Controlling Standard Contracts — The Israeli Version

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The diverse attempts to regulate standard form contracts within the confines of a given legal tradition have not been very successful. In consequence, there has been a greater readiness to take a comparative approach in this area of law than in others. This article takes such a comparative approach to standard form contracts. Special attention is given to the 1982 amendments to the Israeli *Standard Contracts Law* with the aim of suggesting it as a model for adoption, especially in jurisdictions which lack a policy of administrative control.

La réglementation de contrats-types dans le cadre d'une tradition juridique a fait l'objet de plusieurs tentatives sans toutefois offrir de véritable solution. Face à cette situation, l'examen de ce domaine de droit sous l'angle du droit comparé se révèle tout à fait approprié. L'auteur adopte une telle approche dans l'étude des contrats-types. Il porte une attention particulière à l'endroit des amendements à la *Standard Contracts Law* israëlienne dans le but de retenir cette dernière comme un modèle pour les juridictions qui ne possèdent pas de politique en matière de contrôle administratif.

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Synopsis

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Introduction

The use of standard form contracts is wide-spread in the modern marketplace.[1] Although the standard form is more than a hundred and fifty years old,[2] its recognition as a special type of contract in case law and

[1]See W.D. Slawson, "Standard Form Contracts and Democratic Control of Lawmaking Power" (1971) Harv. L. Rev. 529, claiming that "more than ninety-nine percent of all contracts now made are probably standard form contracts". But see T.D. Rakoff, "Contracts of Adhesion: An Essay in Reconstruction" (1983) 96 Harv. L. Rev. 1174 at 1189 n. 57 to the effect that such a claim is not neeessarily accurate. Rakoff nevertheless "speculates" that standard form contracts constitute a majority. See also S. Deutch, *Unfair Contracts: The Doctrine of Unconscionability* (1977) at 1 n. 1. Almost all cases dealt with under the doctrine of unconscionability have involved standard form contracts.

[2]See generally P.S. Atiyah, *The Rise and Fall of Freedom of Contract* (1979).

legislation began a mere twenty-five years ago.[3] This fact is the more remarkable when it is noted that legal scholars have dealt with this issue from the very beginning of this century.[4]

Despite efforts to regulate this area,[5] a general feeling of dissatisfaction exists with what little has been achieved.[6] The lack of a coherent legal tradition on the subject, together with the conviction that more can be done to regulate it, has led to a greater readiness to take a comparative approach in this area than in others.[7] Some of the solutions adopted by case law and legislation were undoubtedly influenced by foreign legal systems. The Israeli innovations on this subject deserve serious consideration as a model for adoption.

The 1982 Israeli *Standard Contracts Law*[8] is not entirely new legislation.[9] Rather, it is an amended version of the 1964 *Standard Contracts Law*[10] which provides for major changes in concept, theory and practice. The 1964 *Law* was a pioneering statute[11] which regulated standard contracts directly through legislation and by imposing a dual layer of judicial and administrative control. The Israeli legal system was able to deviate at a relatively early stage from the traditional attitude to standard contracts because at that time Israeli contract law was in a stage of transition from the influence

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[3]See, *e.g.*, *Henningsen* v. *Bloomfield Motors Inc.*, 161 A.2d 69 at 86 (N.J.S.C. 1960).

[4]Beginning with R. Saleilles, *De la déclaration de volonté* (1901) at 229.

[5]In Europe, regulation has been achieved by statutory intervention. See E.H. Hondius, "Unfair Contract Terms: New Control Systems" (1978) 26 Am. J. Comp. L. 525. In common law countries control has been accomplished primarily through the implementation of judicial doctrines such as those of unconscionability under U.S. law and "unequal bargaining power" under English and Canadian law.

[6]Many articles support this viewpoint. See for example A.L. Rotkin, "Standard Forms: Legal Documents in Search of an Appropriate Body of Law" [1977] Ariz. St. L.J. 599; R. Dugan, "Standardized Form Contracts — An Introduction" (1978) 24 Wayne L. Rev. 1307; Rakoff, *supra*, note 1. For criticism of European approaches, see Hondius, *supra*, note 5, and of the English *Unfair Contract Terms Act 1977*, see S.M. Waddams, "Legislation and Contract Law" (1978-79) 17 U.W.O.L. Rev. 185 at 193-8.

[7]Many comparative publications deal with this subject. See O. Prausnitz, *The Standardization of Commercial Contracts in English and Continental Law* (1937) and later works.

[8]*Sefer HaHukim* No. 1068 (7 December 1982) at 8 [hereinafter cited as 1982 *S.C.L.*]. The official translation of the *Law* into English has not yet been published. I therefore use the unofficial translation of the Ministry of Justice, incorporating changes based on the official translation of the 1964 version.

[9]See the introduction of the 1981 *Draft* of the *Standard Contracts Law*, prepared by the Ministry of Justice, *Hatza'ot Hok* 5742-1981 at 29.

[10]5724-1964, Laws of the State of Israel, vol. 18 at 51 [hereinafter cited as 1964 *S.C.L.*].

[11]With the exception of the Italian law (Italian Civil Code (1942) ss 1142 and 1361). See G. Alpa, "Protection of Consumers Against Unfair Contract Terms: Legislative Patterns of Controlling Adhesive Contracts in Europe" (1979) 15 Willamette L. J. 267 at 270-2.

of English common law to a more original statutory pattern,[12] and therefore was not bound by traditional concepts. Once the need for special control was recognized,[13] it was quickly implemented through a novel form of legislation.

Initially, the 1964 *Law* had little success. Since it was a pioneering legal device, there were no case law precedents to follow and no other statutes with which it could be compared. Caution was inherent in its drafting, primarily due to lack of experience. As a result, some of the potential advantages of such legislation were not realized.[14] Two decades of conservative interpretation by the courts almost reduced the statute to a "dead letter".

