one of its citizens by another. Even if the abandonment of the unconscionability doctrine would be more efficient and

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<sup>18</sup> Shiffrin, op. cit., p. 231.

<sup>19</sup> Op. cit., p. 224.

<sup>20</sup> The locus classicus for “side constraints” on state action is Robert Nozick, *Anarchy, State, and Utopia*, 1974, Ch. 3. A “side constraint” is a moral prohibition falling on each individual agent that rules out any kind of goal-oriented moral reasoning (e.g., welfare maximization).

<sup>21</sup> Shiffrin, op. cit., p. 224.

<sup>22</sup> Many readers would probably regard this (presumed) consequence as unacceptable, but I will not press the point. As moral philosophers know very well, downplaying such consequences is a distinctive mark of nonconsequentialism.

might enable more generous redistribution, there would still be reason to refuse to insert the state's power between citizens to assist exploitative behavior.<sup>23</sup>

*1. Shortcoming One: Irrelevant to Procedural Unconscionability and Substantive Unconscionability Protected by the Liability Rule.*

Shiffrin does not consider procedural unconscionability (forms 3 and 4), that is, legal defenses to the effect that a contract is not the outcome of a truly voluntary agreement. She takes this decision "in part, because disputes about which agreements are truly voluntary often reach an impasse, and, in part, because there is a distinct defense worth pursuing."<sup>24</sup> Shiffrin's reluctance to resort to a criterion of voluntariness is understandable in the context of a nonconsequentialist position. In fact, nonconsequentialist theories tend to run into circularity when their fundamental principles are couched in terms of freedom or voluntariness. Thus, critics claim that the right to freedom cannot have a foundational role because freedom is a moralized concept and, therefore, it must rely on independent normative principles.<sup>25</sup> Similarly, Anthony Kronman claims that contract law depends on distributive justice because the concept of voluntariness --essential to contract law postulates-- barely has meaning in the absence of independent normative principles ascertaining which forms of advantage-taking are permissible.<sup>26</sup> So I believe that Shiffrin's reluctance is justified. She could not account for procedural unconscionability without further theoretical resources.

The "distinct defense" Shiffrin is concerned with is pure substantive unconscionability, which spots contract terms regardless of contract formation. Shiffrin assumes a "will" theory of promising, which roughly "holds that promises bind when they are made by autonomous people under suitable conditions, such that the promise is the free expression of that person's will."<sup>27</sup> Accordingly, she assumes

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<sup>23</sup> Op. cit., p. 235. For an excellent study of deontological self-defeating proposals, like Shiffrin's, see: Guido Pincione and Fernando Teson, Rational Ignorance and Political Morality, Philosophy and Phenomenological Research, forthcoming.

<sup>24</sup> Op. cit., p. 209.

<sup>25</sup> Jeffrey H. Reiman, The Fallacy of Libertarian Capitalism, Ethics 92 (1981); Gerald Cohen, *The Structure of Proletarian Unfreedom*, 12 Phil and Pub Aff 2; G.A. Cohen, Self-Ownership, World-Ownership, and Equality, in Frank S. Lucash (ed.), *Justice and Equality, Here and Now* (1986); David Zimmerman, Coercive Wage Offers, Philosophy and Public Affairs 10 (1981).

<sup>26</sup> Anthony T. Kronman, "Contract Law and Distributive Justice" 89 Yale Law Journal (1979), Sección I, ps. 475-497.

<sup>27</sup> Op. cit., pp. 209-210.

that unconscionable contracts “are made voluntarily, by responsible agents, and under conditions of sufficient information”<sup>28</sup>

Shiffrin is also unable to explain form 2, where the state, via the judiciary, modifies the terms of unconscionable agreements. The self-regarding theory enjoins nonintervention, that is, refusal to enforce, on the basis of a general moral duty not to collaborate with the execution of immoral plans. So understood, the doctrine of unconscionability is not affected by the charge of paternalism. But under form 2 the judge must not merely remain passive, refraining from assisting evildoing. Instead, she must intervene to redress contractual unfairness, even if the contract is procedurally impeccable, that is, even if the parties have given free and informed consent to it. Such interventions typically proceed in the way of takings at “administrative”, noncontractual prices.

The inability to account for form 2 may not be a great problem for Shiffrin, as she also leaves this form out of her discussion:

The unconscionability doctrine, famously, operates as a shield and not as a sword. One may protect oneself against enforcement of an unconscionable contract, but one may not obtain damages for having been subject to an unconscionable offer; nor may one seek restitution for compliance with an unconscionable contract.<sup>29</sup>

However, it is instructive to linger over the question of why the self-regarding theory cannot justify judicial intervention in form 2 without sliding into some form of paternalism. As we saw above, for Shiffrin the conditions of paternalist behavior might be true of an action or an omission.<sup>30</sup> One might think that self-regarding behaviors might also be actions or omissions. Suppose then that a judge intervenes to adjust the price of a contract by arguing that the state has a duty to actively thwart parties’ plans when these plans, if left undisturbed, would violate equality of condition. Moreover, suppose that when the judge is asked about her motives, she makes it clear that she is guided by a self-centered moral reason not to let an exploitative or unfair plan succeed. Does this make sense? Does the judge’s behavior not look like a form of moral paternalism?

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<sup>28</sup> Shiffrin, at 209.

<sup>29</sup> Op. cit., p. 229.

<sup>30</sup> Op. cit., p. 218.

