THE ABUSE OF WARRANTY LAW AS A CONTRIBUTING FACTOR TO CONSUMER PROBLEMS

Thesis for the Degree of Ph. D.
MICHIGAN STATE UNIVERSITY
MICHAEL SUNSHINE
1973

This is to certify that the

thesis entitled

THE ABUSE OF WARRANTY LAW AS A CONTRIBUTING FACTOR TO CONSUMER PROBLEMS

presented by

Michael Sunshine

has been accepted towards fulfillment
of the requirements for

Ph.D. degree in Ag. Econ.

A. Allan Schmid
Major professor

Date May 9, 1973

O-7639

ABSTRACT

THE ABUSE OF WARRANTY LAW AS A CONTRIBUTING FACTOR TO CONSUMER PROBLEMS

By

Michael Sunshine

This study is a formulation of a general theory of consumer problems with durable products. The argument assumes the existence of deceptive behavior by sellers. Following traditional economic theory this behavior is assumed to exist because such behavior is profitable. The central task of this study is to determine the features of the commercial environment which make such behavior profitable. This study proposes that two sections of the Uniform Commercial Code, the basic commercial law in 49 states, sets the framework for making deceptive behavior profitable. These provisions allow the exclusion of traditional warranties by means of a contract under the freedom of contract doctrine.

The demonstration of the illusionary nature of the freedom consumers actually have under this doctrine and the failure of its presuppositions to exist form the base of the policy recommendation of this study. The recommendations are that the exclusions of traditional warranties as allowed in the Uniform Commercial Code not be allowed in consumer transactions. The study concludes

with a consideration of changes in the law in several states, proposed Federal legislation and with an analysis of the likely effects of the implementation of such a policy.

THE ABUSE OF WARRANTY LAW AS A CONTRIBUTING FACTOR TO CONSUMER PROBLEMS

By

Michael Sunshine

A THESIS

Submitted to

Michigan State University

in partial fulfillment of the requirements

for the degree of

DOCTOR OF PHILOSOPHY

Department of Agricultural Economics

1973

ACKNOWLEDGMENTS

Writing a dissertation is a very frustrating experience. This thesis exists largely because of encouragement at critical times from Dr. Hendrik Zwarensteyn. Professor Zwarensteyn's aid came as a teacher of business law, a patient force controlling my tendency to extrapolate and as an author of a very handy quick reference to law. Dr. Allan Schmid's desire for ties to the real world required many appropriate changes in my theoretical conclusions. Dr. James Bonnen made a valiant, if not fully successful, effort to control my tendency to use a rather heavy style and to leave out steps in my reasoning.

This dissertation was written with considerably more freedom than is usually allowed. My committee did not require that I agree with them, but rather that I defend my position. While it is customary for authors to exclude those who provided aid from responsibility for errors, such a disclaimer is especially appropriate here. None of those who aided me in this project are in anything approaching complete agreement with the conclusions.

TABLE OF CONTENTS

Chapter		Page
	INTRODUCTION.	1
	Seriousness of Problem.	3
	Structure of the Problem.	3
	Problems of Evaluation.	6
ONE	WARRANTIES.	13
	Nature of a Consumer Problem.	13
	Expectations and the Uniform Commercial Code.	18
	a. Implied Warranty	19
	b. Reasonability.	21
	c. Express Warranties	27
TWO	TRADITIONAL WARRANTIES AS A CONSUMER PROTECTION POLICY	35
	Contract Law.	35
	Competition and Contracts	38
	Negotiation of Contracts.	41
	Contract Adjustments.	47
	Automobile Experience	48
	Policy Implications of Requiring Effective Warranties.	57
	Absolute Liability as a Policy - Workmen's Compensation.	59
	The Relationship Between Workmen's Compensation and Consumer Protection. . .	66
	Evaluation of Consumer Protection Policies.	67
THREE	TRADITIONAL BUYER PROTECTION AS A PRACTICAL POLICY FOR PURCHASERS OF DURABLE PRODUCTS .	78
	Expectations.	79
	The Solution.	81
	Product Variety	86
	Enforcement	89
	Administrative Agencies	92
	The Ombudsman	94
	Judicial Strain	96
	Product Innovation.	99
	The Role of Small Claims Courts	104

Chapter		Page
FOUR	RECENT CHANGES IN WARRANTY LAW.	114
	Court Action.	116
	Proposed Federal Legislation.	119
	State Legislation Passed.	120
	General Trend	124
FIVE	THE ECONOMIC SIGNIFICANCE OF REQUIRED WARRANTIES.	128
	Effects of Workmen's Compensation Legislation	129
	Effects of Requiring the Traditional Warranties in Consumer Transactions . . .	135
	Voluntary Warranties.	145
	Effect on the Poor.	148
	Summary	149
	LIST OF REFERENCES.	160

LIST OF TABLES

Table		Page
1	U. S. Car Production.	50
2	Industrial Fatalities	61

INTRODUCTION

> "The view has been gaining widespread acceptance that corporate officials and labor leaders have a 'social responsibility' that goes beyond serving the interests of their stockholders or their members. . . . In . . . (a free economy) there is one and only one social responsibility of business--to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition, without deception or fraud. . . . It is the responsibility of the rest of us to establish a framework of law such that the individual in pursuing his own interest is, to quote Adam Smith, 'led by an invisible hand to promote an end which was no part of his intention. . . . '"[1]

The study which follows analyzes the nature of consumer problems with misrepresented products and proposes a change in a few of the legal rules which regulate commerce to yield better performance by manufacturers as they try to maximize their profits. The present commercial environment of manufacturers allows the industrial performance which currently exists. The doctrine of freedom of contract holds that individuals should be allowed to enter any agreement which they find mutually satisfactory. This policy presupposes that individuals can meaningfully negotiate their agreements.

> "The traditional contract is the result of free bargaining of the parties who are brought together by the play of the market, and who meet each other on a footing of approximate economic equality. In such a society there is no danger that freedom of contract will be a threat to social order as a whole."[2]

If individuals cannot negotiate their agreements, then a policy which assumes that they can may lead to very undesirable results. This study argues that the assumption of the doctrine of freedom of contract needed to justify this policy is not generally encountered in the market for consumer goods, and that the results are often unfortunate. The current commercial environment is a distortion of the doctrine of freedom of contract which is used for its justification. The commercial environment and the resulting deception of consumers and the production of goods and services which do not function as a reasonable consumer would expect are neither necessary nor desirable. At issue is the incidence, or who will bear the costs, of losses due to production decisions which lead to unmet reasonable consumer expectations. The current formulation of warranty law allows the seller to shift the responsibility for these decisions to the consumer. The changes proposed in this study would shift the responsibility for the decisions to the party making the decisions. Under this situation one would expect, all other things equal, greater care and concern in decision making. A basic assumption of this study is that the magnitude and seriousness of consumer problems are functions of the operating social policy which determines the party which will be responsible for losses on unsatisfactory products.

Seriousness of Problem

On February 24, 1971, President Nixon in a message to Congress stated:

> "The history of American prosperity is the history of the American free enterprise system. The system has provided an economic foundation of awesome proportions and the vast material strength of the nation is built on that foundation. For the average American, this strength is reflected in a standard of living that would have staggered the imagination only a short while ago. This constantly rising standard of living benefits both the consumer and the producer.
>
> In today's marketplace, however, the consumer often finds himself confronted with what seems an impenetrable complexity in many of our consumer goods, in the advertising claims that surround them and the means available to conceal their quality. The result is a degree of confusion that often confounds the unwary, and too easily can be made to favor the unscrupulous. I believe new safeguards are needed, both to protect the consumer and to reward the responsible businessman. . . .
>
> Accordingly, I am again submitting proposals designed to provide such a Buyer's Bill of Rights by: . . .
>
> --Proposing a Fair Warranty Disclosure Act which will provide for clearer warranties, and prohibit the use of deceptive warranties; . . .[3]

Structure of the Problem

To understand the role of warranties in consumer protection, the nature of "the typical consumer problem" must be developed. The failure of a product's performance to meet the reasonable expectations of a consumer, as will be developed later, provides such a definition.[4] Next, the existing framework of rules leading to the existing consumer problems must be determined and examined. The Uniform Commercial Code (UCC) sets the general rules for the conduct of commercial transactions.[5] The provisions of the UCC allow for freedom of contract between consumers and

sellers even where in reality no meaningful negotiation opportunities exist (although such opportunities are theoretically required for a contract.) Without negotiation or competition in contractual terms the exercise of freedom of contract by strong parties against comparatively weak parties may yield, and in the past have yielded, socially dubious results. The UCC covers considerable ground, but for purposes of this argument only a few sections involving warranties require consideration.[6]

The proposed changes, their effects on social institutions and the economic mechanism by which they change the manufacturers' behavior (to reduce the number of consumer problems) conclude the argument. Since this argument proposes changes which have only recently begun to occur, the analysis of what will happen is necessarily speculative. But, the changes proposed are similar to changes made in laws regulating insurance and industrial safety.[7] Considerations of the changes in behavior which occurred in these fields as the freedom of contract of the parties was restricted should provide insights to both the conditions in which such a change is an effective policy and the changes such a policy can achieve. The theoretical discussion on the nature of "freedom of contract" was developed in discussions of insurance contracts and labor relations at the turn of the century and during the depression of the 1930's. The materials considered in the second chapter, while considered for the insights they

can provide relative to the current problems of consumers, appeared in these earlier debates involving insurance and labor relations. The evidence is limited and relies on analogies, but the direction of behavior change is consistent in all of the cases. This study considers the effects of legal changes which have and will continue to occur with such evidence as is available.

Changing the fundamental commercial rule framework is not the only approach available to society for resolving the problems consumers face in the market. One might propose an extensive program of consumer education.[8] The task will not be easy; the educational approach advocate must answer three questions: what is to be taught, to whom it is to be taught, and how it is to be taught. These questions cannot be easily, if at all, answered. There are two hundred million consumers to be taught about a huge variety of products, at a time when the public does not seem interested in expanding the educational system. One may seriously doubt the feasibility of education resolving consumer problems directly. Further, Ralph Nader has pointed out that the emphasis on driver safety has been promoted by the automobile manufacturers to allow the industry to preserve its exclusive (at the time) control over the design of its product.[9] Thus it can be argued that an educational program may (and apparently did in the case of automobile safety) by shifting resources and concern from more effective techniques, impede rather

than enhance a program of consumer protection. Another alternative lies in using administrative agencies, this complimentary approach is considered below in Chapter Three.

Problems of Evaluation

The policy proposal made in this study is politically conservative. The changes do not call for the creation of any new organization to supervise the behavior of anyone. Rather a restoration of the traditional position of the consumer developed by the courts over hundreds of years of experience in reaching equitable dispute settlement between buyers and sellers is sought. This return to the traditional approach while holding the consumer responsible for his own carelessness in the market will place much of the responsibility for consumer problems on the party which is both mainly responsible for their existence and capable of their elimination, the manufacturer. This study demonstrates that one may reasonably expect that with the return of the traditional rules between buyers and sellers, the manufacturers will find that honest representation and the production of goods meeting the consumers' reasonable expectations are the only means to make a profit. This change seeks to correct a relatively modern contrived nonaccountability created by the manufacturers of consumer products.[10]

Economic programs which require the allocation of scarce resources for one use to another are justified in terms of the trade-off between the net benefits of the

selected program and the lost net benefits of the rejected alternatives. While obtaining the various figures may present problems the arithmetic comparison of the costs and benefits of the justification process is clear.[11] When the proposed change involves a change in the commercial environment, as in the case of the Sherman Antitrust Act or the changes in the UCC proposed in this paper, the evaluation procedure becomes far more speculative. Ideally the positive and negative effects of the change in the full economy must be ascertained and evaluated. Experts debate the magnitude of the benefits which would follow an expenditure for a kidney machine, but the existence of the benefits. The mere existence of the effects of a change in the commercial framework is subject to debate (e.g., does antitrust enforcement raise or lower productivity?).[12] In general these effects, if agreed upon, will not have a market value as in the case of economic projects such as dams or steel mills. Of necessity the conclusion of the advisability of such a change will depend on the weighting which must be arbitrarily placed by political means on the effects that according to those making the analysis believe will occur. In the case of the policy proposed in this study the potential effects which are considered in this study include: 1) the loss of income to those who currently profit from producing defective goods and who will not be able to adapt, 2) the effect of this policy on the cost of goods, particularly as it will effect the poor,

3) the effects of this policy on innovation, and 4) as a policy ultimately dependent on the judicial system it is essential to consider the effects of the policy on an overloaded court system. The combined evaluation of these effects determines the advisability of adopting and subsequently implementing the proposed policy.

The first chapter lays the foundation by considering the nature of consumer problems, the decision making process in a free economy and the nature of a society's consumer protection policy. An analysis of the role contracts play in society, the assumptions of the doctrine of freedom of contract, the emergence of standardized contracts, the sections of the UCC controlling warranties and their exclusion, and the role of warranties in consumer protection are considered in the second chapter. Chapter three begins the evaluation of the trade-offs of this policy with considerations of the effect of the policy on the profitable behavior of manufacturers, the strain caused by the enforcement on the judicial system, and the effects of the policy on product innovation. A comparison of this proposal with related pending legislation is made in the fourth chapter. The fifth chapter returns to the analysis of the policy considering the economic mechanism of the policy's operation, the likely extent of the losses to producers who could not adapt and the effect of this policy on the poor.

FOOTNOTES

[1]Milton Friedman, Capitalism and Freedom (Chicago: University of Chicago Press, 1962), p. 133. This statement, while not philosophically naieve, is deceptively simple. The establishment of a framework of law which will yield the beneficial results is extremely difficult to achieve. The following study illustrate this point by considering one such framework which has failed and various adjustment to this framework of law to improve the performance of the economy.

[2]Justice Francis in Henningnsen v. Bloomfield Motors, Inc., 38 N.J. 358.161 A. 2d 69 at 86 (New Jersey, 1960).

[3]U. S. President. "Consumer Protection," Weekly Compilation of Presidential Documents, Richard M. Nixon, March 1, 1971, pp. 288-289. GS 4.114:7 These proposed laws were not enacted.

[4]This definition is inclusive of virtually all consumer problems, but the legal changes considered in this study will have an effect only on durables of a cost to the consumer, following Federal legislation, of over $5. Warranty legislation will not eliminate consumer problems resulting from credit, governmental bureaucracy, or consumer carelessness.

[5]The UCC was presented by its authors, the American Law Institute and the National Conference of Commissioners on Uniform State Laws in 1952. Seventeen years later it had been enacted (not always in a uniform manner) in forty-nine states (all except Louisiana) the District of Columbia and the Virgin Islands. The UCC was revised in 1958, 1962 and 1966. The 1968 master edition including comments and citations, but excluding forms, had 1,576 pages.

[6]During the 92d Congress both the Senate and the House held hearings on various pieces of legislation which sought to control warranty abuses. The importance of warranties to consumers is shown both by the existence of the hearings themselves and some of the testimony at the hearings.

". . . if mail received by an organization such as the Consumer Federation of America is any indication of

consumer concerns, consumer concern with warranties looms very large." Edward Berlin, (Cousel, Consumer Federation of America). U. S. Congress, House, Committee on Interstate and Foreign Commerce, Consumer Warranty Protection, Hearings before a subcommittee on Commerce and Finance of the Committee on Interstate and Foreign Commerce, House of Representatives, on H.R. 6313, H.R. 6314, H.R. 261, H.R. 4809, H.R. 5037, H.R. 10673 (and similar and identical bills) 92d Congress, 1st Sess., 1971, p. 274.

". . . The Commission (Federal Trade Commission) believes that informative, accurate, clear and fairly written warranties, backed up by warrantors who deliver what they promise, are essential to our free market economy, and that legislation to insure these consumer rights is necessary." Miles W. Kirkpatrick (Chairman, Federal Trade Commission). U. S. Congress, Senate, Committee on Commerce, Consumer Products Warranties and Improvement Act of 1971, Hearings before the Consumer Subcommittee of the C mmittee on Commerce, Senate, on S. 986, 92d Congress, 1st Sess., 1971, p. 33.

". . . The importance of this subject (consumer warranties) to consumers can hardly be overstated. Not only do warranties apply to a broad spectrum of consumer products, but in a marketplace where complex and costly goods are the norm, and repair costs are skyrocketing, they involve a total investment by consumers of millions of dollars annually." Virginia H. Knauer (Special Assistant to the President for Consumer Affairs). U. S. Congress, House, Warranty Hearings, p. 248.

[7]Insurance companies learned that juries would award large judgments to an individual against a powerful firm. To reduce this risk they prepared contracts which removed the discretion of a jury to make such a judgment. Some firms discovered that they could write a contract which would create false expectations of protection but which actually made the policies virtually uncollectable. To correct the injustices of these highly profitable "insurance contracts" the state (New Hampshire in 1855) passed statutes and/or formed commissions to determine the contents of the contract (regardless of its actual contents) which the court would enforce. Three types of regulation are used: 1) the legislature provides the exact wording of the policy, 2) an administrative agency prescribes the exact wording to be used or 3) the legislature provides standards to be administered by an official who may approve or disapprove submitted policies. The complexity of insurance has forces the legislature to give detailed control to administrative agencies which establish terms for convential policies and give approval for new style policies sold to consumers. The state policy

allows the layman to have his reasonable expectations met. See Marion W. Benfield, Jr., Social Justice Through Law: New Approaches in the Law of Contract (Mineola, New York: Foundation Press, Inc., 1970), pp. 131-140. The experience with Workmen's Compensation Legislation is considered in Chapter 5 and Footnote 36 of Chapter 2.

[8]Education is clearly a sine qua non of consumer protection. President Nixon in a section on consumer education in his consumer protection message to Congress stated:

> "Legislative remedies and improved enforcement procedures are powerful weapons in the fight for consumer justice. But as important as these are, they are only as effective as an aware and an informed public make them. Consumer education is an integral part of consumer protection. It is vital if the consumer is to be able to make wise judgments in the marketplace. To enable him or her to do this will require a true educational process beginning in childhood and continuing on." U. S. President, Weekly, p. 293.

For the nature of such a program see U. S. President, President's Committee on Consumer Interests, Suggested Guidelines for Consumer Education: Grades K-12 (Washington, D. C.: Government Printing Office, 1970), Pr 36.8:c76/Ed8. The immensity of the content of such a program is noted at the end of the introduction, "In summary, Consumer Education is vital for all young people because of the competence it can provide in dealing with our modern marketplace. But, all who are concerned with education will recognize that Consumer Education is inherently tied to developing a personal philosophy, finding satisfaction in daily living, and fulfilling a citizenship role in a free enterprise system."

[9]Ralph Nader, Unsafe At Any Speed, (New York: Pocket Books, 1965), pp. 175-178. This citation refers to only one form of consumer education-that done by firms. Nader argues that the automobile industry's efforts in education did not fundamentally serve to improve education, but to divert attention from product defects. It is worth noting that an educational system which teaches consumers to be wary supports the caveat emptor approach to social control--the responsibility for a loss rests with the consumer. This paper argues that placing the responsibility on the consumer leads to very poor results in the market.

[10]Ralph Nader and Donald Ross, Action for a Change, (New York: Grossman Publishers, 1971), p. 4. They use the term "contrived nonaccountability" for different behavior, but the term is extremely appropriate to the problem considered in this paper.

[11]The potential amount of complexity seems to be without limit. Cost-benefit analysis includes the determination of the alternatives and then the listing and evaluating of the costs and benefits of each. These figures are then used in a decision criteria (a system of weighting) for selecting the alternative which will be used. See M. G. Kendall ed., Cost-Benefit Analysis, (New York: American Elsevier Publishing Company, Inc., 1971), for a selection of examples presented at a symposium organized by the NATO Scientific Affairs Committee.

[12]"A fundamental question in antitrust is whether a strong policy against concentrated economic power groups impedes or is conducive to our goals for efficiency and technical progress. . . . Since most small, medium-sized, and larger plants in an industry generally produce a heterogeneous output that crosses over a number of industrial classifications, the problem of ascertaining whether smaller or medium-sized firms are as efficient (or perhaps more efficient-MS) as the larger-sized firms is exceedingly complex."

Eugene M. Singer, Antitrust Economics: Selected Legal Cases and Economic Models, (Englewood Cliffs, N.J.: Prentice Hall, Inc., 1968), p. 4.

CHAPTER ONE

WARRANTIES

Nature of a Consumer Problem

When working with a problem as general as consumer protection and consumer dissatisfaction, considerable care must be given to the foundation to insure that the resulting structure is stable. The general concepts of a study, if the study is to have any value, must lead to policies which result in desirable behavioral changes. Initially the idea of what is precisely happening when a consumer consumes must be set.

> "The purpose of the product is not what the engineer explicitly says it is, but what the consumer implicitly demands that it shall be. Thus the consumer consumes not things, but expected benefits - not cosmetics, but the satisfaction of the allurements they promise; not quarter-inch drills, but quarter-inch holes; not stock in companies, but capital gains; not numerically controlled milling machines, but trouble-free and accurately smooth metal parts; not low-cal whipped cream, but self rewarding indulgence combined with sophisticated convenience."[1]

The view that one does not consume products, but rather flows of services, is not new. A bond is clearly a flow of income and a house is a flow of housing. This might appear to be merely a matter of semantics, but the method of definition makes a difference in consumer products. All too often there is a difference between a car defined as an

object with four wheels and a motor (plus any other non-performance characteristics one might wish to add) and a car defined as a flow of satisfactory private transportation services. A car in constant need of repair might meet the first definition, but would fail to qualify under the second definition as anything other than something which looks like a car.

In many situations the use of the physical descriptions is satisfactory for practical purposes. Agricultural commodities are bought and sold before they exist on the base of physical description. For a system to work in which purchases are made without observation the consumer must receive the product he expected when made the purchase. Wholesale markets have various formal and informal means to insure the level of honesty they require for their efficient operation (the entire transaction can occur by telephone). The situation is obviously different in the consumer markets.

While in this study the differences between wholesale and retail markets can only be treated in passing, certain characteristics may be noted which illuminate the problems faced by consumers. A wholesale market is characterized by high volume, repeat business and low margins. There are relatively few buyers and sellers and since they earn their living through their activities in the market they make an effort to be highly informed. If a seller delivers a product which is below the standards,

the purchaser is unlikely to buy again (repeat business) and is likely to inform other purchases personally at meetings and/or in the trade journals about the poor service he received. These results are likely to follow even if the purchaser refuses to accept the product or returns the product under the formal rules of the market. Under these conditions it is clearly the situation that honest representation is the best policy.

The retail market for consumer durables is different. Durables, by definition, are supposed to last. They are sold in a low volume, relatively high margin and little repeat business (for the same product by the same individual) market. The seller must create the expectations of services in the consumer which will lead him to make the purchase. The actual performance is of secondary importance as consumers have no effective means of publicizing their unsatisfactory experiences.

> ". . . in economic terms, the lack of any practical consumer remedy can operate as an incentive for questionable business methods, particularly when one considers that under modern marketing practices a bad reputation seldom catches up with the violator, and that the probability of effective governmental enforcement is generally low."[2]

That honesty may not be the best (most profitable) policy is a clear possibility. The concern with consumer protection leads one to believe that honesty has been found, by at least some manufacturers and retailers, not to be the best policy. This study, by considering warranty law, provides part of the reason why honesty may not be the

best policy and what action could be taken to make honesty the best commercial policy. The honest behavior with which this study is specifically concerned lies in the efforts of manufacturers when they create expectations of product performance in prospective consumers. Honest behavior would consist of creating only those expectations of performance in the consumer which the manufacturer knows the product's actual performance will meet.

In terms of a particular product, a consumer has two different basic sets of performance expectations. While it may be impossible to construct a definitive list of such expectations, if only because expectations are most clear to consumers only when they are disappointed, a partial listing of the expectations can be hypothesized. As an example consider the case in which a consumer purchases an automobile. He has some general expectations as to automobiles. These might include such considerations as reliability and personal safety. But a consumer does not purchase an 'automobile,' but rather a particular automobile. The selection of a particular automobile follows from other expectations. These expectations might include extra comfort, fast acceleration and/or good gas milage. The first set of expectations are those which concern minimum acceptable performance which one would expect from any unit of the type and which lead the consumer to the decision to purchase a type of product. The second set of expectations differentiate the various

models on the market and lead the consumer to select one rather than another unit of the particular product type.

These consumer expectations come from the promotional activities of manufacturers and retailers. Consumer disappointments, the consumer problems considered in this study, occur when the product's actual performance does not meet the consumers' expectations of performance as created by the promotional efforts of the manufacturers and retailers. When the manufacturer and/or retailer purposefully (and dishonestly) create expectations which they know the product will not meet, they increase the sales of their particular units (the more favorable performance expectations created the more attractive the product) but at the same time this behavior creates consumer problems. The chronic consumer dissatisfaction with the automobile industry indicates that this misleading behavior need not be a short run phenomenon. The tendency for all firms to exaggerate the capabilities of their products need not be the result of collusion, but rather an effort to maintain their competitive positions. The issues involved in innovation and sales under rules creating economic incentives for accurate representation of product capabilities are considered below. Since consumer expectations are produced in a purposeful manner, often with the expenditure of considerable sums of money, and since advertisers exercise great care in determining in advance the effects of their advertisements, when a

consumer has an expectation of performance which is not met by the performance of the product there exists some reason for suspecting that the manufacturer and/or retailer have purposefully mislead the consumer.

