

Consumer Protection and the Criminal Law

Law, Theory, and Policy in the UK

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1 Consumer protection rationales

Introduction

Laws have been used to protect consumers for centuries. These laws have drawn on a variety of legal forms, including criminal law, tort, and contract, to achieve their objectives. In addition to those laws that specify consumer protection as their primary concern, numerous other provisions have the effect of protecting the consumer, for example by streamlining the prosecution of fraud, protecting property, or facilitating litigation.¹ As a result, the boundaries of consumer protection law are not easily drawn. This book is concerned primarily with those laws that have consumer protection as their main objective, and which use the criminal law to achieve this objective.²

This chapter examines the role of law in consumer protection, focusing upon the objectives of consumer protection. In order to achieve this, we need to consider a number of matters. First, we need to identify ‘the consumer’ whom we are concerned to protect. Secondly, we need to consider the relationship between consumer protection and the market economy. It is sometimes argued that the state, through the law, should play only a restricted role in protecting consumers, because consumer protection is most effectively achieved by the operation of free and open markets. Law should be used to ensure that the markets function as freely as possible. Where markets do not work perfectly, the law should intervene to address this failure, provided this can be done cost effectively. Thirdly, this chapter will consider the extent to which consumer protection should concern itself with social, non-market-based goals. While accepting the importance of market and social goals, it is argued that the distinction between the two is not clearly drawn, and that some approaches could be viewed under either heading. Using the language of efficiency and equity

¹ See for example, the Misrepresentation Act 1967, the Theft Act 1968, and the Civil Procedure Rules 1998 (as amended).

² It is recognised that many of these statutes will have additional aims, in particular, the protection of honest traders and the encouraging of fair competition.

rather than market and social goals, Ramsay observes that '[a]n efficient policy is ultimately justified by equity since consumers are able to obtain goods and services of a quality, on terms, and at the price that they are willing to pay'.³ Although helpful for the purposes of structure, the market/social distinction is imperfect in practice. The chapter concludes that the market, underpinned by private law, is an important technique for ensuring that consumers are able to purchase the goods and services that they want, and that intervention which helps the market to function is valuable. However, social goals are being recognised as increasingly important and it is important for any effective consumer protection policy to address both.

Who is a consumer?

Describing something as a consumer protection statute implies that there is someone who can be identified clearly as a 'consumer'. Although the private buyer of goods is perhaps our paradigmatic consumer, she has been joined by a wealth of other economic actors who can lay claim to forming part of that diverse group. As a result, there is the initial difficulty of identifying our subject matter. The first point to note is that there is no universally agreed definition of the term 'consumer', although a number of statutes, both criminal and civil, attempt to define it for their own purposes. One example of such a definition is found in s.20(6) of the Consumer Protection Act 1987, which states:

'consumer'

- (a) in relation to any goods, means any person who might wish to be supplied with the goods for his own private use or consumption;
- (b) in relation to any services or facilities, means any person who might wish to be provided with the services or facilities otherwise than for the purposes of any business of his; and
- (c) in relation to any accommodation, means any person who might wish to occupy the accommodation otherwise than for the purposes of any business of his.

Another example is contained in s.12 of the Unfair Contract Terms Act 1977. This states that a party to a contract deals as a consumer if '(a) he neither makes the contract in the course of a business nor holds himself out as doing so; and (b) the other party does make the contract in

³ Iain Ramsay, *Rationales for Intervention in the Consumer Marketplace* (London, Office of Fair Trading, 1984), p. 12.

the course of a business'. Regulation 2 of the Unfair Terms in Consumer Contracts Regulations 1999 provides a further approach, describing a consumer as 'a natural person who, in making a contract to which these Regulations apply, is acting for purposes which are outside his business'. These definitions suggest that the consumer is a private individual acting in a private capacity. A further paradigm of consumer protection statutes is that the defendant must act in the course of a trade or business.⁴ However, some UK statutes which would undoubtedly be regarded as examples of 'consumer protection' legislation fall outside this description. For example, the Trade Descriptions Act 1968 prohibits the supply of false and misleading information in business to business transactions.⁵ There is also a suggestion that the Act might prohibit misdescriptions applied by private individuals, albeit in limited circumstances.⁶

It seems that the main characteristics of consumer protection statutes are that the supplier acts in the course of a trade or business, the recipient is a private individual, and the recipient acts in a private capacity. It should be remembered that it is important not to limit the term 'consumer' to contracting parties, as that might exclude the ultimate user of goods and services, such as the plaintiff in *Donoghue v. Stevenson* whom Jolowicz describes as 'the law's best known consumer'.⁷ Indeed, it is possible to develop a much wider concept of the consumer than has traditionally been envisaged.⁸ A private individual who receives services from a non-commercial state authority, such as the user of National Health Service facilities or even the recipient of state benefit, might be aptly described as a consumer. As Kennedy has stated, 'consumerism is just as concerned with the supply of services as with goods. The consumer merely becomes the client, or patient, or whatever rather than the shopper'.⁹ We could even go as far as Ralph Nader, the American consumer rights activist, and equate the word 'consumer' with 'citizen'. Scott and Black point out that the consumer interest is involved whenever citizens enter relationships with bodies such as hospitals and

⁴ For discussion of the meaning of this see Richard J. Bragg, *Trade Descriptions* (Oxford, Clarendon Press, 1991), ch. 2.

⁵ See *Shropshire County Council v. Simon Dudley Ltd* (1997) 16 Trading Law 69.

⁶ See *Olgeirsson v. Kitching* [1986] 1 WLR 304, although it is submitted that this case is wrongly decided.

⁷ J. A. Jolowicz, 'The Protection of the Consumer and Purchaser of Goods Under English Law' (1969) 32 MLR 1, 1.