The possibility for the state to take active intervention in a private transaction on nonpaternalist, self-regarding motivations depends on how we demarcate the boundaries of each agent's moral jurisdiction. Shiffrin concedes that, "a full account of paternalism will depend on an account of what sorts of interests and matters legitimately lie within an agent's control."<sup>31</sup> Two alternatives emerge. Either the contract lies within the state's legitimate area of agency and judgment or within the parties'. If the former holds, that is, if parties' transactions lie within the state's control, the possibility of paternalist behavior vanishes, since every conceivable instance of paternalist intervention in private transactions could be vindicated on the grounds of a morally guided self-regarding motivation. So to preserve the distinction between paternalist and self-regarding behavior --which Shiffrin holds--, we must assume that the parties' jurisdiction encompasses the contract. But then, if the latter alternative is true, the judge cannot possibly be guided by a merely self-centered, nonpaternalist concern, because her intervention involves exercising moral judgment on a matter that lies within the parties' control. In contrast, when the judge merely refuses to enforce the contract (form 1 of unconscionability), "she legitimately exercises moral judgment about herself and her range of activity."<sup>32</sup> This asymmetry between intervention and nonintervention holds because the distinction between self-regarding and paternalistic motivations is conditional on autonomy rights. Basically, a nonpaternalist, purely self-regarding motivation to take action on matters that lie within someone else's control is an oxymoron. But a self-regarding, non-paternalist motivation not to collaborate in matters lying within someone else's jurisdiction is always possible.

## *2. Relevant to form 1 but defective because consent removes the unfairness.*

Does Shiffrin's self-regarding rationale really apply to form 1 of unconscionability, in particular to cases of pure substantive unconscionability, where fraud, coercion, necessity and other procedural vices are ex hypothesi absent? Since procedurally perfect agreements are the free expression of the parties' will, it is difficult to see how the content of these agreements could be unfair or inequitable. In fact, according to the maxim "Volenti non fit injuria" (to one who consents no harm is done), acts which would otherwise be impermissible infringe no right when the right holder gives free and informed consent, for instance via a well-formed contract.<sup>33</sup> Shiffrin does not spell out a theory of transactional unfairness, so a conclusive assessment of her view is difficult. Shiffrin might certainly reject the maxim "Volenti non fit injuria." However, according to most plausible moral theories, if a contract has been formed

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<sup>31</sup> Op. cit., p. 218.

<sup>32</sup> Op. cit., p. 226.

<sup>33</sup> Joel Feinberg, Legal Paternalism, in Rolf Sartorius (ed.), Paternalism (1983), at 4.

with free and informed consent, in principle its terms cannot be taken to be unfair or exploitative. This means that, unless a special argument is offered, substantive unconscionability must be considered of the impure or evidentiary variety: grossly inequitable terms can show that contract formation has been vitiated by a procedural defect.

Shiffrin assumes that substantive unfairness is not incompatible with free and informed consent.<sup>34</sup> As said above, this assumption is controversial. Yet there is one natural grounding of it that Shiffrin does not explore. Procedurally perfect agreements could be unfair if they sought to transfer nonwaivable, inalienable rights. In fact, the connection between unconscionability and inalienability is straightforward. Thus Hegel treated a sale on inalienable goods as a limit case of *laesio enormis*.<sup>35</sup> In a similar vein, Shiffrin could claim that contracts seeking to transfer inalienable rights are substantively unconscionable, even if they had been formed via unobjectionable procedures. Because in such cases the *Volenti maxim* would not hold, Shiffrin could claim that the state would be morally implicated if it enforced contracts that violated inalienable rights (e.g., a right to fair treatment). This strategy would be exposed, however, to two serious problems. First, inalienability can hardly be detached from paternalism in the context of nonconsequentialist theories. Preventing individuals from relinquishing or transferring their rights seems “directed at matters that legitimately lie within their control”. If Shiffrin availed herself of this strategy to bolster substantive unfairness, she would commit herself to a paternalist defense of unconscionability, just the defense she wants to avoid. Second, inalienable rights are surely exceptional in liberal theory. Even if the self-regarding theory could explain form 1 of unconscionability on the basis of nonwaivable rights, it would only cover very few cases. In fact, free and voluntary exchanges over the vast majority of liberal rights would still be unobjectionable on the grounds of unconscionability or unfairness.

Shiffrin’s denial that free and informed consent removes a transaction’s unfairness is not sufficient for her argument to work. She must also claim that free and informed consent does not release a third party from moral responsibility in assisting the transaction. However, there is an indication that Shiffrin believes that a third party who aids an exploitative transaction need not be morally implicated when the exploited party has consented to the transaction. In fact, she describes a hypothetical she calls “Supererogatory Refusal” thus:

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<sup>34</sup> Op. cit., p. 209.

<sup>35</sup> G.W.F. Hegel, *Elements of the Philosophy of Right*, edited by Allen W. Wood (1991), § 77 (at 107).

A and B ask C to assist them in their endeavor, claiming that C's participation is essential. C believes that the deal treats B unfairly, but, given B's consent, C does not think that her participation will morally implicate C in the unfairness. Rather, moral responsibility for A's exploitative behavior lies with A alone. C refuses to help anyway, out of concern for B, but not because C believes that facilitation would be morally wrong or that he has a duty not to. C simply wants to protect B.<sup>36</sup>

Shiffrin contrasts this case with another she calls "Self-Regarding Refusal," where C declines her intervention on moral grounds:

A and B ask C to assist them in their endeavor, claiming that C's participation is essential. C believes the deal treats B unfairly and that A is taking advantage of B. C refuses to help on the grounds that assistance would implicate C in the exploitation. C refuses to direct her energies to facilitating an exploitative relationship, believing it both to be immoral to facilitate and an unworthy investment of time and energy, especially given her other commitments and ideals.<sup>37</sup>