Meanwhile, during the 1960's and 1970's, recognition of standard forms as a separate type of contract grew in both case and statutory law in many countries,[15] and by the 1980's the time was ripe for substantial amendment to the Israeli *Law*.[16] Academic criticism of the statute and its interpretation by the courts finally led to a new draft[17] which was enacted in December 1982 and came into force in June 1983.

The innovations and amendments to the *Standard Contracts Law* were based on experience gained from fifteen years of practice with the original version, and a new conceptual framework. The new *Law* provides for a system of guided judicial review instead of regular judicial review, and strengthens the device of pre-screening standard contracts in the Tribunal established for this purpose. The definitions in, and scope of, the statute are clarified to facilitate application of its provisions.

I. The Definition and Scope of Standard Contracts Under Israeli Law

One of the contributions of the Israeli *Law* to the area of standard contracts is the clear definition of the subject, and the precise delineation of the scope and purpose of the *Law*. The definition is of great importance

[12]See A. Bin Nun, "The Israeli Law on Standard Contracts" in *Israeli Reports on the Eighth International Congress on Comparative Law* (1970) 107 at 108.

[13]G. Tedeschi & A.W. Hecht, "The Problem of Standard Contracts" (1959) 16 HaPraklit 132 [a report of the Committee appointed by the Ministry of Justice in Hebrew].

[14]See S. Deutch, "Standard Contracts Act: Failure and Recommendation" (1980) 1 Bar-Ilan Legal Stud. 62 at 65-8 [in Hebrew].

[15]See *supra*, note 5.

[16]See Deutch, *supra*, note 14; D. Friedman, "Reflections on the Topic of Standard Contracts" (1979) 6 Iyunei Mishpat 490 [in Hebrew]; D. Kretzmer, "Notes on the Standard Contracts Law, 5724-1964, in View of its Amendment" (1970) 3 Mishpatim 414 [in Hebrew]; G. Shalev, *Exemption Clauses* (1974) at 36-44 [in Hebrew].

[17]The influence of the above articles on the new *Draft* were mentioned in the official introduction to the *Draft*. See *supra*, note 9 at 28. Such an acknowledgement by the Ministry of Justice is quite rare in Israeli legislation.

in statutory law,[18] because only those agreements defined as standard contracts will be subject to the special rules, while other contracts will continue to be subject to the general contract doctrines.[19] The definition must therefore reflect the special nature of standardized agreements.[20]

There is a considerable difference between the statutory attitude towards definition and the case law approach to it. Statutory provisions designed to protect against unfairness in standard contract terms can establish clearly the parameters of the subject. Conversely, under case law, there is no precise definition of the term; there is not even agreement as to which term should be used to identify this type of agreement. And although many scholars prefer the term "adhesion contracts" to "standard contracts", there is no agreement as to what "adhesion contracts" are. While some consider them to be identical to standard contracts, others consider them to be only one type of standard contract.[21]

The confusion is possible under a case law doctrine which is still evolving. However, such problems need not occur under a statutory definition, where simplicity and consistency can be achieved through careful drafting.

A. The Definition

The term "standard contract" is defined in Section 2 of the Israeli 1982 *Standard Contracts Law* as follows:

> Standard contract means the text of a contract, all or part of the terms of which have been determined in advance by one party in order to serve as conditions

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[18]Under U.S. law there was no clear definition of either standard contracts or adhesion contracts, since the principal doctrine in this area — unconscionability — was never confined to standard agreements. For support for the view that standard contracts are part of the doctrine, see Dugan, *supra*, note 6 at 1308; E.A. Dauer, "Contracts of Adhesion in Light of the Bargain Hypothesis: An Introduction" (1972) 5 Akron L. Rev. 1; Deutch, *supra*, note 1 at 56-7; D. Yates, *Exclusion Clauses in Contracts*, 2d ed. (1982) at 271-5. But see A.A. Leff, "Unconscionability and the Code — The Emperor's New Clause" (1967) 115 U. Pa L. Rev. 485.

[19]For a variety of such controls, see J. Swan & B.J. Reiter, *Contracts: Cases, Notes and Materials*, 2d ed. (1982). About a third of the casebook is devoted to this subject.

[20]See *infra*, notes 26-34 and accompanying text.

[21]See the variety of conflicting definitions in both academic writings and case law: F. Kessler, "Contracts of Adhesion — Some Thoughts About Freedom of Contract" (1943) 43 Colum. L. Rev. 629; A. Lenhoff, "Contracts of Adhesion and the Freedom of Contract: A Comparative Study in the Light of American and Foreign Law" (1962) 36 Tulane L. Rev. 481; I. Macneil, *Contract Exchange Transactions and Relations*, 2d ed. (1978) at 445-7; Rakoff, *supra*, note 1 at 1177; *Henningsen* v. *Bloomfield Motors Inc.*, *supra*, note 3; *Neal* v. *State Farm Insurance Co.*, 188 Cal. App.2d 690, 10 Cal. Rptr 781 (1961); *Graham* v. *Scissor-Tail Inc.*, 28 Cal.3d 807, 171 Cal. Rptr 604, 623 P.2d 165 (S.C. 1981).

> of many contracts between him and persons unidentified as to number or identity.[22]

This definition is completed by defining the word "term" in a standard contract as follows:

> "Term" means a term in a standard contract, and includes a term referred to in the contract and any other term forming part of the bargain even where it is not expressly stated to be so in the contract itself, but does not include a term specially agreed upon by a snpplier and a customer for the purpose of a particular contract.