Expectations and the Uniform Commercial Code

The consumers' expectations might seem to correspond to two different levels of producer performance. The general level of expectations might correspond to the typical performance of the industry while the particular expectations for the selected model would correspond to the typical performance of the particular firm or division. This correspondence to actual producer performance is not the actual situation for two reasons. These performance standards of the firm and industry are not known by consumers and could not form the base of consumer decisions. More importantly, the expectations of consumers come from the promotional efforts of the firms. The promotional efforts may create expectations which approximate the actual performance of the products when the producers promote in an honest manner. But the expectations created may be less than the actual performance in a conservative industry or much greater in a more sensational industry. There is no necessary direct connection between industry performance in terms of the product and consumer expectations since actual performance, through reputation, is only one of several factors.

a. Implied Warranty

The commercial law as embodied by the Uniform Commercial Code (UCC) has provisions for each of these systems of expectations. The general expectations correspond to the implied warranty of merchantability and the particular expectations correspond to express warranties. Section 2-314 sets the standards for the general consumer expectations.

> Sections 2 - 314 - Implied Warranty: Merchantability; Usage of Trade
> (1) Unless excluded or modified (Section 2 - 316), a warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind. Under this section the serving for value of food or drink to be consumed either on the premises or elsewhere is a sale.
> (2) Goods to be merchantable must be at least such as
> (a) pass without objection in the trade under the contract description; and
> (b) in the case of fungible goods, are of fair average quality within the description; and
> (c) are fit for the ordinary purposes for which such goods are used; and
> (d) run, within the variations permitted by the agreement, of even kind, quality, and quantity within each unit and among all units involved; and
> (e) are adequately contained, packaged, and labeled as the agreement may require; and
> (f) conform to the promises of affirmations of fact made on the container or label if any.
> (3) Unless excluded or modified (Section 2 - 316) other implied warranties may arise from course of dealing or usage of trade.

Clearly the standard of merchantability is completely general. This generality is essential because this warranty arises from the act of sale of a good by a dealer in the particular good and the definition of merchantability must apply to all goods sold by dealers.

Does this standard, if indeed it is a standard, provide a manufacturer with meaningful information as to how to design and construct his product so that it will be merchantable. To determine if merchantability does provide behavioral criteria, the term must be considered as it is used by the courts in their decisions. The editors of the Uniform Commercial Code in the Master Edition have compiled under note 9 to section 2 - 314 quotes from decisions which illustrate their understanding of the term 'merchantable.' A selection of these quotes are listed below.

> "An 'implied warranty of merchantability' is a warranty implied by law that goods are reasonably fit for the general purpose for which they are sold." Eimco Corp. v. Joseph Lombardi & Sons, 193 Pa. Super 1, 162 A. 2d 263 (1960).
>
> "Warranty of merchantability in sale of goods means only that the article is reasonably fit for the purpose for which it is sold and does not imply absolute perfection." Schipper v. Levitt & Sons, Inc., 44 N.J. 70, 207 A. 2d 314 (1965).
>
> "Implied warranty of merchantability means that the product is reasonably fit for the purpose intended; it does not imply absolute perfection; and there is no duty on the part of the manufacturer to furnish tools which will not wear out." Jakubowski v. Minnesota Min. & Mfg., 42 N.J. 177, 199 A. 2d 826 (1964).
>
> "While defendant manufacturer of the automobile was not necessarily under an obligation to provide a hardtop model which would be as resistant to roll-over damages as a four-door sedan, the manufacturer was required to provide a hardtop automobile which was a reasonably safe version of such model, and which was not substantially less safe than other hardtop models." Dyson v. Gen. Motors Corp., D. C. Pa. 1969, 293 F. Supp. 1064 (1969).
>
> "Factors other than those concerned exclusively with safety of the product may be important in determining a product's merchantability, and recovery may be allowed on the basis of breach of implied warranty of

> merchantability for damage other than personal injury." Martel v. Duffy-Mott Corp., 15 Mich. App. 67, 166 N.W. 2d 541 (1968).
>
> "Neither the fact that the tractor dealer did all he could to correct the defects in the tractor, nor the ultimate liability of the manufacturer for the defects, relieved the dealer of the obligation imposed by this section as to the implied warranty of merchantability." Ford Motor Co. v. Taylor, __ Tenn. App. __, 446 S.W. 2d 521 (1969).[3]

Merchantability is clearly not revolutionary. The key word is 'reasonable.' Only if this word has any specifiable meaning in a behavioral sense can the standard of merchantability provide direction for a manufacturer.

b. Reasonability

It is not obvious that the word 'reasonable' has any content other than describing the behavior of the courts. The determination of 'reasonable' is a factual matter and would be determined by a jury or a judge acting as a jury. Reasonable may be only what the jury decides in the instant case to be reasonable. If no guide to what will be decided to be reasonable exists, independent of the particular court decision, then the manufacturer must guess at the decisions the courts will make on what would be a purely random basis (i.e., no guide exists.) Reasonable is not the only word of doubtful clarity in the law. Justice Jerome Frank noted,

> "Or, on occasion, the guide to a correct legal conclusion is said to be the 'manifest intention' of the maker of an instrument. Someone has observed that whenever a lawyer says that something or other was the manifest intention of a man, 'manifest' means that the man never really had such an intention. Lawyers use

> what the layman describes as 'weasel words,' so-called 'safety-valve concepts,' such as 'prudent,' 'negligence,' 'freedom of contract,' 'good faith,' 'ought to know,' 'due care,' 'due process,' - terms with the vaguest meaning - as if these vague words had a precise and clear definition; they thereby create an appearance of continuity, uniformity and definiteness which does not in fact exist." (p. 27) This uncertainty is not an unmitigated evil. "Much of the uncertainty of law is not an unfortunate accident: it is of immense social value." (p. 7) This slack in the law allows judges to bring in considerations of justice (also a 'weasel' word).[4]

The word reasonable is defined in Black's Law Dictionary (1951 edition) by a series of synonyms: just, proper, ordinary, unusual, fit and appropriate to the end in view, honest, equitable, fair, suitable, moderate and tolerable. There is clearly some ambiguity in that those qualities denoted by just are not identical to those of ordinary. Still there is not a complete lack of content since words such as careless do not appear on the list. In the Restatement of the Law of Torts the idea of reasonability is considered as follows:

> "The words, 'reasonable man' denote a person exercising those qualities of attention, knowledge, intelligence and judgment which society requires of its members for the protection of their own interests and the interests of others. . . the 'reasonable man' is a man of reasonable 'prudence.'"[5]

The definition of 'reasonable' is clearly not denotative in that it does not list qualities which must be present if something is to be considered 'reasonable.' Neither is the definition connotative in that it does not attempt even a partial listing of all reasonable instances. The definition of 'reasonable' is an intuitive definition - it is believed

that reasonable men can agree on what is reasonable. Clearly this criterium, reasonable, is not salient in that it is so prominent or conspicuous that by itself it would provide a comprehensive guide to action for a manufacturer. To know that a product must be reasonably fit for the ordinary purposes for which it is used is not to have a list of qualities that it must meet such as one might find in commodity grades or Federal Trade Commission orders.

To require all policies to be salient (consisting of a list of clearly understood minimum characteristics) might not be desirable. Justice Frank, while discussing the rescision of contracts based on non-negligent unilateral mistakes, has noted that such clarity is not required for commercial activity.

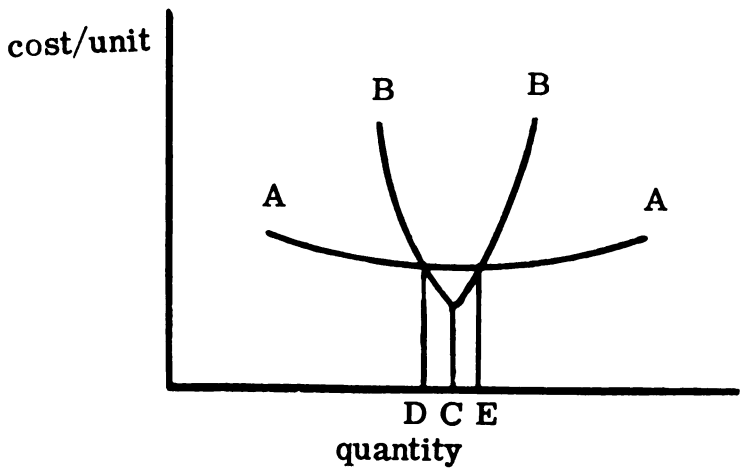
> "In short, the 'security of business transactions' does not require a uniform answer to the question of when and to what extent the non-negligent use of words should give use to right in one who has reasonably relied on them."
>
> "New York, a lively center of commerce, at least to some extent allows relief of such unintended mistakes."[6]

This case, while dealing with a non-negligent unilateral mistake is appropriate to show that complete certainty is not required for commerce. This result is not surprising since risk and uncertainty are basic characteristics of business. Commercial security and just results (which may be difficult to obtain when the rule is salient) must be balanced. The essential quality is not that the term 'reasonable' be defined so clearly that all who understand the word use it in an identical manner in all instances

(e.g., 'line' in Euclidean geometry), and that not to use it in this manner is proof that it is not understood. Rather, the term must have sufficient common usage so that while individuals might disagree in particular instances depending on how they balance the various positions of the contending parties, the resulting decision while it might seem incorrect will not seem completely unreasonable. Unreasonable implies a degree of irrationality and the lack of qualities found in the 'definition' of reasonable. Such irrationality is not claimed when one holds that another is in error.

While the idea of reasonable and therefore merchantability is not salient, in the sense that they do not provide a list of conditions which are necessary and/or sufficient for meeting the requirement, these ideas are not free of content. While some uncertainty may continue to exist a manufacturer does have an idea of whether his product is fit for the ordinary purposes for which it is used. While the ordinary purposes might be subject to some interpretation, again some common understanding exists. If no common understanding existed as to the ordinary use of a product the manufacturer would not know what to produce and offer and the consumer would not know what to purchase. The existence of products and markets requires this wide range of common understanding. The situation is not unlike a normal problem faced by any producer of goods and services. If the manufacturer is

faced by two production processes with cost functions AA and BB he must choose which to use on the base of expected output. Function BB allows the production of goods at a lower cost for quantities between D and E while function AA allows production at any other quantity level at a lower cost.



Businessmen work in a world of uncertainty. If their products must be merchantable they will choose a quality level even when they are not completely sure of the exact standard which will be applied in any particular dispute just as they choose a production process even when they are not sure of the ultimate output level.

It is possible and indeed it is not unlikely that a jury might set an unreasonable 'reasonable' standard. But one may discount both the possibility of this happening frequently and the significance of when it does happen. A standard out of line with the demands of the ordinary use of the product is unlikely to occur because warranties are an established part of the law with a strong base in precedent and because the manufacturer will be able to

appeal any erratic decisions. Even if an erratic decision were to occur the effect would not be serious since the dispute involves only one unit and not the entire production of the firm as in a ruling of a regulatory agency. While the erratic ruling would serve as precedent for future cases, by itself, if it is clearly erratic, it would be unlikely to sway other courts. The warranty of merchantability is a conservative standard that operates at the margin and is unlikely to put an unfair burden on a manufacturer who produces goods which are fit for their ordinary use.

UCC Section 2 - 315 establishes the warranty for fitness for a particular purpose.

> Section 2 - 315 - Implied Warranty: Fitness for a Particular Purpose
>
> Where the seller at the time of contracting has reason to know any particular purpose for which the goods are required and that the buyer is relying on the seller's skill or judgment to select or furnish suitable goods, there is unless excluded or modified under the next section an implied warranty that the goods shall be fit for such purpose.

This warranty differs from the warranty of merchantability in that it is not created by the mere act of a sale by a dealer. This warranty applies only if the buyer acts on the advice of a seller when the buyer has explained the particular use for which he wishes to buy a product. This warranty makes the seller responsible for the advice he provides a buyer about which product is suitable for a particular task.

c. Express Warranties

Section 2 - 313 establishes warranties on the base of promotional activities of the manufacturer, including but not necessarily limited to the written warranties offered by manufacturers to consumers.

> Section 2 - 313 - Express Warranty: By Affirmation, Promise, Description, Sample
> (1) Express warranties by the seller are created as follows:
> (a) Any affirmation of fact or promise made by the seller to the buyer which relates to the goods and becomes part of the basis of the bargain creates an express warranty that the goods shall conform to the affirmation or promise.
> (b) Any description of the goods which is made part of the basis of the bargain creates an express warranty that the goods shall conform to the description.
> (c) Any sample or model which is made part of the basis of the bargain creates an express warranty that the whole of the goods shall conform to the sample or model.
> (2) It is not necessary to the creation of an express warranty that the seller use formal words such as 'warrant' or 'guarantee' or that he have a specific intention to make a warranty, but an affirmation merely of the value of the goods or a statement purporting to be merely the seller's opinion or commendation of the goods does not create a warranty.

While the second part excludes statements considered to be 'puff' from warranties, this provision establishes that when a seller uses samples and/or claims of fact in selling the product, the product's performance must correspond to these samples and/or claims. If the product does not meet the performance claims of the manufacturer then the consumer would be able to recover his financial losses resulting from the purchase. The express warranties take precedence over the implied warranties if they conflict.

If the consumer were to purchase an automobile which accelerates quickly and is used for racing, the reasonable standards of gas milage and engine tuning appropriate for ordinary use would not apply. In a similar manner intracity electric cars would not be judged on the performance standards for 'automobiles,' but rather on the base of the factual claims of the manufacturer. The merchantability standard applies when no express warranty on the particular quality under consideration is present.

Because the express warranties have precedence over the implied warranties the manufacturer may produce a product which fails to meet the standard of merchantability in certain specified ways. All that is required of such a manufacturer is that he create accurate express warranties for these particular qualities of the product which do not meet the traditional expectations. Such behavior is fairly common: paper dresses, disposable diapers and intracity cars. Consider 'paper dresses,' this product would have to meet the standards of merchantability for dresses (e.g. hold together) except for durability. The intracity car would have to meet the standards of merchantability for cars (e.g., reliability) except for speed and range. If the manufacturer should choose to limit his responsibility for his product's performance under particular requirements of the merchantability standard he need only create different consumer expectations by means of actions leading to express warranties. However by the creation of

express warranties under UCC section 2 - 313 the manufacturer can only alter the warranty of merchantability in specific areas as he chooses by creating express warranties different from the standard of merchantability. He could not completely eliminate the standards of merchantability by merely excluding it, as such, in the contract he offers the buyer. He cannot eliminate the criteria of reasonable performance without establishing another performance expectation.

These three sections of the UCC would seem to adequately protect the consumer against misrepresentation efforts by manufacturers and retailers. By the warranty of merchantability the consumer can recover his losses if the unit he purchases is unable to provide the flow of services one would expect from the products of the particular type. The warranty of fitness for a particular purpose establishes the consumer's right to depend on the advice of a seller of a particular product (and hold him financially responsible) when the consumer depends on that advice. The provisions establishing the express warranties allows the consumer to depend on the descriptions, samples, affirmations of fact and promises used by the seller when promoting his product. The prudent consumer would seem to be virtually fully protected against the dishonest seller. This protection would apply to unsatisfactory products which are exceptions to the general run (lemons) and to those situations in which all units are

unsatisfactory due to an error in design. Decisions involving merchantability are based on the relationship between reasonable expectations of performance and the actual performance. Issues of why the performance is unsatisfactory, such as wrongdoing, are not involved. The situation is clearer with "lemons" because they are, by definition, dramatically unsatisfactory. But the source of both lemons (except in cases of random error) and design errors are decisions made by the seller (at some stage of the production process) and it is reasonable that a general commercial policy such as the UCC would not make a distinction based on the particular production decision.

One might reasonably wonder why warranties and warranty problems are so important as shown in the introduction. The reason is that the UCC contains two additional provisions which allow a manufacturer, at will, to remove virtually all of the protections given in the warranty provisions considered above. The option of removing the buyer protections considered above is established in Sections 2 - 316 and 2 - 719 of the UCC.

> Section 2 - 316 - Exclusion or Modification of Warranties
>
> (1) Words of conduct relevant to the creation of an express warranty and words or conduct tending to negate or limit warranty shall be construed wherever reasonable as consistent with each other; but subject to the provisions of this Article on parol or extrinsic evidence (section 2 - 202) negation or limitation is inoperative to the extent that such construction is unreasonable.
>
> (2) Subject to subsection (3), to exclude or modify the implied warranty of merchantability or any part of it the language must mention merchantability and in

case of a writing must be conspicuous, and to exclude or modify any implied warranty of fitness the exclusion must be a writing and conspicuous. Language to exclude all implied warranties of fitness is sufficient if it states, for example, that "There are no warranties which extend beyond the description of the face hereof."

(3) Notwithstanding subsection (2)

(a) unless the circumstances indicate otherwise, all implied warranties are excluded by expressions like 'as is,' 'with all faults' or other language which in common understanding calls the buyer's attention to the exclusion of warranties and makes plain that there is no implied warranty; and

(b) when the buyer before entering into the contract has examined the goods or the sample or model as fully as he desired or has refused to examine the goods there is no implied warranty with regard to defects which an examination ought in the circumstances to have revealed to him; and

(c) an implied warranty can also be excluded or modified by course of dealings or course of performance or usage of trade.

(4) Remedies for breach of warranty can be limited in accordance with the provisions of this Article on liquidation or limitation of damages and on contractual modification of remedy (Sections 2 - 718 and 2 - 719).

Section 2 - 719 - Contractual Modification of Limitation of Remedy

(1) Subject to the provisions of subsections (2) and (3) of this section and of the preceding section on liquidation and limitation of damages

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

(b) resort to a remedy as provided is optional unless the remedy is expressly agreed to be exclusive, in which case it is the sole remedy.

(2) Where circumstances cause an exclusive or limited remedy to fail of its essential purpose, remedy may be had as provided in this act.

(3) Consequential damages may be limited or excluded unless the limitation or exclusion is unconscionable.

> Limitation of consequential damages for injury to the person in the case of consumer goods is prima facie unconscionable but limitation of damages where the loss is commercial is not.

The key point is (1)(b) of Section 2 - 719. This allows an express warranty determined solely by the manufacturer which may be more limited than the traditional warranties established in the other sections of the UCC considered above, to be the only remedy available to the consumer. Under this section the manufacturer may remove by means of a sentence in an unread (and for most consumers unreadable) contract any buyer protection of the base of reasonable expection without creating any alternative expectation of performance except for those of the limited remedy allowed by the manufacturer's contract. All consumer expectations of product performance and manufacturer responsibility after a period of time determined by the manufacturer can be made irrelevant (except for the selling of the product) to recovering a financial loss in the eventuality of unreasonably poor product performance by the use of these limiting and exclusive express warranties. Such 'warranties' are extremely common in consumer contracts. Why the removal of traditional protection is allowed in basic commercial law, the economic effects of this removal of traditional protection and efforts to change this situation are considered in the rest of this study.

> In 1964 Consumer Reports had an article on the problems with automobile warranties which began with the following observation: "It is a good idea to call

to mind now and then the basic characteristic of a manufacturer's warranty - namely, that it functions primarily to limit the seller's liability. The seller says in his warranty that, so far as he is concerned, he agrees to accept a given degree of responsibility for the good he sells you, but for only so long. He sets the time. After that, you are on your own and come what may he will do no more about it."[7]

FOOTNOTES

[1]Theodore Levitt (Harvard Business School), Consumer Reports, March, 1972, p. 134. Quoted with no source from Advertising Age.

[2]Mary Gardiner Jones and Barry B. Boyer, "Improving the Quality of Justice in the Marketplace: The Need for Better Consumer Remedies," Trial, January-February, 1972, p. 361.

[3]These statements were selected from statements in the cases selected by the editors of the UCC to illustrate the meaning of 'merchantability.' They appear in the annotated edition of the UCC under section 2 - 314 note 9, p. 199 of the 1968 Master Edition and pp. 55-56 of the supplement for use in 1972.

[4]Jerome Frank, Law and the Modern Mind, (New York: Tudor Publishing Company, 1936).

[5]American Law Institute, Restatement of the Law of Torts, Volume 2, Negligence, (St. Paul, Minnesota: American Law Institute Publishers, 1934) p. 742.

[6]Ricketts v. Pennsylvania R. Co. 153 F. 2d 757 (2nd cir., 1946). The quotes are at 767 and 765 respectively.

[7]"The Long Warranties," Consumer Reports, April, 1964, p. 165.

CHAPTER TWO

TRADITIONAL WARRANTIES AS A CONSUMER PROTECTION POLICY

> "Accordingly, we hold that under modern marketing conditions, when a manufacturer puts a new automobile in the stream of trade and promotes its purchase by the public, an implied warranty that it is reasonably suitable for use as such accompanies it into the hands of the ultimate purchaser." Justice Francis in Henningsen v. Bloomfield Motors, Inc., 32 N.J. 358, 161 A. 2d 69 at 84 (New Jersey, 1960).

Contract Law

The warranties considered above are part of the law of contracts. To understand the existence of provisions establishing implied and express warranties, the relationship between these warranties, and the resulting social problems which have required new laws and hearings, one must understand the role of contracts in society.

> "A contract is a promise, or set of promises, for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty."[1]

The contract provides the legal assurances essential for the efficient operation of the market system.

> "The predominance of individualism in one sector of the law of contracts may be explained by the fact that this part of contract law is the counterpart, if not the product, of free enterprise capitalism. Contract, in this point of view, is the legal machinery appropriate to an economic system that relies on free

> exchange rather than tradition and custom or command for the distribution of resources."[2]

The law of contract concerning warranties is particularly central to the economic system since this law establishes what must be provided (e.g. reasonable performance) when a product is sold. It is reasonable to expect that different formulations of contract law would lead to different profitable behaviors and therefore to different economic performances.

The law of contracts is not limited to written contracts. Those behaviors such as using a sample or model which create express warranties do not require the existence of a formal written contract. The critical act which must occur for the warranty of merchantability to apply is a sale by a merchant of goods of the type. Just as the law creates a contract where no written document exists, the law may also create a contract which differs from the written contract (some examples are considered in Chapter Four).

> "Even at the risk of oversimplification, the law of contracts may be divided broadly into two sections governed by principles that are inconsistent with, if not diametrically opposed to, each other. At one pole is a body of institutions and doctrines that are influenced by volition. At the opposite pole, freedom of volition is limited, if not suspended, by an ever expanding system of judicial and legislative control."[3]

The sections of the UCC concerning warranties illustrate the operation of these contradictory principles. Sections 2 - 313, 2 - 314 and 2 - 315 create warranties on the base of the behavior of the parties. If a merchant

sells a product by means of a sample, then the courts will act as if both the implied warranties of merchantability and the express warranty of conformity to the sample exist. These warranties have been created by the law and not by any volition on the part of the parties, they might not even be aware that these warranties exist. Sections 2 - 316 and 2 - 719 allow one party to remove the warranties established by the other sections by means of an express warranty which replaces the other implied and express warranties. When presenting a warranty which meets the requirements of sections 2 - 316 and 2 - 719 the more powerful party (in commercial transactions the more powerful party may be either the buyer or sell, but in consumer transactions it would almost invariably be the seller), unilaterally sets the conditions of the transaction. In the case of consumer warranties (this ignores some recent changes in the law in some jurisdictions which are considered in Chapter Four) these unread and often unreadable contracts which greatly limit the buyers' remedies are given precedence over the traditional protections created by the law when these documents conflict. When a limited express warranty is offered in place of all other implied or express warranties there is clearly a conflict. There is also the situation in which the state imposes a contract which comes into effect when a particular act occurs (e.g., a sale by a merchant) which specifically takes

precendence over the contract agreed upon by the parties to the transaction.

> ". . . quasi contractual obligations are imposed by the law for the purpose of bringing about justice without reference to the intention of the parties . . . and sometimes in violation of his intentions."[4]

The quasi contract is critically important to meaningful consumer protection efforts and the changes considered in Chapter Four are of this form.

Competition and Contracts

The precedence of negotiated terms over traditional terms follows from some beliefs about how competition can work to create the most efficient and equiable society. Both the ideas and their age are shown in the following quotes from John Stuart Mill who wrote in 1848 that:

> "We have observed that, as a general rule, the business of life is better performed when those who have an immediate interest in it are left to take their own course, uncontrolled either by mandate of the law or by the meddling of any public functionary. The persons, or some of the persons, who do the work, are likely to be better judges than the government, of the means of attaining the particular ends at which they aim."[5]

> "Instead of looking upon competition as the baneful and antisocial principle it is held to be by the generality of Socialists, I conceive that, even in the present state of society and industry, every restriction of it is an evil, and every extension of it, even if for the time injuriously affecting some class of laborers, is always an ultimate good."[6]

The behavioral implication of this position is that better results will occur if those not involved in the transaction, particularly the government, do not interfere with the actions of the parties and that competition will resolve

any problems. The mechanism by which competition brings the ideal results in contracts (and their coordinated economic relations) is simple, in theory. If a producer offers his product with a poor warranty (e.g., excludes in an express warranty the traditional implied warranties) consumers will presumably refuse to accept his offer if another manufacturer offers an identical product with a better warranty. In this manner the concerns of the consumer and the possibilities of production will be combined to yield a contract which by negotiation contains the joint wisdom of the parties.

The problem with this position lies in the fact that there is no necessary connection between freedom of contract and competition. This is shown in the Sherman Antitrust Act which makes the agreeing to a contract which restricts competition a misdemeanor.

> "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is declared to be illegal. . . ." Sherman Antitrust Act (U.S.C. Title 15, paragraph 1.)

