Dysfunctional Contracts and the Laws and Practices That Enable Them: An Empirical Analysis

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Introduction

A review of purchase agreement forms used by condominium developers in Chicago, Illinois from 2003-2008 (the “Condo Contracts Study”) discovered that 79% contained highly unfair, one sided remedies clauses. Specifically, as detailed in Section I, these forms provided that the buyer’s sole remedy in the event of the seller’s breach was the return of the buyer’s own earnest money. This is not a meaningful remedy since it does not cover any of the losses buyers would normally be entitled to recover under the law due to a breach of the contract, creating—as one court put it—“heads I win-tails you lose” illusory agreements. In essence, these clauses constitute a waiver of the right to recover benefit of the bargain/expectation damages, consequential damages, reliance type damages and the remedy of specific performance. Compounding the unfairness of this limitation of remedy clause is the fact that these same form contracts also provide the seller with recovering substantial damages in the event of the buyer’s breach since the typical remedy was retaining the buyer’s deposit (typically an amount between 5-10% of the purchase price). We argue that these overly one sided remedies clauses create “dysfunctional contracts” because with such clauses one party (the more sophisticated

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4 The Condo Contracts Study was based on a FOIA request of the City of Chicago to view all of the Property Reports filed by developers of condominiums in Chicago, Illinois during 2003-2008 (attached as one of the exhibits to each property report was a form purchase and sale contract for the condominium units that the developer planned to use). Boxes of such filed property reports were made available to Debra Stark’s research assistants and approximately 25 property reports (one report is issued for each condo building) were randomly selected to review for each of those years (for a total of 155 form purchase contracts from a base of 631 property reports). The Condo Contracts Study results are on file with Debra Stark and a detailed analysis of the other contract clauses reviewed under that study appears in a separate article still in progress.
6 See results from the Condo Contracts Study on file with Debra Stark.
party who drafted the form contract) can willfully default and terminate the contract with no harm to the breaching developer\(^7\) (hence the contract provides no true binding agreement from one party) while the other party is bound and would suffer a material harm if they failed to perform. Since the main function of entering into a contract is for both parties to be bound through being exposed to negative consequences if they breach, contracts with these clauses are dysfunctional. Indeed, such contracts could be construed as invalid and lacking in consideration, because one of the parties’ promises are illusory, a conclusion drawn by some courts in Florida, but one that some courts in other jurisdictions have rejected.\(^8\) As discussed in Section III, courts in jurisdictions outside of Florida have also refused to strike down this type of limitation of liability clause under the hard to meet unconscionability test that they applied due to the “clear” wording of these “bargained for” clauses.\(^9\)

But do laypersons truly comprehend what appears to lawyers and judges as clear limitation of liability clauses? And if not, how does this impact on the premise that the laypersons bargained for this result when they signed the purchase agreement form and the application of the unconscionability test for striking down a limitation of liability clause? In Section II we report on a Remedies Experiment we ran that attempts to answer the question of layperson comprehension of the highly unfair limitation of remedy clause found in so many developer form contracts. We found that the results from our experiment reflect a widespread failure of the participants to understand the impact of this type of clause on their rights after a breach, undercutting the premise upon which the unconscionability test rests: that the home purchaser understood the clearly worded limitation clause and therefore bargained for this result. We argue that these results should lead to courts adopting a different set of tests for ruling on the enforceability of limitation of remedy clauses in home purchase contracts, as detailed in Section IV.

\(^7\)Termination of the contract and returning to the purchaser the earnest money they paid is technically a legal consequence of rescission and partial restitution, but is not providing the buyer with a recovery for the losses the buyer suffers due to the seller’s breach and poses no loss to the seller for causing a termination of the contract and no disincentive to engage in strategic defaults.

\(^8\)See, e.g., Port Largo Club, Inc. v. Thomas, 476 So. 2d 1330, 1332 (Fla. Dist. Ct. App. 1985) and Blue Lakes Apartments, Ltd. v. Gowing, Inc., 464 So. 2d 705, 708 (Fla. Dist. Ct. App. 1985) which found such clauses renders the seller’s obligations to be illusory; But see also Tanglewoodland Co.v. Byrd, 256 S.E. 2d 270, 271 (N.C. Ct. App. 1979)(applying Virginia law, court held that since under Virginia law a buyer is entitled to sue for specific performance or breach of contract damages if the seller in bad faith failed to convey title the contract clause did not create illusory obligations by the seller and the clause was made inoperative in such circumstance).

\(^9\)See Section III for a review of such cases.
In light of the widespread presence of these clauses in developer form contracts\textsuperscript{10} and the likely widespread failure of laypersons to understand the impact of these clauses on their rights if the seller has breached the contract, we argue in Section IV that this serves as strong evidence of public harm and the need to reform the unauthorized practice of law rules in many jurisdictions. The unauthorized practice of law rules in many jurisdictions currently allow brokers to fill in standard form purchase contracts,\textsuperscript{11} which

\textsuperscript{10} Clearly, developers in Chicago, the area studied, extensively use these clauses, and perhaps similar studies should be conducted in other cities in other states to determine the level that developers use these clauses in other states. There were a large number of reported appellate court cases where developers used these clauses in Florida and their use is also confirmed in about ten other jurisdictions with appellate court cases reflecting their use.

\textsuperscript{11} See Conway-Bogue Realty Inv. Co. v. Denver Bar Ass’n, 312 P.2d 998 (Colo. 1957) (holding that the preparation of real estate purchase contracts are so “indigenous to the practice of law that it would be illogical to say they are not. But we can also say, as a majority of other jurisdictions have done, that it is in the public interest to permit the limited, outside use of standard, printed forms in the manner stipulated by the chancellor and we so hold.”); Florida Bar v. Irizarry, 268 So. 2d 377, 379 (Fla. 1972)(“…we have limited the permissible scope of activities of real estate brokers to preliminary negotiations and preparation of the contract.”); Cardinal v. Merrill Lynch Realty/Burnet, Inc., 433 N.W. 2d 864, 867 (Minn. 1988)(the provisions of the UPL laws shall not prohibit any one, acting as broker for the parties from drawing or assisting in drawing, with or without charge, papers incident to the sale); Hulse v. Criger, 247 S.W. 2d 855, 862 (Mo. 1952)(“when acting as broker, a realtor may use an earnest money contract form for the protection of either party against unreasonable withdrawal from the transaction, provided that such earnest money contract for, as well as any other standard legal forms used by the broker in transacting such business, shall first have been approved and promulgated for such use by the bar association and the real estate board in the locality where the forms are to be used.”); White v. Dep’t of Labor & Indus., 2006 Mont. Dist. LEXIS 165 (2006) (explaining that a broker has the right to fill in forms as part of negotiations regarding sales of real property); Calvert v. K. Hovnanian, 128 N.J. 37, 44 (1992)(“The Bar Association and the Association of Realtors finally agreed to a settlement that permitted licensed realtors receiving commissions for the sale of residential real estate to prepare the contracts for those sales provided that each contract contain a clause making the contract subject to review by an attorney for the buyer or seller at either party’s option within three business days after execution.”); Duncan & Hill Realty v. Dep’t of State, 62 A.D. 2d 690, 696 (N.Y. App. Div. 1978)(“As long as real estate brokers and agents have not held themselves out to be attorneys at law, have confined their actions to serving their clients in relation to the specific transaction [such as drawing a contract of sale] in which the broker has a financial interest for payment of his services, and have made no charge for these incidental services, such acts have been held by our courts to be proper and not to constitute the unlawful practice of law.”); Oregon State Bar v. Security Escrows, Inc., 233 Ore. 80, 93 (1962)(an exception from the injunction is “the filling-in of blanks under the direction of a customer upon a form or forms selected by a customer. If the customer does not know what forms to use or how to
in turn, has contributed to the practice of home buyers relying on brokers rather than hire a lawyer to protect their interests at the contract formation stage. Two prior studies, one engaged in by a special master at the direction of the Supreme Court of New Jersey, and the other by Professor Joyce Palomar, who focused on the impact of an attorney at the conveyance stage rather than at the contracting stage, failed to show how the public is negatively impacted by having non-attorneys rather than attorneys assist them in their home purchase transaction. These studies and the lack of a showing of public harm has led in part to the Federal Trade Commission and the Department of Justice taking the position that allowing laypersons to perform tasks involved in residential real estate transactions are unlikely to increase the risk of harm for consumers and should be permitted. Consequently, the results from the Remedies Experiment and the Condo Contracts Study are important contributions to the question of public harm and the rules relating to the unauthorized practice of law. In Section IV we propose certain legal reforms to the unauthorized practice of law rules in light of these results.

Section I of this article highlights the relevant results from two empirical studies conducted by the first two authors on major problems with the fairness of purchase agreement forms used by residential real estate developers in Illinois. Section I also discusses the lack of home purchaser understanding of key relevant laws and legal documents examined in an empirical study conducted by Professor Michael Braunstein in Columbus, Ohio. In Section II of this article, we report in detail on the results from our Remedies Experiment. This experiment demonstrated that, contrary to the assumption of many judges, even after carefully reviewing limitation of remedies clauses, a very large percentage of laypersons believed they were entitled to remedies “clearly” (at least to an attorney or judge’s eyes) excluded in the contract clause. In Section III, the article examines and critiques case law on the enforceability of “return of earnest money as sole remedy” clauses. The section notes the split of authority among the reported case law in the U.S. on this issue and why Florida’s approach of providing greater protection to home purchasers is more appropriate. In Section IV, the article proposes four legal reforms to address the problem of dysfunctional contracts that contain highly unfair and problematic remedies clauses in the face of likely significant failure of home purchasers to understand these problematic provisions even when they carefully read them.

direct their completion, then he needs legal advice. If the customer does know what he wants and how he wants it done, he needs only a scrivener.”); Creditors’ Serv. Corp. v. Cummings, 57 R.I. 291, 298 (1937); Bar Ass’n of Tennessee v. Union Planters Title Guar. Co., 46 Tenn. App. 100, 127 (1959); and Perkins v. CTX Mortgage Co., 969 P.2d 93, 99 (Wash. 1999).