Shiffrin claims that, while Supererogatory Refusal involves paternalism, Self-Regarding Refusal does not. The alleged reason is that in Self-Regarding Refusal C decides not to assist on a self-regarding moral motivation not to collaborate with A's wronging B. But in framing Supererogatory Refusal Shiffrin insinuates that B's consent may wipe out C's moral responsibility in assisting A and B to carry out their endeavor. (Shiffrin seems to say that consent may remove C's, but not A's moral responsibility in an unfair transaction.) Now B's consent is by hypothesis also present in Self-Regarding Refusal, because this case models agreements affected by pure substantive unconscionability, that is, free from procedural unconscionability. In regard to such agreements, "given the parties' consent," the judge might also not be morally implicated in the transaction if she participated by enforcing the contract. But then, if the judge were not morally implicated in the transaction, she should enforce the contract on the basis of an underlying moral or institutional duty to enforce contracts. My point is that, even if the parties' consent could not make an exploitative or unfair agreement morally permissible, it could preempt the judge's moral responsibility in assisting them (in the absence of other moral objections). Because

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<sup>36</sup> Op. cit., p. 227 (italics added).

<sup>37</sup> Ibid.

Shiffrin does not rule out this possibility, the self-regarding rationale lies on shaky foundations.

## II. THE CONTRACTARIAN APPROACH.

Unconscionability and other measures associated with paternalism are often seen as inimical to individual autonomy and free choice. However, at least since Mill, social theorists have been aware that some forms of paternalism can be reconciled with the principle of free choice.<sup>38</sup> For instance, Mill claims in the Principles of Political Economy that some kinds of government interference with individuals' choices are taken for the individuals' good without detriment to individual liberty.<sup>39</sup> Maximum-hours legislation is one example. Mill says that such measures are "required not to overrule the judgment of individuals respecting their own interest, but to give effect to that judgement: they being unable to give effect to it except by concert, which concert again cannot be effectual unless it receives validity and sanction from the law."<sup>40</sup> In contemporary economic jargon, such interventions are addressed to avoid collective action problems. Such problems typically arise in prisoner's dilemma situations.<sup>41</sup>

Paternalistic interventions addressed to correct disharmonies between individual and collective rationality in prisoner's dilemma situations do not convey an insulting or humiliating message. When government compels an individual to follow an efficiency-enhancing rule, it doesn't say, "My judgement is superior to yours," but rather something like, "According to widely accepted social science in the absence of government intervention individual rational agents will follow strategies that impair their individual preferences as they see them." It is not on the assumption of irrationality or lack of competence that government takes these measures, but rather on the assumption that individuals are fully rational. Just because individuals act in accordance with the postulates of individual rationality, they will sometimes fail to achieve those outcomes that are rational from a collective perspective.

### *1. Paternalism and Individualized Hypothetical Consent.*

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<sup>38</sup> Donald VanDeVeer, *Paternalistic Intervention* (1986).

<sup>39</sup> J. S. Mill, *Principles of Political Economy* (1894), Bk. 5, Ch. XI.

<sup>40</sup> *Op. cit.*, at 581.

<sup>41</sup> The literature on the Prisoner's Dilemma is copious. See, for instance: Garret Hardin, "The Tragedy of the Commons," *Science*, 162 (13 December 1968): 1243-1248; Gregory Kavka, *Hobbesian Moral and Political Theory* (1986); David Gauthier, *Morals by Agreement*, Oxford: Clarendon Press (1986); David Schmidtz, *The Limits of Government: An Essay on the Public Goods Argument* (1991).

Mill's theory of paternalistic interventions relies on a mismatch between individual and group rationality, but a generalized argument based on the limitations of human rationality might ground other paternalistic measures. Gerald Dworkin famously suggested that "paternalistic" interventions can be defended on the basis of systematic limitations of our cognitive and emotional capacities. He gives the example of Odysseus' choice to be tied to the mast, which was based on his prediction that he would otherwise yield to the Sirens' singing.<sup>42</sup> We can contrast Dworkin's view with Mill's by using economic notions. While Mill was concerned about prisoner's dilemma failures of individual rationality, Dworkin seeks to ground some paternalist interventions on what Herbert Simon termed "bounded rationality".<sup>43</sup> Like Mill's view, Dworkin's account of paternalism is not inconsistent with the principles of liberalism because it appeals to consent: "Under certain conditions it is rational for individuals to agree that others should force them to act in ways that, at the time of action, the individuals may not see as desirable."<sup>44</sup> Dworkin suggests a "hypothetical consent" test to evaluate "paternalist" interferences:

I suggest that since we are all aware of our irrational propensities -- deficiencies in cognitive and emotional capacities and avoidable and unavoidable ignorance-- it is rational and prudent for us to take out "social insurance policies". We may argue for and against proposed paternalistic measures in terms of what fully rational individuals would accept as forms of protection.<sup>45</sup>

Dworkin's test relies on "individualized hypothetical consent."<sup>46</sup> What the test requires is a counterfactual inquiry about what the agent interfered with would have consented to. One difficult issue is to select the group of choices on which paternalistic restrictions can be justified by appeal to hypothetical rational consent: "I suggest that we think of the imposition of paternalistic interferences in situations of this kind as being a kind of insurance policy that we take out against making decisions that are far-reaching, potentially dangerous, and irreversible."<sup>47</sup>

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<sup>42</sup> Gerald Dworkin, *Paternalism*, in Rolf Sartorius (ed.), *Paternalism* (1983), at 29.

<sup>43</sup> Herbert A. Simon, *Bounded Rationality*. In: J. Eatwell, M. Millgate & P. Newman (eds.): *The New Palgrave: A Dictionary of Economics* (1987).

<sup>44</sup> Gerald Dworkin, *Paternalism*, in Rolf Sartorius (ed.), *Paternalism* (1983), at 29.