This act was passed on July 2, 1890. On August 17, 1937 this paragraph was amended to allow 'fair trade' (a contract between the manufacturer and sellers setting a minimum retail price) and on July 7, 1955 changing the penalty for the misdemeanor from $5,000 and/or one year imprisonment to $50,000 and/or one year imprisonment. The Sherman Antitrust Act tried to restore competition by eliminating trusts. The goal, however, was neither the

restoration of competition nor any specific performance, but rather the restoration of the theoretical results of competition. The theoretical results of competition follow from meaningful negotiation in the market and are 'fair' prices and terms. While the general policy, as indicated by the sections of the UCC considered in this study, is one of allowing the parties considerable freedom in the terms of the contract which is to control their particular transaction, restrictions on the freedom of contract are not rare. Section 2 - 719, part 3, of the UCC is such a limitation in that it makes the limitation of consequential damages for injury to the person prima facie unconscionable and thus unenforceable. The terms and often the rates in contracts between consumers and common carriers and insurance companies are not generally subject to negotiation; nor can a man contract himself into slavery.

Approximately eighty years after the enactment of the Sherman Act, the California Legislature passed the Song-Beverly Consumer Warranty Act (considered in Chapter Four) which in part stated,

> "Nothing in this chapter shall effect the right of the manufacturer, distributor, or retailer to make express warranties with respect to consumer goods. However, a manufacturer, distributor, or retailer making express warranties may not limit, modify or disclaim the implied warranties guaranteed by this chapter to the sale of consumer goods."

This provision applies to those express warranties allowable under Section 2 - 316 and 2 - 719 which remove the traditional implied and express warranties. Clearly this

is a limitation on the freedom of contract of the parties to consumer transactions. This corrective legislation resulted from various abuses of freedom of contract between manufacturers and sellers of consumer goods and their customers which led to a situation in which meaningful negotiation was absent and the joint wisdom of the parties did not emerge. The reason for this loss, a relatively recent and probably inevitable effect of mass production and distribution of goods, provides an important key to understanding modern consumer problems.

Negotiation of Contracts

The idea of negotiating a contract involves two parties discussing the terms of the transaction. Mass production assumes a mass market in which the same product is being sold to many different individuals. The negotiation of contractual terms for each of these sales would be extremely expensive as well as confusing since different consumers might have different warranties. The practical alternatives facing a manufacturer of millions of units were: 1) not to use any written contract and thus use the traditional law to distribute the risks between the parties or 2) write a contract which is offered without any negotiation, on a 'take it or leave it' basis, to all consumers as part of the transaction which assigns a particular distribution of the risks. In either case no negotiations between the firm and its millions of customers

occurs. The complexity of contract law is largely due to its function of determining the allocation of risks between the parties. If the manufacturer had chosen not to use a special contract (option 1) then the general law would have have applied.

> "If we view the law of contract as directed to strengthening the security of transactions by enabling men to rely more fully on promises, we see only one phase of its actual workings. The other phase is the determination of the rights of the contracting parties as to the contingencies that they have not foreseen, and for which they have not provided. In this latter respect the law of contracts is a way of enforcing some kind of distributive justice within the legal system. And technical doctrines of contract may thus be viewed as a set of rules that will systematize decisions in this field and thus give lawyers and their clients some guidance in the problem of anticipating future decisions. Thus, for instance, if the question arises as to who should suffer a loss caused by the destruction of goods in transit, the technical doctrine of when title passes enables us to deal with the problem more definitely. In any case, the essential problem of the law of contract is the problem of distribution of risks."[7]

The presence of written contracts (either signed by the consumer as in the case of automobiles or enclosed with the product as in the case of small appliances) indicates that manufacturers have chosen to write the contract which will distribute the risks of performance between themselves and their customers.

These contracts generally serve to limit the rights of the consumer. The negotiation and joint wisdom which justifies the state's enforcement of private contracts may be missing due to grossly unequal bargaining position.

> "The weaker party, in need of the goods or services, is frequently not in a position to shop around for better terms, either because the author of the standard

> contract has a monopoly (natural or artificial) or because all competitors use the same clauses. His contractual intention is but a subjection more or less voluntary to terms dictated by the stronger party, terms whose consequences are often understood only in a vague way if at all. Thus, standardized contracts are frequently contracts of adhesion."[8]

The consumer, in any individual transaction, is clearly the weaker party. He cannot afford to have a contract drawn for each of his purchases, but the seller may have a general (blanks for color, price and other negotiated items) specialized contract drawn which works to his advantage since the cost can be spread over the hundreds, thousands or millions of identical sales. The general law assuring the consumer of reasonable performance would apply (UCC warranties of merchantability and fitness for a purpose) if the seller's contract were not used. The use of these contracts can be considered an effort by manufacturers and sellers to relieve themselves from the responsibility of providing a consumer with a product which performs in a reasonable manner.

In essence the use of these contracts serves to separate the expectation of reasonable performance which is essential to making the sale (if the consumer does not expect the product to perform he is unlikely to make the purchase) and responsibility for the actual performance (beyond the limited express warranty.) Consider the warranty of one of the most reputable of firms, the International Business Machines Corporation (office products division).

> Warranty; Remedy
> The Warranty period for the equipment will be 90 days (one year for electric motors) commencing either upon the first installation of the equipment or nine months after its delivery, whichever first occurs. . .
>
> Standard Warranty/Remedy
> IBM warrants the equipment to be free from defects in material and workmanship upon delivery. In the event of IBM's breach of any warranty, Purchaser's exclusive remedy shall be that IBM will repair or replace broken or defective parts and make necessary equipment adjustments during the warranty period without charge.
>
> . . . . .
>
> NO OTHER WARRANTIES, EXPRESS OR IMPLIED, INCLUDING THE WARRANTY OF MERCHANTABILITY, SHALL APPLY TO THE EQUIPMENT (set in upper case in the contract)

IBM has a reputation (consumer expectation) for quality for which it refuses to assume legal responsibility. The nature of the contract insofar as achieving (or failing to achieve) the joint wisdom of the parties is shown by the conditions concerning breach by the customer.

1. The entire debt shall immediately become due and payable;
2. IBM, in addition to other remedy, may repossess the equipment without notice; and
3. The buyer agrees to pay IBM's costs and expenses of collection and/or repossession, including the maximum attorney's fee permitted by law, said fee not to exceed 25% of the amount due hereunder.

One might accept that this contract does separate expectations from performance, but suppose that competition between suppliers of office equipment will eliminate the problem. The question becomes if, in the real world, competition is operating to eliminate these highly restrictive contracts. The holding of Congressional Hearings, speeches by the President and changes in state laws all

strongly indicate that a problem exists which is not self-correcting. The stability of the problem was illustrated by testimony in the Congressional Hearings. Senator Moss felt that the lack of competition followed from a basic inability of consumers to understand the document.

> "Through extensive hearings the committee has learned that a warranty is a complicated legal document whose full essence often lies buried in century-old legal decisions or complicated State codes or commercial law so that consumer understanding of what a warranty on a particular product means may not always coincide with its legal meaning."[9]

Virginia H. Knauer, Special Assistant to the President for Consumer Affairs, noted that manufacturers exploit this inability of consumers to understand warranty contracts.

> "Recognizing the average consumer's helplessness where legal documents such as warranties are involved, suppliers have practically institutionalized warranties which take away more than they give. And the marketplace has further aggravated the problem by failing, with some exceptions, to provide meaningful competition as to warranty terms."[10]

Fairfax Leary, of the Public Interest Research Group of Virginia, testified that even if consumers did understand the warranties, without legislation the situation would not change.

> "Much consumer legislation in the Congress and at the State level seems founded on the concept of disclosure, usually in the documentation of a sale or credit transaction. One can, justifiably, doubt that many consumers read the printed matter on the paper they sign. It really couldn't do them any good if they did, since no one at the point of sale has or can get any authority to change the company's standard form. The choice is take it or leave it. Nor is comparison shopping apt to do much good. The form may well have been supplied by the trade association for all its members, directly; or indirectly, through a firm selling legal forms."[11]

Again, the IBM contract is instructive as to the position of the consumer

> "IBM shall not be liable for incidental or consequential damages. This agreement constitutes the entire contract between the Buyer and IBM with respect to the equipment, including any parts or equipment furnished as a replacement, and no representation or statement nor expressed herein shall be binding on IBM. The foregoing terms and conditions shall prevail notwithstanding any variance with the terms and conditions of any order submitted by the Buyer with respect to the equipment."

William F. Willier of the National Consumer Law Center, Boston College Law School summed up the situation.

> "The use of warranty disclaimer clauses has become so universal that manufacturers and sellers of consumer goods have effectively repealed the law of merchantability."[12]

Consumers accept these contracts which separate expectation from performance because of consumer ignorance and because of the unequal bargaining strength of the parties. Solving the problem by educating the consumer is unlikely to be effective even if the level of education required were achieved since even lawyers purchase IBM office equipment, if they want to benefit from IBM's patents, on the same contractual terms as the layman.[13] Consumer education while not directly solving the problem, might lead to consumer pressures which would lead to political action restricting the discretionary power of manufacturers and sellers in the terms of the contracts they offer consumers. Solving the problem through equalizing the strength of the parties would require the restoration of much smaller scale industries in which the

buyer and the seller have approximately equal strength. Clearly such a remedial approach is not a reasonable alternative. The corrective actions which have been taken (considered in Chapter Four) have not sought to achieve the joint wisdom of the parties by means of negotiation between the parties. Such negotiation would require both a massive consumer education effort and atomization of firms. Rather through court decisions and/or legislative action the "joint wisdom" of the parties is imposed on the individual parties by governmental decision.

Contract Adjustments

The imposition of "joint wisdom" is not new when meaningful negotiation has become impractical due to corporate size and the requirements of efficient mass marketing.

> "In recent years (1920-21) the tide has set strongly in the other direction. Observation of results has proved that unlimited freedom of contract, like unlimited freedom in other directions, does not necessarily lead to public or individual welfare and that the only ultimate test of proper limitations is that provided by experience. . . . In the law of carriers, the Interstate Commerce Acts of the United States and similar state legislation in regard to intrastate business, have almost destroyed freedom of contract between shipper or passenger and carrier. The rates which the carrier may charge and the facilities which it may furnish are determined by law, not only irrespective of the will of the parties but in spite of contrary expressed intention. The contract of insurance has been similarly defined by legislation. Standard policies of fire insurance have been fixed by statute, and policies must be written according to the terms thus fixed. Other contracts of insurance are often closely regulated so that the bargain opened to parties is whether they will insure or not, with whom they will insure, and for how much; but when these

> fundamental matters are agreed upon, little more scope is left for bargaining."[14]

While the contracts presented consumers allow the profitable separation of performance from expectation of performance the need for corrective action can only be shown by observation of poor results coming from the use of these contracts.

It is quite possible that manufacturers, although offering very poor contracts, in effect adequately guarantee the performance of their products by providing after the sale service for reasonable consumer claims. This behavior would be reasonable in that if it were well known consumers would be more confident (have high performance expectations) in products produced by that company. Such cooperative behavior by manufacturers would eliminate much consumer dissatisfaction. That consumer dissatisfaction is a fact of the current scene strongly indicates that manufacturers not only offer these contracts but also use them. The automobile is both a virtual necessity and an expensive product. Its central role in American society combined with an inclination towards lively warranty and expectation of performance promotion activities has led to Congressional and Federal Trade Commission (FTC) inquiries into the warranty practices of the industry.

Automobile Experience

From November, 1931, until 1960 the automobile industry warranted its product for 90 days or 4,000 miles.

On September 28, 1960, Ford changed to a one year or 12,000 mile warranty and was followed in one day by American Motors and three days later by General Motors and Chrysler.[15] In the fall of 1962, Chrysler under a new president, Lynn Townsend, shifted its advertising account, doubled the amount spent on advertising between 1963 and 1966, made some styling changes, introduced its new models before its competitors and offered a five year or 50,000 mile warranty on the power train. This combination of efforts was quite successful as sales rose by 31% (General Motors sales increased by 7% and Ford by 3%).[16]

The quantification of the effects of the warranty in terms of sales, either total or market share, is probably not possible. The movements in sales represent the combined effect of not only the warranty offered, but also promotional efforts, styling, dealer aggressiveness, demand for recent models in the used market and other factors. The best indication of the expected effect of Chrysler's five-year warranty is the behavior of the professionals in the industry. General Motors, Ford, and American Motors not only quickly matched Chrysler, but offered a slightly better warranty to compensate for the first exposure gained by Chrysler. The speed with which the warranty was copied demonstrates the expected effectiveness, but also makes impossible any statistical proof since Chrysler only had the monopoly on the warranty for a short period.[17] The effect of the five-year

Table 1. U. S. Car Production (Calendar Year)

Year	General Motors number	%	Ford number	%	Chrysler number	%	Total
1956	3,062,413	53	1,669,166	29	870,261	15	5,801,864
1957	2,816,444	46	1,889,703	31	1,222,338	20	6,115,458
1958	2,169,178	51	1,219,422	29	581,244	14	4,244,045
1959	2,555,230	46	1,745,409	31	737,799	13	5,593,707
1960	3,193,161	48	1,892,005	28	1,019,295	15	6,696,108
1961	2,726,562	49	1,689,936	31	648,670	12	5,516,317
1962	3,741,527	54	1,935,208	28	716,809	10	6,935,182
1963	4,077,300	53	1,963,868	26	1,047,722	14	7,637,173
1964	3,956,590	51	2,145,942	28	1,242,162	16	7,739,034
1965	4,949,408	53	2,565,776	27	1,467,553	16	9,329,104
1966	4,448,634	52	2,425,442	28	1,445,616	17	8,598,917
1967	4,117,810	56	1,696,224	23	1,363,696	18	7,406,788
1968	4,592,077	52	2,396,924	27	1,585,591	18	8,843,031
1969	4,421,002	54	2,163,109	26	1,392,454	17	8,219,463
1970	2,979,187	46	2,017,152	31	1,273,459	19	6,545,908
1971	4,852,949	57	2,176,335	25	1,313,306	15	8,578,259

Source: Ward's 1972 Automotive Yearbook, 34th Edition, (Detroit, Michigan: Ward's Communications, Inc., 1972), p. 94.

warranty does not appear so much between the firms, although Chrysler does seem to have a higher market share after the warranties, but in the total sales of the industry. That the effect of the warranty should appear in total sales (automobiles relative to all other goods) rather than in the sales of the individual firms is reasonable since there was little difference between the warranties offered by the various firms, but all of the warranties would lead to higher consumer expectations for automobiles (compared to all other goods). These data are clearly inconclusive. Understanding and predicting automobile (and other products) sales is more of an art than a science. With all of the modern techniques and a virtually unlimited budget the group which analyzed the market situation for the Edsel made a decision which lost Ford a quarter of a billion dollars.

Initially the warranties represented a bargain (increased customer confidence in the industry at a small cost) to the manufacturers. The warranty service costs for the 1965 models averaged between a low of $41 for Chrysler (1.6% of its average car price) to $47 for Ford (2.1% of its average car price.) But the FTC noted in its staff report, "However, as the new extended warranties take hold, as customers learn better their rights under the warranties, as costs of repairs rise, the fulfillment of the terms of the warranty can and is likely to become an expensive responsibility for the automobile manufacturers."[18] The

FTC prediction proved to be correct as the cost more than doubled a couple of years later and the firms reduced the extent of their warranties.

Business Week in an article entitled, "Detroit Tries a U-Turn on Warranties" summed up the experiences of the firms after the FTC study.

> "When Chrysler offered its original five-year, 50,000 mile warranty [on the drive train - MS] (1963 cars), the company was the acknowledged leader in engine and drive component engineering, and increased warranty costs could be written off against the marketing advantage that grew out of the warranty. As a hidden cost-saver, Chrysler retained its 12-month, 12,000-mile warranty (introduced by Ford in 1960 replacing the 90-day, 4,000-mile warranty) on the rest of the car, while Ford, GM and American Motors escalated to a 24-month, 24,000-mile guarantee. Then when all four manufacturers went to the same basic, extended warranty in 1967 - five-years, 50,000-miles on the drive train, and 24-months, 24,000 miles on the rest of the car - no manufacturer had an advantage, and, what is more costs soared. For Ford, the outlay to dealers for warranties between 1966 and 1967 doubled to $120 a car for a total hike of $130 million (similar for other manufacturers) . . . in 1969 alone Ford paid its U.S. dealers $300 million in warranty costs. That sum was double Ford's advertising budget for the year and nearly matched the $325 million that the company spent in retooling for its 1969 line . . . To hold costs down, auto companies began pulling back on their warranties only a year after they all went to the same extended coverage. On the 1968 models they introduced restrictions on warranty transfers . . . On the 1969 models they went further and cut the basic coverage . . . ."[19]

There are two noteworthy elements in this experience. It seems clear that the manufacturers were not aware of the costs consumers had been paying, and continue to pay, to maintain the drive train and other mechanical parts even when they follow the manufacturers' maintenance program (which was required for these warranties to be in effect).

One might reasonably conclude that the manufacturers had not been very interested with the maintenance costs of their customers. Another interesting element is the manufacturers' solution to the maintenance problem. Rather than raising their price and improving their product so that it could meet their warranty claims (and a consumer's reasonable expectation of performance) and/or improving the owner's maintenance program to eliminate product failures, they chose to shift the risks of operation to the consumer by limiting their own financial, if not actual, responsibility for the performance of the product they design, manufacture and assemble.

The FTC found considerable evidence that the automobile manufacturers were marginally, if at all, interested in their products after their sale.

> "Despite all disclaimers, sales are still foremost (they provide the manufacturer's revenue) and service retains the status of a "necessary evil" in much of the automobile business. Some evidence of this is: (a) in one manufacturer's reorganization, service representatives, who had previously separate but equal status with sales personnel, were placed under the regional sales manager; (b) in the training center of another manufacturer prime consideration is given to the training of sales rather than service personnel based on courses given, numbers attending, etc.; (c) in the manufacturers' regional organizations sales personnel outnumber and outrank service personnel. The number of service representatives appears inadequate to handle the number of dealers assigned to them, and these representatives are also assigned nonservice duties to perform; (d) the accountability of dealers to manufacturers for sales is much more strictly enforced than their accountability for service, as shown by checks on dealers and franchise cancellations; (e) one manufacturer's system of company-financed dealers apparently undercut regular dealers' prices on sales, as a means of forcing new car sales in

> an area, with unfavorable consequences for service; and (f) the cancelling of franchises of dealers who have low new car sales volumes, but who perform a larger percentage of service work in their operations."[20]

These contracts, while extending the express warranty of the manufacturers, offered the limited express warranty in place of the traditional implied warranties and any other express warranty. The emphasis on sales and the subsequent solution of returning the risks of design, manufacture and assembly to the consumer demonstrate the nature of these contracts. They not only served to separate expectations from performance, but also to increase the consumers' expectations. Miles W. Kirkpatrick, chairman of the FTC, testifying before the House of Representatives' Hearing summed up the automobile warranty experience.

> "After full consideration of the voluminous record compiled during this investigation, the Commission concluded that the much heralded and heavily promoted warranty programs of American automobile manufacturers during the sixties were, in fact, extremely limited and had failed to provide the purchases with the quality and service he rightfully expected."[21]

If the word 'rightfully' is changed to 'reasonably' the role of the traditional warranties becomes clear. The contracts offered to consumers remove the consumer's right to recover damages if he is sold a defective product. Justice Francis, in a very important case, Henningson v. Bloomfield Motors, Inc., in 1960 noted the nature of contracts based on either section 2 - 719 or on the common law which this section made into statute.

> "Moreover, the language of this warranty is that of the uniform warranty of the Automobile Manufacturers Association, of which Chrysler is a member. . . . The terms of the warranty are a sad commentary upon the automobile manufacturers' marketing practices. Warranties developed in the law in the interest of and to protect the ordinary consumer who cannot be expected to have the knowledge or capacity or even the opportunity to make adequate inspection of mechanical instrumentalities, like automobiles, and to decide for himself whether they are reasonably fit for the designed purpose . . . . But the ingenuity of the Automobile Manufacturers Association, by means of its standardized form, has metamorphosed the warranty into a device to limit the maker's liability."[22]

The corrective policy which the automobile experience indicates should occur was stated by Karl Llewellyn, the principle author of the UCC, many years ago on a different problem.

> "But what [experience in contract law administration] does not fit [the common-law judge] for is to see that there is such a distinction; to see that free contract presupposes free bargain, and that free bargain presupposes free bargaining; and that where bargaining is absent in fact, the conditions and clauses to be read into a bargain are not those which happen to be printed on the unread paper, but are those a sane man might reasonably expect to find on that paper."[23]

Faced with the fact that currently freedom of contract operates without the presuppositions required for the policy, the contract should not be read as it is printed, but rather reasonable terms must be imposed on the parties. By not permitting the exclusion of the traditional warranties, with their base of reasonable coordination between manufacturer created expectations in the consumer and the product's performance, with a limited express warranty, the consumer will be able to defend himself

against misrepresented durable products. Those manufacturers who do not use express warranties to limit their responsibility will not be effected by the change. As is shown in Chapter Four this change can be achieved in at least three different manners.

The objectionable nature of these contracts can be shown by a rather simple a priori argument. If the manufacturer can sell a product without actively and purposefully creating consumer expectations he has no intention of meeting, he has no need to restrict the consumer to the limited remedy of repair or replacement. If the manufacturer uses these contracts to relieve himself of responsibility for consumer expectations he created about the product which he knows will not (in a significant number of cases) be met, but which must be made in order to sell the product, society hardly needs the product. It is hard to imagine a product which consumers need which could be sold profitably only by means of deception. If the public does not need products which can only be sold by deceptive means (with the resulting disappointment of the buyer) then either the manufacturer does not need the contract or society does not need his product. In either case, the contracts are indefensible. It is hard to imagine how a law which encourages deceptive behavior and which is supposedly controlled by meaningful negotiation which does not occur would lead to beneficial results. Removing the discretion of the seller to remove the

traditional buyer protections is not a limitation of freedom of contract; freedom of contract does not exist in the absence of meaningful negotiation and free bargaining.

Policy Implications of Requiring Effective Warranties

Requiring absolute liability (not concerned with negligence) as a policy has its own set of presuppositions which must be met for this policy to be reasonable.

> "The reason for imposing such alliability [irrespective of the positive contract of the parties . . . holding] that there is a warranty of quality in case of sale or contract to sell specific goods, where there is no promise or affirmation in regard to them upon the seller is that the circumstances of the bargain justify the buyer in inferring that the seller by the very act of offering his goods for sale asserts or represents that they are merchantable articles of their kind or are fit for some special purpose, and that the buyer relies upon this implied assertion or representation. Such an implication and justifiable reliance thereon does not exist in every case. The circumstances which must be considered in deciding the question may thus be summarized: (1) Was the seller a manufacturer of the goods, and thus familiar with their construction? (2) Or, if not a manufacturer, was he a dealer in goods of that kind and so a competent judge of their quality? (3) Did the buyer inspect or have an opportunity to inspect the goods, and was the defect latent so that it could not be discovered by such inspection? (4) Apart from opportunity to inspect, were there circumstances showing that the buyer selected the goods relying on his own judgment or showing an intention to take the risk of their quality?"[24]

These conditions seem to be met in consumer purchases of mass produced products.

There remain two points which require consideration at this point. One might suspect that imposing the traditional warranties would place a difficult additional burden on the producers. Above it has been shown that the manufacturers need only meet the reasonable expectations of

consumers which the producer may change by clear statements of likely product performance. But besides the ability to limit their responsibility by creating special expectations the firms have often been operating under the traditional protections when supplying commercial and governmental accounts. The Assistant Attorney General in charge of the Antitrust Division of the Justice Department, Robert W. McLaren stated in his testimony before the Senate Hearings on warranties that:

> "If a contract is negotiated, warranty terms are likely to be the subject of negotiation. If as probably happens more frequently (in a commercial transaction), a transaction is arranged by an exchange of conflicting purchase orders and acknowledgement forms, these forms have been carefully drawn by skilled lawyers so that each is likely to negate the terms of the other. The ultimate result is that the parties to the transaction are left with the same rights and obligations under the Uniform Commercial Code which they would have had if both parties had remained completely silent."[25]

The IBM contract provides that:

> "The foregoing terms and conditions shall prevail notwithstanding any variance with the terms and conditions of any order submitted by the buyer with respect to the equipment."

A sophisticated large scale buyer would have a similar clause in his contract with the net result being that both contracts serve to cancel each other out and any disputes are settled by the general commercial law. Clearly the restrictive contracts are not necessary for commerce and seem to be largely reserved for the individual consumer. If commerce can continue when industry purchases the same items as consumers (e.g., automobiles) under the traditional

rules (the special contractual terms on the purchase order and the sales contract cancel each other out), then one might reasonably expect that commerce would continue if consumers also purchased products under the traditional rules.

Absolute Liability As A Policy - Workmen's Compensation

Policies are important only if they change behavior. Basically this study proposes a policy which removes a contractual approach that allows the seller to shift financial responsibility for his decisions to the buyer under the guise of freedom of contract. This policy would impose an unavoidable liability for performance on the manufacturer. The oldest governmental social reform program in the United States, workmen's compensation, is remarkably similar and gives an indication of how this consumer protection program might function. The principle of workmen's compensation (liability of employers without fault) was first adopted on the Prussian railroads in 1838 and a general compensation bill was passed in Germany in 1884. Britain followed in 1897 and the Federal Government provided compensation to its employees in 1908. Montana passed the first state law in 1909 and between 1910 and 1915 thirty states passed this legislation. By 1920 all but six Southern states had this legislation and in 1948 with passage by Mississippi all the states provided some system of workmen's compensation.[26]

The legal situation which necessitated workmen's compensation was that an employer could escape responsibility for accidents of his employees if he could establish one of three common law defenses: 1) contributory negligence, 2) fellow servant doctrine and/or 3) assumption of risk. If the manufacturer could show that the worker was in some way at least partially responsible for his accident (e.g., careless) or that the accident was caused by another worker or if the accident was normal for the industry (e.g., an occupational disease) then the worker could and would be denied any recovery of his loss. If accidents are viewed as the result of specific persons' behavior, then this system is reasonable.