The three basic elements of a standard form contract are terms which are: (a) fixed in advance by one party only; (b) intended to be used in nıany future contracts; and (c) not subject to negotiation. A contract which does not fulfil these three requirenıents is not subject to the statute.[23]

B. Analytical Background

These three elements comprise the defining features of standard contracts. The definition is not burdened with unnecessary details. The first two elements are the tools by which the standard contracts market operates. Contract standardization and advance preparation of terms by one party facilitate the inclusion of harsh terms. Advance drafting permits the stipulator to replace statutory and common law dispositive provisions with his own privately-made law. The third elenıent, lack of real choice, is the method by whicli tlie public at large is compelled to adhere to the drafter's will. This third element is also the justification for intervention in sucli contracts.[24]

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[22]The translation is based on the 1964 version and the unofficial 1982 translation. See *supra*, note 8.

[23]There is great similarity between the German definition and that of the Israeli statute. The German definition appears in Section 1 of the 1976 *Standard Contract Terms Law*:

> (i) Standard contract terms are all those contractual provisions drawn up for a large number of contracts which one contracting party (the proponent) presents to the other contracting party for his assent. It makes no difference whether the stipulations are contained in a separate instrument or included in the contract itself, what their scope may be, what type of writing is used, or what the form of the contract ınay be.
>
> (ii) Standard contract terms are not involved when and insofar as the contractual conditions are individually negotiated between the parties.

The text was translated by Nina Moore Labson. This translation has been used in every English article on the subject. For the full translation, see, *e.g.*, (1978) 26 Am. J. Comp. L. 568.

[24]This does not mean that there are no advantages or benefits to using standard contracts. See Deutch, *supra*, note 1 at 1, 2 and 253 n. 46; *Restatement (Second) of Contracts* (1979) s. 211, Comment (a). *Contra*, Rakoff, *supra*, note 1 at 1204-6, 1226-8 and 1230-4. On the need for control, see Kessler, *supra*, note 21; K. Llewellyn, *The Common Law Tradition* (1960) at 362; Deutch, *ibid.* at 7-10.

The Israeli statute clearly acknowledges that the standard contract differs considerably from traditional types, but nevertheless is still a contract. Section 24 of the *Law* stipulates that other laws which control contract terms in general still apply. In the 1980 bill which proposed adoption of an Israeli code of civil law, the *Standard Contracts Law* is regarded as one of the contract statutes.[25]

C. *Broadness of the Definition*

The *Law* applies to standard terms, as well as to contracts which are wholly standardized.[26] This approach prevents stipulators from circumventing the *Law* by drafting in advance the most stringent terms and leaving only less important ones open to negotiation. The definition refers to the "text of a contract", even if not yet actually used. This clarification was necessary to permit "abstract control" of standard contracts[27] even before they have been used.[28]

The definition of "term" encompasses both the terms referred to in the contract and other matters which form part of the bargain, even if they are not mentioned in the contract. This part of the definition also encompasses unsigned contracts[29] such as guarantees[30] and ticket purchases.[31] The definition embraces documents and terms which become part of the contract by way of notice.[32]

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[25]*Hatza'ot Hok, Le-Arihat Kovetz Dinei Mamonot*, 5740-1980 [in Hebrew]; an unofficial translation is available, *Codification of Civil Laws*, 5740-1980. The 1964 *Standard Contracts Law* appears among the list of other contract statutes. The list does not include consumer protection statutes, since they are not considered to be part of the civil law.

[26]See *supra*, note 22 and accompanying text.

[27]For the meaning of "abstract control", see *infra*, notes 75-9 and accompanying text. This explanation was offered in the "Explanatory Note" to the *Proposed Standard Contracts Act, Hatza'ot Hok* 5742-1981 at 30.

[28]Another possible interpretation is that the statute refers to the "text" of a standard contract to indicate that, if the text of the contract is prepared in advance (even if typed or printed for every transaction), it is still a standard contract — thereby precluding any circumvention of control by the statute. That situation is probably uncommon and had not been contested in Israeli courts at the time of the drafting of the *Law*.

[29]See Rakoff, *supra*, note 1 at 1177. Only signed documents are included under his definition of adhesion contracts.

[30]The guarantee becomes part of the bargain by way of notice. See Shalev, *supra*, note 16 at 52-8.

[31]Israeli law, even after the enactment of the *Contracts (General Part) Law* 5733-1973, Laws of the State of Israel, vol. 27 at 117, generally follows the English law on the subject. See Deutch, *supra*, note 14 at 73. The leading English cases on point are *Parker* v. *South Eastern Railway Co.* (1973), 2 C.P.D. 416, 36 L.T. 540 (C.A.) and *Thornton* v. *Shoe Lane Parking Ltd* (1970), [1971] 1 All E.R. 686 (C.A.). For U.S. Law, see *Restatement (Second) of Contracts* (1979) s. 211(1), Comment (d) and "Reporter's Note" to Comment (d). For the Canadian viewpoint, see *Heffron* v. *Imperial Parking Co.* (1974), 3 O.R. (2d) 722, 46 D.L.R. (3d) 642 (C.A.).

[32]See G.H. Treitel, *The Law of Contract*, 6th ed. (1983) at 150-6 regarding joinder of documents either by express reference or with no express reference.

A different approach to this issue is taken by Section 2 of the German *Standard Contract Terms Act*,[33] which presents detailed rules as to when a term becomes part of a standard contract. The rules require that there be a reasonable chance to read and understand the terms before they are incorporated into the contract. This section is limited solely to consumers,[34] and the regular rules remain applicable to merchants.