<sup>45</sup> *Ibid.*

<sup>46</sup> I borrow the label from Donald VanDeVeer, *Paternalistic Intervention*, at 75.

<sup>47</sup> *Op. cit.*, at 31.

Dworkin's defense of paternalism does not oppose autonomous choices. On the contrary, hypothetical rational consent would only sanction autonomy-enhancing restrictions: 'I suggest that we would be most likely to consent to paternalism in choice instances in which it preserves and enhances for individuals their ability to rationally consider and carry out their own decisions.'<sup>48</sup>

Whatever the merits of the individualized hypothetical consent position as regards paternalism, it is an inadequate basis for the unconscionability doctrine. There are three reasons for this. First, the typical form of the individualized hypothetical consent view subordinates the legitimacy of a paternalistic interference to what the agent would have agreed to immediately before the interference. The application of this view to the doctrine of unconscionability has special difficulties. Unlike paternalist interventions in criminal or regulatory law, the doctrine of unconscionability typically affects two agents (i.e., the promisor and the promisee). Suppose we want to establish whether a certain nullification on the grounds of unconscionability is justifiable. The individualized hypothetical consent view suggests testing counterfactual consent of each party at a moment immediately before the contract. This counterfactual test will generally yield predictably conflicting results. While the promisor would surely have agreed to the court's paternalistic interference, the promisee might have strongly opposed to it. Since unconscionability curbs both parties' contractual freedom, we have no reason to privilege one party's hypothetical choice to the detriment of the other's. Against this background, how can we settle the dispute?

Second, the doctrine of unconscionability involves not only particular interferences with an agent's contractual liberty but also wide-ranging institutional choices (e.g., empowering courts to nullify contracts) and a vast array of causal effects (e.g., price adjustments). If our counterfactual test is couched in terms of an agent's consent to a particular act of paternalistic interference, all these complexities get neglected. What we need is a perspective from which we can assess whether a social policy of interference can achieve a certain goal. The perspective suggested by the individualized hypothetical consent view is too narrow. Therefore, our approach should be rule-oriented, rather than focused on particular acts.

Finally, a rational person could allow the state to interfere with her less than voluntary choices. To this effect she should follow certain criteria indicating when a choice is not fully voluntary. Indeed, rational hypothetical consent, no less than rational actual consent, must follow certain rules or criteria. One obvious possibility for a rational person is to adopt the legal standard of voluntariness. Procedural unconscionability might be warranted in this way. But, as we saw above, voluntariness is a normative

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<sup>48</sup> Op. cit., at 33.

notion.<sup>49</sup> As Kronman argues, there is no factual basis for deciding that, for instance, force excludes voluntariness but fraud is consistent with it.<sup>50</sup> And a mere appeal to abstract notions of rights or liberty would not suffice, because such notions are also reliant on normative principles. As Kronman remarks, "...we cannot say whether the liberty principle is violated if one person takes advantage of another by concealing valuable information in the course of an exchange, unless we have already decided that it is part of the first person's liberty that he be allowed to exploit the information he possesses in this way and not a part of the other person's liberty that he be free from such exploitation."<sup>51</sup> Therefore, an additional problem of the individualized hypothetical consent view is that it lacks theoretical resources for establishing a principle capable of drawing a line between voluntary and involuntary agreements.

## 2. *The Core of the Contractarian Account.*

The rejection of individualized hypothetical consent naturally leads to a search for other consent-based views of the unconscionability doctrine. Specifically, I submit that the unconscionability doctrine should be understood along contractarian lines, rather than in terms of individualized hypothetical consent. This view accords well with John Rawls's brief treatment of paternalism.<sup>52</sup> Rawls trades on Gerald Dworkin's view of paternalism as an insurance to suggest a contractarian reading of paternalist interventions. Thus, he maintains that "the principles of paternalism are those that the parties would acknowledge in the original position to protect themselves against the weakness and infirmities of their reason and will in society".<sup>53</sup> However, I will not resort to Rawls's own premises, or to any other contractarian theory in particular.<sup>54</sup> Instead, my reasoning will be premised on an "ecumenical" contractarian/contractualist position that differentiates two levels of choice: constitutional choice and sub-constitutional (or in-period) choices.<sup>55</sup> At the

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<sup>49</sup> See text accompanying notes 25 and 26.

<sup>50</sup> Anthony T. Kronman, *op. cit.*, at 475-497.

<sup>51</sup> *Op. cit.*, at 483.

<sup>52</sup> Rawls dedicates three paragraphs of *A Theory of Justice* to this issue: *A Theory of Justice* (1971), at 248-50.

<sup>53</sup> *Op. cit.*, 249.

<sup>54</sup> However, the reader may find helpful to know that I have in mind, apart from Rawls's work, the following pieces of contractarian/contractualist literature: James M. Buchanan and Gordon Tullock, *The Calculus of Consent-Logical Foundations of Constitutional Democracy*, in *The Collected Works of James M. Buchanan*, v. 3, 1999 (original edition, 1962); Ronald Dworkin, *What is Equality? Part 2: Equality of Resources*, 10 *Philosophy & Public Affairs*, 1981; James M. Buchanan, *The Limits of Liberty-Between Anarchy and Leviathan*, in *The Collected Works of James M. Buchanan*, v. 7, 1999 (original edition, 1975). I do not set great store by the distinction between contractarianism and contractualism.