> "The nineteenth-century legal system of employers' liability dervied from the common law of negligence or tort liability. Implicit was the basic assumption that occupational injuries were always the result of someone's fault and that he should bear the costs."[27]

But if accidents are not viewed individually, but rather in total, it becomes clear that the contributory negligence of the worker, the negligence of a fellow worker and the risks of an industry are related to the decisions of the manufacturer.

> "The prevention of occupational accidents and disease is primarily an engineering problem and as such is reducible to terms of pecuniary cost. Industrial safety depends much more upon the construction of plant and equipment, the choice of materals and processes and the safeguarding of machinery than upon the discipline and training of employees."[28]

Table 2. Industrial Fatalities

Year	Coal Mines deaths per million tons[a]	Iron and Steel deaths per million hour exposure[b]	Railroads deaths per ten million train miles[c]
1907	6.78	.7	
1908	5.97		
1909	5.73		
1910	5.62	.5	
1911	5.35	.3	
1912	4.53	.4	
1913	4.89	.4	18.4
1914	4.78	.3	16.5
1915	4.27	.2	10.6
1916	3.77	.3	11.6
1917	4.14	.4	14.5
1918	3.80	.4	17.0
1919	4.18	.4	11.7
1920	3.45	.2	12.7
1921	3.92	.2	7.8
1922	4.15	.2	8.5
1923	3.74	.2	9.0
1924	4.17	.3	6.7
1925	3.85	.2	6.8

Source: U.S. Department of Labor, Bureau of Labor Statistics, Accidents and Accident Rates, Bulletin 490, August, 1929.

[a] p. 159

[b] p. 127

[c] p. 172

These data, the oldest available, indicate a downward movement in fatalities due to industrial accidents. Unfortunately in terms of establishing the effectiveness of workmen's compensation legislation these data are completely inadequate. It is not possible to determine from these data if the downward trend observed was in effect before the enactment of the legislation or if it began as the legislation began to take effect. One may speculate that

the reason the data are not available is that the collection of data is expensive and no one was interested until the data were essential for setting insurance rates. The availability of the data is a function of the concern which led to the enactment of workmen's compensation legislation. Faced with a lack of data the researcher must use the opinions of experts. Before workmen's compensation legislation the National Safety Council (itself formed in the early years of workmen's compensation legislation enactment - 1912) explains the general apathy towards industrial safety as due to: 1) common law defenses which eliminated the manufacturers' responsibility for most industrial accidents, 2) ignorance of the economic losses caused by accidents and 3) the idea that accidents were unavoidable, that they were a price which must be paid for industrial progress.[29]

In terms of evidence the absence of the general accident statistics for the period during which the legislation was being enacted is probably not too critical as interpretation would have been very difficult, if not impossible. Reporting of accidents is doubtlessly a function of damage recovery possibilities, otherwise where would the accident be reported and why bother? There is no necessary and unchanging relationship between the number of accidents which occur (the condition with which a policy advocate is concerned) and the number of accidents reported (the data for program evaluation). Thus workmen's

compensation legislation could have effectively reduced the number of industrial accidents if the number of reported accidents increased, remained unchanged or decreased. The removal of workmen's compensation would probably lead to a decrease in the number of reported accidents. Also workmen's compensation only directly effects the first of the three reasons given for the manufacturers' apathy; a drop in the number of accidents could occur with a change in either of the other two beliefs of manufacturers. The connection between these is shown by the fact that workmen's compensation legislation would not have produced any behavioral changes in manufacturers to reduce the number of accidents unless manufacturers came to believe that accidents were avoidable and not a necessary price of industrial progress. Social policies are inevitably complex and not readily, if at all, subject to indisputable statistical analysis. The researcher when faced with a situation in which no statistical situation would discredit a hypothesis (e.g., industrial accidents up, down or unchanged and the effectiveness of workmen's compensation legislation) and a choice of several alternative causes must use different evidence. He must consider what would be rational behavior for manufacturers under the new rules and the judgment of those who have studied the situation.

With the removal of their effective common law defenses the manufacturers would be financially responsible,

at least to a limited extent, for accidents in their plants. Cost functions for a particular production technique would include in addition to factor costs (e.g., materials and labor) a cost of accidents. To maximize profits the manufacturer would have to minimize not only his factor costs but also his liability for accidents. It is unlikely that faced with injury claims a manufacturer could continue to be unaware of the costs of industrial accidents and maintain the belief that nothing under his control could be changed which would reduce the likelihood of claims. The profit maximizing manufacturer would want something done about these costs. The National Safety Council was formed as these costs began to occur. The workmen's compensation legislation destroyed the three conditions which allowed the manufacturer to remain apathetic to issues of industrial safety.

> "Discovery of the safer way in fact demands close analysis of the particular processes involved in relation to the circumstances, product and organization of the particular plant. The requisite trouble and expense will not be incurred unless strong inducements are brought to bear upon the keeper of the purse."[30]

Workmen's compensation is credited with achieving much of the gain in industrial safety.

Richard T. Ely, noted in a rather charitable manner,

> "Indirectly [workmen's compensation] promotes industrial safety by adding pecuniary incentives to the humanitarian interests of employers."[31]

E. H. Downey, writing less than ten years after the enactment of workmen's compensation legislation by the majority of the states noted,

> "Compensation laws have everywhere given a notable impetus to the safety movement, notwithstanding that the benefits are pitiably small."[32]

He further notes that the National Safety Council was organized AFTER compensation laws had been enacted in twenty states and that its growth corresponded with the growth of the compensation movement.[33] A later researcher in industrial accidents credited workmen's compensation legislation as being the principle force for the improvement in the performance of the manufacturers.

> "By making work injuries immediately and inescapably expensive to employers, workmen's compensation laws [first passed in Switzerland in 1881, but developed by Bismark in Germany and passed in 1855 to reduce the power of a rising socialist party - these laws remove questions of fault - contributory negligence, fellow servant negligence and the assumption of risk defenses could no longer be effectively used MS] have done more to promote [management's] interest in safety than all other influences put together. As the worker's knowledge of his rights under these laws spread, claims increased rapidly in number and the cost to employers grew to such substantial figures, particularly in large, high injury plants, that many of them initiated extensive programs of hazard elimination. They usually were very expensive because of the heavy costs of guarding the machinery, particularly the power transmission machinery [belts and shafts leading from a central steam engine MS], but it soon became clear that the saving of a few deaths or serious permanent disabilities would pay for a lot of guards. A few socially minded employers had begun the correction of obviously serious hazards long before the passage of workmen's compensation legislation, but the great majority had done little or nothing."[34]

The Relationship Between Workmen's Compensation and Consumer Protection

The workmen's compensation experience demonstrates that a manufacturer's performance can be improved dramatically if the manufacturer is made responsible for the losses caused by his poor performance. Since product performance, like industrial safety, is basically a problem in engineering one may reason by analogy on the basis of the experience with workmen's compensation. It seems likely that holding manufacturers responsible for the performance of their products (providing the consumer with means to recover his loss) will lead the manufacturers to exercise greater care to insure that their products will function properly. Before proceeding with an analysis of the implications of a policy of not allowing sellers to eliminate the traditional implied and express warranties by means of an unread and unnegotiated clause in a standard contract, it is worthwhile to consider the beliefs and conditions which prevented progress in industrial safety in light of consumer products. The practical freedom from responsibility of the manufacturer for industrial accidents by means of common law defenses has been achieved in the case of consumer products by means of express warranties. The experience of the automobile manufacturers, sophisticated firms by any criteria, shows that they were not aware of the consumers' costs of their production decisions. Much like industrial accidents were formerly, so is sloppy

workmanship currently viewed as a necessary cost of mass production. Just as imposing an absolute liability for accidents on manufacturers brought increased concern for industrial safety, so will holding manufacturers unavoidably responsible for the performance of their product (because they cannot reduce their limited express warranties as did the automobile manufacturers when faced with the costs of their decisions) bring greater concern in product performance.

Evaluation of Consumer Protection Policies

The policy of changing the basic contract law to preclude exclusion of the traditional implied and express warranties seeks to reduce consumer disappointments due to the difference between consumer expectations of performance and the actual performance. In the light of the difficulties involved in interpreting the automotive sales and the industrial accident data above, one might consider the statistical requirements for evaluating this policy. Two questions are of particular importance: 1) what is the magnitude of the problem? and 2) is the policy, where it has been put into effect, reducing the problem? The fundamental difficulty encountered when seeking to answer these questions lies in the fact that the problem occurs as frustration at the disparity between expected and actual performance. The frustration resulting from this disparity is a mental state. Research techniques do not currently permit a direct quantitative measure of frustration. To be

sure the problem is not new to economics. Demand theory is built on the opposite mental state, satisfaction, which also cannot be directly measured. What must be found is something which is measurable, behavior and/or events, which reflects the mental state.

In terms of frustration there are forms of behavior and events which reflect this mental state: suicide, alcohol and drug consumption, crimes of violence, ulcers and others. Unfortunately the number of these events is not directly related to consumer frustration with products since product failures are not the only source of frustration in a modern society. If this connection could be made, in a manner which would satisfy a large percentage of students of the problem (as industrial accidents serve as a measurable proxy for the unmeasurable level of industrial safety), it would probably be the most satisfactory measure of both the size of the problem and the effectiveness of the solution. Until the development of a system which allows the separation of the effects of the various sources of frustration this approach will remain unusable.

In the case of utility or satisfaction the ordinal measure is made on the basis of the purchases consumers actually make. It might be possible to analyze consumer frustrations of the form relevant to this policy by the purchases consumers do not make. Unfortunately in terms of the analysis, purchases of durables are made only on the

basis of performance expectations while this policy seeks to reduce a disparity between actual and expected performance. Because the products are durable, few subsequent purchases would be based on the performance of the previously owned product. Sales of furniture and major appliances do not lend themselves to analysis of consumer satisfaction or frustration because the same consumers do not purchase the same product frequently. Sales to different consumers are based on expectations rather than actual performance.

While direct analysis from sales is not possible, one might argue that an index of brand loyalty would give an indication of consumer satisfaction. These data would be far from conclusive. A purchase of a durable depends on the expectations of performance not only of the selected brand, but also of all the others available. The appearance of a high level of brand loyalty could result from either good experience with the currently owned units and/or an effective promotional effort. A low brand loyalty situation could follow from poor previous experience and/or a relatively ineffective promotional effort. It is very difficult to imagine how one would interpret an index of brand loyalty. While reputation based on use rather than promotional effort is a factor in sales, it is not the only factor (e.g., retail locations, special sales, and advertising among others). The relative importance of the factors would vary according to the

success of the other factors. Immediately following the introduction of a new model with considerable advertising, expectations of performance may be so great as to overcome previous poor experience with previously owned models. But as time passed and the excitement wears off past experience would probably gain in relative importance. While hardly conclusive the constant and expensive creation of excitement, as in the automobile industry, might lead one to suspect a poor product performance.

The research problem with sales lies in the number of factors, and therefore alternative explanations available to account for any movement. The sales of an individual brand depend not only on its past performance and current promotional efforts, but also on these same factors and price, service, location and other factors for all of the other available brands. If the industry is considered as the relevant unit other problems emerge. The growing demand for some reasonable form of public transportation could be the result of consumer dissatisfaction with the performance of automobiles. While this demand for better transportation services is probably largely based on consumer dissatisfaction with the current structure, the problem goes beyond mere disappointments with the performance of automobiles. The demand for public transportation follows from the nervous strain, pollution, excessive costs including the expected depreciation, and time required for primvate transportation. While giving the consumer means

to collect his losses if the performance of the automobile does not meet the expectations of reasonable consumers will reduce the frustration with automobiles, this policy will not eliminate all of the frustrations related to private automobile transportation. To determine the scope of the problem and the effect of the policy a means of separating the causes of the frustration leading to the demand for public transportation would be required. While the industry analysis eliminates some of the alternative explanations (e.g., competition between brands) the aggregation combines many sources of frustration besides a disparity between product performance and expected performance.

The movement between the cities and the suburbs also involves frustration. Disappointments in the performance of automobiles, washing machines, lawn mowers and other durables characteristic of the suburbs would make urban life more attractive. Again the product failures would account for only an unknown part of the frustrations which would cause a person to move from the suburbs to the cities and face the ample urban frustrations. A net movement from or to the cities relative to the suburbs indicates (perhaps) the greater total frustration, but it does not indicate the amount or how it should be divided between the various sources.

If social movements and sales data include too many alternative explanations besides consumer frustration with product performance, then it might be possible to use

evidence not based on frustration. Rather than working with manifestations of a mental state, specific behavior might be considered. Such behavior would include the production of consumer protection articles (relevant to the particular policy) in magazines or changes in the size of consumer protection staff in governmental bodies or industry. While the connection might not be exact between these numbers and the amount of consumer frustration in the population one might suspect that some connection would exist and could be determined. While a connection probably exists there is reason to doubt that its form can be determined. Before consumerism became a public issue there were relatively few articles and governmental agencies, but from this one would not conclude that consumer frustration with products did not exist. At the other extreme there may be more regulation than problems or the regulation may create many of the problems - the Interstate Commerce Commission (ICC) when regulating the railroads may be in this situation. Again the problem lies in the fact that we are considering a social behavior which is the function of several factors. Public action follows not only from the existence of the problem, but also the awareness of the problem and if dealing with that particular type of problem is currently in style. One cannot equate the seriousness of the problem with the quantity of public response. The desired information, necessary to analyze the effect of the

policy, the magnitude of the problem before the policy cannot be determined by an analysis of the public's action and the number of articles.

A very direct measure of consumer dissatisfaction with products lies in court cases and complaints made by consumers to consumer protection divisions of governmental units. Again the problem lies in the fact that the existence of the problem (the desired information) is only one factor in many involved in the generation of a court case or a complaint. If the consumer does not feel that the courts or governmental agency can do him any good he is unlikely to complain. The lack of complaints is not necessarily an indication of a lack of consumer frustration with product performance. A large number of complaints may reflect effective handling of a relatively small number of consumer problems. A numerical examples makes the situation clearer. If there are actually 1,000 incidents but only 5% are reported due to a lack of faith in the institution there are a total of 50 complaints. If there are actually only 100 incidents, but 75% are reported because of consumer faith in the institution there will be 50% more complaints where there are 90% fewer incidents. The actual number is the desired information, but the only data available would be the number of reported incidents. Without knowing the reporting rate, which will vary according to consumer faith, the length of the form to be filed, the location of offices and doubtlessly many other

factors, there is no way of determining the actual number of incidents from the reported number. The problem is somewhat more complicated in that the reporting rate will change as consumers have experience (good or bad) with the institution and as manufacturers adjust to the institution.

How can a policy be proposed and supported if the researcher cannot establish by means of social movements, sales statistics nor complaints, the scope of the problem nor the effectiveness of the policy? The existence of the problem can be established by appeals to personal experience of virtually any adult and probably most children. The magnitude of the problem will probably remain a matter of opinion. The policy follows from a logical argument as does the freedom of contract policy which it seeks to adjust. Since the argument has been developed in this and the previous chapter there is no need to repeat it at this point. Although the difference may be more one of degree than of kind, in the absence of empirical support the proponents of a policy must present it for public inspection. Those who believe that the policy will be ineffective or counter-productive may present their views. Hopefully when all of the views are presented and defended the proper course of action will emerge most of the time. The lack of firm data is not necessarily bad, this lack forces attention to questions of behavior which may be more critical to the effectiveness of a policy than the size of the existing problem.

FOOTNOTES

[1]Samuel Williston and George J. Thompson, Selections From Williston's Treatise on the Law of Contracts, Revised Edition, (New York: Baker, Voorhis & Co., 1938), p. 1. They are quoting from Restatement of Contracts.

[2]Friedrick Kessler and Malcom P. Sharp, Contracts: Cases and Materials, (Englewood Cliffs, New Jersey: Prentice-Hall, 1953), pp. 2-9, reprinted in Richard D. Schwartz and Jerome H. Skolnich, Society and the Legal Order, (New York: Basic Books, Inc., 1970), p. 155.

[3]Kessler and Sharp, Ibid.

[4]Williston and Thompson, Selections, p. 4.

[5]John Stuart Mill, Principles of Political Economy, Reprints of Economic Classics, (New York: Augustus M. Kelley, Bookseller, 1965), p. 952 (Book 5, Chapter 11, Section 7). This book was first published in 1848.

[6]Mill, Principles, p. 793 (Book 4, Chapter 7, Section 7).

[7]Morris R. Cohen, "The Basis of Contract," Harvard Law Review, XLVI, (February, 1933), p. 584.

[8]Friedrich Kessler, "Contracts of Adhesion - Some Thoughts About Freedom of Contract," Columbia Law Review, XLIII, (July, 1943), 632.

[9]Senator Moss, U. S. Congress, Senate Warranty Hearings, p. 1.

[10]Virginia H. Knauer (Special Assistant to the President for Consumer Affairs), U. S. Congress, House Warranty Hearings, p. 248.

[11]Fairfax Leary (Public Interest Research Group, Virginia), U. S. Congress, House Warranty Hearings, p. 116.

[12]William F. Willier (National Consumer Law Center, Boston College Law School), U. S. Congress, House Warranty Hearings, p. 234.

[13]Large scale buyers may have a general purchase form which cancels out the restrictive terms - purchases of single units don't use these contracts.

[14]Samuel Williston, "Freedom of Contract," Cornell Law Quarterly, VI, (May, 1921), 374.

[15]Federal Trade Commission, Staff Report on Automobile Warranties, Authorized on July 20, 1965, pp. A1-A3, FT 1.2: Au8.

[16]Federal Trade Commission, Staff Report, pp. 31-33.

[17]Federal Trade Commission, Staff Report, pp. A1-A3.

[18]Federal Trade Commission, Staff Report, pp. 143-145.

[19]"Detroit Tries a U-Turn on Warranties," Business Week, July 25, 1970, p. 45.

[20]Federal Trade Commission, Staff Report, p. 195.

[21]Miles W. Kirkpatrick, U. S. Congress, House Warranty Hearings, p. 194.

[22]Judge Francis, Henningson v. Bloomfield Motors, Inc., 161 A 2d 69 (New Jersey, 1960) at 78.

[23]Karl N. Llewellyn, "A Book Review of The Standardization of Commercial Contracts in English and Continental Law, by O. Prauznitz," Harvard Law Review, LII (February, 1939), p. 704.

[24]Samuel Williston, The Law Governing Sales of Goods at Common Law and Under the Uniform Sales Act, Revised Edition, (New York: Baker, Voorhes and Co., Inc., 1948) p. 591, section 231.

[25]Robert W. McLaren, U. S. Congress, Senate Warranty Hearings, p. 221.

[26]Anne Ramsey Somers and Herman Miles Somers, Workmen's Compensation, (New York: John Wiley and Sons, Inc., 1954), pp. 29-34.

[27]Somers and Somers, Workmen's Compensation, p. 18.

[28]E. H. Downey, Workmen's Compensation, (New York: The MacMillan Co., 1924), p. 122.

[29]Somers and Somers, Workmen's Compensation, p. 199.

[30]Downey, Workmen's Compensation, p. 131.

[31]Downey, Workmen's Compensation, p. xxv.

[32]Downey, Workmen's Compensation, p. 132.

[33]Downey, Workmen's Compensation, p. 141 (footnote to page 132).

[34]Roland P. Blake, Industrial Safety, Third Edition, (Englewood Cliffs, New Jersey: Prentice-Hall, Inc., 1963), p. 16.

CHAPTER THREE

TRADITIONAL BUYER PROTECTION AS A PRACTICAL POLICY FOR PURCHASERS OF DURABLE PRODUCTS

Consumer problems, the failure of a product's performance to meet a consumer's reasonable expectation of performance, are the result of conscious decisions made by the management of firms which provide these products. While one might argue that a poor performance of a particular product is the result of an oversight or accident, one cannot reasonably argue that the universal occurrence of poor performances results from a series of independent accidents. Clearly the decisions of the manufacturers leading to unsatisfactory consumer products do not occur by chance. The extent of the problem considerably narrows the range of possible explanations since the reason for the performance must apply to all of the offending manufactuers. One universal influence on all manufacturers of consumer goods which could reasonably affect the quality of goods produced is the set of laws under which the manufacturers operate. These laws controlling commercial transactions may create an environment which encourages poor performance by manufacturers. John R. Commons expressed the relationship in terms of rules.

> "Stated in language of the operation of working rules on individual action [Working Rules of Collective Action] are expressed by the auxiliary verbs of what the individual can, cannot, must, must not, may or may not DO. He 'can' or 'cannot' because collective action will or will not come to his aid. He 'must' or 'must not' because collective action will compel him. He 'may' because collective action will permit him and protect him. He 'may not' because collective action will prevent him."[1]

Expectations

Expectations of performance may be divided into two classes: 1) those expectations the state will enforce either directly (e.g., food and drug safety expectations) or through the courts on the initiative of a consumer (e.g., breach of contract) and 2) other expectations the state will not enforce. Those expectations of performance contained in the valid contract will be enforced by the state. By limiting the consumer to repair or replacement of the good for a limited time as permitted in the UCC (sections 2 - 316 and 2 - 719 in Chapter One, page 30), the manufacturer need not meet a wide variety of reasonable consumer expectations. Enforceable expectations are not necessarily identical with reasonable expectations. A consumer might reasonably expect that a product will be well designed and well manufactured. He might reasonably expect the product's performance to correspond to the performance claims made by the seller either verbally or in advertisements. The consumer might reasonably expect that if the product fails to meet these reasonable expectations he could receive a refund. With the exercise of the

power to exclude the traditional protections of consumers as permitted by the UCC these reasonable expectations of consumers were not enforceable in the courts.[2]

It may be the case that consumers often prefer inexpensive and poorly made products over expensive and well produced products. A policy which would preclude the production of products of low quality might operate against the interests of some consumers. Requiring the warranty of merchantability and the express warranties created by the activities of the seller does not preclude the production of inferior products. If the product is presented in such a manner as to lead the consumer to expect poor performance (e.g., the durability of paper plates as compared to china) then the consumer would not reasonably expect a "well manufactured" product (i.e., he would not expect china plate performance from paper plates). The consumer problems considered in this study do not come from low cost products which are represented as being inferior (which is to say that the reasonable expectation of average performance does not exist), but in cases of products which do not meet the reasonable performance expectations of the consumer. The price of the inferior product which is represented as average or superior may be more than, equal, or less than the average price for goods of the type. But the problem with these goods is not their price, but rather the failure of these goods to meet the reasonable performance expectations of consumers. Purchase decisions are

made by considering price and expectations of performance; when a consumer is disappointed he is surprised not by the price (which is known), but by the product's performance or lack of performance. The policy proposed in this study does not set prices or control advertising, but merely requires that the product's performance meet whatever performance expectations the manufacturer chooses to create in a reasonable consumer.

The Solution

As an economic issue consumer problems are a matter of industrial performance. In terms of legislation the proper policy issue in the case of consumer protection consists of the placing of each of the various consumer expectations into one of two classes. Either the expectation will be legally and economically enforceable (worth winning considering costs and awards) or it will be a legally and/or economically unenforceable expectation. Legislation may make an expectation enforceable by disallowing the virtually universally exercised manufacturers' discretionary power to exclude the expectation from court enforcement by means of the contract.

Requiring the traditional consumer protection of the common law as an implied condition of sale would have, with no other change, an important effect on the severity of those consumer problems resulting from the failure of the product to meet the reasonable performance expectations of the buyer. Even if the manufacturers continue making

extravagant claims, which the performance of their products does not meet, the consumer would have gained an important alternative. If as part of the contract for the good being sold the seller (by explicit clauses or by implied clauses which could not be excluded) warrants the good to be merchantable, then should the good subsequently prove not to be merchantable the consumer could receive financial compensation from the manufacturer for his financial loss. While continuing to suffer the inconveniences and perhaps psychic losses associated with a poorly performing product the consumer would no longer suffer the additional financial loss of the purchase price. The severity of consumer problems would be reduced. The seller, rather than the consumer, would be financially responsible for the special claims he makes and for meeting the standard levels of performance in his products considered appropriate by the courts for products of the particular type.

The removal of the discretionary power of the manufacturers to exclude the traditional consumer protection of the common law does not place the consumer in a riskless position. Of course, a consumer who, after purchasing a product, decides that he does not want a particular product which corresponds to the claims of the manufacturer and the general standards for products of the particular type would have no additional recourse. The proposed strengthening of the consumers' position will not protect consumers against sales claims which are not affirmations of fact, but rather

"puffing." "Puffing" is a fairly difficult activity to specify; in the final analysis the courts will decide if a contested specific claim is an affirmation of a fact or mere "puffing." As a judicial decision it is subject to change over time. The prudent manufacturer, to avoid losses, will stay safely and clearly within "puffing" if he is going to engage in "puffing" activities. The consumer would not be protected against flaws that a reasonable inspection would have revealed. Nor would a consumer have his unreasonable interpretations of the manufacturer's claims (including duration of performance) or of a product of the particular type's performance enforced by the courts. The consumer is not protected against problems resulting from his improper use or maintenance of the product. Basically the proposed change does not protect the consumer against his own carelessness in the market. It provides protection only in the areas in which the consumer cannot exercise care because the complexity of the product precludes the consumer's making a meaningful determination of its quality.