⁸ For discussion see I. Ramsay, *Consumer Protection: Text and Materials* (London, Weidenfeld and Nicolson, 1989), ch. 1 and C. Scott and J. Black, *Cranston's Consumers and the Law* (3rd edn London, Butterworths, 2000), pp. 8–11.

⁹ I. Kennedy, *The Unmasking of Medicine* (The 1980 Reith Lectures) (London, Allen and Unwin, 1981), p. 117. Cited in Ramsay, *Consumer Protection*, pp. 11–12.

libraries.¹⁰ The Molony Committee, which was set up in 1959 to consider and report on changes to consumer law, opined that the consumer is 'everybody all of the time'. However, the committee did not suggest this as a working definition of the term, limiting their ambit to the purchase of or obtaining on hire purchase goods for private use and consumption.¹¹ This illustrates the numerous contexts in which an individual could be regarded as a consumer. It is interesting to note that when the idea of the Citizen's Charter was taking shape, there was some discussion about whether it should be referred to as the 'Consumer's Charter'. The former title was agreed upon, as the term 'consumer' was seen as 'narrow [and] econocratic'.¹² Equating 'consumer' with 'citizen' has the benefit of enabling us to look beyond the narrow economic function of the consumer, and to consider the individual's wider role in society. This is important in areas such as financial services where a strict economic definition of consumer might exclude private investors.¹³ It thus becomes easier to see rights against the state as consumer issues. However, there is the danger that the term 'consumer' could become almost meaningless. Indeed, it could be argued that the legacy of the Citizen's Charter is that citizens have increasingly been treated as consumers, rather than consumers as citizens.¹⁴

This book does not propose to offer a prescriptive definition of the consumer. It is concerned to examine the way in which criminal law is used in the context of consumer protection in the UK, but the UK has no agreed definition of the consumer. Few could deny that the Trade Descriptions Act 1968 and the Consumer Protection Act 1987 are properly described as consumer protection statutes, even though they take different approaches to whom they protect. It is therefore suggested that we should eschew a narrow definitional approach to the concept of the consumer, recognising that statutes may legitimately take different approaches to this issue. Nevertheless, we should recognise that this book is primarily concerned with those statutes which aim to protect the buyers of goods and services from the misbehaviour of traders and which use the criminal law to do so.

¹⁰ See Scott and Black, *Cranston's Consumers and the Law*, pp. 8–11.

¹¹ Board of Trade Final Report of the Committee on Consumer Protection (the Molony Committee) Cmnd 1781/1962, para. 16.

¹² S. Hogg and J. Hill, *Too Close to Call: Power and Politics – John Major in No. 10* (London, Warner, 1995), p. 94.

¹³ See P. Cartwright, 'Consumer Protection in Financial Services: Putting the Law in Context' in P. Cartwright (ed.), *Consumer Protection in Financial Services* (Deventer, Kluwer, 1999) and C. J. Miller, B. W. Harvey, and D. L. Parry, *Consumer and Trading Law: Text Cases and Materials* (Oxford, Oxford University Press, 1998), pp. 5–6.

¹⁴ A. Barron and C. Scott, 'The Citizen's Charter Programme' (1992) 55 MLR 526.

Consumer protection and the market system

The perfect market

When examining why we intervene in the market to protect consumers, it is possible to take the so-called ‘perfect market’ as a starting point. This is helpful even if we doubt that such a system is attainable in reality. Free market economic theory suggests that if the characteristics of a perfect market could be created, there would be no need for regulation. In one of the leading studies, *Rationales for Intervention in the Consumer Market Place*, Ramsay identifies the characteristics of the perfect market as follows:

- (i) there are numerous buyers and sellers in the market, such that the activities of any one economic actor will have only a minimal impact on the output or price of the market;
- (ii) there is free entry into and exit from the market;
- (iii) the commodity sold in the market is homogeneous; that is, essentially the same product is sold by each seller in the particular market;
- (iv) all economic actors in the market have perfect information about the nature and value of the commodities traded;
- (v) all the costs of producing the commodity are borne by the producer and all the benefits of a commodity accrue to the consumer – that is, there are no externalities.¹⁵

Those who champion the idea of the perfect market see markets as efficient and effective tools for maximising consumer welfare. The expressions ‘free market economics’ and ‘free market economists’ are used in this context for want of a better term. It is recognised that this is not a perfectly homogeneous group. This approach, which is associated primarily with the Chicago School, makes assumptions about the ways in which markets operate.¹⁶ First, it assumes that individuals are rational maximisers of their own satisfaction. In other words, they know what they want, and will make logical, consistent choices in accordance with their wishes. Secondly, it assumes that by their choices, consumers influence producers and so dictate the way that the market operates. By making choices in accordance with their wishes, consumers send signals to traders. If traders do not respond to these wishes they will lose custom and, ultimately, be forced to exit the market. The consumer is therefore sovereign.

¹⁵ Ramsay, *Rationales*, pp. 15–16.

¹⁶ For a useful discussion see Scott and Black, *Cranston’s Consumers and the Law*, pp. 26–9.

The market system can be viewed as desirable for two main reasons. First, it is economically desirable because it is efficient. Traders compete with each other to win custom, thereby raising standards and lowering prices. Secondly, it is seen as ideologically desirable that individuals' choices should be respected, rather than a choice made on their behalf by the state. Indeed, many supporters of the free market seem as much influenced by ideological matters as by efficiency arguments.¹⁷ The free market recognises that different consumers are likely to be prepared to endure different levels of product safety and quality for different amounts of money. Where this is the case, a variety of products will be supplied with different levels of quality and safety for different prices. It is for consumers to act rationally in accordance with their own preferences and decide upon the level of safety or quality that they are prepared to purchase.