12 In re Opinions No. 26 of the Comm. on the Unauthorized Practice of Law, 654 A.2d 1344, 1345, 1351(N.J. 1995).

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I. Highlights From Two Empirical Studies in Illinois and an Empirical Study in Columbus Ohio

As previously noted, a key finding from the Condo Contracts Study in Chicago, Illinois was that in 79% of the form contracts reviewed, the contracts contained terms that provided no remedy to the condo unit purchaser to cover the purchaser’s losses from the seller’s breach or to deter the seller from strategic, willful defaults. At the same time, however, the seller/developer in such contracts did retain valuable remedies that they would enjoy should the buyer default in her obligations under the contract. The form contracts reviewed overwhelmingly contained a clause where the buyer’s sole and exclusive remedy in the event of the seller’s breach was termination of the contract and return of the buyer’s own earnest money (an obligation that would exist without it being identified as the buyer’s sole remedy16). This creates a waiver of other more meaningful remedies to address the seller’s breach, such as specific performance, benefit of the bargain, reliance, or consequential damages, without explicitly setting forth these rights and saying these rights are now waived. In only 4% of the sampled form contracts did the remedies clause permit to a buyer compensatory/bargain type remedies available under the law in the event of the seller’s default that would exist had the contract been silent on the issue of remedies. In the same form contracts, sellers were granted the compensatory remedy of liquidated damages (in the form of retention of the buyer’s earnest money—typically under those contracts at somewhere between 5-10% of the purchase-price amount) in 68% of the contracts, and were permitted all available remedies in the event of the buyer’s default in 23% of the contracts.17

Equally important to any limitation of remedies clause is how the contract treats attorney’s fees for enforcing the agreement. Unless the contract provides for attorneys’ fees to the prevailing party, few buyers could afford bringing a lawsuit to challenge the validity of limitation of remedy clauses and seek more meaningful remedies in the event of the seller’s default since the attorneys’ fees are likely to be substantial, sometimes even exceeding their damages claims.18 According to the Condo Contracts Study, only 14% of the contracts contained a provision that the prevailing party in a lawsuit relating to the purchase contract would be entitled to attorneys’ fees.19 This causes purchasers under 86% of these form contracts to be far less able to bring a claim for specific

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16 When a buyer deposits a sum of money with the seller or with a third party with the expressed intent that it be used to pay a portion of the purchase price if the deal is closed and serve as security if the buyer defaults, and in fact the deal does not close due to the seller’s default or other reasons excluding the buyer’s default, then the seller is obligated to repay that amount of money to the buyer if the seller has already deposited the sum of money entrusted to it. See Kopis v. Savage, 498 N.E. 2d 1266 (Ind. Ct. App. 1986).

17 See Condo Contracts Study, supra note 4.

18 According to one source, fees associated with litigating a lawsuit range from thirty to sixty percent of the total recovery. See JEFFREY O’CONNELL, THE LAWSUIT LOTTERY: ONLY THE LAWYERS WIN 86 (1979). When the claim involves a construction defect, experts are likely to be necessary, adding to the typical costs of litigation.

19 See Condo Contracts Study, supra note 4.
performance or damages when the seller has breached the contract and to challenge the limitation of remedy clause if applicable.\textsuperscript{20}

The serious problems with remedies clauses in condo purchase agreements found in the Condo Contracts Study is also reflected in a survey of over one hundred attorneys in Illinois conducted by Stark and Choplin (the “Attorney Survey”).\textsuperscript{21} In the Attorney Survey, when asked in an open-ended question what terms in the condo purchase contracts they have seen that were highly unfair or highly problematic, 51\% referred to the limitation of liability to the seller or the limitation of remedies to the buyer as of chief concern. When asked to rate their level of satisfaction with various terms in the condo purchase contracts they have seen, when responding about remedies available to the buyer, 32\% rated their level of satisfaction “1” (with 1 being the lowest level of satisfaction and “7” being the highest), another 22\% rating it with a “2”, 15\% rated it with a “3”, leaving only a total of 29\% who rated it with a “4” or better. In addition, 69.6\% of the attorneys surveyed reported a “7” and 92.1\% reported a “6” or “7” on a 1-7 scale that they felt strongly that home buyers would not raise the same points as attorneys would on their own. This opinion was supported in the results of the Remedies Experiment in connection with spotting problems with the unfair remedies clauses of the contract. These results suggest the positive impact from having an attorney represent the homebuyer at the contract formation/negotiation stage or under an attorney approval of the contract. But it should also be noted that only 35\% of the attorneys reported that they were successful in negotiating to modify or delete highly unfair or problematic terms in the developer’s form contract greater than 50\% of the time. As discussed in Section IV, this result suggests the need to create legislation to ensure that the most unfair and problematic terms that developers use in their form contracts, especially ones that laypersons do not understand, are dealt with in legislation. Finally, we asked attorneys to report how often major disputes arose between the parties after the contract was signed (before or after closing the deal). Approximately half (50.5\%) reported that such major disputes arose in only 1-10\% of the matters they handled, with only 3.8\% reporting experiencing such major disputes more than 50\% of the time, but only 9.7\% reporting they never had a major dispute arise after the contract was signed.\textsuperscript{22} The fact that most reported such a low percentage of major disputes arising (1-10\%) may explain why the

\textsuperscript{20} If the contract is silent on the recovery of attorney’s fees for a suit based on the contract, unless there is an applicable statute to the contrary, the prevailing party is not entitled to an award of its attorney’s fees.

\textsuperscript{21} The Attorney Survey was based upon dissemination of an online survey designed to elicit the opinions and experiences of Illinois real estate attorneys regarding residential real estate form contracts prepared by developers with a focus on the level of fairness of the terms to buyers and ability of the lawyers to negotiate for better terms, but covering other related matters. [hereinafter “Attorney Survey”]. The form was sent to Illinois State Bar Association and Chicago Bar Association members, various residential real estate attorneys who had listings on lawyers.com, alumni of The John Marshall Law School, and real estate lawyers located on Martindale-Hubbell directory. In total 108 lawyers submitted responses to the survey. The full results from this survey are on file with Debra Stark and a detailed analysis of that study appears in a separate article still in progress.

\textsuperscript{22} \textit{Id.}
special master in New Jersey noted no evidence of public harm from having homebuyers unrepresented by attorneys. But we disagree that having even 1-10% of homebuyers have no remedies when the seller has breached a contract to sell them a home is acceptable and does not pose a public harm worthy of state intervention. For example, states require automobile drivers to obtain casualty insurance due to the likelihood of getting in a car accident and the need for motorists to be insured to pay for the damage done to other motorists who cause accidents. One might imagine a very large percentage of claims made each year, yet in 2009, only 1% of policyholders brought bodily injury claims and the average amount paid on those claims was $13,462. Only 5% of policyholders brought a claim for collision damages, and the average amount paid on these claims was only $2,869.23 Similarly, in order to close on a federally insured home loan, the borrower must obtain casualty insurance on the home even though in 2008 only 7% of insured homes experienced a claim (94% of such claims for property damage including theft) on their homeowner’s insurance policies.24 Just as there is federal and state law in place to require insurance to cover car crashes and damage to homes even though the percentage of claims for such events is in the 1-10% range, there should be state laws in place to require specially trained and licensed attorneys to represent homebuyers at the contract formation stage. Such representation provides a type of “insurance” because the attorneys can review the contract, spot problems, and negotiate changes to the contract to address those problems and, consequently, put homebuyers in a far better position when major disputes arise in 1-10% of the deals. If unable to negotiate for changes to address the problems, the lawyer will make the buyer aware of the risks and some buyers may choose not to proceed with the deal and seek out a safer deal.25

There is another empirical study on the impact of attorney representation of home purchasers that has relevant findings. In Braunstein’s study, noted earlier, recent purchasers of homes in the Columbus, Ohio area in the fall of 1989 were interviewed in lengthy telephone conversations.26 He had 132 homebuyers surveyed where 41% had hired their own lawyer to represent them in some aspect of the purchase and the rest had not.27 He noted that many of those who hired a lawyer did so where the lawyer was involved “fairly early” in the process, but it is not clear if this means at the time the contract was being negotiated.28 When asked why they hired a lawyer the most articulated reason was a vague “to protect me” answer, apparently without any further details.29 Braunstein notes several areas where the purchasers failed to understand basic real estate laws as applied to their deal: (i) 50% did not know whether their deed was a general warranty deed, a limited warranty deed, a quit claim deed, or some other type,

23 INSURANCE INFORMATION INSTITUTE, INSURANCE FACT BOOK 2011 69.
24 Id. at 99.
25 The area of major dispute most reported in the Attorney Survey was the physical condition of the home (86%), followed by failure to complete on time (58.1%); failure of a condition to close (44.1%), breach of contract (37.6%), title defects (35.5%) and other (12.9%).
26 Odd Man Out, supra note 15, at 469.
27 Id. at 471.
28 Id.
29 Id.
(which impacts on liability of the seller to the buyer for defects in title and encumbrances), (ii) although many knew they had taken title as joint tenants (only 22.6% did not know how they took title) almost 50% of those who knew they took as joint tenants did not know the significance of how they held title (such as rights of survivorship which might not be what the buyers intend if the couple is a second marriage with children from the first marriage), and (iii) a large percentage of buyers displayed a substantial lack of understanding of title insurance, with only 7% realizing there were any exceptions to their policy, and more than half not knowing that title insurance did not cover faulty construction but did cover adverse legal claims to the house and land.\(^{30}\)

Equally problematic is the fact that an overwhelming majority of buyers were not given a copy of the title policy until at or after the closing\(^{31}\) when it is difficult or too late to address title problems disclosed in the title commitment. Some of the home buyers also did not realize that the real estate agent’s primary loyalty is to the seller and not to the buyer unless the buyer’s agent or a dual agent.\(^{32}\)

These results reflect that these homebuyers were ignorant of important legal matters relating to their home purchase, suggesting that they should have been represented by an attorney who would be aware of these matters and ensure that the buyer’s goals and expectations are met. Having said that, a disturbing finding from the telephone interviews was that purchasers who used lawyers were not better informed on relevant legal matters, not more satisfied with the purchase transaction, and not less likely to avoid disputes than those who did not.\(^{33}\)

These results show poor lawyering by the attorneys who represented those home buyers\(^{34}\) and underscores the need for attorneys who handle this area of law to be specially trained and licensed in it to provide real value to their clients as described in Section IV.\(^{35}\)

II. Consumer Understanding of Remedies Experiment

**Summary of Background Laws Relating to Contract Remedies Experiment**

Under the common law, the most common contract remedies that can be sought when a party breaches an agreement to sell or buy real estate are: (1) “specific performance” (i.e. the right to force the other party to close the deal with the buyer paying the purchase price and the seller deeding the property to the buyer),\(^{36}\) (ii) “benefit

\(^{30}\) Id. at 476.

\(^{31}\) Id.

\(^{32}\) Id.

\(^{33}\) Id. at 479.