The problem of determining the standards to be used in fixing responsibility for product failures after they have been used by consumers is not new. In Henningson v. Bloomfield Motors, Judge Francis considered the automobile manufacturers' contract condition on this question.

> "The manufacturer agrees to replace defective parts for 90 days after the sale or until the car has

> been driven 4,000 miles, whichever is first to occur, if the part is sent to the factory, transportation charges prepaid, and if examination discloses to its satisfaction that the part is defective. It is difficult to imagine a greater burden on the consumer, or a less satisfactory remedy. Aside from imposing on the buyer the trouble of removing and shipping the part, the maker has sought to retain uncontrolled discretion to decide the issue of defectiveness. Some courts have removed much of the force of that reservation by declaring that the purchaser is not bound by the manufacturer's decision. . . . In the Mills case (Mills v. Maxwell Motor Sales Corporation, 181 N.W. 152 (Nebraska, 1920), the court said:
>
> > "It would nevertheless be repugnant to every conception of justice to hold that, if the parts thus returned for examination were, in point of fact, so defective as to constitute a breach of warranty, the appellee's right of action could be defeated by the appellant's arbitrary refusal to recognize that fact. Such an interpretation would substitute the appellant for the courts in passing upon the question of fact, and would be unreasonable." Supra, 181 N.W. at 154.
>
> Also suppose, as in this case, a defective part or parts caused an accident and that the car was so damaged as to render it impossible to discover the precise part or parts responsible, although the circumstances clearly pointed to such fact as the cause of the mishap. Can it be said that the impossibility of performance deprived the buyer of the benefits of the warranty?" 161 A. 2d 69 at 78, 79.

The manufacturer can make the first decision as to his responsibility in light of the buyer's use of the product, but the buyer may have the issue decided by the courts if he believes that the manufacturer's decision is unreasonable. The use of the courts to settle these disputes is not created by the reintroduction of the traditional consumer protection of the common law.

The partial elimination of financial loss by the consumer follows directly from the proposed changes in the UCC and does not depend on any change in behavior by the manufacturers. It is unlikely that the manufacturers will

continue their past behavior, which would no longer be profitable in the face of new and unavoidable responsibility for the performance of their product. With the traditional protection restored to the consumer, (by the elimination of the provisions allowing the manufacturer to restrict the consumers' remedy to the exclusive and highly limited recourse of repair and replacement) the manufacturers would (to avoid paying refunds) have to produce a product which would meet two sets of performance expectations. Their products would have to perform as goods of their type are expected to perform and to perform to the level of reasonable consumer expectations created by the manufacturers' specific claims of product performance. The first group of expectations based on average performance with products of the general type could not be avoided by the manufacturer by means of a clause in the contract (they could, as considered below, be avoided by promotional activities of the manufacturer.) If sold as a product of a particular type, the product must meet the traditional levels of performance. If to do so the manufacturer must improve his product, then the economic incentives of remaining in business will require him to improve his product.

To a large extent the "traditional" expectations of performance of a product of a particular type are subject to change by a manufacturer. If a manufacturer clearly specifies at the time of sale and in his

promotional activities that his product performs at a lower level than consumers would reasonably expect, these lower standards would be applied to his product. Thus a manufacturer could produce and sell, without fear of refunds a "throw away" car provided he clearly promotes it as such (as in the promotion of paper dresses). A merchantable product is one that performs to the expectation level of a reasonable man. Obsolescence is a rather special situation.[3] A consumer would be protected if the product became obsolete because of poor production decisions (the product fails to meet the reasonable expectations of products of the general type) but the consumer would not be protected against obsolescence resulting from technological improvements or changes in fashion (claims in fashion would probably be considered 'puff').

Product Variety

It is possible that all manufacturers might decide to produce (and promote as such) a "throw away" car. This production decision would not be unprofitable because of breach of contract difficulties, but it might be socially undesirable for ecology reasons. Ecological considerations are not a topic of this study, but it is possible to briefly consider the possibility that this policy would tend to create ecological problems (wasteful production due to limited durability of the product). If all existing manufacturers were to produce a "throw away" car

or other short lived substitute for a formerly durable product, this act would seem to create a profitable market for a new manufacturer who would produce a product which would meet the traditional consumer expectations (and promote it as such). Competition will prevent exclusively extreme industrial performances either in the direction of poor quality and low price or high quality and high price. The mix that will result (and which will be subject to constant change) will depend on a wide variety of social actions besides any change in warranty law. As an example the production of a "throw away" car would be discouraged by a high 'salvage tax' which would raise the ownership costs but encouraged by 'socialized medicine' which would lower the operating costs (assuming that "throw away" cars would be less substantial and thus their occupants more prone to physical injury - socialized medicine would reduce the differential in insurance premiums on medical insurance between safer and more dangerous cars.) The ecological result of this or any other policy effecting quality decisions will be subject to constant change depending on other policies.

This reintroduction of the traditional warranties by clarifying the differences in performance between products should increase the variety of products made available. Rather than limiting the available choices to one level (a strict interpretation of what a merchantable appliance of a particular type might be) as might happen

if a agency regulation were used, the reintroduction of the traditional warranties will lead to meaninful diversity. The consumer often cannot determine the various differences in performance between various brands of the same product and must assume that they are all approximately equal in performance. As the performance claims become more related to the actual performance manufacturers will be able to introduce products which are not merely another brand of the same general type. The availability of diverse products performing similar functions depends on the ability of the consumer to differentiate between them. As an example only very accurate descriptions would allow the Timken Company to produce 35 types of tapered roller bearings in 11,000 sizes.[4] Honesty and accuracy in representation increases the variety offered to consumers.[5]

The act of selling implies the existence of the standards involved in merchantability.

> "In view of the principle that the whole purpose of the law of warranty is to determine what it is that the seller has in essence agreed to sell, the policy is adopted of those cases which refuse, except in unusual circumstances, to recognize a material deletion of the seller's obligation. Thus, a contract is normally a contract for a sale of something describable and described. . . ."[6]

If the consumer did not have any expectations he would not know what to buy. The producer would not know what to manufacture and the retailer would not know what to stock. While it may not be possible to state precisely the general expectations of society concerning particular products,

reasonably precise expectations must exist and be known for commercial transactions to occur.

A product's performance may meet the standards for a product of the particular type and yet a consumer problem might exist because the product failed to meet the extra performance expectations created by the manufacturer. The proposed changes in the UCC would require, to avoid paying refunds, that if a manufacturer chose to make additional claims for his product, then the product's performance must meet a consumer's reasonable interpretation of the claims. The manufacturer may avoid meeting these consumer expectations merely by not creating these expectations. The manufacturer must decide for each consumer expectation he might create whether the additional income from larger sales and/or higher price would exceed the cost of creating the expectation and the costs of improving the product so that its performance will meet the consumers' reasonable expectations.

Enforcement

Even small policy proposals seldom, if ever, confine their full effects to the problem to which they are directed.[7] Removing the discretionary contractual power of manufacturers creates, by means of the availability of the police power of the state, a situation in which the product's performance must meet a reasonable man's expectation of its performance. But the shift in economic

incentives (profitable patterns of production) leading to a more satisfactory behavior (honest representation) by the manufacturer does not follow merely from the act of removing a few paragraphs from the UCC in the case of consumer transactions. The manufacturers' behavior changes because he knows that a deceived consumer can turn to the state and through the courts or some other institution use the police power to receive a refund of all or much (depending on the benefits he received from the product) of his purchase price resulting from a breach of contract (implied warranty of merchantability) by the manufacturer.[8] In making this compensation the manufacturer suffers a loss; to remain in business he will change his behavior to avoid these losses. But the striking of the paragraphs from the UCC might have an adverse effect on the dockets of the courts if the courts were used to enforce the traditional protections of the consumer. Specifically, the proposed change might flood the courts with consumer complaints. The effect on the judicial system might be so damaging as to make this policy, however beneficial to the consumer, a poor social action. The danger of flooding the courts could be eliminated with the use of another institution.

Since the concept of merchantability developed in the judicial system the enforcement of the policy proposed in this study has been set in the courts. The policy consists of imposing a loss on producers who manufacture goods which do not meet the reasonable performance

expectations of consumers. The agency which imposes these losses is not predetermined by the policy. Any agency which could impose the loss efficiently could be used to implement the policy. The courts are not the only social institution which could impose a loss on manufacturers for producing non-merchantable products. The imposition of losses might be accomplished by administrative agencies and/or an ombudsman system. In the section below these non-judicial institutions are considered as possible alternatives to the courts for making misleading behavior privately unprofitable. The consideration is not exhaustive, but rather seeks to illustrate the relative merits of the available institutions. The use of one of these institutions does not preclude the use of another and one might reasonably expect that the several institutions could function in a complementary manner in aiding consumers. But with the particular policy under consideration in this study effective administration depends on the ability of the injured consumer to make his complaint known and to receive compensation for the failure of the product to meet his reasonable expectations. If an institution is not designed to handle individual problems and order compensation, then it is not suitable for enforcing this particular policy. The same institution, while unsatisfactory for this particular policy, might be suitable for other important consumer protection policies, e.g., removing

unsafe products from the market before they are sold to consumers.

Administrative Agencies

A governmental agency could impose these losses. Occasionally agencies do impose penalties for poor performance. However, problems exist in the use of administrative agencies. Agencies, and courts, have been subject to influence by the industries they regulate and may perform badly for the individual consumer.

> "Under normal conditions private management is inevitably the dominant 'organizing' force. When the industry, after a period of reform, has been stabilized at a new level, management direction becomes the primary influence. Paradoxically, this phenomenon may be reinforced by a vague, broad delegation of administrative power! Such a delegation is a source of administrative strength in the initial reform period. The implied objectives and the climate of opinion give directing significance to the generalities of the statute. But when these objectives are realized, the statutory vagueness may no longer yield a sense of mandate. External forces rush in to fill the vacuum."[9]

The agencies generally prefer to avoid court action for reasons of efficiency, and settle for cease and desist orders which apply only to the future and do not aid the damaged consumer.

> "Under the Clayton Act and Trade Commission Act, all that the Commission's (FTC) order can do is to direct the respondent to "cease and desist" from the unfair method or other practice in question, or if the order concerns Section 7 or 8 of the Clayton Act, to divest itself of the stock held or rid itself of the directors chosen contrary to law. The act does not expressly confer any general power, of the kind possessed by a court of equity, to compel restitution, or otherwise to so mold the decree as to do substantial justice under the circumstances. Of course, no damages can be awarded, or mandatory order entered. Where,

> therefore, the unfair act has already accomplished its purpose, and there is no occasion for repeating it, the Commission cannot give relief."[10]

This limitation has its effects on consumer protection:

> "Anyone who believes that the provision for injunctive relief is an adequate tool as far as the FTC is concerned is oblivious to the history of that agency and its frustrations in trying to accomplish something in the consumer area. Anyone that practices before the FTC . . . is familiar with the fact that industry has little difficulty, and there are numerous cases substantiating this, in dragging out a cease and desist proceeding before the Commission for 5, 6, 7 and 8 years without even going to court. And with a very clear understanding as to what, at most, will happen at the end of that period if a violation is determined; they will be told that they were naughty boys and urged not to violate the act again. In short, injunctive relief. Provision for injunctive relief only is the most single self-defeating aspect of the FTC's procedures at this time."[11]

If penalized, the effect on the company is quite limited. These agencies have a rather time consuming procedure (when compared to a small claims court) which is reasonable for the considerable amounts of money often under consideration. But this procedure can make the effort on the part of a consumer, if feasible at all, more trouble than the award is worth. In terms of consumer protection, procedural delay can be fatal. Before the governmental agency even receives enough complaints to act the company can gain substantial profits by using a deceptive practice. Additional profits can occur before the agency finishes its procedures and appeals and makes its decree. Some companies have continued with profitable deceptive practices even after receiving cease and desist orders (at the risk of

being found to be in contempt of court). Fundamentally the difficulty lies in the fact that deceptive practices are profitable and often privately good business. The Holland Furnace Company case provides an excellent example of the limitations of the administrative agency approach under the present rules.[12] Miles W. Kirkpatrick, the chairman of the FTC, recognizes this problem.

> "Moreover, there is no surer means by which the Commission can perform its role of consumer protection than by framing its orders so as to insure the those who have profited wrongfully from proven violations are denied the fruits of their wrongdoing."[13]

The Ombudsman

The problems of controlling administrative agencies led to the creation of an institution which has the speed and flexibility needed to control deceptive commercial behavior. The Swedish Parliament created the office of Supreme Procurator (Hogste Ombudsmannen) in 1713. Since that time this office has continued to exercise a general supervision to insure that laws and regulations were complied with, and that public servants discharged their duties properly.[14] The legislature recognized that it was one thing to pass a law and something quite different to have it carried out as the legislature desired. The institution of Ombudsman in Sweden was designed to afford the legislature control at the lower levels and has three particular qualities: 1) the Ombudsman is an independent and non-partisan representative of the legislature, usually provided for in the constitution, who supervises the

administration of laws passed by the legislature, 2) he deals with specific complaints from the public against administrative injustice and maladministration and 3) he has the power to investigate, criticize and publicize, but not to reverse administrative action.[15] In the Swedish form this tool of "administrative remedy" (the heading for Ombudsman articles in both Reader's Guide to Periodic Literature and Index to Legal Periodicals) is not suitable for resolving contractual disagreements between consumers and manufacturers. This does not mean that the Ombudsman institutions provides no services to consumers, but rather that the consumer problems under consideration here are not the result of maladministration and thus not amenable to the pure Ombudsman approach.[16]

Would a modified Ombudsman approach effectively aid consumers? A Consumer Ombudsman of some form would work to insure that the laws are being followed. He is concerned with the ways in which laws and regulations are being followed; he is not expected to dispute their validity.[17] The problems consumers face with products do not follow from goods laws not being properly followed (the assumption of the Ombudsman approach), but rather from archaic, socially poor laws followed to the letter. Basically, under the current contract laws of the UCC, which are being followed to the letter and size of print (the exclusion of merchantability must be in large print), the consumer does not have a legitimate complaint on which an

Ombudsman could operate. If the laws were changed as proposed here, the Ombudsman, when aiding consumers, would be deciding contract cases which is not an appropriate activity. He would be performing a quasi judicial function under a different name.[18]

Judicial Strain

In cases of deceptive practices, the consumer and seller are in an adversary situation characterized by considerable bad faith. The decisions required to resolve these disputes are of a judicial nature. The basic standards of this policy, that of a reasonable man and product merchantability, find their meaning in the decisions of the judicial system. Allowing the consumer to threaten a seller who has sold him a non-merchantable product, with a convincing threat of court action is not the same situation as a massive number of cases brought by dissatisfied consumers. However attractive having one's day in court might be in theory, actually going to court is both expensive and inconvenient. Court action is a last resort used only if an acceptable resolution of the dispute cannot be arranged.

The parties will not go to court if the court's decision can be predicted with certainty.

> ". . . the litigation process is designed to provide a framework within which parties with a present, concrete dispute can put their problem before a court, clarify and narrow the bounds of the dispute, give the court the material which it needs to know in order intelligently to resolve the dispute, and to do all

> this in a manner which insures, insofar as possible, that the resolution of the dispute will both appear and be a just one."[19]

If the law is clear and there are no real disputes as to issues of fact or issues of law, then there is nothing to present in litigation--the outcome is certain or certain enough not to justify the expense of litigation. Thus, if the product is clearly not merchantable or if the consumer's expectation of its performance are beyond what any court would consider reasonable, the parties, on advice of their lawyers, will settle for what they both know the winner in court would obtain. The borderline cases will not go to court because the consumer can only win compensation of his actual losses which would be fairly small in a borderline situation. For most consumer purchases the court must award the consumer a full refund or the expenses would exceed the settlement. Only when the parties do not agree if a particular product is merchantable and when the potential settlement is considerable would a case actually go to court. Cases involving good faith disagreements as to the merchantability of a good which would involve enough loss to the consumer to justify court action would be extremely rare (probably limited to automobiles and housing), and even these cases would eliminate future cases by establishing the likely outcomes of similar cases in the future.[20]

Since court action lowers the net return to the winner and increases the net loss of the loser, the courts

will be a very unattractive means of settling the dispute. Many contracts are signed which are later regretted, but active court enforcement is not required because the parties know the outcome of a court procedure. In obtaining the desired performance from the party that would lose, a high probability of getting a particular court decision is nearly as effective as actually getting the decision (as well as more convenient and less expensive for both parties). When the criteria of performance for merchantability are established for the special characteristics of modern products, few if any changes will probably be needed in the traditional criteria, the contested cases will be rare. Allowing the consumer the traditional common law protection should not flood the courts with cases. Avoiding court action when the outcome can be reasonably predicted is a necessary and general practice.

> "Not only is the existence of ordinary legal relationships generally unrecognized by the layman; even when the unexpected happens, and the legal basis of a relationship is bared, the formal machinery of the law is seldom involved. It could not, indeed, become so involved without a revolutionary increase in the scale of such machinery. In the criminal law, for instance, it is estimated that only one-seventh of all felony prosecutions in the United States end in jury trials."[21]

The potential of using the police power of the state (by means of a court order) if the party will not "voluntarily" do the action which is sought (e.g., refund the purchase price of a non-merchantable product) is critically important. For the policy to reduce consumer

dissatisfaction the certainty of loss is essential and can be achieved effectively by the mere availability of court action as a reasonable consumer recourse. The actual imposition of losses on manufacturers by the courts is not required. The manufacturer will "voluntarily" produce a merchantable product if he knows the consumer can easily obtain a refund of the purchase price by going to court if the product would be found not to be merchantable. While not precisely known and subject to some change these standards are those for which the consumer made the purchase--he must have expected something or the manufacturer would not have known what to produce, the seller what to stock or the purchaser where to look. The "voluntary" behavior will follow from the potential of bringing a case and would occur even if no case were ever brought. The benefits to the consumer of restoring as a practical alternative his traditional common law protection do not depend on placing the judicial system under significant additional strain. The manufacturers' change in behavior will become necessary because of the consumers' potential ability to bring a successful case rather than on an actual court action.

Product Innovation

Introducing a new consumer product is an economic decision which generally involves considerable risk.[22] Under the policy of restoring traditional consumer protection a

manufacturer must for profitable production limit his claims to those levels of performance his product can achieve. Generally these claims will be less tantalizing to consumers than the most enticing claims (limited slightly by considerations of credibility) of his advertising agency. Since the manufacturer's presentation will be less effective under his new legal environment (all other factors assumed to be unchanged) one might conclude that he will be able to convince fewer consumers to buy and try his new product. Presenting a new consumer good in the market would also be less attractive financially because to avoid giving refunds the manufacturer will have to correct product failings which now appear only when the product is in general use. Consumers will no longer have to accept, until the end of the warranty period, minor repairs and adjustments which do not really correct basic errors made in production or design.

If the manufacturer chooses to test his product, rather than make refunds on unsatisfactory units, then the manufacturer will spend more on research and testing to be sure that his product actually will function properly in the hands of the consumer. From the view of the entire economy this additional testing by the manufacturer is not an additional cost. Under the present situation the consumer performs the testing when he purchases and uses the product. The changes proposed in the UCC would promote

a more economical and reasonable procedure of testing as the testing will occur by the manufacturer before the product is mass marketed. This policy shifts more of the cost of testing from the consumer to the manufacturer. But to the party deciding whether to introduce a new product the increased testing will be an additional cost and will add to the financial risk of the proposed introduction. It might seem that the manufacturer under his new legal environment, will find new products both more expensive to build and design and harder to promote. The proposed restoration of traditional consumer protections might so increase the risks of product innovation as to be more damaging to the consumer than the consumer problems the policy seeks to control. This conclusion, that restoring the traditional protection of consumers will seriously inhibit innovation, follows from only a partial consideration of the risk situation involved in the successful introduction of a new product. When buying a new product the consumer also carries some risks in new product introductions and his situation will also change.

If relative to producing and introducing a new product nothing changed with the reintroduction of the consumers' common law protection except that the effectiveness of promotion was lowered and development costs increased, then product innovation for the consumer market might be severely limited. But the manufacturer does not carry all of the risks involved in the introduction

of a new product. When the new product enters the market, the consumer must decide (under conditions of considerable uncertainty as to the product's performance) if he is interested in the product the manufacturer has brought to the market with a set of performance claims. If he is interested he must decide if he will try the product immediately, or if he will wait until others have tried the product and until the problems associated with a new product have been eliminated. By removing the financial loss of the consumers in the eventuality of a new product performing poorly relative to reasonable expectations of its performance, trying new products soon after their introduction will be made more attractive to the consumer.[23] The use of money-back guarantees (on low price items) indicates that manufacturers believe that consumers are hesitant to bear the financial risks of poor product performance. However, much of the appeal to the manufacturer of a money-back guarantee is that it inspires consumer confidence (expectations of performance) at a low cost since many consumers will not exercise their right to a refund on a low priced item.

While the reintroduction of the traditional consumer protection will limit the creativity of the manufacturer's claims it will also create consumer confidence in the claims which the manufacturer does make. The manufacturer will continue to make claims in order to induce consumers to purchase his product; the difference is that for

profitable sales the product must meet a reasonable man's interpretation of these claims. Advertising new products currently serves to introduce a new product and to overcome consumer skepticism. While a manufacturer will continue to buy advertising to introduce his product and present his performance claims he will not have to spend great sums of money merely to overcome consumer skepticism. The consumer knows that the producer will suffer any losses resulting from the product's failure to meet reasonable performance expectations. Total advertising expenditures for the introduction of a new product should fall. Consumer acceptance of new products will increase since consumers would no longer have to fear a total loss on a new product, which will make introducing new products of merit more attractive. New products, introduced with the most promising claims the product can meet, would have a stronger demand which would allow the manufacturer to recover his greater costs in insuring the actual performance of his product. While the actual outcome will depend on the particular product it is quite possible that the reduced promotional expenses and increased consumer demand (greater volume in the initial production runs) for new products MIGHT more than compensate for the increased testing expenses (increased for the manufacturer - decreased for the economy as a whole) to yield lower consumer prices.

The Role of Small Claims Courts

A remaining issue lies in the effectiveness of the policy within a given institutional framework. Since this policy depends on the potential use of the courts, the conditions of actual use are critical. If the actual use of the courts is costly and inconvenient the consumer could only use (and threaten to use) the courts when his loss was considerable. As a practical matter the courts would not be available to compensate a consumer for losses of relatively small amounts of money and the manufacturer could safely and profitably ignore the threat of court action on a significant scale. If the court action is available to the consumer at a low cost and minimally inconvenient form, the threat of a potential action is very real for a moderate performance failure of a product. Under the low cost situation the manufacturer would have to exercise considerable care to insure that his products' performance meet the traditional expectations of products of the particular type and a reasonable man's interpretation of the manufacturer's special claims. The goal of restoring the consumers' traditional protections is not the change in wording of the UCC; the goal consists in changing the manufacturers' decision making environment so that he will be encouraged to exercise greater care and concern for his product's performance. This policy would be most effective under a low cost court system.

Since contract cases are appropriate for small claims courts the reintroduction of the traditional buyer protection will be very dramatic where these courts operate.[24] For a small expenditure and a minimum amount of time the consumer can use the police power of the state to receive compensation for his losses on purchases of products which are not merchantable. The manufacturer will have no practical alternative but to make the product merchantable (or lose money by making refunds). The ready availability of low cost court action will leave the manufacturer who desires to remain in business no choice but to produce a merchantable product (at least the vast majority of the units must be merchantable) which meets his claims. The small claims court will provide the potential court action needed to bring the desired industrial performance (more care and concern) in the production of both minor and major appliances.

The simplicity of the question (is a particular performance of a product less than a reasonable man would expect from a product of the type and the special claims of the manufacturers?) allows practical recourse to the regular judicial system in cases involving losses greater than the maximum allowed in small claims proceedings. In cases involving larger sums of money the traditional protections and care, with their larger costs to the parties and society, of the regular courts are appropriate. While a consumer suffering a major loss would have to threaten the use of a

fairly expensive procedure the costs would remain moderate to the loss because of the relative simplicity of the merchantability question.[25] Breach of contract of an implied or explicit warranty of merchantability is a much simpler (less expensive) case to win than fraud which requires the showing of intent or other tort cases which require a demonstration of wrongdoing.[26] For major losses the traditional court system would provide the essential potential of court action if the consumer can sue successfully under contract law rather than tort law. If the traditional common low protections were to be reinstated for consumers by the removal of the discretionary contractual power of manufacturers the courts are capable in their present form of providing the potential of court action.

FOOTNOTES

[1]John R. Commons, Institutional Economics: Its Place in Political Economy, (Madison: University of Wisconsin Press, 1959), p. 71 (Chapter 2 [2-2-4]). The original copyright is 1934. The UCC is an important part of the set of working rules of commercial transactions which indicate what firms can, must or may do or make without fear of collective action.

[2]In Black's Law Dictionary (1968) "Reasonable" is defined by a series of synonyms: just, proper, ordinary, usual, fit and appropriate to the end in view, honest, equitable, fair, suitable, moderate and tolerable. Absolute certainty as to what will be found to be reasonable is not necessary or possible.