D. Elements Not Required Under the Definition

The definition is not limited to contracts entered into in a monopolistic situation.[35] Nor is superiority of bargaining power required by the definition,[36] although it probably exists in most instances. In one decision,[37] the Israeli Supreme Court decided that courts should intervene in standard contracts primarily when a monopolistic situation exists. In a later decision,[38] however, this approach was not followed.[39]

The definition does not mention elements such as small print, unintelligible language, the fact that the contract was not read, and related matters. Although these factors contribute to the problem, they are not the cause of it. Reading and understanding the terms does little good if the adherent party has no power to change them. It is clear from the definition of "term" under the Israeli statute that only specific negotiations and agreement can exempt a term from the application of the act, and mere knowledge of its contents is insufficient.[40]

The statute is not limited to consumer transactions.[41] It is of a general nature and covers commercial transactions as well. The term "consumer"

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[33]See O. Sandrock, "The Standard Terms Act 1976 of West Germany" (1978) 26 Am. J. Comp. L. 551 at 558-60.

[34]Section 24 of the German statute.

[35]Nor does such a requirement appear in the German statute.

[36]See A. Corbin, *Corbin on Contracts*, Supp. ed. by C.K. Kaufman (1984), Part I, s. 559C at 571-5 to the effect that bargaining power is useless unless there is a genuine opportunity to use that power. Therefore, it is the nature of the agreement which is important, not the relative power of the parties.

[37]C.A. 764/76 *Shimoney* v. *Mifalei Rekhev Ashdod Ltd* (1977), 31(3) P.D. 113.

[38]St C.A. 1/79 *Keshet Cleaning Enterprises Ltd* v. *A.G.* (1980), 34(3) P.D. 365.

[39]*Ibid.* at 374.

[40]In C.A. 280/71 *Gidon* v. *Hebra Kadisha* (1972), 27(1) P.D. 10, the adherent party knew and understood the term later invalidated in court; he even tried to change it, but to no avail. Under the facts of this case he had no real choice of applying to another supplier. Knowledge of a term in an adhesion contract has little value if no alternative choice is open to the adherent.

[41]See G. Shalev, "Government as a Party to a Standard Contract" (1983) 12 Mishpatim 595 at 605-6 [in Hebrew].

is not even mentioned in the *Law*.[42] Although the problem of standard contracts is more critical in consumer transactions, it also exists in commercial cases.[43]

The 1982 statute removed two requirements which were included in the 1964 version, where a standard contract was defined as "a contract for the supply of a commodity or service". The 1964 version proved to be an obstacle because in several instances the contracts under consideration could hardly be described as for either supply of a commodity or of a service. In one of the early cases,[44] the court decided that the sale of a lottery ticket provided neither a commodity nor a service, and therefore the ticket's exemption clause was not subject to the *Law*'s control. In later decisions this interpretation was overruled,[45] and other problematic transactions were also recognized as contracts for the supply of services.[46] It became evident, however, that the section caused unnecessary complications, and this part of the definition was removed from the 1982 version.

Another element of the 1964 statute discarded under the 1982 *Law* was the requirement that standard terms be fixed in advance "by the person supplying the commodity or service". This meant that terms which were dictated by the purchaser rather than the supplier were not subject to the *Law*.[47] Accordingly, the case of a giant food-processing company which presented its standard contracts to farmers who would then have to adhere to the terms if they were to sell their products to industry[48] would have been exemptcd from the *Law*'s control. In order to avoid this result, the 1982 version defines a supplier as the person who proposes the standard terms of the contract, regardless of his status as seller or purchaser.

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[42]See the German statute which, although general in nature, includes several sections effective only in consumer transactions. See in particular ss 2 and 10-2. And see Sandrock, *supra*, note 33 at 556.

[43]Under the U.S. doctrine of unconscionability a similar question arises. See S. Goldberg, "Unconscionability in a Commercial Setting: The Assessment of Risk in a Contract to Build Nuclear Reactors" (1983) 58 Wash. L. Rev. 343 at 346-9, strongly supporting the view that unconscionability should also be applied in a commercial setting. See also Deutch, *supra*, note 1 at 57 and 70-1.

[44]C.A. 604/69 *Green* v. *Mifal Hapais* (1971), 25(1) P.D. 401.

[45]C.A. 508/71 *Holawy* v. *Mifal Hapais* (1972), 27(1) P.D. 38; C.A. 782/72 *Naiem Fares* v. *Mifal Hapais* (1977), 32(1) P.D. 770.

[46]See *Gidon* v. *Hebra Kadisha*, *supra*, note 40, regarding a form authorizing the erection of a gravestone; *"Zur" Hebra Lebituha* v. *Wesung* (1971), 26(1) P.D. 190.

[47]But see Rakoff, *supra*, note 1 at 1177 to the effect that according to his definition of adhesion contract, the main obligation of the adhering party is the payment of money.

[48]That was the case in the landmark decision in *Campbell Soup Co.* v. *Wentz*, 172 F.2d 80 (3d Cir. 1948).

E. Negotiated Terms

The definition of "term" excludes from the scope of the statute those terms "specifically agreed for the purpose of a specific contract". The rationale behind this expression is evident: when a term is agreed upon between the parties there is no ground for deviating from traditional contract law doctrines.[49] However, there is a danger that the definition might be too narrowly interpreted. The Italian experience with standard contracts revealed that the requirement that certain conditions are invalid unless specifically approved in writing was overcome by a simple signature of the adherent party regardless of any real understanding or approval of the actual terms. The result was that the Italian regulations were of little help to consumers.[50]

The reasonable interpretation of this definition is that only when a meaningful alternative exists, and actual consent is reached, will the terms be considered to be specifically agreed upon. If there is no possibility of changing or negotiating a term in return for other concessions, it cannot be considered a negotiated term. Some questions are still left unresolved. Who must then prove that a term was negotiated? What alternatives must be proven to have been available in order to exempt a term from control by the statute?