The perfect market only exists where the requirements set out in Ramsay's list are met, although we may still have competitive markets where not all are present. If we have numerous buyers and sellers competing with each other, no individual trader should be able to influence price appreciably by varying output.¹⁸ By ensuring that there is free entry into and exit from the market, we ensure that anyone who wishes to enter a particular market may do so, and that anyone who does not respond to consumer demand will be forced to exit the market. By having perfect information, we ensure that the choices that consumers make are fully informed, and so likely to give effect to their true wishes. Where externalities do not occur we can be sure that only the parties to a transaction are affected by that transaction, and so the price of the transaction reflects its value to the parties. Free market economics tells us that where these factors are present there is no need for the state to intervene. However, that does not mean that the state has no role in the free market, as we will now see.

The market, the state, and the law

Although free market economics is frequently associated with rolling back the frontiers of the state, this does not mean that the free market requires the state to lose its role in all areas.¹⁹ On the contrary, for the market

¹⁷ See C. Fried, *Contract as Promise: A Theory of Contractual Obligation* (Cambridge, Mass., Harvard University Press, 1981) and P. S. Atiyah, 'The Liberal Theory of Contract' in P. S. Atiyah, *Essays on Contract* (Oxford, Clarendon Press, 1990), p. 121.

¹⁸ F. M. Scherer, *Industrial Market Structure and Economic Performance* (2nd edn, Boston, 1980), p. 10.

¹⁹ Andrew Gamble, *The Free Economy and the Strong State: The Politics of Thatcherism* (2nd edn, Basingstoke, Macmillan, 1994), ch. 2.

to function effectively it is vital that the state retains its strength. Frank Knight observed that ‘the [market] system as a whole is dependent upon an outside organisation, an authoritarian state . . . to provide a setting in which it can operate at all’.²⁰ The state should, therefore, not be seen as an alternative to the market, but as an essential part of the market system. Hutchinson similarly comments that ‘[w]ithout a state willing or able to define and protect property rights, enforce contracts and prevent involuntary transactions, maintain a circulating medium, and curtail monopoly and anti-competitive behaviour, there is no market in any real or meaningful sense’.²¹ The state is therefore vital to set up and enforce the structure in which the market operates. This is done through the mechanism of law. Law determines the ‘rules of the game’ in the first place, and acts as an umpire to interpret and enforce those rules.²² For example, competition/anti-trust law ensures that markets are open and that competition exists. Property law sets out the rules of property and so determines rights of ownership, and explains how title can pass. Criminal law ensures that such rights are protected. As the market is premised upon the importance of exchange, the rules of contract law have to be set out. There is no inherent conflict between a strong state, strong laws, and the free market.

Although the state has to be strong for the market system to function effectively, the state only imposes its views on citizens in order to ensure that parties are held to their agreements. It is individuals’ choices that count, rather than those of the state. As a consequence, laws prohibiting fraud and force are seen as protecting the private rights of citizens rather than enforcing the state’s aims on those citizens.²³ The prime method by which choices can be demonstrated and effected is through the private law of contract. The next section considers the use of the private law to protect consumers within the context of the market. It focuses on the role and limitations of the law of contract, but also considers the place of the law of tort. Although contract law could be viewed as a technique of regulation, and so might be thought of as more appropriately placed in our discussion of techniques of regulation, its almost symbiotic relationship with the market has led it to be considered here.²⁴

²⁰ F. Knight, ‘Some Fallacies in the Interpretation of Social Cost’ (1924) 38 QJEcon 582 at 606.

²¹ A. Hutchinson, ‘Life After Shopping: From Consumers to Citizens’ in I. Ramsay (ed.), *Consumer Law in the Global Economy* (Aldershot, Dartmouth and Ashgate, 1997), p. 25 at p. 31.

²² See M. Friedman, *Capitalism and Freedom* (Chicago, Chicago University Press, 1962).

²³ See J. Raz, ‘Promises in Morality and Law’ (1982) 95 Harvard LR 916.

²⁴ For an excellent examination of contract law as a form of regulation see H. Collins, *Regulating Contracts* (Oxford, Oxford University Press, 1999).

The use and limitations of private law

The role of contract

The law of contract is central to the effective working of the market. Contracts provide a mechanism through which individuals can express their preferences, create agreements with others, and ensure that those agreements are fulfilled. Contract law provides a framework through which the market can function. The classical theory of freedom of contract has been central to the development of contract law and its relationship with the market. As Sir George Jessel famously argued: '[i]f there is one thing which more than another public policy requires it is that men of full age and competent understanding shall have the utmost liberty of contracting, and that their contracts entered into freely and voluntarily shall be held sacred and shall be enforced by courts of justice'.²⁵ Although championed by the 'New Right' in the 1980s, classical theory was originally associated with left-wing movements in the nineteenth century, concerned that the people should be allowed control over their destinies.²⁶

Classical theory's emphasis on freedom of contract is a natural consequence of putting faith in the market. Consumer sovereignty demands the means by which the consumer can exercise choice. If we accept that consumers are rational maximisers of their own satisfaction, then it is logical that they should decide the transactions into which they wish to enter, and the terms upon which those transactions will be entered. Intervention by the state beyond that agreed by the parties is therefore anathema to the traditional idea of contractual freedom. Classical theory was characterised by free dealing and non-intervention in substantive matters. It was concerned with fairness, but primarily in relation to procedure rather than substance, acting as an 'umpire' to be appealed to when a foul is alleged.²⁷ However, it is a moot point whether the law of contract ever championed the kind of freedom to which Sir George Jessel alluded. Despite the significant extent to which classical theory has been emphasised in writing, some commentators question how influential it was in practice. Reiter refers to Jessel's view as 'simply wrong',²⁸ and Atiyah notes several ways in which contractual freedom was limited,

²⁵ *Printing and Numerical Registering Co. v. Sampson* (1875) LR 19 Eq 462 at 465.