[3]"Obsolescence occurs with or without 'planning.' With respect to things, obsolescence occurs under three conditions. It occurs when a product literally deteriorates to the point at which it can no longer fulfill its functions-bearings burn out, fabrics tear, pipes rust . . . replacement is required. This is obsolescence due to functional failure. Obsolescence also occurs when some new product arrives on the scene to perform these functions more effectively than the old product could. This is obsolescence due to substantive technological advance. . . . But obsolescence also occurs when the needs of the consumer change, when the function to be performed by the product are themselves altered." Alvin Toffler, Future Shock, (New York: Bantam Books, Inc., 1970), p. 68 (Chapter 4-Temporary Needs).

[4]"Bearings: Roller, Split," Thomas Register of American Manufacturers, Volume 1, (New York: Thomas Publishing Co., 1972), p. 432.

[5]It is worth noting that this industrial diversity developed under contractual conditions a consumer would face if disclaimers of implied warranties were not allowed.

[6]American Law Institute and the National Conference of Commissioners on Uniform State Laws, "Official Comment 4,

UCC, Section 2 - 313, 'Express Warranties by Affirmation, Promise, Description, Sample,'" Uniform Laws Annotated, Uniform Commercial Code, Master Edition, Vol. 1, (St. Paul, Minnesota: West Publishing Co., 1968), p. 173.

[7]"Rules never generate behavior exactly appropriate to the contingencies from which they are derived, and the discrepancy grows worse if the contingencies change while the rules remain inviolate." B. F. Skinner, Beyond Freedom and Dignity, (New York: Knopf, 1971), p. 172.

[8]The profitability (award exceeding the party's cost of litigation) to the party is central to the exercise of a legal right. The class action increases the potential award considerably, but does not change the questions subject to litigation (except if the class is a legitimate class) nor the cost of litigation. Therefore class actions by raising the profitability of litigation might lead to an exercise of a legal right which an individual could not profitably use. But in cases, such as the warranty provisions of the UCC, where the party's difficulties follow from the substance of the law rather than the procedures of the judicial system, class actions will not provide a means of obtaining justice.

[9]Louis L. Jaffe, Judicial Control of Administrative Action, (Boston: Little, Brown and Company, 1965), p. 13.

[10]Gerald C. Henderson, The Federal Trade Commission, A Study in Administrative Law and Procedure, (New York: Agathon Press, Inc., 1968), p. 71.

[11]Edward Berlin (Counsel for The Consumer Federation of America), U. S. Congress, House Warranty Hearings, p. 278.

[12]On May 4, 1954 the FTC filed a complaint against the Holland Furnace Company. The complaint alleged that the company engaged in practices which were to the prejudice and injury of the public and competitors of the company, and constituted unfair acts and practices in commerce and unfair methods of competition in commerce within the intent and meaning of the Federal Trade Commission Act. The company, on September 15, asked for a temporary restraining order to stop the FTC from holding any hearings until 1) its appeals to the FTC were disposed of, 2) motions before the examiner were disposed of, 3) any subsequent appeal from those rulings were disposed of and 4) it might make an offer of settlement or proposal of adjustment. The FTC pointed out that the company's appeals pending at that time included a motion for suspension and referral, a

motion for a preliminary hearing, and an application for stay of proceedings--among other motions. The court ruled that the FTC could hold the hearings as schedule. (See Trade Cases, 1954, Commerce Clearing House, Inc. 67,859). On July 7, 1958 the FTC issued a cease and desist order for the following activities:

1. Representing, directly or indirectly, that any of its employees are inspectors or are employees or representatives of governmental agencies, or of gas or utility companies.
2. Representing, contrary to fact, that its salesmen or servicemen are heating engineers.
3. Representing that any furnace manufactured by a competitor is defective or not repairable or that the continued use of such furnace will result in asphyxiation, carbon monoxide poisoning, fires, or other damage, or for any other reason, when such is not a fact.
4. Tearing down or dismantling any furnace without the permission of the owner.
5. Representing that a furnace which has been dismantled cannot be reassembled and used without danger of asphyxiation, gas poisoning, fires, or for any other reason, when such is not a fact.
6. Requiring the owner of any furnace which has been dismantled by respondent's employees to sign a release absolving the respondent of liability for its employees' negligence, or of any other liability, before reassembling said furnace.
7. Refusing to immediately reassemble, at the request of the owner, any furnace which has been dismantled by respondent's employees.
8. Misrepresenting in any manner the condition of any furnace which has been dismantled by respondent's employees.

On August 5, 1959 the company was ordered by the court to obey and comply with this order. (See Trade Cases 1965, 71,360) Holland petitioned the Supreme Court of the United States for a writ of certiorari which was denied. In 1961 Holland appealed the cease and desist order on the grounds that it had not had a fair hearing (the hearing lasted for 88 days during which over 5,200 pages were collected). This complaint was found to be without merit. The order was made permanent on November 7, 1961. (See Trade Cases, 1961, 70,132) On January 27, 1965, the FTC petitioned to bring a criminal contempt proceeding because the company "knowingly, willfully and intentionally" violated and disobeyed the August 5, 1959 court order. The company, its president and two sales managers were found guilty of contempt. (See Trade Cases, 1965, 71,360) Only the most optimistic could consider this eleven year performance effective consumer protection.

[13]U. S. Congress, House Warranty Hearings, p. 198.

[14]Sten Rudholm, "The Chancellor of Justice," in Donald C. Rowat, ed., The Ombudsman, Citizen's Defender, Second Edition, (Toronto: University of Toronto Press, 1968), p. 17.

[15]Rowat, The Ombudsman, p. xxiv.

[16]The Swedish Ombudsman can aid the consumer with his problems when the government supplies the good or service. While these services are important and increasing, this study is concerned with goods and services supplied in the free market.

[17]John F. Smyth, "The European Commission of Human Rights," in Rowat, The Ombudsman, p. 166.

[18]One could, of course, give the Consumer Ombudsman judicial powers and still use the Ombudsman title. This procedure would seem to be both unnecessary (why not call him a consumer judge?) and confusing (what would 'ombudsman' signify?).

[19]Harold Shepherd and Byron D. Sher, Law in Society, An Introduction to Freedom of Contract, (Brooklyn: The Foundation Press, Inc., 1960), p. 9.

[20]Different judicial systems would determine different minimal levels of money in dispute to justify the action. For many cases the dispute must be at least $10,000 for a trial in the Federal Courts. The cost of legal representation ($40 per hour, minimum, in Lansing, Michigan) requires that the sum be substantial for a trial in a regular state court. A small claims court (considered below) with its minimal costs would allow smaller claims to be profitably considered.

[21]H. Laurence Ross, Settled Out of Court, The Social Process of Insurance Claims Adjustment, (Chicago: Aldine Publishing Company, 1970), p. 4.

[22]". . . You must now spend far more to launch a product than you did a few years ago--and stand ready to lose more. Of the roughly 100,000 soap, food, snacks and other products that will bomb in supermarkets during the 1970s--out of a total of 120,000 introductions--the advertising expenses alone will add up to an estimated

$5 billion for those being test marketed and $7 billion or $8 billion for those introduced nationally. . . . New product (all products) failure rates now run as high as 80%, and the waste in research and development has been estimated at 70% or more." "New Products: The Push is on Marketing," Business Week, March 4, 1972, pp. 72-73.

[23]"Why is it. . . that over the last 10 years, in spite of growing sophistication in marketing and research, no perceptible improvement has been made in the success ratio of new products? Have we, in fact, reached a new-product saturation level where consumers have turned off because of the number of me-too entries tried year after year? Are consumers no longer gratified by fresher breath, a richer coffee, a whiter wash, but searching for different values? Have government regulations and consumerism actually destroyed the marketing leverage we previously enjoyed and blocked our ability to recognize what consumers really want in the new-product area?" "New Products: The Push in on Marketing," Business Week, p. 77. The article continues and concludes that with the loss of 'marketing leverage' (which in the use here can only mean deceptive advertising) it is now more important to create new products with meaningful product differences. In other words it is in the manufacturers' interest to honestly represent an improved product. This behavior would be reinforced by the liability changes proposed in this paper.

[24]Every state except Colorado, Indiana and Nebraska has some kind of small claims court. For a description of these courts (in a table) and an analysis of their performance see: "Buyer vs. Seller in Small Claims Court," Consumer Reports, October, 1971, pp. 624-629. The Consumer Report study found, "With all their limitations, the small claims courts in our study were the best general means we've yet discovered for breaking the impasse between consumers and sellers." (p. 627) Their suggestions for change included:

1. "Every state should establish a system of small claims courts where proceedings are informal and strict rules of evidence are not required. . .
2. The maximum size of suits admissable as small claims should be $1,000. . .
3. Neither plaintiffs nor defendants should be permitted to have attorneys in small claims courts. . .
4. The use of small claims courts as debt-collection egencies must be curtailed. . .
5. The use of small claims courts as a place of redress should be promoted by agencies serving the poor, by bar associations, and by the court itself.
6. The courts should be brought to the people. Small claims courts should ride circuit, going regularly into the poor neighborhoods and sitting nights and

> Saturdays for the benefit of working people. While justice may be blind, it is not lame, and the distance to the courthouse is often unbridgeable by the poor.

The small claims court procedure in Michigan is found in Public and Local Acts: Michigan Session of 1968 (Lansing, Michigan: Legislative Service Bureau, 1968), pp. 231-234. The small claims court procedures are part of a law designed to revise the organization of the district courts in Michigan.

Each district court is to have a small claims division with the judges of the district court serving as judges in the small claims divisions (600.8401). These courts shall be confined to cases for the recovery of money when the amount does not exceed $300 (600.8402). The action is begun by an affidavit filed with the clerk or deputy clerk of the district court. The form of the affidavit was to be written by the Supreme Court of Michigan. A copy of the affidavit is served by certified mail along with instructions to bring any materials necessary for the defense (600,8404). The date for appearance is to be between 15 and 30 days from the date of the notice (600.8406). "No attorney at law, except in his own behalf, collection agency or agent or employees thereof or person other than the plaintiff and defendant . . . shall take part in the filing, prosecution or defense of litigation in the small claims division. Corporations may be represented by a full-time employee who is not an attorney at law. Plaintiff or defendant may demand and remove the case to the district court. The judge will inform both parties of this right prior to trial and also inform the parties of all rights waived if they choose to remain in the small claims division." (600.8404). The rights waived include right to counsel, right to trial by jury and any right to appeal (600.8412). The court to be used is that of where the cause of the action arose or the county in which the defendant is established or resides (600.8420). A fee of $5.00 is charged for filing the affidavit and a fee of $1.00 is charged for each copy which is to be mailed to a defendant by the clerk (600.8420). The prevailing party in any action receives the costs of the action (600.8421). Actions of fraud, libel and slander and actions against the state or any other governmental agency are not permissible in a small claims procedure (600.8424). "In hearings before the small claims division witnesses shall be sworn. The judge shall conduct the trial in an informal manner so as to do substantive justice between the parties according to the rules of substantive law but shall not be bound by the statuatory provisions or rules or practice, procedure, pleading or evidence, except provisions relating to privileged communications, the sole object of such trials is to dispense expeditious justice between the

parties. There shall be no jury nor shall a verbatim record of such proceedings be made." (600.8411).

[25]". . . If the buyer is compeled to contest the question of negligence (tort law rather than contract law) with the seller, he will find it very difficult to recover. In the nature of the case the evidence will be chiefly in the control of the seller, and the expense of even endeavoring to make out a case of this sort will be prohibitive in cases involving small amounts. Moreover, if the buyer cannot recover from the seller (dealer or manufacturer) he cannot recover from anyone for the defective character of the goods which he has bought. The wrong done by the sale of defective materials to the manufacturer who later sold the goods cannot form the basis of action by the ultimate buyer. Consequently, the real wrongdoer who has caused the ultimate injury escapes. On the other hand, if the manufacturer is held to an absolute liability irrespective of negligence, it will unquestionably increase the degree of care which he will use, and if in any case he is compelled to pay damages for breach of warranty where the real cause of the defect was inferior material which he himself innocently purchased, he will have a remedy over against the persons who sold him this inferior material, and his damages will include whatever he himself has had to pay for breach of warranty. Thus the loss will be borne ultimately by the person who would be responsible." Williston, The Law Governing Sales of Goods, p. 620 (Section 237a).

[26]Tort means wrongdoing. The elements which must be proven to win a tort case in fraud are:

"1. misrepresentation or concealment of a material fact.
2. intentionally made (with knowledge of the falsity)
3. with intent to deceive.
4. reliance by the other party.
5. resulting in loss or injury."

Hendrik Zwarensteyn, Introduction to Business Law, Revised Edition, (East Lansing, Michigan: Michigan State University, 1963), p. 99.

CHAPTER FOUR

RECENT CHANGES IN WARRANTY LAW

The thrust of this study has been that consumer problems have developed because manufacturers have been able to escape from financial responsibility for their poor production decisions.[1] This immunity has resulted from the abuse of the doctrine of freedom of contract to justify the exclusion of the traditional warranty of merchantability and the express warranties which would be created by their behavior. This abuse of the freedom of contract in consumer transactions has recently led to limited corrective action by some states, Congress and the courts. This section will consider four of these moves. The analysis of these changes will consider only their effect on freedom of contract and the traditional implied and express warranties.

At the Congressional hearings on bills involving restrictions of the freedom of contract to exclude the warranty of merchantability there was testimony to the effect that such an action would not be in the best interest of consumers. Richard W. McLaren (Assistant Attorney General, Antitrust Division, Department of Justice) testified in favor of the approach used in the

Administration's bill which was not reported out of the Senate committee:

> "We believe that consumers are best served when they have available a wide range of choices between competing consumer products and competing warranties and guarantees given in connection with these products. We believe that consumers have a right to be well and fully informed as to the nature of that choice. Generally, so long as the consumer is informed of and adequately understands whatever warranties or services are offered, a supplier should be free to offer consumer products with no warranties, with comprehensive warranties or with warranties limited in substantive content and duration."[2]

In other words, there should be no limit on the freedom of contract of manufacturers so long as the consumer is aware of what he is being offered. The issue of the likely extent of competition in consumer warranties has been considered in Chapter Three and is considered again in Chapter Five, at this point it is sufficient to note that other testimony at these Congressional hearings held that competition in warranty terms was virtually non-existent. The Senate committee did not agree with Mr. McLaren and reported out a bill (considered below) which restricted the manufacturers' freedom of contract.

Another argument presented at the hearings held that the use of disclaimers of implied warranties was proper and should not be restricted by the government. Alan Weber (counsel for the Gas Appliance Manufacturers Association, Inc.) testified:

> "Traditionally manufacturers have disclaimed all implied warranties in their express warranties. This device is used primarily to disclaim responsibility and obligations over which they have no control

> (e.g., air conditioning systems assembled by an independent contractor with components of several manufacturers)."[3]

While the word 'traditionally' may be a poor choice, this argument illustrates a basic problem, fixing of responsibility. If the manufacturer is not responsible because the contractor assembled the individual parts and if the contractor is not responsible because he didn't manufacture the defective part, then what is the position of the consumer? The consumer, the one party who has no responsibility for the failure, pays for the repair work. The approach in warranty reform has been to hold the manufacturer responsible. This procedure is not as unfair as it might seem since: 1) the manufacturer can refuse to sell to an incompetent contractor (and can determine competence as well as the consumer) and 2) the manufacturer could recover his loses for warranty service from a contractor whose incompetence caused the failure. The Senate Committee did not feel that the consumer would be protected by maintaining the manufacturers' freedom of contract.

Court Action

Berg v. Stromme (Wash., 484 P. 2d 380 [1971])

This case, decided by the Supreme Court of Washington on April 22, 1971, greatly limits the effect of standardized contracts in its jurisdiction. Dr. Berg purchased a Pontiac which he claimed had so many things wrong that he felt justified in rescinding the deal.

Seeking damages for the depreciated value of the automobile, costs of repairs and time lost Dr. Berg sued the dealer (Stromme) who had sold him the automobile. At the close of Dr. Berg's case the superior court (trial court) on Stromme's motion ordered a dismissal with prejudice on two grounds: 1) that the article had been purchased by trade name and that sale was, therefore, without warranty (the buyer did not depend on the seller's advice) and 2) Berg had signed a disclaimer of warranty.[4] The court of appeals affirmed, with one judge dissenting (they affirmed only on the grounds of the written waiver of warranty), the supreme court granted review and reversed the court of appeals and the superior court. The decision has a distinct tone of anger.

> "The issue, as we see it, is whether the buyer, despite the printed disclaimer of warranty, was entitled under the circumstances and conditions of the purchase, to receive delivery from the dealer of a new automobile that would operate with reasonable efficiency, safety and comfort. Evidence of the seller's representations were relevant to this issue, however, because it shows that the purchase resulted from negotiations, item by item, as to the color, size, weight, horsepower and body style of the vehicle and the kinds of optional extra equipment to be put on it, such as power brakes, power steering, tilt-steering wheel, soft-ray glass, power-operated rear window, power seat, air conditioning, super-lift shocks - and a host of other times of extra equipment not included in the standard price of the car of that size, type and model.
>
> "The printed documents constituting the written agreement between the parties and the execution of them in writing will show, we think, why printed disclaimers of warranty in the purchase of new automobiles are now regarded with increasing disfavor by the courts. . . . Although competent parties may make any lawful contract they choose, there exists a strong presumption that the buyer, in negotiating the purchase

> of a brand new car from a dealer, after discussing and agreeing upon all of the details as to its style, type, price, equipment, accessories and condition of delivery, would not in the same agreement negate and undo his bargain by disclaiming the right to a car of merchantable quality. Merchantable quality in a new car means a car that is reasonably safe, trouble free and dependable . . . and that it is reasonably suited for the purpose for which it was manufactured"[5] (at 381, 382).
>
> "The purported disclaimers of warranty in the conditional sale contract form and the waiver of warranty in the purchase order form highlight the absurdity of a rule of law which elevates these bland and substantially meaningless terms and conditions above the individually and expressly negotiated terms and conditions, and gives them controlling effect over specifically agreed upon items and conditions of the contract. To adhere to such a rule means that the law presumes that the buyer of a brand new automobile intends to nullify in general all of the things for which he has specifically bargained and will pay. We would presume the buyer does just the opposite" (at 385).

This decision allows the parties full freedom of contract in that it does not invalidate any particular type of contractual condition, per se.

> "Parties to an agreement may make any contract that comports with general law and if 'a seller positively and expressly refuses to give any warranty, and the contract is not induced by fraud, no warranty of any kind can be implied by law.' Jones v. Mallon . . . 101 P 2d 332 . . . But to come within these principles, the burden is upon the dealer to show with particularity just what the buyer is waiving, that is, which particular defects or conditions the purchaser of a brand new automobile explicitly waives.
>
> "Thus, in the sale of a brand new automobile, there does exist an implied warranty of fitness . . . The parties may agree to do more or to do less, but unless there is proof of explicit departure from this norm, the presumption is that the dealer intended to deliver and the buyer intended to receive a reasonably safe, efficient and comfortable brand new car.
>
> "These principles do not, we think represent a drastic departure from, but rather an adaptation of the prevailing trends in the law of torts to the law of contracts . . . this court adopted the rule of strict liability against the manufacturer - not the dealer -

> in accordance with modern views . . . Strict liability - liability without proof of negligence - in torts has been applied to the retail dealer despite disclaimers of warranty with greater and impressive frequency . . .
>
> ". . . Waivers of such warranties, being disfavored in law, are ineffectual unless explicitly negotiated between buyer and seller and set forth with particularity showing the particular qualities and characteristics of fitness which are being waived" (at 386).

In essence this decision makes disclaimers of warranties in standardized contracts unenforceable in the State of Washington. If the seller can convince the buyer knowingly to purchase an item which may only appear to be what he desires to purchase (not merchantable), then he may do so. 'As is' sales are permissible under the decision, but not if the 'as is' (or other disclaimer of warranties) is lost in a mass of fine print and not fully understood by the buyer.

Proposed Federal Legislation

Magnuson-Moss Act S.986 (92d Congress, 1st Session)

Going beyond Berg v. Stromme the Senate passed on November 8, 1971 (no warranty bill passed the House during the 92d Congress) the Magnuson-Moss Act. This act provides in Section 108 entitled Limitations on Disclaimer of Implied Warranties:

> "(a) There shall be no express disclaimer of implied warranties to a purchase if any warranty in writing or service contract in writing of a consumer product is made by a supplier to a purchaser.
>
> (b) For purposes of this title, implied warranties may be limited only as to duration and only to the duration of a warranty in writing of reasonable

> duration, if such limitation is conscionable and is set forth in clear and unmistakable language and prominently displayed on the face of the warranty."

While according to Berg v. Stromme it was possible (although fairly unlikely in the case of purchasers of new products) for the manufacturer to openly negotiate with the consumer and exclude the implied warranty of merchantability, under the Magnuson-Moss Act such complete exclusions would not be possible. But the manufacturer would be free to limit the duration of the implied warranties provided such a limitation were conscionable.[6] The burden of proof of the duration not being conscionable would seem to lie with the consumer. As a practical matter the manufacturer would continue to be free to limit warranties to a year or less even though the consumer might reasonably expect the item to last much longer.[7] Considerations of what would be a conscionable limitation of warranty duration, when the consumer is aware of this argument, may require too great a level of sophistication to be of value to consumers when protecting themselves.

State Legislation Passed

1) Uniform Commercial Code 2 - 316A

Maryland and Massachusetts have removed the manufacturers' discretion to exclude implied warranties and much of their discretion to limit their express warranties in the area of consumer warranties by passing 2 - 316A which is an amendment to the UCC of these states.

> "The provisions of section 2 - 316 shall not apply to sales to consumers as defined by section 9 - 109 (Maryland), services or both. Any language, oral or written, used by a seller of consumer goods and services, which attempts to exclude or modify any implied warranties of merchantability and fitness for a particular purpose or to exclude or modify the consumer's remedies for breach of those warranties, shall be unenforceable, provided however, that the seller may recover from the manufacturer any damages resulting from breach of the above described warranty.
>
> "Any language, oral or written, used by a manufacturer of consumer goods, which attempts to limit or modify a consumer's remedies for breach of the manufacturer's express warranties, shall be unenforceable, unless the manufacturer provides reasonable and expeditious means of performing the warranty obligation."[8]

The Massachusetts law:

> The provisions of section 2 - 316 shall not apply to sales of consumer goods, services or both. Any language, oral or written, used by a seller or manufacturer of consumer goods and services, which attempts to exclude or modify any implied warranties of merchantability and fitness for a particular purpose or to exclude or modify the consumer's remedies for breach of those warranties, shall be unenforceable.
>
> Any language, oral or written, used by a manufacturer of consumer goods, which attempts to limit or modify a consumer's remedies for breach of such manufacturer's express warranties, shall be unenforceable, unless such manufacturer maintains facilities within the commonwealth sufficient to provide reasonable and expeditious performance of the warranty obligations.[9]

In this form the manufacturer cannot limit the duration of the implied warranties to a duration he finds convenient. Thus in a dispute a consumer, after using the product for 90-days or one year, need only prove that the performance of the good has not been to the level of reasonable man would expect to recover his loss (the depreciated value of the good). He would not have to prove the unconscionability of the limitation of the duration as well as the

unreasonable performance of the product as would have been the case with the proposed Federal legislation. The relationship between clarity and litigation is well illustrated by these laws. The annotated codes for use in 1972 listing these laws include no cases or law journal articles which were based on these laws.

2) Song-Beverly Consumer Warranty Act (California Civil Code 1790)

This California act went into effect on March 1, 1971.[10] Unlike the approach in Maryland and Massachusetts this law is not an additional paragraph to the UCC, but rather a different law which when a conflict between it and the UCC occurs the Song-Beverly Consumer Warranty Act prevails. Section 1790.3 Law Governing; reference to Commercial Code:

> "The provisions of this chapter shall not affect the rights and obligations of parties determined by reference to the Commercial Code except that, where the provisions of the Commercial Code conflict with the rights guaranteed to buyers of consumer goods under the provisions of this chapter, the provisions of this chapter, the provisions of this chapter shall prevail."

This act removes the freedom of contract of the parties to consumer transactions.

> "Any waiver by the buyer of consumer goods of the provisions of this chapter, except as expressly provided in this chapter, shall be deemed contrary to public policy and shall be unenforceable and void" (1790.1).[11]

This law further provided that express warranties may not be used to exclude the implied warranties.

"Nothing in this chapter shall affect the right of the manufacturer, distributor, or retailer to make express warranties with respect to consumer goods. However, a manufacturer, distributor, or retailer making express warranties may not limit, modify, or disclaim the implied warranties (merchantability and fitness for a particular purpose) guaranteed by this chapter to the sale of consumer goods (1793)."

The effect of the bill was limited by the amendment of 1971 which went into effect on January 1, 1972. This amendment among other changes added Part C to Section 1791.1.

"As used in this chapter:
(a) "Implied warranty of merchantability" or "implied warranty that goods are merchantable" means that the consumer goods meet each of the following
(1) Pass without objection in the trade under the contract description.
(2) Are fit for the ordinary purposes for which such goods are used.
(3) Are adequately contained, packaged, and labeled.
(4) Conform to the promises or affirmations of fact made on the container or label.
(b) "Implied warranty of fitness" means that when the retailer, distributor, or manufacturer has reason to know any particular purpose for which the consumer goods are required, and further, that the buyer is relying on the skill and judgment of the seller to select and furnish suitable goods, then there is an implied warranty that the goods shall be fit for such purpose.
(c) The duration of the implied warranty of merchantability and where present the implied warranty of fitness shall be co-extensive in duration with an express warranty which accompanies the consumer goods, provided the duration of the express warranty is reasonable; but in no event shall such implied warranty have a duration of less than 60 days nor more than one-year following the sale of new consumer goods to a retail buyer. Where no duration for an express warranty is started with respect to consumer goods, or parts thereof, the duration of the implied warranty shall be the maximum period prescribed above.
(d) . . .