\(^{34}\) Braunstein did note that of the 41% who said they hired their own lawyers to help them purchase the house, a later question revealed that 9 of the 54 did not pay the lawyer any fee and 2 of the 54 said they had never met or spoke with their lawyer about the matter. Id. at 471 n. 5.

\(^{35}\) Alan M. Weinberger, *Further Observations on Using the Pervasive Method of Teaching Legal Ethics in Property Courses*, 51 ST. LOUIS U. L.J. 1203 (2007)(“Transactional real estate practice generates a greater proportion of legal malpractice claims than any other field [twenty-five percent]”).

of the bargain damages” also sometimes referred to as “expectation damages,” which is based upon the difference between the fair market value of the real estate on the date of the breach and the contract price (so if the contract price is $100,000 but the fair market value is $115,000 and the seller has breached the contract, the buyer can recover $15,000 in expectation damages), (iii) “reliance damages” based upon any expenditures made by the non-breaching party in order to perform under the contract (so if the seller has breached the contract and the buyer has incurred expenses to obtain a loan commitment such as paying for an appraisal of the home, or has incurred expenses to inspect the home, the buyer can recover these expenses as their reliance damages), (iv) “rescission and restitution”, which means termination of the contract and return of any sums the non-breaching party has paid to the other party (such as the earnest money), (v) “consequential damages,” which are damages that arise due to the breach of the contract, that the breaching party could reasonably anticipate would occur, and which the non-breaching party could not have reasonably avoided (such as the buyer having to pay a fee to the lender to get the same interest rate on the loan when the interest rates have risen after the originally scheduled closing date), (v) “liquidated damages”, which is an agreement in the contract that the damages that the breaching party will owe has been set at a specified amount such as, for a breach by the buyer, the amount of money serving as the earnest money deposit (typically an amount between 5-10% of the purchase price), and this amount is due generally notwithstanding the actual damages the non-breaching party might otherwise recover (i.e. if the actual damages end up being more or less than the liquidated amount the liquidated amount would control) but the amount must be a reasonable estimate of damages at the time the contract is entered into.

With the exception of the remedy of liquidated damages, these other remedies exist even if a contract is silent on the issue of remedies. When a contract attempts to limit any of these otherwise available remedies, this is called an “exculpation clause” or “limitation of liability” clause and this is what exists in the “clearly unfair” and “vaguely unfair” contract conditions categories described below. As will be discussed in detail in Section II, most exculpation/limitation of liability clauses are enforced, but in extreme cases, some courts will not enforce these clauses. The list of remedies described above (except for the remedy of liquidated damages) would all apply to the “fair” contract condition. The possibility of recovering attorney’s fees to enforce the agreement is a special category, and is not covered by the common law as a remedy for breach of the contract. To recover attorney’s fees for enforcing the agreement and seeking remedies after a breach one needs either to specially provide for this in the agreement (as done in the fair contract condition but not in the clearly unfair or vaguely unfair contract

37 Id. at 724.
38 Id. at 727-728.
39 Id. at 748.
40 Id. at 727.
41 Id. at 733. To be enforceable, the amount must be a reasonable estimate at the time the parties enter into the contract of the amount of damages the non-breaching party will sustain. Id. at 735. But some courts will look at the actual damages and if far less than the liquidated amount might rule that the liquidate amount is a penalty and not enforceable. Id.
conditions) or there must be a statute on point that covers the situation (for example a consumer fraud claim). There are also limits to the combination of remedies that a non-breaching party can recover (such as not being able to recover both specific performance or benefit of the bargain damages but also reliance type damages), and we asked participants questions related to that, but since this knowledge is not relevant to how the contract remedies clause should be drafted, we are not reporting in this article the results from those questions.

The Consumer Remedies Experiment

This experiment was originally inspired by a similar experiment conducted by Stolle and Slain (1997). In their study, participants imagined that they were injured while using exercise equipment at a health club in one scenario and imagined that their car was scratched in a repair shop in another. Participants reviewed the exculpation clauses in the gym’s and the shop’s contracts. The language, if enforceable, would have severely restricted the gym’s and the shop’s liability. As a result, two-thirds of their participants correctly identified that there was a clause that prevented their recovery in a lawsuit. This experiment investigated participants’ abilities to do so for remedies clauses in home purchase contracts.

Methods

Participants

One hundred and seventy-seven undergraduate students completed the questionnaire for course credit. Participants were randomly assigned to conditions: 52 to the fair condition, 65 to the clearly unfair condition, and 60 to the vaguely unfair condition. The sample was 64.9% female, 62.5% white, 13.6% Hispanic, 5.7% Asian American, 5.7% African American, and 2.3% Native American. The majority of participants identified as Democrats (52.3%), followed by Independents (19.3%), Republicans (13.6%), Libertarians (7.4%), and Green Party (3.4%). Participants rated their family income levels as high (6.8%), upper-middle (39.7%), middle (42.0%), or low (8.0%). These participants had little to no personal experience with scenarios like the one described in this experiment. Asked whether they had ever had an experience similar to this one and to respond on a 7-point scale with 1 representing "not at all similar," 4 representing "somewhat similar," and 7 representing "very similar." The average response was 1.37. Participants were also asked how reputable they thought most professional real estate developers are in general on a 7-point scale with 1 representing

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42 Fleischmann Distilling Corp. v. Maier Brewing Co., 386 U.S. 714, 717 (1967) (“The rule here has long been that attorneys' fees are not ordinarily recoverable in the absence of a statute or enforceable contract providing therefor.”).

43 The participant responses on this issue reflected a lack of knowledge of such limitations. Details of these results are on file with the second author.

44 Dennis P. Stolle & Andrew J. Slain, Standard Form Contracts and Contract Schemas: A Preliminary Investigation of The Effects of Exculpatory Clauses on Consumers’ Propensity to Sue. 15 BEHAV. SCI. & LAW 83(1997).
"not at all reputable," 4 representing "somewhat reputable," and 7 representing "very reputable." The average response was 4.20.

**Materials and Procedure**

Participants entered the laboratory and were given a randomly assigned questionnaire with either a fair, clearly unfair, or vaguely unfair remedies clause.

In the **fair condition**, the remedies clause read: “In the event of default by Seller or Buyer, the Parties are free to pursue any legal remedies at law or in equity. The prevailing party in litigation shall be entitled to collect reasonable attorney’s fees and costs from the losing party as ordered by a court of competent jurisdiction.” This clause provides both parties with equal protection. Both parties are free to pursue all of the legal remedies described above and liabilities were reciprocal.

In the **clearly unfair condition**, the remedies clause read: “In the event this sale is not closed within sixty (60) days from the date hereof, and Buyer is not then in default, then Seller shall, upon written request of Buyer, return Buyer’s earnest money and this Agreement shall become null and void. Seller’s liability in the event of Seller’s breach of the contract shall be limited to the return of Buyer’s earnest money. In the event of Buyer’s default hereunder then the Seller shall retain the earnest money as Seller’s liquidated damages and sole remedy.” This clearly unfair clause is problematic from the perspective of the buyer, because if the seller defaults the seller’s liability is limited to the return of the buyer’s earnest money. By contrast, if the buyer defaults, the seller would retain the buyer’s earnest money (a significant sum of money at five percent of the purchase price under the scenario we described in the study). That is, the seller—unlike the buyer—never risks their own money and the buyer, in essence, has waived four potentially significant remedies listed above (specific performance, benefit of the bargain/expectation damages, reliance damages, and consequential damages) even though those remedies are not specifically noted as being waived in the clause.

In the **vaguely unfair condition**, the remedies clause was identical to the remedies clause in the clearly unfair condition except that the words “in the event of Seller’s breach of the contract” were dropped from the second sentence making that sentence simply read “Seller’s liability shall be limited to the return of Buyer’s earnest money.” This change makes it unclear under what circumstances the seller’s liability is limited to return of buyer’s earnest money; it could potentially relate to only a termination of the contract due to a failure of a condition to closing occurring such as the buyer obtaining financing as contrasted with having the limitation of liability clause also cover a seller default situation. Since the language is broad it is likely a court would interpret it to cover the default situation and the clause is likely to have the same affect as the clearly unfair contact condition clause.

Participants were then told to imagine that they had performed all of the duties required by the contract. They had deposited 5% of the purchase price as earnest money ($10,000) under the contract. They wished to close the deal, but the seller refused. They suspected that the seller had received a better offer and their attorney advised them that the seller would be in breach of the contract if the seller did not close. In addition, if the
deal did not close, they would still owe their attorney $300 in fees for the work performed on the deal. They had already paid $400 for an inspection of the home and $450 for the appraisal report on the home and a credit check to get a loan to purchase this home. They were told to imagine that based upon an appraisal of the home, the purchase price under the contract was $15,000 lower than the property appraised for and that if they desired to buy a comparable home the purchase price would likely be $15,000 higher. In addition, interest rates had risen since they first locked in the interest rate. The mortgage broker told them that obtaining the same loan with the same interest rate on another house would cost an additional $1,000.

Participants were then asked to answer a series of questions regarding the actions they would take in the scenario and their interpretations of the rights they would have under the contract. These questions along with participants’ responses in each of the three conditions are described next in the results section.

Results

Participants were asked to briefly explain what they would do in similar circumstances. We were curious to see if those in the fair condition stated they would seek more remedies than those in the unfair conditions in light of the different remedies language in the fair versus unfair contracts. Responses were categorized as pursuing legal remedies such as suing or speaking to an attorney or not pursuing remedies beyond the return of the earnest money. When responses were ambiguous as to which category was most appropriate, responses to subsequent questions were used to disambiguate the appropriate category. When it was not possible to disambiguate responses, they were dropped from analysis. Of the participants who answered the question and had clear responses, more participants indicated that they were inclined to pursue remedies in the fair condition (43/48 or 89.6%) than in the clearly unfair condition (38/55 or 69.1%) or in the vaguely unfair condition (30/47 or 63.8%). These differences were statistically significant, \( \chi^2(2, N=150)=9.27, p<.01 \).