²⁶ See P. S. Atiyah, 'Freedom of Contract and the New Right' in Atiyah, *Essays on Contract*, p. 355 at p. 357.

²⁷ P. S. Atiyah, *The Rise and Fall of Freedom of Contract* (Oxford, Clarendon Press, 1979), p. 404. For an even stronger defence of individual autonomy see R. Nozick, *Anarchy, State and Utopia* (Oxford, Blackwell, 1974).

²⁸ B. Reiter, 'The Control of Contract Power' (1981) 1 OJLS 347.

even in the so-called heyday of classical theory.²⁹ Nevertheless, the philosophy of classical theory was influential, and can be used to explain many of the characteristics of twentieth-century contract law.

Classical theory's aversion to intervention on the grounds of substantive fairness can be justified on a number of different grounds. Collins identifies four main propositions which underlie this, none of which convinces him.³⁰ It is worth saying a few words about these, as they provide both an authoritative summary of the key characteristics of classical theory and a useful critique of its principal arguments.

First, classical theory's adherents argue that most instances of apparent unfairness turn out to be illusory. For example, most terms which appear to be unfair will be balanced by corresponding benefits, such as a reduction in price. As a result, it is difficult to determine that a voluntary exchange is unfair.³¹ Collins accepts that we should not jump to conclusions concerning the unfairness of transactions, and that unfair contracts are more difficult to detect than might first be thought. However, he recognises that unfair contracts do exist, and that the important point is to engage in a detailed examination of the particular circumstances of the transaction, and to take the whole picture into account.³²

Secondly, it has been argued that approaches which allow contracts to be challenged on the basis of fairness will make it more difficult to construct markets, a prime aim of contract law. Several statutes allow contracts to be challenged on the basis of substantive unfairness, although different terms are used in different contexts. For example, the Unfair Terms in Consumer Contracts Regulations 1999 allow the courts to strike down a term in a consumer contract which 'contrary to the requirement of good faith causes a significant imbalance in the parties' rights and obligations under the contract to the detriment of the consumer'. Also s.137(1) of the Consumer Credit Act 1974 allows a consumer to challenge a credit bargain on the grounds of its being extortionate. Although these provisions look appealing from the point of view of equity, there is an argument that they create uncertainty for the contracting parties, which makes it difficult for those parties to predict how their transactions will be judged. Collins questions this. First, he argues that business people do not regard planning documents as central to transactions and that as a result of this, uncertainty about legal

²⁹ Atiyah, *The Rise and Fall of Freedom of Contract*.

³⁰ Collins, *Regulating Contracts*, ch. 11.

³¹ See M. J. Trebilcock, 'The Doctrine of Inequality of Bargaining Power: Post Benthamite Economics in the House of Lords' (1976) 26 *University of Toronto Law Journal* 359.

³² *Regulating Contracts*, pp. 258–9.

enforceability will seldom affect entry into transactions.³³ Secondly, he suggests that business people place great emphasis on their expectations, represented by such factors as the long-term business relation and the customs of the trade. As a result, general clauses such as good faith may be helpful in allowing decisions to be made in accordance with expectations. He concludes that most commercial parties 'would expect the legal system to decline to enforce terms in the planning documents that impose extremely harsh bargains'.³⁴

The third argument that could be used to criticise intervention is that where the law attempts to regulate fairness, this tends to backfire. Epstein puts forward this view in the context of intervention on the grounds of unconscionability: '[w]hen the doctrine of unconscionability is used in its substantive dimension, be it in a commercial or consumer context, it serves only to undercut the private right of contract in a manner that is apt to do more social harm than good'.³⁵ One example that has been given is that the setting of interest-rate ceilings may exclude poor consumers from the market altogether.³⁶ Another is that minimum-wage laws may lead to employers employing fewer people. Collins suggests that this will depend on the market in question, and points out that there is some empirical evidence that measures such as minimum-wage laws have led to a decrease in unemployment.³⁷ The evidence of the effects of minimum standards of this sort is ambivalent.³⁸

Finally, it is sometimes argued that where genuine unfairness does occur, the most effective remedy will be to tackle the market failure that caused it. The issue of market failure is examined in some detail below and so is not considered in detail here. Suffice it to say that steps which correct market failure are desirable in helping the market to function, for example by generating competition and correcting information deficits. However, they cannot create perfect markets and will be limited in the extent that they protect consumers, particularly the most vulnerable. Collins concludes that regulation of unfair contracts can be desirable, and that such measures comprise an important ingredient of the legal system. He favours both 'open textured rules' rooted in private law, and

³³ Ibid. p. 269.

³⁴ Ibid. p. 271.

³⁵ R. Epstein, 'Unconscionability: A Critical Reappraisal' (1975) 18 *Journal of Law and Economics* 293 at 315.

³⁶ See D. Cayne and M. J. Trebilcock, 'Market Considerations in the Formulation of Consumer Protection Policy' (1973) 23 *University of Toronto Law Journal* 396.

³⁷ D. Card and A. B. Krueger, *Myth and Measurement: The New Economics of the Minimum Wage* (Princeton, N. J., Princeton University Press, 1995).

³⁸ See A. Leff, 'Unconscionability and the Crowd: Consumers and the Common Law Tradition' (1970) 31 *University of Pittsburgh Law Review* 349.

public regulation. Many other commentators doubt whether intervention has the harmful effects that have been suggested.³⁹ If we accept that intervention may be valid, for example in order to help ensure fairness for the consumer, our next step is to examine some of the ways that intervention in contract law can take place.