The German statutory approach to these questions provides some direction. The burden of proof that the terms were "individually negotiated" lies with the proponent. In order to exempt individually negotiated terms from the statute, it must be proven that the other party had an opportunity to change them. It is possible that interpretation of the Israeli statute will resemble that of the German one, as the definitions contained in the two are quite similar.[51]

F. Terms Not Subject to Control by the Statute

Section 23 of the Israeli statute exempts four kinds of terms from the act. Where a term: (1) determines the monetary consideration which the customer must pay, (2) conforms with conditions laid down or approved by an enactment, (3) confirms an international agreement to which Israel

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[49]See K.F. Berg, "The Israeli Standard Contracts Law 1964: Judicial Controls of Standard Form Contracts" (1979) 28 Int'l & Comp. L.Q. 560 at 566.

[50]For criticism of the Italian approach to standard contracts see G. Gorla, "Standard Conditions and Form Contracts in Italian Law" (1962) 11 Am. J. Comp. L. 1 and Alpa, *supra*, note 11.

[51]See *supra*, note 23, regarding the similarity of the second part of the German definition to the latter part of the Israeli definition of "term". This issue was never raised in the courts under the 1964 statute, which is identical to the 1982 version on this point.

is a party, or (4) forms part of a collective labour agreement, it is not subject to the *Law*. The latter three exceptions are not of major significance. A collective labour agreement is negotiated by representatives of both parties and therefore cannot be regarded as a standard contract. When a contract conforms to legislation or formally approved international agreements, it is not a normal case of standard terms being imposed by one party.

The first provision is, however, of great importance, since it draws a clear line between standard terms and visible terms. The monetary term is distinguishable from other standard contract terms by its greater visibility. It is one of the few terms in a contract about which the customer will normally be knowledgeable, and also one of the few in respect of which competition exists between different sellers. Even when the price is fixed in advance, the contractor knows exactly what he is entering into. His assent is real, and there is no surprise with regard to this provision. This does not mean that price cannot be unfairly imposed on a party to a contract, but such imposition is not part of the phenomenon of standardized contract terms and should therefore be dealt with under other contract doctrines.

II. Judicial Review and Abstract Pre-Screening of Standard Contracts Under Israeli Law

A. The Purpose Clause

The first section of the 1982 *Standard Contracts Law* states: "The purpose of this law is to protect customers from prejudicial terms in standard contracts." It apparently adds nothing to the *Law*'s detailed provisions, and one might ask, therefore, what objective is served by this purpose clause. The answer can be found in the history of the judicial application of the 1964 *Law*.

The difficulties encountered in the application of the 1964 *Law* also serve as a good example of the problems involved in regular judicial review. The 1964 statute empowered the courts to invalidate a restrictive term[52] in a standard contract when it appeared to be "prejudicial to customers or gives an unfair advantage to the supplier (which is) likely to prejudice customers".[53] A similar provision also exists under the 1982 version.[54] The

[52]Under the 1964 *Law* not every term was subject to judicial intervention, only those defined as "restrictive terms".

[53]1964 *S.C.L.*, *supra*, note 10, s. 14.

[54]1982 *S.C.L.*, *supra*, note 8, s. 3.

term "prejudicial" is essential in both *Laws*[55] and parallels the unconscionability clause of America's *U.C.C.*

Of seventeen cases reported on the subject[56] up to 1980, in only two instances[57] was a standard contract clause invalidated as "prejudicial".[58] The court in most cases preferred to resort to other doctrines, such as insufficient notice,[59] public policy[60] and good faith,[61] to aid customers, rather than rely on the statute specifically enacted for the purpose.

The case law under the 1964 *Standard Contracts Law* exposed some of the basic deficiencies of non-guided judicial review of standard contracts. Those decisions are evidence of inconsistent application of the doctrine, preference for other doctrines, adherence to obsolete ideas on freedom of contract, and a clear trend towards conservatism. Statutory guidelines cannot replace judicial discretion, but a declaration of the *Law*'s purpose can at least eliminate some of these problems. The purpose clause clarifies for the courts the need to concentrate on the fairness of the transaction.

B. The Broad Scope of Application

Part of the conservative attitude revealed by the case law under the 1964 *Standard Contracts Law* was due to various restrictions governing the application of judicial review. Under the 1964 *Law* not every term was subject to judicial intervention. Section 15 enumerated under the title "restrictive terms", a list of nine types, and only those terms which fit into one of the listed types was subject to judicial review. This limitation was designed to assure suppliers that not every term in a standard contract would be subject to examination. However, this resulted in the exemption from control of some harsh terms. This enumeration of types of terms was severely criticized by several commentators,[62] and it was removed from the text of the 1982 *Standard Contracts Law*.

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[55]The term "Mekapcah" which can be best translated in English as "prejudicial" appears in ss 3, 4, 12, 14, 16, 17, 19, 20 and 21 of the 1982 *S.C.L.*, *ibid.*

[56]See Deutch, *supra*, note 14 at 86-102.

[57]Mo. 545/67 *Ornan* v. *Israel Lands Administration* (1968), 67 P.M. 284; C.A. 280/71 *Gidon* v. *Hebra Kadisha*, *supra*, note 40. In three other cases it was relied on as one of the grounds for invalidation. Deutch, *ibid.* at 86 n. 96.

[58]Even more surprising is that in both instances, the invalidated terms attempted to limit freedom of religion, which is certainly not normally an object of standard contracts.

[59]C.A. 285/73 *Lagil Trampolin* v. *Nahmias* (1974), 29(1) P.D. 63.

[60]For example, C.A. 493/69 *State of Israel* v. *Hadad* (1970), 24(1) P.D. 7; C.A. 764/76 *Shimoni* v. *Mifalei Rekhev Ashdod Ltd*, *supra*, note 37.

[61]C.A. 148/77 *Rot* v. *Yeshufe* (1979), 33(1) P.D. 617.