<sup>55</sup> Viktor J. Vanberg, *Rules & Choice in Economics*, 1994, at 218.

constitutional level, fundamental principles or rules for coordination and (fair) cooperation are selected. At the sub-constitutional level, individuals make particular transactions. Unlike the individualized hypothetical consent view, this approach is oriented to principles and rules. This “ecumenical” view—I will also assume—insists that people have a right to dispose of their just holdings by contract. Most contractarian/contractualist theories accord with this assumption.<sup>56</sup> For instance, James Buchanan and Loren Lomasky say that contractors will require “that all persons be free to enter and to exit from private contracts, to make voluntary exchanges without collective constraint, and to enter any occupational category.”<sup>57</sup> Much the same is true of Ronald Dworkin’s theory of equality of resources. Dworkin says “that the idea of an economic market, as a device for setting prices for a vast variety of goods and services, must be at the center of any attractive theoretical development of equality of resources.”<sup>58</sup> In fact, Dworkin’s egalitarian initial auction allocates private property rights, which the just owner can relinquish or transfer. Moreover, when Dworkin discusses the place of liberty in his theory of justice, he defends a “principle of abstraction,” which “establishes a strong presumption in favor of freedom of choice.”<sup>59</sup>

Contractarianism can cope with the three difficulties that motivated our rejection of the individualized hypothetical view. First, it does not evaluate particular interferences with freedom of contract, but rather principles or rules of contract regulation. For example, contractarianism must compare unhampered freedom of contract and a system of freedom of contract qualified by procedural unconscionability. Therefore, contractors are distanced from the particular positions they will/might occupy as a result of the operation of contract rules. Buchanan and Vanberg state the connection between generality and impartiality in concise terms:

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<sup>56</sup> The proposition has one important qualification, because Rawls’s theory is in this regard ambiguous. On the one hand, Rawls leaves the choosing of a property regime at the original position as an open question. However, Loren Lomasky has persuasively argued that Rawlsian contractors would adopt a private property regime; see: Loren Lomasky: Libertarianism at Twin Harvard, *Social Philosophy and Policy*, Volume 22, Number 1 (Winter 2005). On the other hand, Rawls seems to endorse freedom of contract in placing contract law outside the realm of the basic structure; see: Liam B. Murphy, *Institutions and the Demands of Justice*, *Philosophy & Public Affairs* 27, n° 4, at 258.

<sup>57</sup> James B. Buchanan and Loren E. Lomasky, *The Matrix of Contractarian Justice*, in *The Collected Works of James M. Buchanan*, v. 17, 1999, at 402.

<sup>58</sup> Ronald Dworkin, *op. cit.*, at 284.

<sup>59</sup> Ronald Dworkin, *What Is Equality? Part 3: The Place of Liberty*, 73 *Iowa Law Review*, 1987, at 25.

The more general rules are and the longer the period over which they are expected to be in effect, the less certain persons can be about the particular ways in which alternative rules will affect them. They will therefore be induced to adopt a more impartial perspective and, consequently, they will be more likely to reach agreement.<sup>60</sup>

Sometimes contractarians use the more direct expedient of placing a veil of ignorance or uncertainty over the contractors at the constitutional choice. In any case, contractarianism is apt to do away with the discrepancy between the promisor and the promisee that threatened the individualized consent view.

Second, parties at the constitutional choice must consider social policies and their associated institutional rules. According to contractarians, constitutional consent involves a complex decision-making process. Instead of considering rules on a case-by-case basis, they discuss the overall effects of rules. To this effect, the parties are assumed to possess all relevant knowledge in psychology, economics, and social theory. So they know what effects various institutional arrangements will have in practice. Among other things, contractors will discuss possible side-effects of various powers awarded to government and the courts.

Finally, at the constitutional choice contractors do not consider the doctrine of unconscionability in isolation but along with other fundamental principles of contract law. Thus, they must lay down rules that define voluntariness in exchange, that is, that establish which constraints are consistent with voluntariness in sub-constitutional or in-period choices.<sup>61</sup> Because such rules must be justified by voluntary choice at the constitutional level, mutuality of advantage constrains the possible outcomes. For instance, parties at the constitutional level could only allow a particular form of advantage-taking if it works “to the long run benefit of those disadvantaged by it,” or “to the benefit of all concerned.”<sup>62</sup> While a purely procedural criterion could run into an infinite regress, a “reflective equilibrium” or “multilevel, conjectural” approach, combining procedural and substantive elements, can produce a meaningful notion of voluntariness that serves to support the whole structure.<sup>63</sup> The contractarian approach assumes that voluntariness at the constitutional choice can be more easily assessed by substantive criteria. For instance, low exit costs from a collective arrangement

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<sup>60</sup> James M. Buchanan and Viktor J. Vanberg, “Interests and theories in constitutional choice”, in Viktor J. Vanberg, *Rules and choice in economics*, 1994, at 171.

<sup>61</sup> Viktor J. Vanberg, *Individual choice and institutional constraints*, *The normative element in classical and contractarian liberalism*, in *Rules & Choice in Economics* (1994).

<sup>62</sup> Kronman, *op. cit.*, at 486, 488.

<sup>63</sup> Vanberg, *op. cit.*, at 226; Rawls, *op. cit.*, at 48-51.

characteristically indicate free choice. From a contractarian perspective a non-arbitrary line between voluntary and involuntary agreements can be drawn. (This opens a way out of the impasse Shiffrin is worried about.<sup>64</sup>)

### *3. How the Contractors Choose a Narrow Interpretation of the Unconscionability Doctrine.*

How would the contractors proceed to design the rules of contract law, and, in particular, a doctrine of unconscionability? We have assumed that contractors choose a basic regime of freely transferable property rights. However, as we saw above, contractors must draw a line between voluntary and involuntary agreements. So they will complement a principle of free alienation of rights with, for instance, the defenses of incompetence, fraud, misrepresentation, duress, and necessity. (It is assumed here that these defenses serve mutual advantage.) Once the standard of voluntariness is set in this way, contractors might consider—in accordance with Gerald Dworkin’s suggestion—taking out an insurance policy against “potentially dangerous” less than voluntary agreements. They will make this decision if they calculate that the traditional defenses do not provide sufficient protection. Since such defenses are often difficult to prove, contractors might avail themselves of a doctrine of unconscionability to deter fraud and deceit in a cost-effective way (e.g., avoiding prohibitive evidence costs).<sup>65</sup> Thus, the doctrine might be used to neutralize or ameliorate the deleterious effects of less than voluntary sub-constitutional transactions. A doctrine of procedural unconscionability is a natural supplement to the traditional defenses, because it presumes nonvoluntariness when contract formation has been vitiated by certain procedural defects. But impure substantive unconscionability could also work as a cost-avoiding presumption, because some agreements are so harsh that no competent, informed and fully rational person would have consented to them.