Intervention in contract

Under the classical notion of contract the focus of control was upon procedural matters. As a result, doctrines of duress, fraud, and misrepresentation developed.⁴⁰ Attempts to tackle the fairness of the substance of contract law were more limited. More recently, however, we have seen increased statutory intervention in the substance of contract law, both by removing undesirable terms and imposing desirable terms.⁴¹ Examples of the former are found in, for example, the Consumer Credit Act 1974, the Unfair Contract Terms Act 1977, and the Unfair Terms in Consumer Contracts Regulations 1999, and of the latter are found in *inter alia* the Sale of Goods Act 1979 and the Supply of Goods and Services Act 1982. The Unfair Contract Terms Act 1977 is concerned primarily with exemption clauses, invalidating some, and subjecting others to a test of reasonableness. The Unfair Terms in Consumer Contracts Regulations 1999 provide, *inter alia*, that a term shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract, to the detriment of the consumer. Both pieces of legislation allow certain terms to be challenged on the grounds of fairness. The Consumer Credit Act 1974 also allows terms to be challenged on the basis of substantive unfairness. Section 137(1) of the Act allows the court to re-open a credit agreement so as to do justice to the parties, where it finds a credit bargain to be extortionate. There are weaknesses with this provision, and suggestions have been made for its reform. In particular, it suffers from the requirement that the victim has to commence the action. By contrast, under the Unfair Terms in Consumer Contracts Regulations, it is possible for interested groups, such as the Consumers' Association, utilities regulators, and the Director General of Fair Trading, to challenge terms on the grounds of fairness.

³⁹ See M. A. Eisenberg, 'The Bargain Principle and its Limits' (1982) Harvard LR 741 and Gordley, 'Equality in Exchange' (1981) 69 Cal LR 1587.

⁴⁰ It has also been possible to create a strict test of incorporation of terms to ensure that particularly unfair terms are not deemed part of the contract. See *Interfoto Picture Library Ltd v. Stiletto Visual Programmes Ltd* [1988] 2 WLR 615.

⁴¹ Although common law notions such as undue influence have also become more visible.

When examining implied terms it is helpful to draw a distinction between two situations. First, terms can be implied to give effect to the wishes of the parties. We can classify these terms as those implied in fact. For example, it may be clear that the parties intended a particular term to be part of the contract, but did not explicitly include it. Where this is done, it can be said to be in accordance with the market system and the philosophy of contractual freedom, as the court is merely giving effect to the intention of the parties.⁴² The second situation is where terms are implied in law. These implied terms, such as those under the 1979 Act, are mandatory, and so cannot be excluded by the parties. They are therefore implied, not to reflect the wishes of the parties, but to reflect the wishes of the state.⁴³ Although it might be possible to argue that mandatory implied terms reflect the standards that the parties would have agreed to had they been able to negotiate on the basis of full information, this does not appear to be the basis on which they are implied in reality. The Sale of Goods Act 1979 provides a useful illustration of how terms may be implied in law. For example s.14 of the Act requires that goods be of satisfactory quality and reasonably fit for their purpose. Section 14(2A) states that goods are of satisfactory quality ‘if they meet the standard that a reasonable person would regard as satisfactory, taking account of any description of the goods, the price (if relevant) and all other relevant circumstances’. The standard is intentionally vague, allowing the courts to determine what is reasonable in all the circumstances. Section 14(2B) provides a list of factors that may be considered where relevant, such as freedom from minor defects, safety, and durability.

English law does not have a general requirement for terms to be fair. Lord Denning made some steps towards such a provision in the famous case of *Lloyds Bank v. Bundy*, but there remains no general test of fairness.⁴⁴ There have been suggestions that the law might impose a general duty to trade fairly, or create a general provision which would allow contracts to be challenged on the basis of extreme unfairness, perhaps couched in terms of unconscionability. The traditional free market arguments against such measures have been set out above, but they fail to convince. There are good reasons to be wary of re-writing contracts, but there are sound reasons for challenging provisions that are so unfair that we can classify them as unconscionable. One reason is that it is

⁴² Although it could be argued that, in reality, the courts imply terms, not on the basis of the parties’ intention, but on the basis of how the parties should behave.

⁴³ For a discussion of paternalism in consumer law see below.

⁴⁴ [1974] 3 All ER 757. This can be contrasted with s.2–302 of the Uniform Commercial Code in the USA which gives a power to the courts to refuse to enforce a clause or contract that is unconscionable.

difficult to separate matters of procedure from matters of substance. The willingness of classical theory to challenge contracts on the grounds of procedural unfairness but not substantive unfairness assumes that there is a clear distinction between the two. This is not always so. The point is well put by Kronman when he explains the different advantages one party may enjoy over another and which make the transaction unfair:

the advantage may consist in his superior information, intellect, or judgment, in the monopoly he enjoys with regard to a particular resource, or in his possession of a powerful instrument of violence or a gift for deception. In each of these cases, the fundamental question is whether the promisee should be permitted to exploit his advantage to the detriment of the other party.⁴⁵

Viewed this way, the distinction between procedural and substantive unfairness is muddled. If a consumer finds himself to be the victim of a substantively unfair bargain we look to see why he entered it. We can nearly always point to some procedural factor which has made the resulting contract unfair, but some of these we accept (such as greater knowledge or skill in bargaining) while others we do not accept (such as deception or violence). Part of the task of consumer law is to determine which factors can be taken into account and when. This is a difficult task. Atiyah offers 'a word of caution against the belief that we can wholly separate our ideas of fair procedures from our ideas of fair results'.⁴⁶ He goes so far as to conclude that 'when there is some gross imbalance, something serious enough to offend our sense of justice, it will usually be found that some remedy is available'.⁴⁷ This brings us to a second argument in favour of having a general power to intervene on grounds of unfairness. Although there are techniques that allow the courts to intervene on grounds of fairness, would it not be more desirable to create a transparent rule which allows them to do this openly, rather than under the guise of some other doctrine? The Unfair Terms in Consumer Contracts Regulations have certainly gone some way towards allowing unfair terms to be removed, but as we have seen, they are subject to important limitations. A general rule against unconscionability, or a general duty to trade fairly would, it is submitted, be desirable, provided it was clearly formulated. This is considered in more detail in chapter 6.