[62]See Deutch, *supra*, note 14; Friedman, *supra*, note 16; Berg, *supra*, note 49.

The breadth of judicial review under the 1982 *Standard Contracts Law* gives it a considerable advantage over legislative control, which is limited solely to a list of forbidden terms.[63] Section 3 of the 1982 *Law* empowers the judiciary and the Tribunal to invalidate or change terms prejudicial to customers, but when doing so they must also take into account other terms of the contract and all related circumstances.

Section 3, which is the general provision of the 1982 *Standard Contracts Law*,[64] centers attention on one basic phrase, "prejudicial to customers". The same phrase was used in Section 14 of the 1964 *Standard Contracts Law* and therefore judicial interpretation of that *Law* is relevant to the new statute. In one decision, the term "prejudicial" was interpreted as follows:

> The word "prejudicial" is a degrading word. It includes the requirement that the limiting of a contractual right will be distasteful. There is a need that the exemption be unjustifiable and especially a provision which does not come to protect legitimate economic interests of the other party — the supplier.[65]

In the past, a question which caused considerable dispute in the Israeli Supreme Court[66] was whether such a term necessarily had to be unfair to customers at large, or whether it was sufficient for the unfairness to be caused to a single customer. Today, this issue is specifically dealt with by Section 19, which covers judicial review. Section 19(b) indicates that courts should take into account the special circumstances of the case at issue, a clear indication that a clause which is prejudicial to an individual customer under the circumstances of the transaction should be invalidated even when not prejudicial to customers at large. In the Tribunal, specific circumstances cannot be considered because only abstract control is involved, and the test to be applied is whether the term is potentially prejudicial to customers.

The power of the courts and the Tribunal to review terms in standard contracts is now both general and virtually unlimited.

C. Presumptive Unenforceability

Section 4 of the 1982 *Standard Contracts Law*, which provides that ten types of terms are presumptively unenforceable, is one of the most striking innovations in the new *Law*. It does not resort to a list of forbidden clauses,

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[63]See Ministry of Justice of Israel, *Hok HaHozim HaAhidim 5743-1982: Divrei Hesber* (1984), an unoffical explanation of the *Law* at 25-6 [hereinafter cited as the 1984 *Memorandum*]. A translation is also available, *Standard Contracts Law 5743-1982: Memorandum.*

[64]There are special provisions which specifically empower the Tribunal (ss 17-8) and the courts (s. 19) to invalidate prejudicial clauses. See *supra*, note 8.

[65]*Green* v. *Mifal Hapais*, *supra*, note 44 at 401 *per* Justice Witkon [translated from the Hebrew, emphasis added].

[66]See Deutch, *supra*, note 14 at 96-8.

which precludes flexibility and discretion in judicial decisions. Instead, it clearly indicates which terms are unenforceable in the absence of special circum,stances. The transfer of the burden of proof should avoid some of the problems encountered under the old *Law*, where, for example, arguments that a standard term was unfair were rejected because the buyer could not provide sufficient evidence in support of his claim.[67]

Section 4 outlines ten types of term which are *prima facie* prejudicial. These, in turn, are divided into two categories. Some terms are presumptively unenforceable *per se*, others only when unreasonable. The first group includes subsections 4(1), 4(4), 4(6), 4(7), 4(8) 4(9), 4(10) or portions of them. The second group includes subsections 4(1), 4(2), 4(5), 4(6), 4(9) or portions of them. All these provisions primarily concern three sorts of terms: (1) those which limit the supplier's liability or limit the customer's rights under law or contract, (2) clauses limiting a customer's right to resort to the courts and terms which would restrict his reliance on the rules of evidence, and (3) terms which limit the customer's freedom to contract or permit the supplier to change the contract unilaterally.

Subsections 4(1) and 4(6) are of special interest.[68] These subsections presumptively invalidate clauses which exempt the supplier from liability under the law or which limit a customer's right to remedies. This means that limitations on statutory dispositive provisions in standard contracts are presumptively unenforceable.[69] For instance, under the *Israeli Contracts (Remedies for Breach of Contract) Law*[70] the injured party has the right to specific enforcement or to rescind the contract together with the right to compensation. When a supplier includes in a standard form a provision invalidating one of those remedies, it will be *prima facie* invalid.

The 1982 *Standard Contracts Law* does not specifically explain how these presumptions can be overcome. The courts must undertake this duty. There are, however, some guidelines in the *Law*. Section 3 states that each term should be examined in light of "the terms of the contract in their

[67]See Deutch, *ibid.* at 88 to the effect that in six cases this claim was rejected because it was not properly presented in court.

[68]See *supra*, note 8. Another interesting provision is subsection 4(3), which deals with a term transferring the supplier's liability to a third party. In recent years some building construction enterprises have transferred their liability to unknown contractors. In many of these instances, such a clause will also be classified as an exemption to statutory liability and therefore also subject to subsection 4(1).

[69]See O. Lando, "Standard Contracts: A Proposal and a Perspective" (1966) 10 Scandinavian Stud. in Law 129 at 136 to the effect that as early as 1964 a German decision stated that "a rule belonging to the *jus dispositivum* or private law becomes a required part of the contract, *jus cogens*, when it is a question of a contract of adhesion". This approach was later adopted by the German legislature. Under Israeli law, however, it would only be presumptively unenforceable.

[70]5731-1970, Laws of the State of Israel, vol. 25 at 11.

entirety and of all other circumstances". This points to two methods for repudiating the presumption of unenforceability. One is to prove that the circumstances of the case justify the term in question. For example, a term limiting the liability of merchantability in used goods can be justified because the goods are used and the exemption clause is known to the purchaser. Alternatively, other terms in the contract may justify the exemption clause. It is unclear, however, whether every term must be considered, or only those which are subject to control by the 1982 *Standard Contracts Law*.[71] On the other hand, Section 3 specifically refers to contract terms in their entirety, thereby permitting consideration of every term, even those not subject to the *Law*.