Parties at the constitutional choice will try by all means to protect freedom of choice. Thus, contractarianism is inimical to strong paternalism.<sup>66</sup> This is not inconsistent

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<sup>64</sup> See text accompanying note 25.

<sup>65</sup> Richard A. Epstein, *Unconscionability: A Critical Reappraisal*, see note 1. Anthony Kronman makes a similar point with respect to the warranty of habitability in residential leases. He regards it as a fraud protection rule grounded on efficiency reasons. If the warranty were a disclaimable default rule, the tenant could waive it and still remain protected by the general remedy of fraud. But the proof of fraud is often difficult and expensive to produce. So if the warranty were waivable, the courts could consider many fraudulent leases valid and society would have to endure a serious welfare loss. Anthony Kronman, *Paternalism and the Law of Contracts*, 92 *Yale L. Rev.* (1983).

<sup>66</sup> John Rawls, *A Theory of Justice*, § 39; James B. Buchanan and Loren E. Lomasky, *The Matrix of Contractarian Justice*, see note 57; John Rawls, *Political Liberalism* 1993, Lecture VIII.

with endorsing a doctrine of unconscionability at the constitutional level. A self-protection against nonvoluntary agreements is not strongly paternalist. Feinberg makes this point very persuasively:

The central thesis of John Stuart Mill and other individualists about paternalism is that the fully voluntary choice or consent of a mature and rational human being concerning matters that affect only the individual's own interests is such a precious thing that no one else (and certainly not the state) has a right to interfere with it simply for the person's "own good."<sup>67</sup>

This allows interventions with (potentially) self-damaging behaviors that result from less than fully voluntary choice. Among these interventions are procedural unconscionability and impure substantive unconscionability, as defended above. According to Feinberg, "people can rightly be prevented from harming themselves (when other interests are not directly involved) only if their intended action is substantially nonvoluntary or can be presumed to be so in the absence of evidence to the contrary."<sup>68</sup> While Feinberg calls these policies "weak paternalism," I contend that they should not count as paternalism at all, because they do not meet conditions (b) and (d) of Shiffrin's definition. In effect, it is the contractors' choice that lies at the bottom of the doctrine, and, therefore, its application does not involve the substitution of the court's judgement or agency for the contracting parties'. Nor is the doctrine applied on the grounds that the court regards its judgement or agency to be, in some respect, superior to the parties'. Instead, the doctrine is applied on the grounds that via the contractarian technique the parties can be assumed to have consented to this "intervention."

Setting the precise contours of the doctrine of unconscionability involves a complex contractarian reasoning. Contractors know that the transference of property rights constitute an essential ingredient of their ability to pursue various plans of life. But they are also aware of their risk to make nonvoluntary agreements because of misinformation, cognitive deficiencies, irrational calculations, and so on. What kind of insurance policy will contractors take out? Contractors should weigh the importance of free choice and the risks of self-damaging nonvoluntary agreements. Some authors suggest that state interventions in this field should be widespread and coercive. For instance, Duncan Kennedy defends a very intrusive paternalist policy in contract

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<sup>67</sup> Joel Feinberg, *Legal Paternalism*; italics added.

<sup>68</sup> *Ibid.*, at 17; italics added.

law.<sup>69</sup> For Kennedy, compulsory terms can cure “false consciousness,” which covers such differing things as underestimation of risk, augmentation of the discount rate, unsupported confidence in others’ future behavior, and erroneous appreciation of long term consequences of submissive relationships.<sup>70</sup> Kennedy claims, “Courts using the doctrine of unconscionability like to put their decisions on grounds of unequal bargaining power... But it’s often obvious that they are concerned not with power but with naiveté, or with lack of ability to make intelligent calculations about what one can afford on one’s budget.”<sup>71</sup> In these cases, “the decision maker has to take the beneficiary under his wing and tell him what he can and cannot do”.<sup>72</sup>

Paternalism has received new impetus from research in behavioral decision theory.<sup>73</sup> In fact, psychologists and experimental economists have studied some of the mistakes that Kennedy treats under the label of “false consciousness.” Behavioral decision theory assumes that these mistakes derive from cognitive mechanisms, rather than from capitalist alienation. Loss aversion, framing, hindsight and other cognitive biases explain a number of mistakes that people systematically commit in making judgements and decisions.<sup>74</sup> Because some of these irrational factors affect many contracting or consumer decisions, “behavioral law and economics” advocates paternalist interventions in contract law, like the striking down of onerous liquidated damages clauses and warranty disclaimers, and the regulation of financial markets. Unlike Kennedy, behavioral paternalists opt for nonintrusive, noncoercive varieties of intervention. For instance, Cass Sunstein proposes “libertarian” paternalism, according to which private and public organizations should establish arrangements that influence people’s choices in ways that will further their interests but that nonetheless let them free to opt out if they prefer to follow different strategies.<sup>75</sup> Unlike Kennedy’s paternalism, “libertarian” paternalism does not attempt to influence people’s behavior by blocking free choice. For instance, it recommends default rules. Similarly, Colin Camerer et al. defend “asymmetric paternalism,” which promotes

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<sup>69</sup> Duncan Kennedy, *Distributive and Paternalist Motives in Contract and Tort Law, With Special Reference to Compulsory terms and Unequal Bargaining Power*, 41 *Maryland Law Review* (1982).