Freedom of contract provides a degree of protection to the consumer, but experience has shown that consumers cannot be expected to fulfil the role attributed to them by market theory. Intervention in the law of contract in the way mentioned above has made significant inroads

⁴⁵ A. Kronman, 'Contract Law and Distributive Justice' (1980) Yale LJ 472 at 480.

⁴⁶ P. Atiyah, 'Contract and Fair Exchange' in *Essays on Contract*, p. 329 at p. 333.

⁴⁷ *Ibid.* p. 338.

into the notion of contractual freedom and has done much to improve consumer protection. However, it should be remembered that contract law suffers from certain limitations which mean that it is unable always to provide an appropriate degree of protection for the consumer. The main limitations are the doctrine of privity and the existence of transaction costs.

Contract and privity

A major limitation in the ability of the law of contract to protect consumers is the doctrine of privity of contract. The doctrine states that, in general, a contract cannot confer rights or impose obligations on someone who is not party to that contract.⁴⁸ For example, a consumer cannot generally sue a manufacturer in contract for producing faulty goods (vertical privity), nor can he sue a retailer in contract for supplying faulty goods which were purchased on his behalf by a friend (horizontal privity). There has been criticism of the doctrine and both academic and judicial support for reform. In *Darlington Borough Council v. Wilshier Northern Ltd* Steyn LJ argued that 'there is no doctrinal, logical, or policy reason why the law should deny effectiveness to a contract for the benefit of a third party where that is the expressed intention of the parties'.⁴⁹ If the law of contract is seen as having among its functions a deterrent role, it will be important that the person who is best able to determine the characteristics of a product is subject to liability. In some cases, it will be impossible to sue the retailer, for example if he has become insolvent or cannot be traced, and so the consumer may be left without a remedy. The consumer will only have a remedy against the manufacturer in tort if the product is not merely defective, but dangerous.⁵⁰ There may be some cases where the court will find a collateral contractual relationship between manufacturer and purchaser, and bypass privity rules, but such situations will be rare.⁵¹ The law relating to privity was recently reformed by the Contracts (Rights of Third Parties) Act 1999. This followed the Law Commission Report *Privity of Contract: Contracts for the Benefit of Third Parties*,⁵² and has made it easier for consumers to take action. The main change is that a third party may now enforce a contractual provision, either if the contract contains an express term to that effect, or if it purports to confer a

⁴⁸ See for example *Tweedle v. Atkinson* (1861) 1 B&S 393.

⁴⁹ [1995] 1 WLR 68. Mitchell describes privity as 'a rule which is almost universally regarded as unjust'. See C. Mitchell, 'Privity Reform and the Nature of Contractual Obligations' (1999) 19(2) *Legal Studies* 229 at 230.

⁵⁰ But see the wording of Part I of the Consumer Protection Act 1987.

⁵¹ See for example, *Carlill v. Carbolic Smoke Ball Co. Ltd* [1893] 1 QBD 256.

⁵² Law Commission Report no. 242, 1996.

benefit upon him. The third party, in these circumstances, will be given rights as though he were party to the contract. It is not proposed to go into detail about the changes here.⁵³ The Act does protect consumers in specific circumstances, but leaves the doctrine largely intact.

Tort

In 1951 Glanville Williams identified the principal aims of tort as: appeasement, justice, deterrence, and compensation.⁵⁴ There will be both conflicts and overlaps between these aims, and they are by no means exhaustive. Jones argues, for example, that we should add loss distribution and economic efficiency to the list.⁵⁵ The effect of tort law is to transfer resources from one party to another in order to return the victim to her position prior to the commission of the tort. The rules of tort law provide a framework for establishing when and how this can be done. If looked at from an economic point of view, tort liability rules provide an incentive for producers to take cost-effective measures to prevent defects. Some of the limitations inherent in the law of contract can be addressed through the law of tort. For example, the consumer who is given a defective product by a friend and suffers injury will have a right of redress against the producer of that product in the law of tort, either under the tort of negligence or Part I of the Consumer Protection Act 1987. However, tort law is subject to its own limitations which may place obstacles in the way of consumers' obtaining access to justice. Whereas contract law is concerned primarily with agreements made by the parties, tort law imposes duties irrespective of the parties' intentions, and irrespective of any contractual relationship.⁵⁶ This may seem to be wider than contract, but in some ways it will not be so. First, tort liability often only arises where the plaintiff can prove fault. Under *Donoghue v. Stevenson* a manufacturer owes a duty of care in negligence to the ultimate consumer of the manufacturer's product.⁵⁷ However, this duty will only give rise to liability where it has been breached: that is, where the plaintiff can prove fault against the manufacturer. Unlike strict liability in

⁵³ For material discussing the proposed changes, see e.g. Mitchell, 'Privity Reform', J. Adams, D. Beylveled, and R. Brownsword, 'Privity of Contracts – The Benefits and Burdens of Law Reform' (1997) 60 MLR 238, F. Reynolds, 'Privity of Contract' (1997) 113 LQR 53 and S. Smith, 'Contracts for the Benefit of Third Parties: In Defence of the Third Party Rule' (1997) 17 OJLS 643.