Participants were asked how similar they thought the remedies clause in the contract was to those used by most professional real estate developers. They answered on a 7-point scale with 1 representing "not at all similar," 4 representing "somewhat similar," and 7 representing "very similar." This question was intended to get a sense of whether they assumed the remedies clause was typical or not. If there was no statistical difference in the results among the three conditions this could indicate that there was no knowledge of what is customary. Based on the results from the Condo Contracts Study, the correct answer under the fair condition would be a “1” not at all similar, but the correct answer under the vaguely unfair condition would be a “6” and under the clearly unfair condition a “7.” By contrast, participants in the fair condition gave the fair clause an average of 4.9 on this scale, while participants in the clearly unfair condition gave it a 4.7, and participants in the vaguely unfair condition gave it a 4.8. These responses were not different by a statistically significant amount between conditions, \( F(2, 174)=0.40, p>.05 \). The finding that ratings differed so drastically from the results from the Condo Contracts Study suggests that the participants did not know what type of remedies clauses are customary. This result underscores the need for consumers to have the necessary contractual scripts and schemas to protect themselves.
Our participants lacked these scripts and schemas.

Participants rated how difficult they found it to understand the language of the remedies clause in the contract on a 7-point scale with 1 representing "not at all difficult," 4 representing "somewhat difficult," and 7 representing "very difficult."

Prior to running the experiment, we thought that both the fair and clearly unfair remedies clauses were easy to understand and the vaguely unfair clause was more difficult because it was not clear what situations the limitation of remedies related to. While the participants would not have known all of the precise remedies available in the absence of an exculpation/limitation of liability clause, they would at least, we thought, recognize they are limited to getting their own money back. Contrary to this original prediction, all participants rated it “somewhat difficult” and differences were not statistically significant, F(2,174)=0.92, p<.05. Participants in the clearly unfair condition rated this clause a 4.6 in difficulty, participants in the fair condition rated it a 4.3, and participants in the vaguely unfair condition rated it a 4.2, but this difference was not statistically significant despite the major differences in these remedies clauses. Based on the other results from the Consumer Remedies Experiment, it appears that the clearly worded fair remedies clause was “somewhat difficult” for them to understand because they did not precisely know what “legal remedies” were available to them “at law or in equity”—legal terminology that any lawyer or judge would readily understand but apparently not understandable to laypersons. Similarly, the clearly worded unfair remedy clause was also “somewhat difficult” for them to understand perhaps because many were not precisely sure what the words like “sole remedy” meant. Their admitted difficulties understanding the clauses most likely accounts for their difficulties identifying the portions of the remedies clause that would prevent them from recovering, an issue discussed below.

Participants were asked how likely they would be to demand that the Seller pay for their losses and to rate how successful they thought they would be if they demanded that the Seller pay for their losses on the same 7-point likelihood scale described above. Prior to running the study, we would have thought that participants who were given the fair remedies clause would have been most likely to make this demand, followed by the vaguely unfair and clearly unfair clauses. After all the fair remedies clause would have given the participants who were given that clause grounds for making this demand. Contrary to this original prediction, the type of remedies clause did not have a substantial effect on participants' ratings of how likely they would be to make this demand. Participants given the fair clause rated their likelihood of making this demand a 5.8; participants given the clearly unfair clause rated their likelihood a 5.5; and participants given the vaguely unfair clause rated their likelihood a 5.6. These ratings were quite high, above “somewhat likely” and below “very likely,” but did not statistically differ across condition, F(2,172)=0.42, MSE=2.88, p>.05. The finding that participants’ responses did not differ across the different remedies clauses reflects a lack of understanding of the impact of the contract remedies language on their rights to recover their losses (why make a demand for losses if you are unlikely to be able to recover on this demand). It may also reflect a failure to understand the types of losses they could be recovering or not depending on the language in the contract, with some
viewing the loss of their earnest money paid as their only loss (perhaps due to the language in all three contracts that refer to this possible loss) versus the range of other losses they would be compensated for under the law.

Participants were also optimistic on the question of how successful they thought they would be in making demands. If knowledgeable of the impact of the remedies clause language, participants who were given the fair remedies clause would rate they would likely be successful and participants who were given the vaguely unfair and clearly unfair clauses would rate they were less likely to be successful. In distinction from these outcomes, participants in the fair condition were unduly pessimistic and participants in the clearly unfair and vaguely unfair conditions were unduly optimistic about their chances given how those remedies clauses read. Responses were all in the “somewhat successful” range and did not differ across the different remedies clauses by a statistically significant amount, F(2,172)=1.57, MSE=2.66, p>.05. Participants given the fair clause rated their likelihood of success as 4.5, whereas participants given the clearly unfair clause rated their likelihood a 3.9 and participants given the vaguely unfair clause rated their likelihood a 4.2, small differences without statistical or practical significance. These results suggest that participants did not understand the legal consequences implications of the remedies clauses they were given or possibly confined their understanding of “losses” in the two unfair conditions to their earnest money.

Following Stolle and Slain (1997), participants were asked whether the remedies clause in the contract might prevent them from recovering on their demand. We asked this because participant answers to the question of their likelihood of success may have been influenced by their beliefs regarding the legal system (i.e., whether the legal is fair or rigged against them), rather than making an appraisal based upon the actual reading all about the remedies clauses. To address this question and focus more specifically on the reading of the remedies clause, participants were asked as a simple yes or no question whether they thought that the remedies clause in the contract as opposed to other factors might prevent them from recovering on their demand. The normative answer was "no" in the fair condition and "yes" in the clearly unfair and vaguely unfair conditions. Consistent with the normative answer, approximately two thirds of participants (68.0%) in the fair condition correctly answered "no." This left, however, approximately one third of the participants given the fair clause who failed to comprehend how fair the fair remedies clause was. While 65.6% of participants who were given the clearly unfair clause correctly answered "yes," 34.4% failed to comprehend how the wording of that clause would prevent them from recovering on their demand. The percentages in the Remedies Experiment who stated “yes:” there is a limitation on what remedies they can recover is similar to the percentage in Stolle and Slain’s (1997) experiment who identified the clause that limited their ability to recover in a lawsuit from a complete contract provided to the participants. But, we did not provide an entire contract in the Remedies Experiment, and only provided them with the limitation of remedies clause. When we asked them to circle the portion of the clause that limited their remedies (discussed in the next section) participants were much less likely to correctly do so than the two-thirds who stated “yes,” suggesting that this may have been a guess by those who could not correctly explain their response. Also troubling, was the finding that only 44.1% of participants who were given the vaguely unfair remedies
clause correctly answered “yes,” so more than half of the participants (55.9%) failed to comprehend how the wording of that clause would prevent them from recovering on their demand. The differences between these groups were statistically significant, $\chi^2 (2,173)=13.43$, $p<.01$ with the participants in the vaguely unfair condition the most likely to fail to comprehend how the remedy clause would affect their likelihood of succeeding in recovering their losses. This is consistent with one of our hypotheses that consumers under the vaguely unfair clause are less likely to realize how their remedies have been reduced than those in the clearly unfair clause. It should be noted however, that the other two conditions also reflected a significant amount of inaccurate understandings on this issue.

**Participants were asked to circle the portions of the remedies clause that might prevent them from recovering.** Given the fair clause where nothing prevented them from recovering, 17 participants out of 52 (32.7%) incorrectly circled something. In the clearly unfair clause, the words “limited to” in the sentence “Seller’s liability in the event of Seller’s breach of the contract shall be limited to the return of Buyer’s earnest money” was the key portion that prevented recovery. Likewise, in the vaguely unfair clause, the words “limited to” in the sentence “Seller’s shall be limited to the return of Buyer’s earnest money” was the key portion that prevented recovery. Only a minority (17 participants out of 65; 26.2%) correctly circled those words in that sentence given the clearly unfair clause. Even fewer (6 participants out of 57; 10.5%), however, correctly circled those words given the vaguely unfair clause. This difference between the clearly unfair and vaguely unfair clauses was statistically significant, $\chi^2 (1,N=122)=8.03$, $p<.01$.

**Participants were asked how likely they would be to seek advice from an attorney on the 7-point likelihood scale described above.** Ratings were high for all three conditions, but were not lower in the fair condition than in the clearly unfair and vaguely unfair conditions, $F(2,174)=0.17$, $MSE=1.38$, $p>.05$. Participants rated themselves a 6.3 (very likely) on this scale in the fair condition, 6.3 in the clearly unfair condition, and 6.2 in the vaguely unfair condition. This finding suggests that it is not clear to the participants what rights they have under the remedies clauses and would benefit from the advice from an attorney on this.

**Participants were asked assuming their attorney had advised them that a lawsuit was possible to rate on the likelihood scale described above how likely they would be in successfully recovering what they desired in a lawsuit.** This question is similar to the earlier question of the likelihood of recovering losses upon demand, but is different in two ways. This question, by referring to a lawsuit clarifies that a judge is making the decision now versus “demands” where the seller may be deciding. Second, by referring to recovering what they “desire” this question expands on the recovery notion by asking them to consider what they desire (for example getting the property) versus just recovering their losses (such as earnest money and out of pocket expenses). The normative answer should have been 7 (very likely) for participants who were given the fair clause, 1 (not at all likely) for participants who were given the clearly unfair clause, and 1.5 for participants who were given the vaguely unfair clause, in light of the summary of background laws on contract remedies previously provided. Contrary to these normative answers, responses were all slightly above “somewhat likely” and while
they differed by an amount that is considered marginally significant, F(2,174)=2.94, MSE=1.82, p=.06, they did not differ by amount that would have practical consequences. The responses of the participants given the fair clause were 5.2 on average, the responses of the participants given the clearly unfair clause were 4.8 on average, and the responses of the participants given the vaguely unfair clause were 4.5 on average. Again, since the responses to this question on likelihood of being successful in a lawsuit across conditions did not statistically differ, this is evidence that consumers did not understand the impact of the contract language on what they can recover for a breach of contract.

Participants were asked how successful they thought they would be in a lawsuit to recover five specific losses: (1) attorney's fees for negotiating the contract and handling the matter before the default (an example of reliance damages), (2) attorney's fees for handling the litigation (only recoverable if the contract provides for this or a statute does that applies), (3) the $400 paid for the inspection and $450 for the appraisal report and credit check to obtain the loan (examples of reliance damages), (4) the $10,000 for the difference between the fair market value of the home and the purchase price (the expectation/benefit of bargain damages), and (5) the $1,100 to obtain a new loan at the same rate (although rates have risen) to close on the purchase of a home (an example of consequential damages). In addition to this general question regarding how successful they thought they would be on each of these items, participants were asked more specifically as “yes” or “no” questions whether the remedies clause or any laws on remedies might prevent them from recovering. In general, participants who were given the fair remedies clause were unduly pessimistic and participants who were given the clearly unfair and vaguely unfair remedies clauses were unduly optimistic. Each of these results reflecting a major lack of understanding of the impact of the contract language on what they could recover.