It is important to note that this change which limits the duration of the implied warranties was not the result of

poor experience with the Song-Beverly Act. The amendment took effect only ten-months after the original act went into effect - obviously there was not enough time to learn the effects from practical experience of enforcing implied warranties after more than one year. This change continues protection for consumers who purchase products which fail within the express warranty period or one year, whichever is less. But the 1971 amendment removes protection from consumers who are unfortunate enough to purchase a poorly designed or built product which fails after the express warranty period or one-year, whichever is less.

General Trend

Whether in the form of no time limit as in the Berg v. Stromme decision and the UCC section 2 - 316A of Maryland and Massachusetts or with a limit on duration as in the Magnuson-Moss Act and the amended Song-Beverly Consumer Warranty Act consumers are no longer losing the implied warranties of merchantabllity and fitness for a purpose by means of one-sided standardized contracts. Warranty legislation at the state level is becoming common. Approximately forty bills (twenty states) were pending in late 1971 or introduced for the 1972 season.[12] The legislation in Maryland and Massachusetts and to a limited extent, California, adequately meets the policy proposed in this study for the implied warranties of merchantability and fitness for a particular purpose.

However, this legislation fails to provide the consumer with adequate protection against the failure of products to meet the express warranties created by sellers in the act of selling. While these states allow a consumer to recover his losses if a product fails to function in the general purpose for which such products are purchased, the consumer has no contractual recourse if his unit fails to meet the special claims and/or samples used when the product was sold if the manufacturer excluded any but his limited express warranty in the standard contract. The restoration of the implied warranty of merchantability is an important step in allowing the consumer to protect himself against misrepresented products, but it is not a full restoration of the traditional rights of buyers. As a result of this legislation contracts eliminating the implied warranties are becoming relatively rare. The next chapter considers the economic effects on consumers of this change in the commercial law framework.

FOOTNOTES

[1]This is not, of course, completely correct. Certain problems of consumers are not related to warranty difficulties as considered in footnote 3 of the Introduction. Also if a firm produces an unsatisfactory product, eventually its reputation will suffer and the firm might have to terminate its operation. This process can be very slow, wasteful and this penalty for poor performance does not provide any relief for consumers who have suffered losses with the poorly made products.

[2]U. S. Congress, Senate Warranty Hearings, p. 223.

[3]U. S. Congress, Senate Warranty Hearings, p. 173.

[4]A leaning towards one side of a cause for some reason other than a conviction of its justice. Blacks Law Dictionary, 5th Ed. Rev., p. 1343.

[5]"i.e. a serviceable automobile capable of transporting a driver and passengers with reasonable efficience, comfort and security upon the roads and highways of the state." at 383

[6]"Conscionable" does not appear as a legal term in Black's Law Dictionary, Bouvier's Law Dictionary, nor in Words and Phrases - however "Conscience" appears in Words and Phrases where it is considered synonymous with "good faith."

[7]The Federal Government provides asset depreciation ranges for use in computing income taxes. These could serve as an estimate of the useful life a consumer could expect from a product.

Item	Lower Limit (Yrs.)	Upper Limit (Yrs.)
Typewriters	8	12
Automobiles	2.5	3.5
Restaurant Equipment	8	12
Dwellings	45	
Pool Tables	8	12

See Department of the Treasury, Internal Revenue Service, Depreciation, Amortization and Depletion, (Washington: U. S. Government Printing Office, 1972), Publication 532 (2-72), T22.44/2:534/4, pp. 20-22. The government and the consumer both expect products to function in a satisfactory manner for periods much longer than the 30-days or one year periods during which the manufacturer will guarantee his production decisions.

[8]Maryland, Annotated Code of the Public General Laws of Maryland, (Charlottesville, Va.: The Michir Company, 1972) Article 95B, went into effect July 1, 1972.

[9]Massachusetts, Annotated Code of Massachusetts, (Charlottesville, Va.: The Michir Company, 1970), Article 101B - added by 1970, 880, approved September 1, 1970 effective 90 days thereafter.

[10]California, West's Annotated California Codes, Civil Code, (St. Paul, Minn.: West Publishing Co., 1973).

[11]". . . a sale 'as is' or 'with all faults' means that the manufacturer, distributor, and retailor disclaim all implied warranties that would otherwise attach to the sale of consumer goods under the provisions of this chapter (1791.3). This exclusion is not effective 'unless a conspicuous writing is attached to the goods which clearly informs the buyer, prior to sale, in simple and concise language of each of the following:

(1) The goods are being sold on an 'as is' or 'with all faults' basis.

(2) The entire risk as to the quality and performance of the good is with the buyer.

(3) Should the goods prove defective following their purchase, the buyer and not the manufacturer, distributor, or retailer assumes the entire cost of all necessary servicing or repair." (1792.4).

[12]George P. Lamb (Association of Home Appliance Manufacturers), U. S. Congress, House Warranty Hearings, p. 317 and 'Statement of National Automobile Dealers Association', U. S. Congress, House Warranty Hearings, p. 463.

CHAPTER FIVE

THE ECONOMIC SIGNIFICANCE OF REQUIRED WARRANTIES

> ". . . Even if there is no negligence, however, public policy demands that responsibility be fixed wherever it will most effectively reduce the hazards to life and health in defective products that reach the market. It is evident that the manufacturer can anticipate some hazards and guard against the recurrence of others, as the public cannot. Those who suffer injury from defective products are unprepared to meet its consequences. The cost of an injury and the loss of time or health may be an overwhelming misfortune to the person injured, and a needless one, for the risk of injury can be insured by the manufacturer and distributed among the public as a cost of doing business." Justice Traynor in "Escola v. Coca Cola Bottling Co. of Fresno", 24 Cal. 2d 453, 150 P 2d 436 at 440-441, (Cal., 1944).

The return to the traditional relationships between buyers and sellers proposed in this paper will require thousands, if not millions, of decision makers of firms producing consumer goods to determine which, if any; changes in production and promotion activities, they will make to adjust to the changed commercial environment (i.e., strengthened rights of consumers). These decisions involving promotion and production adjustments require the experience and judgment of experts working in the firms. Those outside the firms who propose the changes are limited to considering the general trends by which firms will adjust to the changed environment. Since adjustments to

changing conditions are largely the result of trial and error testing, these adjustments are subject to only the most general type of prediction by even the experts of the firms. Those outside of the particular industry (and for many decisions those inside the firm as well) will not be able to predict the specific changes, such as changing from 22 gauge metal to 20 gauge.[1] But it is possible to determine the decision structure facing the firm when required to provide consumers with the warranties of merchantability and fitness for a purpose.

Effects of Workmen's Compensation Legislation

Fortunately the workmen's compensation experience provides an example of a similar change in the law (a shift in risk from a weaker party to a stronger party who has the power to control the rate of loss) which allows an analysis based on actual adjustments rather than speculation of changes in the future.[2] The decision structure facing a manufacturer who has been required to assume responsibility for the on the job injuries of his employees is similar to the decision structure he would face if made responsible for the financial injuries of his customers when he sells a faulty product. With the development of workmen's compensation legislation the employers' legal position was changed. No longer was he virtually immune (by means of acceptable common law defenses based on contributory negligence, fellow servant rule of

negligence or assuming the risks of the job) but rather he had nearly absolute liability (fault was not considered when these defenses were no longer effective).[3] To avoid payments to compensate employees for industrial accidents he had to make a number of choices.

The most basic of these choices was whether he should remain in business or whether he should stop; but this decision is misleading. The decision as to how or whether to adjust is made at the microeconomic level of the firm; the justification of the shift in responsibility lies in the effect on the entire economy - a macroeconomic situation. If one firm stops operating (a microeconomic change) due to the new legislation, but, rather than closing down and holding idle the fixed resources the firm formerly used, the firm sells the business to another firm which continues to utilize the fixed resources, then, in a macroeconomic sinse there has been no change. Since the past fifty years have been a period of generally rising production, this legislation, while it caused many changes at the microeconomic level, did not seem to seriously limit the productive capacity of the economy. An analysis of the microeconomic decisions of the firms in adjusting to workmen's compensation legislation is considered in some detail since it provides a good example of what may be expected as firms adjust to stricter warranty provisions.[4]

The adjustments to the macroeconomic policy of workmen's compensation legislation occurred at the

microeconomic level of the firm. Living with the imposition of considerably increased liability required several decisions. The firm which decides to remain in business or to take over another business must determine whether it costs will be lower if the firm continues with the present practices and pays compensation for the injuries which will result, or whether it should change its current practices and spend resources on safety programs to reduce the cost of injuries. If the reduction in payments (directly by the firm or indirectly by insurance premiums) is greater than the interest on the cost of the safety program, then instituting the safety program is a profitable activity for the firm. 'Safety program' like 'improving quality' is an abbreviation for a whole series of complex firm decisions. A firm does not have a choice of 'safety programs,' each with its known costs and benefits to be taken from a shelf. Rather each firm must study its particular hazards and adapt techniques which have proven to be of value in other situations to its particular conditions and perhaps develop new safety techniques designed for its particular situation.

If a firm should decide to lower the costs of its unavoidable liability for employees' safety by means of improved conditions in its factory (or lower warranty costs by improving quality) the firm must decide specifically which activities it will use. Safety programs can include as component parts better lighting, less noise, non-slip floors, air conditioning, dust control, posters,

shorter working hours, automation of hazardous operations, shielding, speeches by the company's president on the importance of safety, direct drive tools rather than belts and shafts, and dress regulations among other possible specific changes. Each of these 'specific' programs are subject to some adjustments: noise may be reduced considerably or hardly at all, lighting may be improved for the entire factory or merely in certain work areas. The degree of change is determined (in theory) by improving the situation until the interest payments on the cost of the improvement exceed the decrease in payments to employees for injuries over the same time period. The choice problem is complicated further by the interdependence of these specific approaches. Depending on the particular situation in the factory a combination of specific changes may be more or less effective in lowering the costs of the firm's payments for industrial accidents than the sum of the individual programs.

An advocate of workmen's compensation legislation could have listed the various improvements which firms could make to reduce the number and seriousness of industrial accidents and he could have predicted that if the legislation were adopted, firms would incorporate these techniques in their operations to lower their direct payments and/or insurance premiums. The estimates of the firms before the program will be high because they will be based on the currently available means, but the actual cost

will be based on the lowest cost combination of these means and others to be developed and because they might have designed their estimates to demonstrate the impractability of the scheme. The advocate of the general policy could, as shown below, demonstrate that by changing the incidence of the cost of industrial accidents from the employee to the employer, that the total of the expenditures for compensation for industrial accidents and their prevention (cost of the safety programs) would be less than the losses due to injuries and the cost of prevention before the passage of the legislation. This conclusion is true both at the microeconomic (if one includes both the firm and its employees in the same unit) and the macroeconomic level.[5]

Assuming that the worker receives only his actual loss in compensation for an accident, the only change resulting from the legislation is that the employer rather than the employee suffers the losses of industrial accidents. To reduce his payments the employer can make his factory a safer place to work. Since the reduction in payments (the amount of loss due to industrial accidents) exceeds the costs of the safety program, the sum of losses due to industrial accidents plus the costs of the safety programs is less after the institution of workmen's compensation than the losses due to industrial accidents would have been without the legislation. The employer may feel that the legislation has created losses since he had to make payments

(direct or insurance) only after the legislation became effective. But in terms of the microeconomic unit of the firm and its employees the legislation does not create losses. The losses are created by the conditions in the factory; workmen's compensation legislation merely changes the location of the financial responsibility for the losses. The laws have the effect of lowering total losses because the party which must carry the responsibility for the losses has and will exercise profitable options which reduce the number and seriousness of industrial accidents.

The reduction of loss for the entire society is the macroeconomic result of the imposition of liability on the firms for the safety of their employees. By shifting the losses of poor performance to the party capable of changing the performance an incentive of greater profit is created for a better performance. This is true for the individual firm and for the entire economy. A reduction in economic loss for a society will follow if two conditions are met: 1) the policy shifts an existing loss and does not create a previously non-existent loss (e.g., making the payment a penalty rather than compensation) and 2) the loss is shifted to a party capable of profitably taking action to reduce the loss. Both of these conditions were met in the workmen's compensation example and both, as will be shown, of these conditions are met in the trend in warranty changes. A reduction in total cost while beneficial, is not sufficient to justify a program. The

effect of increased responsibility for performance on innovation must also be considered.[6]

Effects of Requiring the Traditional Warranties in Consumer Transactions

The consumer protection program of requiring manufacturers to warrant the performance of their products in a meaningful manner (merchantability and fitness for a purpose), like workmen's compensation legislation, shifts rather than creates losses. The losses, poor performance of consumer products, are created in the production decisions of the manufacturers. As the financial responsibility for product performance by means of required warranties of merchantability and fitness for a purpose is placed upon manufacturers of consumer goods they are faced with the necessity of making several decisions. For each product the manufacturer must decide if its continued production under the new rules will be or could be made profitable. Considering the decisions selected by the editors of the Master Edition of the UCC to exemplify their understanding of the standard of merchantability (see above - Chapter 1, p. 20) the standard of merchantability is clearly conservative. Few, if any, products currently available in the market are so difficult to manufacture that manufacturers would find them impossible to build, at a commercial price, to a level of performance that would meet the expectations of a reasonable man. The

passing of these few products from the market which can now be sold only by means of deceptive advertising creating unmet expectations would likely be mourned by few. Producers of products which function as a reasonable consumer would expect could continue profitably with their current production practices.

The nature of the criteria of merchantability are critical to both the number of products which will be commercially possible and the protection this policy will provide consumers. If the standard were placed quite low the number of changes required of manufacturers would be minimal and the protection of consumers would likewise be minimal. At the other extreme, if any product not incorporating the highest possible standards was not considered to be merchantable, then manufacturers would be greatly limited and consumers would not be able to purchase moderately priced products. Clearly such a policy would not benefit consumers. When a policy is based on a standard of reasonability specific predictions of future decisions is not possible, but two lines of reasoning lead one to doubt that the actual policy of requiring the warranty of merchantability will operate at or near either extreme.

First, the more important judicial references to the standards of merchantability, as listed in the Master Edition of the UCC clearly lie in the center. Courts in the past, and there seems to be no reason to expect a

radical change in the future, have considered that merchantability only requires that the product be able to moderately perform the function for which a reasonable consumer would purchase the produce; a superior performance is not required. Secondly the conservative nature of the standard is also shown in the relationship between implied and express warranties. One might compare a Chevrolet with a Rolls Royce to determine the relevant standards for an 'automobile.' The Rolls Royce purchaser spends several times as much as the Chevrolet purchaser because he has been led to believe that the Rolls Royce is a superior car. This difference in expectations is based on the promotional activities of the manufacturer and dealers. Much of this difference in performance expectations is based on express warranties (e.g., hand polished paint, leather seats, and a car so quiet that the clock is the loudest sound), and a reputation for quality which has been carefully nurtured. The difference in expectations is not based on the qualities covered by the warranty of merchantability (does it work as an automobile). In terms of the implied warranties the standards would be very similar for a Rolls Royce and a Chevrolet. The dissatisfied Rolls Royce owner might be upset because the car did not meet the express warranties or the puff claims of Rolls Royce promotion, although the performance would be considered satisfactory in a Chevrolet. The purchasers' expectations of performance differ because of different express warranties having been created (and

often disclaimed) and different puff statements. If Chevrolet promotion claimed that as a fact a Chevrolet would perform like a Rolls Royce, then the standards would be identical and would include the Rolls Royce express warranties created by the actions of the sellers of Rolls Royce automobiles.

The basic economic effects of imposing an additional liability on manufacturers for the performance of their product is, if poor products are being produced, to create an additional cost to the current method of production and thus to create an incentive to improve the product's performance. The cost of providing the required warranty service (the repair costs would otherwise be paid by the purchaser) is related to several qualities of the product. The manufacturer may reduce his warranty expenses by making his product differently: more performance testing, building in repairability, using heavier materials, more care in design, improved inspection techniques and/or other techniques to improve the reliability and performance of the product. Alternatively he could reduce the claims made for his product. In either case the products' perform- will correspond more closely to the consumers' expectations. These changes will tend to increase the price of the product (which has been improved) to the consumer and it might seem that this policy would harm the poor.[7] But the total cost of the product (sale and maintenance) is the economically important cost. The effect of this policy on the 'total

cost' is considered below. The particular decision as to which means to use to improve the performance so as to lower warranty costs belongs to the manufacturer as he would be responsible for the results under a system requiring meaningful warranties.

Production decisions both before and after any legislative action will be made in an effort to maximize profits. Determining the optimum combination of warranty payments and product improvements occurs when the manufacturer improves the product until the cost of improving the product exceeds the reduction in warranty costs corrected for changes in the price of the product and the number sold. With greater certainty of product performance consumers should have a greater demand for the improved product. The individual manufacturer should be able to sell the same quantity at a higher price, or a larger number at the old price or more likely a somewhat greater quantity at a somewhat increased price.[8] The complexity of the decisions both in production and pricing requires that the manufacturers have considerable discretion in choosing how they adapt to their increased liability for their products' performance due to the required warranties in order that society obtain reasonable rather than arbitrary results. To reduce his losses the manufacturer may either terminate production of a particular product or reduce his responsibility by clearly limiting his claims of performance for his products. The particular alternative chosen

by the manufacturer will depend on if he believes a profit can be made from a product which is accurately represented to consumers. The action taken will vary between different manufacturers within industries.

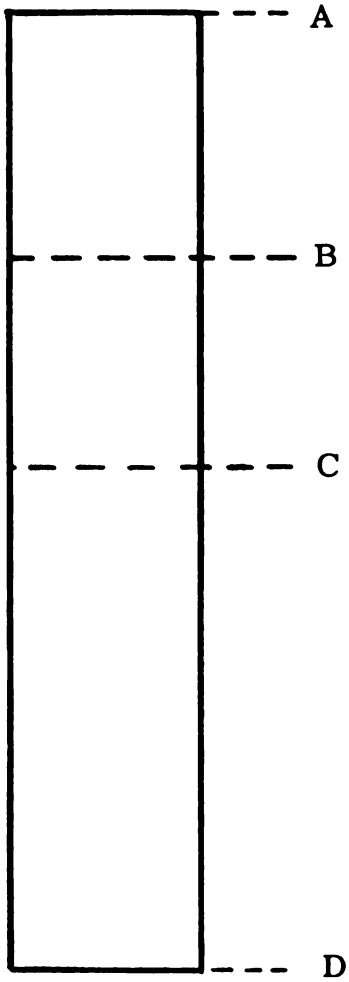
The changes in warranty law merely require manufacturers to warrant the performance of their product to the expectation level of a reasonable man (in the final analysis if the parties cannot reach agreement, a judicial decision). If they take definite action to reduce the consumers' expectation of performance they will reduce their warranty costs.

In terms of the entire range of consumer products only general expectations of changes can be formulated that would follow if the policy were enacted. It would be unlikely that manufacturers will accept the costs of a warranty program under the new policy without making efforts to reduce costs. These adjustments to bring the performance of the product to the level of expectations of a reasonable consumer would be of the form of more accurate advertising, improving the capabilities of the product and increasing the reliability of the product by means of increased testing, better design, greater care in production, and/or reducing advertising claims. All of these efforts would reduce total losses (currently repair or replacement costs to the consumer or warranty costs to the manufacturer) more than such efforts would cost. Any change (which works as planned) the manufacturer were to

make to reduce his warranty costs (which the consumer currently pays when the product is repaired or discarded) would reduce the losses suffered as a result of poor product performance by the microeconomic unit of the manufacturer plus his customer. Since these savings can be summed (the program does not lead to waste at another level) this policy will lead to an improved use of resources.

The effect on profits of imposing meaningful warranty obligations on manufacturers will vary according to their current production and promotion activities and the effect of the change in policy on mass production and innovation.[9] Some products, particularly new products, might experience a large increase in demand with an improvement in consumer confidence and the manufacturers of such products would enjoy a considerable increase in profits. Consumers are hesitant to purchase new products because of the risks of 'bugs' and doubts as to whether the product will actually perform as the manufacturers claim. This policy shifts these risks from the buyer to the seller. Therefore, new products will be more attractive to consumers with the return of the traditional warranties. This increased attractiveness of new products will be reflected in increased demand and probably increased profits for manufacturers of new products who have worked out the 'bugs' and made realistic claims.[10] But the introduction of new products will remain a very risky enterprise. The

lure of greater profits leads firms into the introduction of new products both before and after any change in the responsibility of the manufacturer to his customer. By increasing consumer acceptance of new products this policy should reduce the risks of innovation and lead to the introduction of more products.[11] In general this policy of requiring a meaningful warranty should lead to a moderate increase in profits for those manufacturers producing a product whose performance is well enough known to be warranted. The cost of a commodity is the sum of the original cost and the operating costs (including repair). This policy shifts the repair costs from operating costs to original costs when an effective warranty is required. If the manufacturer takes any action to reduce his warranty costs then that part of the original costs which pays for the warranty (and the costs of improving the product) will presumably (otherwise the manufacturer is raising rather than lowering total cost which is unlikely) be less than the repair costs the consumer would otherwise be paying. While the original cost, which will include a charge for the product improvements and the warranty protection, will be somewhat greater than previously, the total cost which includes the reduction in the repair expenses to be paid by the consumer will be less than previously.



The total cost of a product is AD. The production costs (including profit) is CD. AB represents the operating costs of the product including repairs due to normal wear and tear. Repair costs due to poor production decisions are represented by BC (the magnitude is unknown to the consumer).

At the present time the consumer pays CD to acquire the product and then BC to correct for poor production decisions - his total expenditure (ignoring operating expenses) is BD. The implied warranties would shift BC from the consumer to the producer and thus the purchase price would become BD rather than CD. It might not seem to make any difference if the consumer pays BD in two steps or if the same amount is paid when the product is purchased - but this is incorrect. If the manufacturer can improve his product (increase CD) and in so doing reduce the costs due to his poor production decisions (decrease BC) by a greater amount he will be able to offer his product at a lower total cost (BD will be less) to consumers at the same profit per unit. The lower price should increase sales and profits. Under the present rules manufacturers find it profitable to reduce CD even if BC increases a greater amount increasing total cost to the consumer. While the cost to the consumer will possibly remain BD, under the proposed policy the manufacturer has a profit incentive to improve his product which is not operating under the present rules.

This policy does not add expenses to the total producer-consumer unit. The servicing units required by the producer for providing warranty service already exist and are currently supported by the consumer of products requiring repairs. While some manufacturers will probably create their own repair service (Sunbeam Appliances currently use this approach) at the present time on the base of current practice it appears that the use of

franchised 'independent' repair stations is most economical. Under this policy the manufacturers' improvements to avoid the costs of warranty service would include design for repairability which would allow faster and better repair by the service industry at a lower cost.[12] With a lower total price (assuming the same amount for profit per unit) the manufacturer should be able to sell more units for a greater total profit. This policy by lowering the total cost of consumer goods, rather than damaging the manufacturer, will increase the profits of the producers of consumer goods.

Producers of products which cannot be sold profitably if their performance must be warranted would suffer under the proposed policy. They would naturally oppose the policy, but not on the grounds that it will make producing unsatisfactory products unprofitable. Consumer oriented legislation is generally attacked as imposing governmental bureaucracy on the efficient workings of the market which has yielded the vast array of goods the consumer now has at his disposal. A similar argument, clearly inappropriate, will probably be applied to this policy. While there may be dire predictions of substantial damage if this policy is enacted, very few producers will not be able to adapt to the new rules when their choice becomes either to produce a merchantable product or not to produce a product at all.[13]

Voluntary Warranties

If this result of increased profits or the manufacturer of satisfactory products is accepted, an explanation is required to explain the fact that firms which seek to maximize profits have not voluntarily offered meaningful warranties. One can only automatically conclude that what is true for the industry (increased profitability) is true for the individual firm at the risk of committing the fallacy of composition.[14] Comprehending the situation facing the individual firm, rather than the industry as a whole, is critical to understanding individual voluntary action. If a manufacturer were unilaterally to adopt a policy of offering a meaningful warranty, the sales price of his product would be higher (the total cost to the consumer including sales price and repair costs would be unchanged or lower) than the sales price of the products of competing firms.

If the consumers' consideration of price when making their purchase decisions rests entirely (or largely) on the base of the sale price of the product which is known and ignores repair costs (due to a lack of interest and/or information) then the higher price required for the additional warranty protection will shift consumers to other brands. Shifting away from an improved brand which sells for more, but has a lower total cost works against the consumer. The unprofitability to the individual manufacturer of improving his product probably helps the

poor who would be most likely to make the shift (to the inferior product which would be selling without the warranty protection). If at the other extreme consumers were to base their purchase decisions on the total cost (this possibility assumes that the consumers know the cost of the repairs that will be required) the additional charge for the warranty protection would have no effect, and the changes made by the manufacturer to reduce his warranty costs, if passed to the consumer, would result in a less expensive and more attractive product. The feasibility of offering meaningful warranties on a voluntary basis depends on the information consumers use for making decisions. Since an effective educational program would be essential for a unilateral improvement in quality by a manufacturer to be profitable, such a move is unlikely to occur.[15] Unfortunately the same conditions (consumer consideration of only part of the cost and the need for education) which limit a unilateral improvement in quality favor a unilateral decrease in quality. A decline in the quality of consumer goods is a common complaint of consumer groups. Unilateral voluntary improvements in quality rarely occur because the conditions for their profitability rarely exist.