⁵⁴ G. Williams, 'The Aims of the Law of Tort' (1951) 4 CLP 137.

⁵⁵ See M. Jones, *Textbook on Torts* (4th edn, London, Blackstone Press, 1993), p. 14.

⁵⁶ Although there will be occasions when tort law depends on the parties entering into a relationship, for example, in relation to negligent statements or liability of employers.

⁵⁷ [1932] AC 562.

contract, this is often difficult to establish. Secondly, the law of tort does not, in general, allow recovery for pure economic loss. If a consumer buys a defective washing machine the consumer will be able to recover damages from the supplier in contract. If the washing machine had been given to the consumer as a present, he would not be able to seek redress, either from the supplier or the manufacturer. This is because the consumer is not part of a contractual relationship, and there is no general right in tort to recover damages for the cost of putting a product right, which is classified as pure economic loss. This contrasts with the situation where the washing machine burns a hole in the consumer's kitchen floor. Here the consumer would be able to recover damages for the cost of correcting that as the product has caused property damage outside itself.

Just as there has been state intervention in the law of contract, so there has been in the law of tort. Since the implementation of Part I of the Consumer Protection Act 1987 there has been strict liability for defective products and so seeking compensation for injury caused by defective products is, in theory at least, easier than before the Act. However, the dearth of case law on Part I and the width of the development risks defence raise doubts about the extent to which the provision has improved consumer protection in practical terms. To a large extent, seeking redress under the law of tort remains illusory for many consumers.

Private law and transaction costs

Perhaps the main limitation of private law is that it relies upon the victim for its enforcement. A rational individual will not enforce the law unless the expected benefit exceeds the expected cost, and in the case of many consumer disputes the costs of ensuring redress will be prohibitive. These 'transaction costs', in particular enforcement costs, pose the greatest obstacle to consumers' ability to rely on the market for protection. Transaction costs include search costs, and bargaining costs, as well as enforcement costs. The difficulties of securing optimal information through search are dealt with in detail later in this chapter.⁵⁸ Difficulties presented by bargaining costs are obvious. Consumers often do not have the time, skills, or inclination to bargain effectively and make informed decisions accordingly. But it is in relation to enforcement costs that we see particular difficulties. Litigation is time-consuming, uncertain, and expensive, particularly as costs have traditionally been paid by the unsuccessful party. These obstacles are compounded by other factors.

⁵⁸ See below, p. 20.

First, many difficulties of substantive law face the consumer. Problems of establishing causation where there has been personal injury, and of showing fault where the action is in negligence, are obvious examples. These obstacles increase the likelihood that an action will be unsuccessful, and so the risks involved in taking action. Secondly, private law remedies will only be effectively utilised where consumers are aware of their rights.⁵⁹ There can be little doubt that steps have been taken to improve awareness, with publications such as *Which?* and television programmes such as *Watchdog* informing consumers of action they can take, but there is still a long way to go. The Office of Fair Trading (OFT) has long regarded the publication of booklets and leaflets to explain consumer rights as one of its key functions, and there is evidence that techniques such as distributing leaflets can be beneficial.⁶⁰ Furthermore, it is interesting to note that the Financial Services Authority, which has been given the responsibility for regulating financial services in the UK, has, as one of its regulatory objectives, 'public awareness', alongside the more traditional objectives for a financial regulator of market confidence, protection of consumers, and reduction of financial crime. The Authority has said that it will work alongside government departments, business and consumer groups to promote financial literacy, consumer information, and advice. The importance of consumer awareness has also been recognised at an international level. The UN Guidelines for Consumer Protection state that '[g]overnments should develop or encourage the development of general consumer education and information programmes' and that '[c]onsumer education should, where appropriate, become an integral part of the basic curriculum of the educational system. . .'.⁶¹ There can be little doubt that ignorance of the law is one of the principal impediments to consumer protection and that measures to eradicate this ignorance will be an important part of an effective consumer policy.

A further matter for concern with private law is that it may have undesirable distributive effects. Wilhelmsson has argued that by emphasising individual claims consumer law reproduces injustice. As litigation will generally only be undertaken by more affluent and better-educated consumers, only they will be protected effectively.⁶² This is examined later in

⁵⁹ See the discussion of consumer education in H. Beales, R. Craswell, and S. Salop, 'The Efficient Regulation of Consumer Information' (1981) 24 *Journal of Law and Economics* 49.

⁶⁰ H. Genn, *Meeting Legal Needs? An Evaluation of a Scheme for Personal Injury Victims* (Oxford, Centre for Socio-Legal Studies, 1982).

⁶¹ It is interesting to note the UK Government's decision to have citizenship taught in schools as part of the National Curriculum in the light of this.

⁶² Wilhelmsson, 'Consumer Law and Social Justice' in Ramsay (ed.), *Consumer Law in the Global Economy*, p. 217.

the context of discussing social justice. Recent developments in the civil justice system have been designed to improve access to justice for less affluent consumers, for example, raising the limit of the county court's small claims procedure, and streamlining case management, but the extent to which they are likely to be successful is unclear.⁶³ Leff's observation that 'one cannot think of a more expensive and frustrating course than to seek to regulate goods or contract "quality" through repeated law suits against inventive "wrongdoers"' rings true.⁶⁴

Market failure

It is widely accepted that the perfect market considered above does not exist in reality, and it is clear that the private law on which it is based suffers from limitations that make it an inadequate basis for protecting consumers. Howells and Weatherill describe the idea of the perfect market as being 'as alluring as it is unrealistic'⁶⁵ and Cranston has likened the free market economist to 'the foolish man who built his house upon the sand'.⁶⁶ Certainly, the characteristics of the perfect market could never, it is submitted, be created in their entirety. However, this does not mean that discussing free markets is pointless. One possible consumer protection policy would be to try to create, as far as is possible and cost effective, the conditions of a perfect market. The next section looks at the reasons why market failure might occur and considers the appropriate responses that the law might make to this.