<sup>70</sup> *Op. cit.*, 626-8.

<sup>71</sup> *Op. cit.*, 634.

<sup>72</sup> *Ibid.*

<sup>73</sup> Daniel Kahneman, Paul Slovic, and Amos Tversky (eds.), *Judgment under uncertainty: Heuristics and biases* (1982).

<sup>74</sup> Cass Sunstein, *Behavioral Analysis of Law*, *U. Chicago Law Review* (1997); Christine Jolls et al., *A Behavioral Approach to Law and Economics*, 50 *Stan. L. Rev.* 1471 (1998); Russell B. Korobkin & Thomas S. Ulen, *Law and Behavioral Science: Removing the Rationality Assumption from Law and Economics*, 88 *Cal. L. Rev.* 1951 (2000).

<sup>75</sup> Cass R. Sunstein and Richard H. Tahler, *Libertarian Paternalism Is Not an Oxymoron*, 70 *University of Chicago Law Review* (2003).

regulations that create benefits for those who do not act in their best interests because of errors that lead them astray, while letting those who act in their best interests to do so without interference.<sup>76</sup> These authors say that “a policy is asymmetrically paternalistic if it creates large benefits for those who are boundedly rational [...] while imposing little or no harm on those who are fully rational...”<sup>77</sup> Asymmetric paternalism has various applications in contract law. The defenders of this position mention as examples default rules, provision or re-framing of information (protection of credit consumers, of investors, etc.), cooling-off periods, and limiting consumer choices (for example, deadlines to avoid procrastination).

I suggest that the contractors, even though they are aware of findings in cognitive psychology, will adopt a narrow interpretation of the doctrine of unconscionability for three reasons. First, contractors know that judges and regulators will be also subject to cognitive mistakes, and that a strong doctrine of unconscionability can be counterproductive in many ways. In particular, policymakers, judges included, usually underestimate the risk that their decisions will have harmful consequences and often are overconfident in their ability to manipulate extremely complex social processes to achieve their goals. Regulatory miscalculation can produce tragic outcomes, because, as Gerald Gaus observes, the realm of social policy is characterized by profound uncertainty.<sup>78</sup> This problem is only exacerbated in the case of judges, who, because of the special features of the adversarial process, have at their disposal a very limited leeway to implement social policies and correct possible mistakes.

The fundamental point is that contractors are assumed to be knowledgeable in economics and social theory, so they will eschew counterproductive applications of the unconscionability doctrine. (In this respect, the contractarian approach strikingly contrasts with Shiffrin’s hard nonconsequentialist position.<sup>79</sup>) Let me give just two examples of counterproductive use of the unconscionability doctrine. First, contract prices can adjust to the risks deriving from a new and significant unconscionability ruling, possibly harming the class of contracting parties the court sought to protect. For instance, if courts start applying a very strong doctrine of unconscionability in residential contracts, rents will increase, harming particularly the poor. Second, as any other form of insurance, a strong doctrine of unconscionability will be beset by moral hazard effects. Thus, it will aggravate miscalculation and other forms of irrationality

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<sup>76</sup> Colin Camerer et al., Regulation for Conservatives: Behavioral Economics and The Case for “Asymmetric Paternalism”, University of Pennsylvania Law Review January 2003.

<sup>77</sup> Op. cit., p. 1219. (CHECK PAGE)

<sup>78</sup> Gerald F. Gaus, Why all Welfare States (Including Laissez-Faire Ones) Are Unreasonable, 15 Social Philosophy and Policy 1998, at 16.

<sup>79</sup> See text accompanying note 23.

in contracting settings. This can become a negative feedback process. Instead of inducing contracting parties to exert more care, the doctrine will likely encourage irresponsibility and hence greater dependency. Individuals will become more fallible and, this, in turn, will call for more intrusive varieties of unconscionability doctrine.<sup>80</sup>

Second, as Jeffrey J. Rachlinski has recently argued, though people utilize heuristics that make them vulnerable to erroneous judgements, they are also able to correct their mistakes and to restructure decision problems so as to minimize the probability of mistake.<sup>81</sup> People can learn from their mistakes and adapt their behavior. At the same time, says Rachlinski, people can hire private experts, like financial planners, attorneys, and insurance agents, who can make more reliable decisions in contexts where cognitive mistakes are common. Rachlinski concludes that, if the evidence from cognitive psychology is considered in its entirety, it does not support invasive forms of paternalism.

Finally, interest groups could “exploit” the doctrine of unconscionability to pursue rent-seeking goals. Indeed, litigation cannot be taken as an exogenous variable in the strategic interaction between interest groups and government.<sup>82</sup> Although lifetime tenure makes federal judges less susceptible to special interests, interest groups can influence judicial decisions directly and indirectly; directly by manipulating the information that nurtures the judicial decision-making and indirectly by influencing the political process related to judicial appointments and promotions. Contractors will seriously consider the negative side-effects of allowing the courts to transfer property via the doctrine of unconscionability. Loren Lomasky makes this point very clearly with respect to government powers:

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<sup>80</sup> But Eric Posner has presented an argument that runs in the opposite direction. Assuming a welfare state, which produces moral hazard effects, he claims that “restrictive contract doctrines”, like usury laws and unconscionability, can correct those perverse incentives by increasing the cost of credit contracts and thus discouraging the poor to take excessive financial risks. I find this argument dubious as applied to the unconscionability doctrine. Even if this doctrine actually raises the cost of credit, the poor can be encouraged to take expensive loans if they can predict that the courts will nonetheless bring down loan interests to affordable levels. I believe that unconscionability might add to the welfare state’s distortions, rather than detract from them. See: Eric A. Posner, *Contract Law in the Welfare State: A Defense of the Unconscionability Doctrine, Usury Laws, and Related Limitations on the Freedom of Contract*, *Journal of Legal Studies*, June 1995.