(1) Recovery of attorney’s fees for negotiating the contract and handling the matter before default:

On the question of the likelihood of recovering attorney's fees for negotiating the contract and handling the matter before the default, the normative answer should have been a 7 among participants who were given the fair remedies clause, a 1.5 among those given the clearly unfair remedies clause, and a 2 among those given the vaguely unfair remedies clause based on the laws relating to contract remedies summarized earlier. Consistent with these normative answers, the remedies clause affected participants’ judgments by a statistically significant amount, F(2,174)=3.95, MSE=3.71, p<.05, although the majority of responses were in the “somewhat likely” range. Responses of participants who were given the fair clause (M=4.8, slightly above “somewhat likely”) differed from the responses of participants who were given the clearly unfair clause (M=3.7, slightly below “somewhat likely”), t(115)=3.08, p<.01, and the responses of participants who were given the vaguely unfair clause (M=3.1, slightly below “somewhat

45 These fees to handle the deal should be treated like other reliance type damages, although a court might confuse this with attorneys’ fees relating to enforcing the agreement (i.e. litigation costs) and mistakenly not permit a recovery of the pre-litigation attorneys fees.
likely”), \(t(110)=4.97, p<.01\). The responses of participants who were given the clearly unfair and the vaguely unfair clauses did not differ from each other once error control is taken into consideration, \(t(123)=1.90, p>.017\).

To try to understand the factors that could have affected participants’ judgments of the likelihood of recovering attorney’s fees for negotiating the contract and handling the matter before the default, participants were also asked to indicate as simple “yes” or “no” questions whether there were any portions of the remedies clause or, in a separate question, any laws of remedies could prevent them from recovering. The normative answer should have been “no” among participants who were given the fair remedies clause and “yes” among participants who were given the clearly unfair and vaguely unfair remedies clauses since, this should be construed as a reliance type damage and under the fair condition the buyer has not waived her right to recover this. Consistent with these normative answers, 73.1% of the participants who were given the fair remedies clause correctly identified that the remedies clause they were given would not prevent them from recovering, leaving 26.9% of the participants who incorrectly believed that there were portions that could prevent them from recovering. More troubling, however, was the finding that 55.4% of participants who were given the clearly unfair remedies clause and 51.7% of participants who were given the vaguely unfair remedies clause (i.e., fewer than half) incorrectly believed that no portions of their remedies clauses would prevent them from recovering attorney’s fees for negotiating the contract and handling the matter before the default, even though the clauses, especially the clearly unfair one, clearly state the buyer’s sole remedy in the event of the seller’s breach is return of the buyer’s earnest money. The differences between groups were marginally significant, \(\chi^2(2, N=177)=5.95, p=.05\), but the number of participants who failed to understand how their remedies clause would prevent them from recovering was troubling.

(2) Recovery of attorney’s fees for handling the litigation (only recoverable if the contract provides for this or a statute does that applies).

On the question of recovering attorney’s fees for handling the litigation, the normative answer is 7 “very likely” under the fair condition and 1 “not at all likely” in the clearly unfair and vaguely unfair conditions, because laws of remedies prevent plaintiffs from recovering attorney’s fees for handling litigation unless the contract states otherwise and the fair condition contract clause provides for recovering those fees to the prevailing party. Our participants were not lawyers and so they were not likely aware of this requirement to recover attorney’s fees for handling the litigation. Perhaps because the fair condition explicitly spells out recovery of attorney’s fees in this situation and the other two conditions did not, responses differed according to the remedies clause that participants were given by a statistically significant amount, \(F(2, 174)=14.15, \text{MSE}=3.12, p<.01\). Responses of participants who were given the fair clause (\(M=4.8\), slightly above “somewhat likely”) differed from the responses of participants who were given the clearly unfair clause (\(M=3.2\), slightly below “somewhat likely”), \(t(115)=5.37, p<.01\), and the responses of participants who were given the vaguely unfair clause (\(M=3.5\), slightly below “somewhat likely”), \(t(110)=3.93, p<.01\). The responses of participants who were given the clearly unfair and the vaguely unfair clauses did not differ from each other, \(t(123)=0.92, p>.05\). Despite these statistically significant differences, the participants
who received the clearly and vaguely unfair clauses were unduly optimistic and the participants who received the fair clause were unduly pessimistic once we consider the normative answers. Participants who were given the fair remedies clause were not statistically less likely (38.5%) to believe that there were portions of the remedies clause that would prevent them from recovering attorney’s fees for handling the litigation than participants who were given the clearly unfair remedies clause (49.2%) or participants who were given the vaguely unfair remedies clause (48.3%), $\chi^2(2, 177)=1.59$, $p>.05$. A very large 70.8% who were given the clearly unfair clause, and 76.3% who were given the vaguely unfair clause incorrectly believed that there were no laws of remedies that would prevent them from recovering on this issue, while 23.1% of participants who were given the fair clause incorrectly believed there were laws of remedies that would prevent them from recovering on this issue (participants’ responses did not differ according to the remedies clause they received, $\chi^2(2, 176)=0.73$, $p>.05$) These results reflect a material misunderstanding of the law relating to recovery of attorney’s fees in an action to enforce the contract.

(3) Recovery of the $400 paid for the inspection and $450 for the appraisal report and credit check to obtain the loan (examples of reliance damages)

On the question of recovering the $400 paid for the inspection and the $450 for the appraisal report and credit check to obtain the loan, the normative answer should have been a 7 among participants who were given the fair remedies clause, a 1.5 among those given the clearly unfair remedies clause, and a 2 among those given the vaguely unfair remedies clause for the reasons previously explained in the summary of the law of contract remedies. Responses differed according to the remedies clause that participants were given by amounts that are considered marginally significant, $F(2, 174)=2.64$, MSE=3.56, $p=.07$. Participants who were given the fair remedies clause rated their likelihood of recovering the $400 paid for the inspection and the $450 for the appraisal report and credit check higher than participants who were given the clearly unfair remedies clause (M=4.7 for the fair clause versus M=3.9 for the clearly unfair clause) and participants who were given the vaguely unfair remedies clause (M=4.0), but by amounts that failed to reach statistical significance once error control was taken into consideration, $t(115)=2.24$, $p>.017$ for the difference between the fair and clearly unfair conditions and $t(110)=1.81$, $p>.017$ for the difference between the fair and the vaguely unfair conditions. The difference between the clearly unfair and the vaguely unfair clauses also failed to reach statistical significance, $t(123)=0.23$, $p>.05$. The fact that these differences were marginally significant, but not fully significant, suggests that while some participants understood that the unfair remedies clauses would prevent them from recovering on this issue, many did not.

Further evidence that many participants did not understand how the unfair remedies clauses would prevent them from recovering the $400 paid for the inspection and the $450 for the appraisal report and credit check comes from their answers to the “yes” or “no” question of whether there were any portions of the remedies clause that would prevent this recovery. The differences in responses between participants given the different remedies clauses did not reach statistical significance, $\chi^2(2, 177)=1.16$, $p>.05$. Of the participants given the fair remedies clause, 36.5% incorrectly thought that the
remedies clause would prevent them from recovering these expenses, and 53.8% of the participants in the clearly unfair and 60% of the participants in the vaguely unfair remedies clause mistakenly thought that their remedies clauses would not prevent them from recovering these expenses. This high level of lack of understanding of the impact of the exculpation/limitation of liability clause language is much higher than predicted and contrary to assumptions made by courts on consumer understanding of such clauses.

(4) Recovery of the $10,000 for the difference between the fair market value of the home and the purchase price (the expectation/benefit of bargain damages)

On the question of whether participants believed that they could recover the $10,000 for the difference between the fair market value of the home and the purchase price, the normative answer should have been a 7 among participants who were given the fair remedies clause (since it reserved all rights and remedies under the law which would include this type of expectation damages), a 1 among those given the clearly unfair remedies clause (since this clause clearly limited the buyer’s remedy to return of the earnest money), and a 1.5 among those given the vaguely unfair remedies clause (since this clause not as clearly limited the buyer’s remedy for a seller breach to return of the earnest money). Contrary to these normative answers, responses did not differ according to the remedies clause that participants were given, $F(2,174)=1.64$, $MSE=3.35$, $p>.05$. That is, the average rating of 3.37 for the fair clause, 3.32 for the clearly unfair clause, and 2.82 for the vaguely unfair clause were not different by statistically significant amounts. The average ratings on this question were also lower than the average ratings on the question regarding recovering the $400 paid for the inspection and the $450 for the appraisal report and credit check suggesting that participants were generally skeptical that they could recover on such a large amount or that $10,000 even represented a true loss. Indeed, some of the qualitative responses reflected a sense that this type of recovery was inappropriate. Some of the responses included: “not really money I'm out, never owned the house in full,” “seems not solid, by that I mean that it's hard to award buyer with theorized money,” and “The seller does not have to reimburse the buyer for offering a good deal.” These responses reflect a lack of understanding of the concept of benefit of the bargain/expectation type damages, which is a less obvious “loss” than out of pocket expenses related to performing under the contract. This result underscores the importance of a home-buyer being represented by an attorney at the contract formation stage or under an attorney approval of the contract condition to negotiate for a “fair” remedies clause and also to advise the buyer after a breach that they may be entitled to this type of recovery. In addition, participants also did not understand how the unfair remedies clauses would prevent them from recovering the $10,000 for the difference between the fair market value of the home and the purchase price as evidenced by their answers to the “yes” or “no” question of whether the remedies clause would prevent them from recovering on this issue. While 50% of participants given the fair remedies clause incorrectly thought that their remedies clause would prevent them from recovering on this issue, 60% given the clearly unfair clause and 55% given the vaguely unfair clause thought so. These between-group differences were not statistically significant, $\chi^2(2,177)=1.17$, $p>.05$. 

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(5) Recovery of the $1,000 to obtain a new loan at the same rate (although rates have risen) to close on the purchase of a home (an example of consequential damages)

On the question of whether participants believed that they could recover the $1,000 to obtain a new loan at the same rate (although rates had risen), the normative answer should have been a 7 among participants who were given the fair remedies clause (since the contract clause reserved all rights and remedies which would include consequential damages\textsuperscript{46}), a 1 among those given the clearly unfair remedies clause (since this clause clearly limited liability for the seller’s breach to return of the earnest money), and a 1.5 among those given the vaguely unfair remedies clause (since this clause less clearly limited the liability to return of the earnest money in the event of the seller’s breach of the contract). However, the 3.62 rating by participants who were given the fair clause was not higher than the 3.12 rating by participants who were given the clearly unfair clause or the 3.08 rating by participants who were given the vaguely unfair clause by a statistically significant amount, F(2,174)=1.44, MSE=3.34, p>.05. In addition, answers to the “yes” or “no” question on whether the remedies clause would prevent them from recovering on this issue did not differ depending upon the remedies clause, \( \chi^2(2,177)=0.58, p>.05 \). The 51.9\% of participants who thought that the fair clause might prevent this did not differ from the 58.5\% who thought that the clearly unfair clause might prevent it or the 53.3\% who thought that the vaguely unfair clause might prevent it. Similar to the results on recovery of benefit of bargain/expectation damages, the percentage of participants who thought they could recover this consequential damage, even in the fair condition, is much lower than for the out of pocket type reliance damages, reflecting a lack of consumer awareness of the appropriateness of recovering consequential damages as a loss.