Consumers do not all buy a product on the basis of total cost of sale price. Some consumers probably buy on the basis of the monthly payment and others on a carefully constructed and reasonably accurate prediction of the total

cost. It is not possible to determine directly where most consumers lie on this range of buying strategies.[16] But the sellers tend to aim their efforts at a middle position as they stress both the price and some 'guarantee' of performance to reduce the consumer's expectation of total operating costs. The manufacturer cannot recognize this diversity of approaches by consumers and make a different offer to each consumer.[17] Rather, he must determine the one offer which will yield the largest profit. The manufacturer can make different offers to different types of consumers by means of a service contract. The manufacturer could sell a product with a minimal warranty to appeal to those consumers most interested in a low sale price, and then offer a service contract at an additional charge to those concerned with total cost.[18] Only if all customers purchase the service contract will the manufacturer have as much incentive to improve his product as he would with required warranties of merchantability and fitness for a purpose. Consumers have additional freedom when given the choice to buy the warranty protection in the form of a service contract. But service contracts and warranties are not substitutes except in the area of keeping the product working. The chief weakness of service contracts compared to required warranties for the consumer is that the consumer cannot return the product for a refund if the performance of the product should fail to meet the expectations of a reasonable man. If the

manufacturer refused to perform his duties properly on a service contract, he would breach the service contract rather than the sales contract as would be the case if the same duty were required by a warranty in the sales contract. The service contract, by adding another contract in addition to the sales contract, serves to isolate the manufacturer from responsibility for promotional claims and poor production decisions which lead to poor product performance, but not to a total breakdown of the product. The sales contract is basic to consumer protection and is unchanged by an additional service contract.

Effect on the Poor

One might argue that the requiring of implied warranties this policy will raise the price of products and thus be burdensome to the poorer households. The sale price alone is a particularly unsatisfactory guide to purchases for the poor. The total cost (sale price and repair costs) are particularly important when one has limited funds to allocate and the poor will benefit from the lowered total cost which would follow from this policy. Few things are less valuable and more frustrating than an appliance which is broken and cannot be repaired because of a lack of money.[19] The poor do not benefit from the availability of defective products.[20] The poor more than the affluent need the protection of the warranties of merchantability and fitness for a purpose in which the

sale price will include a large charge for the warranty protection. The poor are the group least able to pay the costs of working out the bugs in a new product. The major benefit of this policy for the poor might lie in the availability of used products with a better life expectancy than those now available because of the production decisions made in response to the required warranties of merchantability and fitness for a purpose. Requiring the implied warranties by encouraging honest representation of products (with a subsequent improvement in quality) will not be detrimental to the poor.

Summary

There is a tendency in consumer protection discussions to view the problem as a confrontation of consumers and sellers. This study does not propose that sellers make large profits by purposefully misleading consumers. The position of this study is that such practices are bad business leading to reduced profits. Misleading the consumer, while profitable in the short-run for some individual firms, is unlikely to be a profitable long-run strategy for an individual firm or an industry. Consumer confidence is an important factor in sales when the consumer is free to choose between a wide variety of products and brands. The lower profitability of misleading consumers follows from the substantial expenditures which must be made in advertising to create consumer confidence in any claim. Prices might be lower and/or profits greater

if these expenditures could be reduced for the manufacturer who has a product which meets his claims and which can be sold on its merits. But consumer skepticism must be reduced by more then new claims. The policy proposed in this study, by actually making sellers responsible for their claims, can reduce consumer skepticism. Reputable sellers will recognize that this policy is both pro-consumer and pro-seller. This policy will improve consumer satisfaction and will raise the profit levels of firms which supply the consumer with improved products.

While the change to accurate representation is a profitable change, it is not a change which an individual firm could profitably make. It is very likely that consumers would not believe the claims of the manufacturer that he would stand behind his product even if he actually intended to do so. This change, if it is to be profitable, depends on a change in the attitude of consumers. A well publicized change in the law could successfully change the attitudes of consumers as well as their legal position. The lack of individual firms making the change to a meaningful guarantee of their product does not prove that such a change if made in the economy as a whole would lower profits, but rather that given the level of consumer skepticism such a change would be unprofitable for an individual firm.

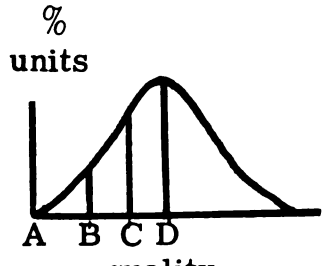
In the case of any change in general law designed to alter the environment of complex decisions of countless

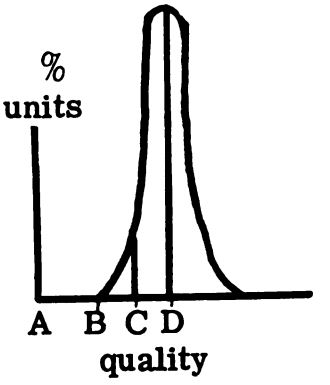
individuals those proposing the change while perhaps unable to make specific predictions should be able to indicate the general directions of change the public could expect. The change removing the contrived nonaccountability achieved by the purposeful abuse of the "freedom of contract" by manufacturers will require them to be directly concerned because they will bear the costs of failure with the performance of their products. This change in commercial law encourages (by making higher profits occur if the manufacturer operates with greater care and concern with his product) certain desirable activities (accurate advertising and the production of merchantable products) and makes the socially dubious activity of creating unmet expectations pointless due to a loss in profit. Since with the warranty protection the product will be sold in terms of its total cost rather than merely on sale price not including repairs, the manufacturers will be concerned with lowering the total costs of a commodity rather than merely the sale price. To increase their profits they will exercise greater concern and care in designing materials, and construction. Deceptive advertising leading consumers to underestimate repair costs will not occur since the product will be sold with the repair costs largely prepaid. Requiring warranties of merchantability and fitness for a purpose will create incentives leading to voluntary decisions by manufacturers which will result in improved products and more accurate advertising. To

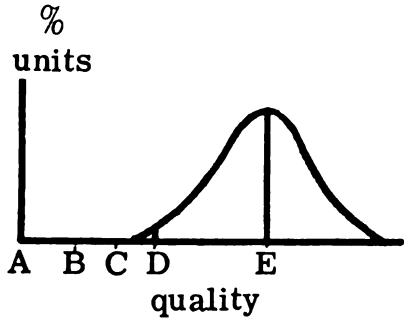
return to Milton Friedman, "It is the responsibility of the rest of us to establish a framework of law such that the individual in pursuing his own interest is, to quote Adam Smith again, "led by an indivisible hand to promote an end which was no part of his intention."

FOOTNOTES

[1]The decision will depend on several factors. Assume a quality distribution of this form. Those units between A and B would be lemons and clearly non-merchantable. Those between B and C would be poor, but subject to some dispute - on these units the consumer could get a partial refund. Those beyond C would be of merchantable quality. The average quality level, D, would be merchantable. Faced with the necessity of making complete refunds for the units between A and B and partial refunds for those units between B and C the manufacturer would make some attempts to reduce the number of units in these groups. The manufacturer could improve the inspection techniques which should make the product more standardized - while the average quality is unchanged, more units are at the average level and fewer units are at the A to B and B to C levels. It is also possible that the manufacturer will improve the materials used or the design employed. In this case the distribution might remain unchanged, but the average quality will be improved and fewer units will be in the A to B or B to C range. The average quality has improved from D to E. The mix that companies will actually use between more inspection, better materials and improved design will vary according to their relative effectiveness and cost. Most firm will probably reduce the number of unprofitable units (those between A and C) by using all of these methods.







[2]There is a difference in the need for protection against losing future income through an industrial accident and making an unfortunate purchase. This difference in need might account for the much earlier adjustment to the special qualitites of an industrial economy of workmen's

compensation as compared to consumer protection. The mechanism of operation, rather than the reasons for the relative development are of interest in this study.

[3]Lawrence M. Friedman and Jack Ladinsky, "Social Change and the Law of Industrial Accident," Columbia Law Review, LXVII, (January, 1967) p. 50.

[4]It would be possible that while workmen's compensation did not seem to seriously disturb production, the requiring of the traditional consumer warranties would upset and severely limit production. The best evidence against any such hypothetical problems is that some firms have been operating very successfully for several years without using disclaimers. Also the industries have not been arguing that any such production problems would result from making disclaimers of implied and express warranties unenforceable. Their arguments have been that disclosure of terms would be a better approach than governmental restrictions on the terms which courts will enforce.

[5]This argument is a slight variation on basic production economics. If the producer has only one way to do a job, method X, then the job will have a particular cost C. If the producer is given a choice of means to do the job, methods X, Y, Z, then the cost will be no more than C. If methods Y and Z are more expensive than method X, then the new options will not be used. In the same manner if method X is some current production procedure with its resulting accidents and method Y is a different production procedure with more expenditures on safety and a reduction is losses due to accidents, then the cost to the employer will not be greater than that of method X if the employer may choose between methods X and Y. Workmen's compensation shifted the employee's loss to the employer making the proper unit of analysis in the determination of the benefits of safety programs the employer-employee unit, rather than just the employer. If the program gives only compensation, then it does not create losses in society; it merely shifts financial responsibility.

[6]As another example consider the case of the Santa Barbara, California oil slick in January 1969. The Federal Government to eliminate such negligence in the future imposed 'absolute liability without cause.' "'Absolute liability without cause' was acceptable because it was fair. If all competitors abide by a regulation, then an individual competitor can live with it." This policy shifted the private cost from being not more than $100,000 work of lost oil to the several millions of dollars damage (the matter is still being settled) other individuals and

communities suffered. Under the new rules the oil men realized that their safety performance was not adequate. See Walter Hickel, Who Owns America, (New York: Paperback Library, 1971), pp. 93-94, (Chapter 4, section 2).

[7]It might be that the poor have a short time horizon (high time rate of discount) and thus desire a lower price now rather than a better performance in the future. Thus the imposing of implied warranties in a meaningful way which result in an increased price (sale) may be damaging the poor. This is a function not only of the time rate of discount, but also of the likely increase in price and the increased protection for consumers. Since the implied warranties cannot be excluded in several jurisdictions at the present time and prices have not risen considerably in these areas (that would have been well publicized!) this change in the remainer of the country seems unlikely to damage the poor by significantly raising the prices of goods. Also the poor often pay the highest prices and their complaints about quality indicate that they do not buy products with little concern for future performance. Not knowing how efficiently to purchase products is not equivalent to not caring how the products perform. See David Caplovitz, The Poor Pay More: Consumer Practices of Low-Income Families, (New York: The Free Press, 1967).

[8]The conclusions for the industry are uncertain because of conflicting effects. Profits would increase as the demand for the product increased since a better product is more attractive compared to all other products than a poorly made product. But an improvement in quality may lead to less demand (fewer units replaced) with the result of over-capacity developing in the industry. The new effect of these two forces depends on the particular product and its market.

[9]This policy should have no effect on mass production, which is using division of labor to achieve greater efficiency. In order to insure the performance of the product the manufacturer may engage in more testing and inspection, but these activities are consistent with mass production. Mass production depends on mass distribution. Requiring manufactures to limit their claims to the actual capabilities of their products might limit the enchanting power of the resulting ads to create demand to such an extent that mass distribution would not be possible. There are several reasons to doubt that such a drop in demand will occur. First, most of the enchanting effects of ads (e.g., the beautiful woman next to the car) are pure puff and therefore not limited by this policy - under this policy the consumer would be assured that his reasonable expectations would be met. Second, all ads will be under

the same rules and an ad which is less enticing may be just as effective if all of the other ads are also less enticing. Third, consumers are going to spend their income - the volume lost in one area will be made up in another. Most important, any drop in volume will be compensated for by closing the least efficient plants (a process which is constantly occurring), not by a return to the handicraft methods of the past. There is no feasible alternative to mass production in a modern economy.

[10]If the costs of testing are excessive leading to a retail price which is too high for profitable production - the failure of the product is not the result of the required implied warranty of merchantability which required the testing. Excessive testing is the result of uncertainty with the performance of the product. If it is expensive to determine if the product will function as promised, then it seems likely that the owning of the products would be expensive if the testing were not done. The poor cannot afford to purchase products with uncertain performance characteristics. Offering the poor the opportunity to buy poorly designed and poorly manufactured products, by relieving the manufacturer of financial responsibility for the performance of his products seems to be of dubious social value.

[11]These warranties should create confidence in product performance in a manner similar to the effect of 'brand names' (when the consumer has had good experience with the product). The consumer will expect products to work (and will be protected if they fail to work). In creating well founded confidence (and substituting to a large extent for brand names) this policy would make market entry easier for new firms and thus stimulate competition and perhaps lower prices.

[12]As a general effect of this policy an improvement in the quality of products would result. However, it might be preferable for products to be impermanent. This conclusion requires that three conditions be met: 1) that advancing technology lower the cost of manufacture much more than repair which remains as a handicraft, 2) that product innovation comes at such a rate that consumer will not want a well-made more expensive product because they will be exchanging it for the new products to come, and 3) that the flow of new type products will restrict the investment consumers will want to make in any existing product, so that they will be able to spend more on the new products. See Toffler, Future Shock, pp. 56-57. In terms of durable consumer products one may question if any of these conditions are met now or likely to be met in the future. "Repairability is subject to much of the same

technology as manufacture. The lack of interest in repairability follows from the limits of voluntary action by manufacturers to improve their product (considered below in the text) rather than any necessary difference between manufacturing and repairing. The second condition may be exactly backwards; if the consumer plans to change products he will be interested in the resale value which will be higher if the second owner expects good performance from the product. The case of the using of impermanent products because they are less expensive is doubtful since if the consumer is going to use the product for any length of time the policy is this argument leads to a more permanent, but less expensive (total cost) product. Toffler's description is accurate in situations of rapid turnover with no concern for resale which is true in women's fashions, but it does not apply to consumer durables where fashion is not a major consideration. Even in clothing fashions there are indications that the youth may not be as susceptible. See Charles A. Reich, The Greening of America, (New York: Bantam Books, 1970), p. 344 (Chapter II).

[13]The elimination of these products might be valuable to society in other ways. Ecological considerations would seem to require that the production of poorly made products which waste resources (frequent replacement) be restricted. Those concerned with maximizing satisfaction would also favor economic restrictions on the production of products which are almost certain to disappoint the consumer. These are certainly grounds for objecting to the production of non-merchantable goods by allowing the use of disclaimers for the warranty of merchantability and fitness for a purpose. However, the justification used in this study is that the shift to not allowing disclaimers of implied warranties is consistent with the principles of high levels of knowledge and freedom of contract in market transactions. These principles are essential for maintaining a satisfactory free market and avoiding governmental controls.

[14]The fallacy of composition is to conclude that what is true for the part is also true for the whole or to conclude that what is true for the whole is true for the part. Thus an industry (the whole) may have an increased gross profit, but each firm (the part) may have reduced profits if more firms have entered the industry.

[15]It is very difficult for a consumer to determine if, on the average, product A with a lower price and more restricted warranty is a better purchase than product B with a higher price and more inclusive warranty. The essential datum is average repair cost and this is not

available nor can it be calculated by studying the product before making a purchase.

[16]Consumers buy particular brands on the base of considerations other than price. A major purpose of advertising is to create different expectations of performance (e.g., status, convenience or economy) which may or may not be accurate. The policy proposed in this paper will make the manufacturer responsible for meeting reasonable interpretation of his claims which should lead to a reduction in brand differentiation (one merchantable washing machine will be very similar to another) and an increase in the importance of price. Therefore this policy will tend to limit consumer considerations in purchasing to expectations, price and total cost.

[17]While the elimination of disclaimers of implied and express warranties reduces the variety in contracts which may be offered consumers, this removal of disclaimers does not limit the variety of products (as long as they function as described) which may be profitably offered. By increasing the consumers' knowledge of likely performance this change in commercial law should lead to greater product diversity. Consumers will no longer discount performance claims (since the manufacturers will be responsible for meeting their promises) and thus the consumers will not consider all the products of a type to be basically identical. Buyer knowledge is the required base for significant product differentiation.

[18]Service contracts would seem to provide the consumer with an estimate of the repair costs he is likely to face. But they may serve, when the consumer is aware of them, to mislead him into underestimating repair costs. The repair industry is a very high fixed cost industry - most of the expenses, equipment and labor, must be paid even if there is no work. The firm could profitably offer a service contract for slightly more than the cost of the parts if this low price led other consumers to purchase the product without a service contract. Those consumers who did not purchase the contract would pay the full price for service which is largely a charge to cover the fixed costs. The service contract may be a promotional effort to increase sales of the units and to thus make more efficient use of the repair services which are largely fixed in size regardless of the demand for the services.

The best datum for determining if service contracts have this misleading effect, average repair costs, is not available to the consumer and probably even the manufacturers often have only a vague idea. Profitability by departments in high fixed cost industries is subject to

considerable change by means of bookkeeping manipulations (is the overhead charged to service contract customers or to regular customers or to both and in what proportion?) Thus profitability figures alone on service contract operations would not provide the information required to test the accuracy of this suggestion. While an interesting idea, using service contract rates to mislead consumers is peripheral to the changes in commercial law considered in this study.

[19]It is unlikely that the poor would knowingly purchase a seriously defective product which they knew was quickly going to fail merely because it is a few percent less expensive. The time rate of discount required to make such a purchase rational is unreasonably high. Buyer naivete is a more reasonable explanation for the purchase of poorly made products by the poor and this naivete is consistent with complaints on the quality of the product.

[20]It is possible, but unlikely, that the poor might benefit from having poorly made products available. This is true if they could repair them at a lower cost than the manufacturer could either repair them or build them so that the products would be merchantable. As a general policy, the poor would probably benefit more from the availability of well built and designed used products than from poorly built new products. The used products would probably be both less expensive and more functional.

LIST OF REFERENCES

LIST OF REFERENCES

American Law Institute. Restatement of the Law of Torts, Volume 2, Negligence. St. Paul, Minn.: American Law Institute Publishers, 1934.

American Law Institute and The National Conference of Commissioners on Uniform State Laws. Uniform Laws Annotated: Uniform Commercial Code, Master Edition, Vol. 1. St. Paul, Minn.: West Publishing Co., 1968.

"Bearings: Roller, Split," Thomas Register of American Manufacturers, Volume 1. New York: Thomas Publishing Co., 1972.

Benfield, Marion W. Jr. Social Justice Through Law: New Approaches in the Law of Contract. Mineola, N. Y.: Foundation Press, Inc., 1970.

Berg v. Stromme 79 Wash. 2d 184 484 P. 2d 380 (Washington, 1971).

Black's Law Dictionary, Fifth Edition. St. Paul, Minn.: West Publishing Co., 1968.

Blake, Roland P. Industrial Safety, Third Edition. Englewood Cliffs, N. J.: Prentice-Hall, Inc., 1963.

"Buyer vs. Seller in Small Claims Court," Consumer Reports, October, 1971.

California. West's Annotated California Codes, Civil Code. St. Paul, Minn.: West Publishing Co., 1973.

Caplovitz, David. The Poor Pay More: Consumer Practices of Low-Income Families. New York: The Free Press, 1967.

Cohen, Morris R., "The Basis of Contract," Harvard Law Review, XLVI (February, 1933), p. 584.

Commons, John R. Institutional Economics: Its Place in Political Economy. Madison, Wis.: University of Wisconsin Press, 1959.

"Detroit Tries a U-Turn on Warranties," Business Week, July 25, 1970, p. 45.

Downey, E. H. Workmen's Compensation. New York: The MacMillan Co., 1924.

Escola v. Coca Cola Bottling Co. of Fresno 24 Cal. 2d 453, 150 P 2d 436. (Cal., 1944).

Federal Trade Commission. Staff Report on Automobile Warranties. Authorized July 20, 1965. FT 1.2:Au 8

Frank, Jerome. Law and the Modern Mind. New York: Tudor Publishing Co., 1936.

Friedman, Lawrence M. and Ladinsky, Jack, "Social Change and the Law of Industrial Accidents," Columbia Law Review, LXVII (January, 1967) p. 50.

Friedman, Milton. Capitalism and Freedom. Chicago: University of Chicago Press, 1962.

Henderson, Gerald C. The Federal Trade Commission, A Study in Administrative Law and Procedure. New York: Agathon Press, Inc., 1968.

Henningsen v. Bloomfield Motors, Inc., 38 N. J. 358, 161 A. 2d 69. (New Jersey, 1960).

Hickel, Walter. Who Owns America. New York: Paperback Library, 1971.

Jaffe, Louis L. Judicial Control of Administrative Action. Boston: Little, Brown and Co., 1965.

Jones, Mary Gardiner and Boyer, Barry B., "Improving the Quality of Justice in the Marketplace: The Need for Better Consumer Remedies," Trial, January-February, 1972, p. 361.

Kendall, M. G. Cost Benefit Analysis. New York: American Elsevier Publishing Co., Inc., 1971.

Kessler, Friedrich, "Contracts of Adhesion - Some Thoughts About Freedom of Contract," Columbia Law Review, XLIII, (July, 1943), p. 632.

Kessler, Friedrich and Sharp, Malcolm P. Contracts: Cases and Materials. Englewood Cliffs, N. J.: Prentice-Hall, Inc., 1953.

Levitt, Theodore, "Quote," Consumer Reports, March, 1972, p. 134.

Llewellyn, Karl N., "A Book Review of The Standardization of Commercial Contracts in English and Continental Law, by O. Prauznitz," Harvard Law Review, LII (February, 1939), p. 704.

"The Long Warranties," Consumer Reports, April, 1964, p. 165.

Maryland. Annotated Code of the Public General Laws of Maryland. Charlottesville, Va.: The Michie Company, 1972.

Massachusetts. Annotated Code of Massachusetts. Charlottesville, Va.: The Michie Company, 1970.

Michigan. Public and Local Acts: Michigan, Session of 1968. Lansing, MI.: Legislative Service Bureau, 1968.

Mill, John Stuart. Principles of Political Economy. Reprints of Economic Classics. New York: Augustus M. Kelley, Bookseller, 1965.

Nader, Ralph. Unsafe At Any Speed. New York: Pocket Books, 1966.

Nader, Ralph and Ross, Donald. Action for a Change. New York: Grossman Publishers, 1971.

"New Products: The Push is on Marketing," Business Week, March 4, 1972, pp. 72-73.

Reich, Charles A. The Greening of America. New York: Bantam Books, 1970.

Ricketts v. Pennsylvania R. Co., 153 F. 2d 757 (2nd Cir. 1946).

Ross, H. Laurence. Settled Out of Court, The Social Process of Insurance Claims Adjustment. Chicago: Aldine Publishing Company, 1970.

Rowat, Donald C. ed. The Ombudsman, Citizen's Defender, Second Edition. Toronto: University of Toronto Press, 1968.

Shepherd, Harold and Sher, Byron D. Law in Society, An Introduction to Freedom of Contract. Brooklyn: The Foundation Press, Inc., 1960.

Singer, Eugene M. Antitrust Economics: Selected Legal Cases and Economic Models. Englewood Cliffs, N. J.: Prentice-Hall, Inc., 1968.

Skinner, B. F. Beyond Freedom and Dignity. New York: Knopf, 1971.

Somers, Anne Ramsey and Somers, Herman Miles. Workmen's Compensation. New York: John Wiley and Sons, Inc., 1954.

Toffler, Alvin. Future Shock. New York: Bantam Books, Inc., 1970.

Trade Cases. Chicago: Commerce Clearinghouse, Inc., 1961, 1965.

U. S. Congress. House. Committee on Interstate and Foreign Commerce. Consumer Warranty Protection. Hearings before a subcommittee of the Committee on Interstate and Foreign Commerce, House of Representatives, on H.R. 261, H.R. 4809, H.R. 6313, H.R. 6314, H.R. 6037, H.R. 10673 (and similar and identical bills) 92d Cong., 1st sess., 1971.

U. S. Congress. Senate. Committee on Commerce, Consumer Products Warranties and Improvement Act of 1971. Hearings before the Consumer Subcommittee of the Committee on Commerce, Senate, on S. 986, 92d Cong., 1st sess., 1971.

U. S. Department of Labor. Bureau of Labor Statistics. Accidents and Accident Rates. Bulletin 490 (August, 1929).

U. S. Department of the Treasury. Internal Revenue Service. Depreciation, Amortization and Depletion. Washington: Government Printing Office, 1972.

U. S. President. President's Committee on Consumer Interests. Suggested Guidelines for Consumer Education: Grades K-12. Washington, D.C.: Government Printing Office, 1970.

U. S. President. Weekly Compilation of Presidential Documents, Richard M. Nixon, March 1, 1971.

Ward's 1972 Automotive Yearbook, Thirty-fourth Edition. Detroit, Mi.: Ward's Communications, Inc., 1972.

Williston, Samuel, "Freedom of Contract," Cornell Law Quarterly, VI (May, 1921), p. 374.

Williston, Samuel. The Law Governing Sales of Goods at Common Law and Under the Uniform Sales Act, Revised Edition. New York: Baker, Voorhis & Co., Inc., 1948.

Williston, Samuel and Thompson, George J. Selections From Williston's Treatise on the Law of Contracts, Revised Edition. New York: Baker, Voorhis & Co., 1938.

Zwarensteyn, Hendrik. Introduction to Business Law, Revised Edition. East Lansing, Mi.: Michigan State University, 1968.