Other terms of a standard contract can certainly be taken into account when judging the validity of standard terms. Such other terms should be considered when they provide customers with benefits not available under existing law and those benefits constitute a fair equivalent for the displaced protection.[72] For instance, when a supplier displaces a customer's right to repudiate the contract by giving him the right to free repairs for a year and such a right does not exist under the relevant law, it is possible that the limitation will be upheld. But a right to free repairs scarcely justifies exclusion of consequential damages if there is not proportional value between the right conferred and that taken away. In exceptional cases, even the exclusion of consequential damages may be justified. For example, in a commercial setting where there is no equivalence between the value of the transaction and possible damage, an exemption can be justified.[73] This will depend upon reasonable commercial usage and the existence of a commercial rather than a consumer setting. It is clear, however, that the presumption cannot easily be rebutted. The supplier must prove that the standard form is reasonably balanced in order to displace the presumption of unenforceability.

It is possible to overcome the presumption of unenforceability in government contracts when the purpose of an exemption clause is to protect legitimate state interests. For example, subsection 4(4) deals with a term which allows the supplier to change the terms of the contract after it has been signed. The right of government to renegotiate contracts has been upheld in American courts and can be equally justified under this *Law* when

[71]See *supra*, note 52 and accompanying text.

[72]See Dugan, *supra*, note 6 for a similar text.

[73]See *Photo Productions Ltd* v. *Securicor Transport Ltd* (1980), [1980] A.C. 827, [1980] 1 All E.R. 556 (H.L.).

the term is a necessary outcome of economic reality.[74] When such a commercial practice is based on reasonable economic interests it may possibly overcome the presumption.

The second category of provision under Section 4 presumptively invalidates specific terms when certain rights or duties are unreasonably restricted. For instance, in subsection 4(1), a term which unreasonably limits the liability of the supplier under the contract is presumed to be prejudicial. The reason for the distinction between limiting statutory dispositive rights and limiting contractual rights is quite evident. There is an obvious difference between taking away statutory rights enacted to achieve a balance between the parties and restricting rights created by the contract itself. In the latter case, unless the restriction is unreasonable the contract should be regarded only as creating more restricted rights, rather than as one without this limitation.

D. Abstract Pre-Screening by the Tribunal

The most original innovation of the Israeli *Standard Contracts Law* is the power of a Tribunal to approve or invalidate standard contract terms. This method of control was originally provided for by the 1964 *Standard Contracts Law.* However, it was unsuccessful, and substantial amendments were introduced in the 1982 *Standard Contracts Law.* The basis of the control system under both acts is the power of the tribunal (in the past a Board[75]) to approve a standard contract and thus immunize it from judicial intervention, or to disapprove a term and thus invalidate it. The examination takes place in the abstract. In a 1969 amendment to the *Law,*[76] the Attorney General was authorized to challenge prejudicial terms before the Board, but this power was never used.

The theoretical benefits of pre-screening standard terms via a Tribunal are evident with regard to both suppliers and customers. The advantage for suppliers is that once a contract is approved by the Tribunal it is immunized from judicial scrutiny. The Tribunal can also guide suppliers in advance as to which terms are valid and which are prejudicial, thus saving them from future uncertainty in court proceedings. For customers, the Tribunal is potentially of even greater importance, because a term annulled by a Tribunal protects all customers who adhere to the contract, whereas a judicial decision would be *res judicata* only between the parties.

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[74]For additional examples, see Shalev, *supra,* note 41 at 611.

[75]See *infra,* note 81 and accompanying text.

[76]*Standard Contracts (Amendment) Law* 5729-1969, Laws of the State of Israel, vol. 23 at 151.

Unfortunately, the 1964 Board did not operate as well as expected. Only about sixty standard contracts[77] were submitted for its scrutiny during the 18 years of its existence. This was generally[78] attributed to the voluntary nature of the scheme. However, that was not the only reason for its lack of success. Imperfect drafting of the original version, flaws in the procedure followed by the Board,[79] the restricted scope of application of the *Law* and the limited power to intervene granted to both courts and the Board all weakened the effectiveness of the *Law.*

The 1982 *Standard Contracts Law* was enacted with the intention of remedying the deficiencies of the 1964 *Law.* The amendments concerning administrative control had a three-fold purpose. Judicial control was substantially strengthened, increasing the incentives for voluntary submission of contracts to the Tribunal; the structure and proceedings of the Tribunal were greatly improved; and greater emphasis was placed on the power to challenge prejudicial terms in standard contracts.[80]

Chapter two of the 1982 *Standard Contracts Law* sets out the structure of the new Tribunal. Section 6 establishes a Tribunal for Standard Contracts, a body designed to handle this subject exclusively. Under the 1964 *Law,* standard contracts were examined by a Board originally established to control antitrust cases. Only a negligible amount of the Board's time was devoted to standard contracts.[81] This resulted in delays and superficial handling of the cases.[82]

The Tribunal consists of 12 members,[83] headed by two District Court judges.[84] Other members of the Tribunal are appointed by the Minister of Justice for a period of three years, and at least two representatives of consumer organizations are selected for appointment.[85] Proceedings before the Tribunal are conducted by a bench of three members.[86] Every bench must be headed by a judge and also include at least one representative of a consumer organization.[87] Thus, two panels can sit at the same time.

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[77]Deutch, *supra,* note 14 at 112-7 describes fifty-one applications from 1964 to 1979. From 1980 to 1982, a few additional applications were submitted to the Board.

[78]See, *e.g.,* Kretzmer, *supra,* note 16.