Participants were also asked about their likelihood of success in a lawsuit to force the Seller to sell the home to them at the contracted for purchase price (the remedy of “specific performance”). Participants answered this question on a 7-point scale with 1 representing "not at all likely," 4 representing "somewhat likely," and 7 representing "very likely." Normative answers were 7 given the fair clause (since this clause reserved all rights and remedies under the law which would include the right to specific performance), 1.5 given the clearly unfair clause (a very low likelihood because of the clear language that says return of the earnest money is the Seller's sole liability in the event of Seller's breach, but as discussed in Section II, the possibility of a court refusing to enforce this clause if there is a showing that the seller is engaging in a strategic default\textsuperscript{47}), and 2.0 given the vaguely unfair clause (since this clause also limited

\textsuperscript{46}This type of loss naturally arises from the breach due to the delay in closing on the loan for another property as a result and would be awarded as consequential damages if a court determines the breaching party should have reasonably anticipated this type of loss under the circumstances (such as the presence of a financing contingency in the contract) and provided the non-breaching party show she had taken reasonable steps to avoid this loss.

\textsuperscript{47}It is difficult to quantify the likelihood of enforcement in the clearly and vaguely unfair clauses since there is a difference of opinion among the jurisdictions. Courts in Florida
liability of the seller to return of the earnest money but was not as clear this would include the circumstance of a seller breach of the contract. Contrary to these normative answers, the 4.27 average rating among participants who were given the fair clause was not higher than the 4.5 rating among those given the clearly unfair clause or the 4.3 rating among those given the vaguely unfair clause, F(2,173)=0.30, MSE=3.21, p>.05. These results demonstrate not only that the participants who were given unfair clauses were overly optimistic, but also, it appears, that these participants had no idea how the wording of the clause would undermine their attempt to force the seller to sell the home to them. In the other direction, but equally wrong, the participants in the fair condition were unduly pessimistic on their chances of obtaining specific performance and appeared to fail to understand that the words “free to pursue any legal remedies at law or in equity” (emphasis added) means an action for specific performance. There could, however, have been factors other than the remedies clause that could have affected participants’ responses.

To focus participants’ attention on the remedies clause in particular, participants were asked as a “yes” or “no” question whether they thought there were any portions of the remedies clause that might prevent them from forcing the Seller in a lawsuit to sell the home to them at the contracted for purchase price. The normative responses were “no” given the fair clause and “yes” given the clearly unfair and vaguely unfair clauses. However, 26.9% of participants given the fair clause incorrectly said “yes” and only 35.9% correctly said “yes” given the clearly unfair clause and 31.7% correctly said “yes” given the vaguely unfair clause. The responses did not even differ between the groups by a statistically significant amount, \(\chi^2(2, N=177)=2.20, p>.05\). The fact that 64.1% in the clearly unfair condition and 68.3% in the vaguely unfair conditions failed to realize the exculpation/limitation of remedy clause would prevent them from obtaining the important remedy of specific performance underscores the lack of consumer understanding of such exculpation/limitation of remedy clauses even when clearly focusing on the words used in the clauses in answering questions on these clauses.

Participants were asked to circle the portions of the remedies clause that might prevent them from forcing the Seller in a lawsuit to sell the home to them at the contracted for purchase price. Given the fair clause where nothing prevented them from doing so, 20 participants out of 52 (38.5%) incorrectly circled something. In the clearly unfair clause, the words “limited to” in the sentence “Seller’s liability in the even of Seller’s breach of the contract shall be limited to the return of Buyer’s earnest money” was the key portion. Likewise, in the vaguely unfair clause, the words “limited to” in the sentence “Seller’s shall be limited to the return of Buyer’s earnest money” was the key portion. Only a minority (13 participants out of 65; 20.0%) correctly circled those words in that sentence given the clearly unfair clause. Even fewer (5 participants out of 57; 8.8%), however, correctly circled those words given the vaguely unfair clause. This difference between the clearly unfair and vaguely unfair clauses was not statistically significant, but would be considered marginal, \(\chi^2(1, N=122)=3.04, p=.08\).

are unlikely to enforce the clauses, while courts in other jurisdictions are more likely to enforce it, unless in some jurisdictions there is a showing of “bad faith” as defined by that court. See Section III.
Participants were asked how likely they thought a court of law would uphold the remedies clause in the contract they signed on a 7-point scale with 1 representing "not at all likely," 4 representing "somewhat likely," and 7 representing "very likely." The normative answers were 7 given the fair clause (since this clause is mutual and reserves all rights under the law), 5.0 given the clearly unfair clause (which, although very unfair, is still somewhat likely to be enforced since, as discussed in Section III, based on a review of reported decisions, it appears that most courts have enforced this type of exculpation/limitation of liability clause, although Florida courts have found such clauses to create illusory agreements and have consequently not enforced this type of clause), and 4.5 given the vaguely unfair clause (since this clause is not as clear that it covers seller’s breach a court might rule it does not limit remedies in such circumstance). The alternative remedies clauses affected responses, F(2,174)=3.03, MSE=2.02, p=.05. Average likelihood ratings given the clearly unfair clause (M=5.1) were lower than the ratings given the fair clause (M=5.8) by a statistically significant amount, t(115)=2.57, p<.05, but not lower by a statistically significant amount than ratings given the vaguely unfair clause (M=5.5), t(123)=1.14, p>.05. These responses were about correct for the unfair clauses since the case law on this issue is mixed, but too low for the fair clause. Before being encouraged by their “correct” rating in the unfair and clearly unfair conditions, it should be noted that based on their answers to prior questions they did not understand the impact of these clauses on what they could or could not recover.

Participants were asked how fair they thought the remedies clause was to the buyer on a 7-point scale with 1 representing "not at all fair," 4 representing "somewhat fair," and 7 representing "very fair." These fairness ratings were affected by the type of clause, F(2,174)=3.98, MSE=1.04, p<.05. Average fairness ratings were higher (M=4.44) by a statistically significant amount given the fair clause, but the ratings given the clearly unfair clause (M=3.98) did not differ by a statistically significant amount from the ratings given the vaguely unfair clause (M=3.95). Given the dramatic difference in fairness of the fair condition clause (normative answer was 7) as contrasted with the clearly unfair and vaguely unfair clauses (normative answer was 1), the fact that the averages hovered in the middle range is further evidence that participants did not understand or appreciate the impact of the language used in the contracts on what rights they would otherwise have had. While some of the participants were able to judge how fair the clauses were, many did not.

III A Review and Critique of Judicial Treatment of “Return of Earnest Money as Buyer’s Sole Remedy” Clauses in Home Purchase Contracts

Based on a review of reported appellate court decisions, courts that have been asked to enforce a contract clause that provides that the buyer’s sole remedy for the seller’s default is return of the buyer’s earnest money have enforced such clauses when this limitation of remedy is clearly provided for in the contract, with the notable

exception of courts in Florida. In some of these cases the buyer failed to timely raise (or raise at all) the argument that the clause might be unconscionable, unreasonable or creates an illusory agreement, and, consequently, the court did not address these issues when enforcing the limitation of remedy clause. But courts in Utah and Washington did address arguments raised by buyers that such clauses were unconscionable, against public policy, unfair or unreasonable, and concluded in these cases that the clauses were enforceable, even awarding attorneys’ fees to the defaulting seller when the buyer sought to obtain additional remedies in these cases. In addition, some courts that would generally enforce this type of limitation of remedy clause, have articulated a narrow exception to enforcement if the seller’s default was in “bad faith” or if the seller had engaged in fraud or deceptive acts. Some courts have defined this “bad faith” exception

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2003) (contract contained limitation of remedy for seller breach to return of the earnest money and court enforced this when the seller breached by selling the real property to a third party for more than the contract price with the buyer; court stated it would enforce the limitation of remedy clause absent a waiver of the clause. Hereinafter “Lespinasse”); Markowitz v. Ne. Land Co., 906 F.2d 100 (3d Cir. 1990)(court ruled that under Pennsylvania law, clause that limits buyer’s remedy if seller breaches to return of the earnest money and interest on it when clearly stated in the contract as the sole remedy is enforceable and thus the seller was not obligated to complete construction within two years of the contract date causing the contract to be subject to the Interstate Land Sales Full Disclosure Act. Hereinafter “Markowitz”); Simpson Dev. Corp., v. Herrmann, 155 Vt. 332, 583 A.2d 90 (Vt. 1990)(court enforced the limitation of remedy clause noting that the buyer failed to raise proper objections to it in a timely fashion, but also noting the plain meaning of the provision in enforcing it. Hereinafter “ Simpson”); Hunter v. Wilshire Credit Corp., 927 So. 2d 810 (Ala. 2005)(court enforced limitation of buyer’s remedy for seller’s breach to return of earnest money; but buyer did not raise and court did not address issue of unconscionability or illusory promise—rather they focused on which of two contract controlled. Hereinafter “Hunter”); Claiborne v. Wilson, 572 So. 2d 1197 (La. Ct. App. 4th Cir. 1990)(court enforced limitation of remedy clause for seller’s breach to return of buyer’s earnest money; buyer claimed coerced into agreement to extend the closing date but did not raise other claims to challenge the limitation of remedy clause and court did not address other claims. Hereinafter “Claiborne”); and O’Shield v. Lakeside Bank, 781 N.E. 2d 1114 (Ill. App. 2003)(court enforced limitation of buyer’s remedy upon seller’s breach to return of buyer’s earnest money; but buyer’s only challenge was that it was a liquidated damages clause and thus should allow specific performance in the alternative, an argument the court rejected; court did not address any other challenges to its enforcement. Hereinafter “O’Shield”).

See Simpson, Lespinass, Markowitz, Hunter, Claiborne and O’Shield cases in supra note 48.

See Goodwin and Torgerson cases in supra note 48.

Id.