<sup>81</sup> Jeffrey J. Rachlinski, *The Uncertain Psychological Case for Paternalism*, 97 *Nw. U. L. Rev.* 1165 (2003).

<sup>82</sup> Elhauge, Einer R. 1991. Does interest group theory justify more intrusive judicial review? *Yale Law Journal* 101 (1): 31–110; Miller, Geoffrey. 1994. *The True Story of Carolene Products*. In *Law and Justice: Cases and Readings on the American Legal System* edited by D. A. Nance. Durham: Carolina Academic Press.

If the rules of the political game allow for taking and then redistributing property just so long as a majority can be assembled to testify that they are acting for the sake of some lofty ideal of social justice—perhaps one that goes by the name of “justice as fairness”—then it is predictable that those rules will be frequently and extravagantly bent in the service of interests that are neither impartial nor likely to advance the positions of the least well-off. Knowing this, contractors will be loath to afford *carte blanche* to proliferation of allegedly welfarist measures.<sup>83</sup>

For that matter, contractors will be reluctant to frame the unconscionability doctrine so as to facilitate rent-seeking and subsidies via litigation.

A contractarian approach places strict limits to the use of the unconscionability doctrine. In general, contractors will rationally regard the presumptions of nonvoluntariness stemming from the doctrine as rebuttable, because they know that an absolute prohibition can have unpredictable negative outcomes. For instance, contractors can authorize courts to treat under procedural unconscionability financial contracts that use mathematical or graphic devices intended to exploit systematic cognitive mistakes made by inexperienced contracting parties, particularly when this is conjoined with gross substantive unconscionability. But they will likely obligate the courts to consider counterevidence that the contract was a rational choice given the economic or social circumstances surrounding the agreement.

Would the contractors likely adopt a conclusive presumption of nonvoluntariness under any special conditions? Mill famously defends one exception to anti-paternalism: the slavery contract. Liberals often regard the slavery contract as substantively unconscionable, because the buyer wants to obtain the seller’s right to liberty, which is inalienable. Unlike Mill and other liberals, contractarianism should treat slavery contracts in a procedural, nonsubstantive fashion. Thus, contractors could use the concept of “inalienable rights” as a rhetorical device to establish a conclusive presumption of nonvoluntariness. Feinberg comes close to this position when he says: “There is, of course, always the presumption, and a very strong one indeed, that those who elect to ‘sell’ themselves into slavery are either incompetent, unfree, or misinformed.”<sup>84</sup> But he takes the presumption to be rebuttable: “The supposition is at least possible, therefore, that every now and then a normal person in full possession of

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<sup>83</sup> Loren E. Lomasky, *Libertarianism at Twin Harvard*, *Social Philosophy and Policy*, Volume 22, Number 1 (Winter 2005), LOCATE PAGE.

<sup>84</sup> Feinberg, *op. cit.*, at 12.

her or his faculties would voluntarily consent to permanent slavery.”<sup>85</sup> However, I believe that from a contractarian perspective a conclusive presumption of nonvoluntariness could be justified by the name of “inalienability.”<sup>86</sup> In fact, contractors might rationally relinquish their liberty to sell themselves into slavery because they know that precommitment is a rational strategy for boundedly rational agents. As Jon Elster points out: “...binding oneself is a privileged way of resolving the problem of weakness of will; the main technique for achieving rationality by indirect means.”<sup>87</sup> On this view, inalienability would be a sort of legal fiction.<sup>88</sup> Thus contractors might use a precommitment strategy, under the legal fiction of “inalienable rights”, in order to protect their individual autonomy from irrational and irreparable choices.<sup>89</sup>

## CONCLUSION

The self-regarding approach is very limited in scope and is unable to explain why the state’s responsibility is morally implicated given the parties’ consent in procedurally perfect agreements. But I believe that underlying these shortcomings there is a more fundamental problem. The self-regarding theory solely looks at the substance, not the procedure of unconscionable contracts. The contractarian approach illuminates the procedural thrust of the doctrine of unconscionability. In liberal theory contracts can only be illegitimate when the parties’ consent is somehow vitiated. In principle, substantive unconscionability can only be an indirect way to prove procedural unconscionability. According to the contractarian approach, even substantive unconscionability deriving from the putative transference of inalienable rights has at bottom a procedural rationale. This means that “pure” substantive unconscionability is a mirage. The contractarian approach explains all these features in an elegant and parsimonious fashion.

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<sup>85</sup> Ibid.

<sup>86</sup> For an alternative view, which explains inalienability in terms of negative externalities, see Guido Calabresi and A. Douglas Melamed, *op. cit.*

<sup>87</sup> Jon Elster, *Ulysses and the Sirens, Studies in Rationality and Irrationality*, 1979, at 37.

<sup>88</sup> On legal fictions, see: Lon L. Fuller, *Legal Fictions* (1967).

<sup>89</sup> They could use a precommitment strategy as well to protect their political liberty via constitutional constraints. For an analysis of constitutionalism as a form of precommitment, see: Stephen Holmes, *Precommitment and the Paradox of Democracy*, in Jon Elster and Rune Slagstad (eds.), *Constitutionalism and Democracy*, 1988.