[79]See Deutch, *supra,* note 14 at 117-25.

[80]See the 1984 *Memorandum, supra,* note 63 at 42-3.

[81]See Deutch, *supra,* note 14 at 115.

[82]See Deutch, *ibid.,* schedule 1 at 113-4.

[83]Section 6(b) of the 1982 *S.C.L., supra,* note 8.

[84]Section 6(c) of the 1982 *S.C.L., ibid.* The District Court is a High Court in Israel. At present two judges of the Jerusalem District Court are serving on the Tribunal.

[85]*Ibid.,* ss 6(d) and (e).

[86]*Ibid.,* s. 7(a).

[87]*Ibid.,* s. 7(b).

In order to permit it to function with discretion and flexibility, the Tribunal is exempt from the rules of evidence and civil procedure.[88] The Tribunal's decisions can be appealed to the Supreme Court[89] and are open to inspection by the public.[90] When the Tribunal annuls or varies a term it must publish its decisions in at least two daily newspapers.[91]

The old system of voluntary submissions was changed to one incorporating both voluntary and involuntary features. The voluntary proceedings are detailed in Chapter Three of the 1982 *Standard Contracts Law*. A supplier may apply for approval of his standard contracts,[92] and the Tribunal has broad powers to permit individuals and groups to participate as respondents.[93] A contract can be approved for a period of up to five years,[94] and during that period a plea against the contract because of a prejudicial term will not be heard by the Tribunal or a court. The Attorney General can, however, apply for annulment even within that period if circumstances have changed.[95]

The power of the Tribunal to amend or annul prejudicial terms is detailed in Chapter Four of the *Law*.[96] Annulment usually affects contracts made after the date of the decision,[97] but the Tribunal has the power to decide whether a decision should affect contracts already entered into although not fully performed.[98] Several changes were introduced in the annulment power of the Tribunal. Section 3 of the 1982 *Law* states that the Tribunal should annul or amend prejudicial terms, thus emphasizing the power of annulment rather than that of approval. In addition, under the 1964 *Standard Contracts Law*, the Board could only annul the challenged term.[99] Under the 1982 version, when it is possible to vary a term to avoid the unfair results the Tribunal has the power to amend it.

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[88]*Ibid.*, s. 9. See also the explanatory note to s. 7 of the original bill, *supra*, note 10 at 32.

[89]*Ibid.*, s. 10.

[90]*Ibid.*, s. 11(a).

[91]*Ibid.*, s. 11(b).

[92]*Ibid.*, s. 12(a). Under the 1982 version the whole contract must be approved, rather than only the "restrictive terms" of the 1964 version. The Tribunal must therefore carefully examine every term and consider the contract as a whole before approving it. This attitude also prevents confusion among customers, who can rarely distinguish between approved terms and other terms. See the 1984 *Memorandum*, *supra*, note 63 at 53.

[93]*Ibid.*, s. 12(b). A similar provision existed under s. 5 of the 1964 *S.C.L.*

[94]*Ibid.*, s. 14.

[95]*Ibid.*, s. 14(c).

[96]*Ibid.*, ss 17 *et seq.*

[97]*Ibid.*, s. 18(a).

[98]*Ibid.*, s. 18(b). See M.A. Eisenberg, "The Bargain Principle and Its Limits" (1982) 95 Harv. L. Rev. 741 on the distinction between "half-completed bargain promises" and "executory contracts". This distinction resembles that in s. 18(b), although the sections are not identical.

[99]An example of the dilemma under previous versions is described in the 1984 *Memorandum*, *supra*, note 63 at 62.

Another change in this area was the authorization for various groups to apply for annulment of a standard term by the Tribunal. Section 16(a) of the *Law* states:

> The Attorney General or his representative, the Commissioner of Consumer Protection under the *Consumer Protection Law*, 5741-1981, any consumer organization and public authority designated by regulations or customer organization approved by the Minister of Justice for a particular matter may apply to the Tribunal for the annulment of a prejudicial term of a standard contract.

It is questionable whether the Attorney General's representative will use his power to intervene; it is far more likely that the Commissioner of Consumer Protection and the two leading consumer organizations will take action. Since the *Law* includes various terms of presumptive unenforceability, at least in this area, some action will probably follow.

An anticipated change to the *Law* is provision for mandatory submission of standard contracts to the Tribunal where a monopoly exists. This has been proposed and will almost certainly be approved under the new Restrictive Trade Practices Bill.[100]

The drafters of the statute clearly preferred control of standard contracts by the Tribunal to control by the courts. Only the Tribunal can approve a contract or invalidate a term; and only the decisions rendered by the Tribunal are binding before both courts and the Tribunal. The Tribunal is empowered to continue with its proceedings even when the same contract is under consideration by a court; and when a court decision is given it is not binding on the Tribunal. However, in the case that the Tribunal disregards a judicial decision, an appeal can be made to the Supreme Court for a final resolution of the case.

Conclnsion

The problems involved in regulating standard contracts are too complicated to be solved by the use of a single device. There is no consensus as to which are the best means to control this area of the law. The Israeli version can serve as a model for adoption, especially in those jurisdictions where a policy of administrative control does not exist. Other doctrines used for the purpose of controlling this area such as unconscionability or "inequality of bargaining power" are of limited value and are not directly related to the problem of standard contracts.

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[100]*Hatza'ot Hok*, no. 1647 of 5744-1983 at 39, s. 28(a)(1).

The 1982 Israeli statute presents a balanced approach to regulating standard contracts. It rejects long lists of forbidden clauses. It still acknowledges the value of judicial review, but emphasizes more administrative action. The burden of proof is transferred to the supplier, who is better equipped to deal with it. The tribunal may examine closely the whole spectrum of economic and moral issues involved in standard contracts.