See Kooloian v. Suburban Land Co., 873 A.2d 93, 98 (R.I. 2005) (“This Court consistently has held that in the absence of ‘fraud, bad faith, illegality, misconduct, or any other factor that might alter the legal relationship of these parties’ damages for the breach of a contract to purchase real estate are limited in accordance with the terms of the
to be the situation where the defaulting party has represented she has title to the property
to be sold when she knows she does not, or when she has taken steps to impede her title
after the purchase contract has been signed.\textsuperscript{53} For example, the court in \textit{Kooloian v.
Suburban Land Co.},\textsuperscript{54} ruled that it would not enforce a contract provision that limited the
buyer’s remedy for the seller’s inability to convey good title to the buyer to return of the
buyer’s earnest money because the seller had contracted to sell certain real estate to a
purchaser when the seller had already sold the real estate to someone else.\textsuperscript{55} The court
therefore affirmed the trial court’s awarding to the buyer of damages for loss of bargain
in that case.\textsuperscript{56} There is a long line of cases where courts grant reduced damages for non-
willful type failures to convey good title but full damages for willful failures due to a
recognition that there are many possible causes for title to not be marketable that are not
the seller’s fault.\textsuperscript{57} But the narrow issue of remedies upon breach based on a non-willful
failure to be able to convey marketable title is not the focus of this article. Rather, this
article focuses more on the situation where the seller in default has used the limitation of
buyer’s remedies clause in order to “pick its deal” and cancel any deals where the
property appreciates in value after the contract has been signed and before the closing of
the sale or the situation when the breach is for any other reason.\textsuperscript{58}

The court in \textit{Goodwin v. Hole No. 4 LLC},\textsuperscript{59} exemplifies the approach of enforcing
the limitation of remedy clause when it is expressly provided for in the contract, narrowly
interpreting what is procedural and substantive unconscionability, but potentially
providing a “bad faith” exception to enforcement of the clause if it is shown to have been
exercised by the seller because the property has appreciated in value.\textsuperscript{60} Because the court
in \textit{Goodwin} engaged in mental gymnastics and faulty common assumptions to justify

\begin{footnotes}
\item[53] See \textit{Kooloian}, supra note 52.
\item[54] Id.
\item[55] Id. at 98.
\item[56] Id. at 100.
\item[57] See 11-60 \textsc{Arthur L. Corbin, Corbin on Contracts} § 60.10 (Desk ed. 2011).
\item[58] \textit{Goodwin}, 2007 U.S. Dist. Lexis 56271.
\item[59] Id.
\item[60] Id. at 13.
\end{footnotes}
enforcing a highly unfair contract limitation clause against a consumer who was likely deceived into entering into the purchase contract, we engage in a thorough analysis of the details of this decision.

In Goodwin, the buyer agreed to buy and the seller agreed to build and sell to the buyer a home adjacent to a golf course. The contract provided that if the buyer defaulted the seller may elect either to retain the earnest money as liquidated damages or pursue specific performance instead and if the seller defaulted, buyer’s sole and exclusive remedy was to receive a return of buyer’s earnest money, plus 10% interest on the earnest money from the date of its deposit. The buyers argued that they thought the limitation of remedy clause was only intended for non-intentional defaults by the seller and that they could still sue for specific performance if the seller intentionally defaulted. The court ruled that there was no ambiguity on intent regarding when this clause would apply based on the clear limitation of remedies language in the contract and were dismissive of the buyers’ claim that they misunderstood the limitation of remedy clause noting that the entire contract had been explained to the buyers by the broker. The court also ruled that a letter the buyer received from the broker about locking in the price of the unit for a specified purchase price by signing the contract did not create an ambiguity relating to the limitation of remedy clause in the contract. Although the court acknowledged that Utah “courts endeavor to construe contracts so as not to grant one of the parties an absolute and arbitrary right to terminate a contract,” the court found that the limitation of remedy clause did not do this because the seller would still have to return to the buyer the earnest money they paid plus ten percent, and because the buyers also had a right to terminate the contract if they failed to obtain financing or if they disapproved certain disclosures. The court also rejected the buyer’s arguments that the limitation of remedy clause was an unenforceable liquidated damages clause because the clause simply provided for a return of earnest money rather than an agreed upon measure of damages. The court also rejected the buyers’ argument that the seller breached Utah’s implied covenant of good faith and fair dealing because this implied covenant cannot create rights and duties inconsistent with express contractual terms and since the parties had bargained for the limitation of remedy clause “it would be unjustified for the Goodwins [the buyers] to expect more than the remedy provided for in paragraph 16—the return of their earnest money plus ten percent interest on it. The parties contracted specifically for the purpose of allowing Hole No. 4 (the seller] to use paragraph 16 as an escape valve.”

The court also ruled there was no evidence of substantive unconscionability or that the seller had engaged in a deceptive act or practice. The court noted the heavy burden and very demanding test required for a finding that certain terms of a contract are substantively unconscionable: “the terms must be so one-sided as to oppress an innocent

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61 Id. at 2.
62 Id. at 5.
63 Id. at 20.
64 Id.
65 Id. at 24.
66 Id. at 26-27.
67 Id. at 13.
party...The situation must be conscience-shocking or ‘one in which no decent, fair-minded person would view the results without being possessed of a profound sense of injustice.” 68 The court further noted that even if the court were to find the clause to be “wholly unreasonable” this would not alone establish substantively unconscionability. 69 The court added that there is no indication that the clause left a “harsh or unreasonable effect on the Goodwins” since they had the remedy of return of their earnest money plus 10% interest on it and the buyers could have bargained for a different remedies provision but instead agreed to the provision as written. The buyer also argued that the clause violated the state’s consumer sales practices act (UCSPA) because the clause allowed the seller to “pick its deal” (if property appreciated in value between when the contract was signed and closing the seller could terminate with no damages assessed against it and sell to someone else for more and if the property stayed the same or depreciated in value the seller could close with the buyer at the contracted for purchase price). The court emphasized that the seller had a legitimate reason for this limitation of buyer remedy clause: that the seller had difficulty estimating the costs to perform the construction of the home due to the location of the home on a hilltop and thus needed this limitation of remedy to extricate itself from the contract should the construction costs exceed the purchase price. 70 The court noted there was no evidence that the seller used the limitation of remedy clause to get out of a deal in order to sell to another party for a higher price (i.e. if the clause were used by the seller to “pick its deal” based on appreciation or depreciation of the value of the property), which the court seemed to imply could be the basis for a finding that a seller took advantage of another party in violation of the UCSPA when it stated: “Because there is no evidence Hole No. 4 actually used paragraph 16 to take advantage of any party, the Goodwins’ argument fails to support any inference of bad faith.” 71

The court also ruled that there was no evidence of procedural unconscionability. The court noted six relevant factors for a finding of procedural unconscionability, which focuses on the manner in which the contract was entered into and if it led to the complaining party having no meaningful choice:

“(1) whether each party had a reasonable opportunity to understand the terms and conditions of the agreement; (2) whether there was a lack of opportunity for meaningful negotiation; (3) whether the agreement was printed on a duplicate or boilerplate form drafted solely by the party in the strongest bargaining position; (4) whether the terms of the agreement were explained to the weaker party; (5) whether the aggrieved party had a meaningful choice or instead felt compelled to accept the terms of the agreement; and (6) whether the stronger party employed deceptive practices to obscure key contractual provisions.”

In applying these factors to the facts of the case the court stated that the buyers’ strongest argument of procedural unconscionability was that the contract used in this case differed

68 Id. at 27.
69 Id. at 31.
70 Id. at 17.
71 Id. at 31.
from the state’s approved form of purchase and sale agreement, but stated in bold face type at the top of the contract that the form was required by Utah law. The court stated that this might have caused the buyers not to have a reasonable opportunity to understand the terms or that the seller had employed deceptive practices to obscure key contractual provisions. However, the court stated, there was no evidence that the seller was the stronger party in the bargain since the buyers were represented by a broker. In addition, the court noted that the broker had told the buyers that the contract had been modified, flagging the specific modified provisions including the clause limiting the buyer’s remedy in the event of the seller’s failure to perform. The court also took as accurate that this broker had also “reviewed each of the terms of the REPC [the real estate purchase contract] with the Goodwins.” The court also dismissed the letter from the broker to the buyer as a basis for a finding of procedural unconscionability because there was no indication that the seller had reason to know the buyers were relying on that letter to think they were locking in the purchase price to the exclusion of terms in the purchase contract that the contract superseded any and all other previous agreements. The court ruled that this language in the contract made any such reliance on the letter “unreasonable.” Finally, the court noted that there may not have even been a conflict with the letter since if the seller had not exercised its right to terminate by returning the earnest money and ten percent interest, the buyers could have bought the unit for the contracted for purchase price, hence locking in the purchase price amount.

There are many problems with the court’s reasoning and application of laws to the facts in the case. The first area of critique relates to the “facts” that the court relied upon in interpreting the intent of the parties relating to the limitation of remedy clause. The court took as fact the seller’s allegations that the broker “summarized the terms of the REPC [contract]” and in a later telephone conversation “explained all of the REPC’s provisions to the Goodwins.” We find these “facts” to be highly implausible. The real estate purchase contract here was based on the Utah State form purchase contract that is six pages long and single-spaced. It would take at least twenty minutes to simply quickly look at each of the words in the contract (let alone take time to stop and try to think about what these words mean and which options to choose that are offered in the form contract). The amount of time it takes to fully comprehend the contract would also have to include the time it takes to explain what rights the parties would have had absent these contract terms and how the terms change these rights. To make it all concrete, the explainer would have to provide examples of scenarios of how problems could arise and how those likely problems would be resolved if the contract were silent and how they would be resolved under the contract terms. The first author of this article devotes at least 15-20 hours of class time in her law school real estate transactions courses to review the laws that relate to the terms of typical home purchase contracts and review various typical scenarios of issues that can arise and how different contract terms can affect the rights and obligations of the parties under these scenarios. She spends at least 3 hours on contract remedies clauses and remedies laws generally since it is a highly complicated area of law. It is unlikely that real estate brokers are trained to the same level as attorneys on all of these laws and how the contract terms affect the rights of the parties. It is also unlikely that a broker could impart all of this explanation to a buyer when “reviewing” the contract terms with the buyer.
Furthermore, the buyer’s assertion that they did not understand what was meant by the “clear” language (clear at least to any good lawyer) in the contract that limited their remedies in the event of the seller’s breach rings as authentic in light of the results of our Remedies Experiment reported in Section II. Adding to the buyer’s difficulty in understanding the limitation of remedies clause here is the fact that the clause does not expressly spell out that if the construction costs exceed the seller’s estimates, this is the basis for the seller to terminate the contract. The purchaser was probably completely unaware of this risk and did not think of this possibility when reading this portion of the contract. If the main or sole purpose of the broad termination clause was to address the possibility of construction costs exceeding estimates, then why not specify this in the contract (as the contract narrowly specifies the buyer’s right to terminate with no liability if the buyer fails to obtain financing)? Perhaps the seller did not want the buyer to be aware of this risk to a locked in purchase price deal.