Absence of competition

Markets may fail through the absence of competition. If the market is to function effectively, it is important that no individual firm or group of firms has sufficient power to influence price. However, '[t]he notion that rival suppliers must dance to the consumer's tune is false where the consumer's influence is thwarted because of a lack of competition'.⁶⁷ The

⁶³ See Scott and Black, *Cranston's Consumers and the Law*, pp. 110–20.

⁶⁴ A. A. Leff, 'Unconscionability and the Crowd – Consumer and the Common Law Tradition' (1970) 31 *University of Pittsburgh Law Review* 349 at p. 356. However, it may not be as expensive as public regulation. See S. Shavell, 'Liability for Harm Versus Regulation of Safety' (1984) 13 *J Legal Stud* 357.

⁶⁵ G. G. Howells and S. Weatherill, *Consumer Protection Law* (Aldershot, Dartmouth and Ashgate, 1995), p. 1.

⁶⁶ R. Cranston, 'Consumer Protection Law and Economic Theory' in A. J. Duggan and L. W. Darvall (eds.), *Consumer Protection Law and Theory* (Sydney, The Law Book Company, 1980), p. 243.

⁶⁷ Howells and Weatherill, *Consumer Protection Law*, pp. 2–3.

law can play an important role in avoiding monopolies and, in particular, in controlling abuse of a monopolistic or oligopolistic position. This could be done by removing behavioural restrictions such as cartels, and structural restrictions such as monopolies themselves. In practice, it may be unrealistic to expect perfect competition. In some cases there will be natural monopolies, where it is less costly to society for production to be carried out by one firm than by several.⁶⁸ There are different ways of responding to this, and it is not possible to examine them in any detail here.⁶⁹ Suffice it to say that some markets will be subject to structural problems that make having numerous competitors unrealistic. Indeed, competition may even be undesirable, for example if it discourages innovation because of the risk of competitors taking up a product developed by their rival. Laws of intellectual property are thus used to suppress competition in the broader public interest. For these reasons, the aim is often said to be 'workable' rather than 'perfect' competition. Although the former term could be criticised as unduly vague and flexible, it is submitted that it reflects a realistic approach to what can, and should, be achieved by way of competition.⁷⁰

Barriers to entry

Free entry and exit are aspects of the market over which governments have a significant amount of control. Subject to international obligations, it would be possible to allow any trader who wishes to do so to enter a particular market, and to allow that trader's business to fail if unsuccessful. In reality, governments elect to impose barriers to entry and exit in certain sectors of the economy. Barriers to entry are generally imposed through prior approval schemes. For example, banks must be authorised by the Financial Services Authority, and anyone accepting a deposit from the public without authorisation commits an offence.⁷¹ Prior approval is seen as justified because of the risks to consumers from unauthorised banks, who may be poorly capitalised, and the risk to the financial system at large from bank failure. Although prior approval has been the subject of criticism, it is widely viewed as an essential element of the banking regulatory framework.⁷² Governments show an equal reluctance to allow free exit from the market where banks are concerned. A bank whose

⁶⁸ A. I. Ogus, *Regulation: Legal Form and Economic Theory* (Oxford, Clarendon Press, 1994), p. 30.

⁶⁹ See Ogus, *ibid.* pp. 30–3.

⁷⁰ See Howells and Weatherill, *Consumer Protection Law*, pp. 443–4.

⁷¹ Banking Act 1987.

⁷² See for example K. Dowd, *Laissez-Faire Banking* (London, Routledge, 1993).

failure is thought to have implications for the soundness of the financial system will not be allowed by governments to exit the market through insolvency – the so-called ‘too big to fail’ doctrine. There will be arguments against free entry in other areas too, particularly where the risks posed by a particular sector are seen to be great, such as pharmaceuticals.⁷³ Although free entry and exit are seen as characteristics of the perfect market, they are characteristics which governments, in general, are not prepared to endure in all sectors. Indeed, it is interesting to note that a recent report for the OFT argued that misleading and false information is particularly likely to be provided where barriers to entry and exit are relatively small.⁷⁴ A final point to note is that barriers to entry are not only imposed by governments through prior approval schemes. In some cases, there will inevitably be high entry costs to an industry, for example if a new business has to lay new pipelines for the supply of water or gas. This, too, will make it difficult for new business to enter the market and so will limit the benefits of competition.

Product homogeneity

The requirement of product homogeneity is closely linked to that of perfect information. The market is said to fail where there are qualitative differences within a particular product market, such that consumers are unable to compare like with like. This is most relevant in the context of advertising. Traders can use artificial product differentiation to create illusory differences between similar products, for example through brand advertising.⁷⁵ This is considered in relation to information below, and in relation to the protection of economic interests in chapter 6.

Information deficits

One of the characteristics of the perfect market is that economic actors, including consumers, have ‘perfect information’ about the nature and value of commodities traded. In reality, we know that consumers can face difficulties in obtaining and using information about products they are considering purchasing. They may suffer from information asymmetry in that they know less than another party (generally the supplier) and will frequently suffer from some information imperfections (in the

⁷³ See ch. 5.

⁷⁴ *Consumer Detriment Under Conditions of Imperfect Information* (Office of Fair Trading Research Paper II, August 1997), p. 103.

⁷⁵ See I. Ramsay, *Advertising, Culture and the Law: Beyond Lies, Ignorance and Manipulation* (London, Sweet and Maxwell, 1996), pp. 6–7 and 30–40.