The court’s assertion that the parties had “bargained” for the limitation of remedy clause in the contract, is also highly questionable. The buyers signed the contract and the contract contained the limitation of remedy clause, but this does not necessarily mean that both parties had “bargained” for this term or, as the court concluded, that they had done so to allow the seller to escape liability in the event of high construction costs. Clearly the seller who revised the standard statutory form of contract to reduce the full range of remedies that the standard form contract provided\(^2\) intended it, but there is no evidence that this was the buyer’s intent or that the buyer had “bargained” for this result. In general, when a seller is a professional developer and the buyer is a consumer/home buyer, the contract form is supplied by the seller and few points, other than the purchase price, closing date, and amount and interest rate of the loan, are filled in and possibly negotiated over.\(^3\) It appears that the majority of home buyers in the United States do not

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\(^2\) The statutory standard form contract was required to be used by brokers but could be modified by the parties. The form provided for at the buyer’s election one of the following remedies: (a) cancelation of the contract and, in addition to return of the buyer’s earnest money, a sum equal to the earnest money deposit; or (b) sue to the seller to specifically enforce the contract, or (c) accept a return of the earnest money and pursue any other remedies available under the law.

\(^3\) See supra note 11 with cases noting that brokers can fill in the blanks of form purchase agreements. See also Smith v. Boyd, 553 A.2d 131, 135 (R.I. 1989) (“We note that as the written contract was to be drawn up by the realtors, the parties and their realtors had to discuss what was to be stated in the written agreement. The purchase-and-sales-agreement form is a standardized document, but nevertheless a real estate agent must fill in the blanks. To fill in the blanks, the appropriate information must be discussed by the parties and their agents.”); and Gustafson v. V.C. Tayor & Sons, Inc., 35 N.E.2d 435, 437(Ohio 1941)(when describing the blanks that get filled in stated: “supplying of simple, factual material such as the date, the price, the name of the purchaser, the location of the property, the date of giving possession and the duration of the offer requires ordinary intelligence rather than the skill peculiar to one trained and experienced in the law.”). This supports the likelihood that other than those blanks, other points in the contract are unlikely to be discussed and negotiated over, especially if the buyer does not hire an attorney to review the contract.
have an attorney representing them in the negotiation of the terms of the purchase contracts they enter into, most likely only skim the lengthy purchase agreements they sign, and as reflected in our Remedies Experiment, many consumers who actually carefully read and try to analyze the typical limitation of remedies clauses do not understand what rights they are giving up when agreeing to this clause. So, in general the court’s statement that the parties could have bargained for a different remedy clause while technically true, more importantly is not reflective of the reality of experience of home purchase transactions for the vast majority of home purchasers.

Courts need to engage in this fiction because otherwise buyers could argue that they failed to read or understand any term of the contract that they later regretted and this would erode the goal of certainty of contract. Courts may need in the typical case to engage in this fiction, but they should be aware that in fact it is a fiction, and in cases where the terms are very unreasonable and one-sided, should keep this fiction in mind. In this case, that fiction is further buttressed by the fact that the buyer was induced to enter into the contract with the letter from the broker that spoke of locking in a certain purchase price—the very opposite of what they in fact accomplished when they signed this contract due to the wording of the limitation of remedy clause. We highly doubt the broker who allegedly “explained all of the terms of the contract to the buyers” informed the buyers that with this clause the seller could terminate the deal for any reason, including informing the buyer that the seller would do this if the construction costs exceeded the seller’s estimates. Because the seller could terminate under this clause for any reason with little consequence, this clause eroded the buyer’s basic goal of entering into the contract to lock in a specific purchase price for the property.

Perhaps if the court better understood how little many consumers understand when they read remedy clauses (as evidenced by the Remedies Experiment in Section II) and how little the broker likely explained to them (compared with what a good attorney would), the court might not have concluded that the buyer had bargained for this limitation of remedy or was unjustified in expecting more than the limited remedy provided. The buyers asserted that they thought they could sue for specific performance. They thought that the clause limiting their remedy only related to defaults that the seller could not avoid (for example if the seller did not have good title to the real estate through no fault of their own). While the language in the clause seems clear to attorneys, the results from the Remedies Experiment shows that many consumers do not really understand how this type of clause affects their rights when the seller defaults and tend to have a high expectation of the right to force a defaulting seller to specifically perform the contract. Also, since the seller reserved the right to specific performance

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74 As indicated in note 11 supra, many states permit brokers to fill in form purchase contracts and do not require an attorney to represent the home buyer with the contract formation and according to the data in Odd Man Out, supra note 15, at least 59% of the home buyers in their study in Ohio were not represented by an attorney.

75 As Justice Holmes famously noted “the life of the law has not been logic: it has been experience.” THE COMMON LAW 1 (1881).
should the buyer default this may have caused the buyers to assume they would have similar rights.\textsuperscript{76}

The \textit{Goodwin} case also underscores the very narrow band of protection that is afforded to consumer/home buyers when they enter into form contracts prepared by sophisticated developers. As the court noted, “wholly unreasonable” terms that “severely limits their legal remedies while providing advantages to [the seller]” does not establish substantive unconscionability, due to the high burden for a contract term to be considered unconscionable.

Although we critique the unconscionability test articulated by the court in \textit{Goodwin} as applied to consumer-business transactions, we acknowledge that it is the prevalent test adopted by courts. Having said that, the court’s dicta that there is no indication that the clause left a harsh or unreasonable effect on the buyers because they had the remedy of return of their earnest money, plus ten percent interest, reflects a failure to recall and place appropriate emphasis on what rights a buyer is ordinarily entitled to if a contract were silent on this issue. The law provides to buyers of real estate a right to compel the seller to sell to the buyer at the contracted purchase price (“specific performance”) since real estate is considered to be unique and this right is the essence of what has been bargained for in the contract. So, by limiting the buyers here to return to them of their own money, the limitation of remedy clause takes away this critical right. In addition, if the buyer can show that the fair market value of the property exceeds the contract price, the buyer can instead sue for this difference as “expectation damages” instead of seeking specific performance and this right was also taken away under the limitation of remedies clause (an important remedy if the seller’s title to the real estate is seriously impaired). It appears that the buyers in \textit{Goodwin} did not present evidence on the fair market value of the property they had contracted to purchase because this evidence is not required to obtain specific performance as it is to obtain expectation damages. This does not mean that the limitation of remedy clause did not have a profound negative impact on the buyer’s rights as a consequence of the seller’s failure to perform under the contract. In addition to what is lost by the limitation clause, the court over-emphasized what was still retained by the buyers under it. One could argue that the remedy of return of the buyer’s own earnest money provides no real “contractual” remedy at all. If a buyer deposits money with a seller or a third party (unless that money were in the nature of consideration for an option to purchase or a gift to the seller), either as security for the buyer’s performance or to apply to the purchase price, when the buyer has performed and the seller fails to close, the money is the buyer’s and the seller is indebted to the buyer for the amount deposited with the seller.\textsuperscript{77} This obligation to repay the earnest money exists

\textsuperscript{76} See ROBERT B. CIA LDINI, INFL UENCE: THE PSYCHOLOGY OF PERSUASION ch. 2 (2007). , for a discussion on reciprocity effects and expectations.

\textsuperscript{77} Although the return of this money is also covered under the contractual remedy of restitution, it has been construed as in the nature of recovering a debt owed to the purchaser when it was given to the purchaser to be applied to the purchase price. Kopis v. Savage, 498 N.E. 2d 1266, 1270 (Ind. Ct. App. 1986). See also Stoebuck & Whitman, supra note 36, at 734 (“the buyer who seeks a refund of earnest money is arguably not
without the need for a clause in the contract calling for this return of money as the buyer’s sole “contract remedy.” The only true added remedy in the case was requiring the seller to provide interest on the earnest money.

The court’s conclusion that there was no evidence of bad faith in the case is also problematic. As previously noted, the contract remedies language failed to expressly address the situation of construction costs exceeding the purchase price. If this were the sole or main purpose for the limitation of remedy clause in the event the seller failed to close, then the contract clause should have expressly been limited to this or other intended scenarios. This change is necessary to put the buyers on better notice that their deal was actually conditioned upon the construction costs not exceeding the seller’s estimates and would be similar to how the contract explicitly created a condition to closing that the buyer obtain financing. This is in contrast with creating a broadly worded termination right that could implicitly encompass a contemplated risk. It would be odd for example to create a general right of the buyer to fail to close and terminate the contract with no liability and then later claim they did so because they failed to obtain a needed loan to close. By creating the broad based right to terminate without liability, a party is reserving the right to make any number of post hoc justifications for terminating to avoid the argument that they did so because they could now get a better deal from someone else. Also problematic is the fact that the limitation of remedy clause does not include a bad faith type exception that the court refers to. This failure may evidence an intention by the seller to reserve the right to use the clause in an opportunistic fashion (to terminate if the fair market value of the property has gone up). The court could have ruled that the clause, since not so expressly limited, created an illusory agreement (as courts in Florida have).

The court only briefly applied some of the facts of the case to the law relating to procedural unconscionability. The court focused on the fact that the seller had changed the Utah approved form of contract as a basis for the buyer to argue that they did not have a reasonable opportunity to understand the terms of the contract or to argue that the seller engaged in deceptive acts. The court was correct to point out that the broker informed the buyer that the standard form had been revised, but as previously noted, the court placed too much reliance on the broker’s ability (and perhaps desire) to inform the buyers of the legal consequences of these changes relevant to the remedies issue. In addition, the court placed far too much weight on the fact that the buyers received “representation” from the broker and thus might have been the “stronger party in the bargain.” As between a real estate developer whose business includes routinely entering into purchase contracts and who undoubtedly had legal counsel relating to the development, and the buyer who may have never before entered into a purchase contract and who apparently did not have the benefit of a lawyer’s advice at the time the buyers entered into the contract, it is clear that the seller was the more sophisticated party. Hence, they misapplied the “stronger party” factor in analyzing the procedural unconscionability claim. Finally, as previously noted, the court did not place adequate weight on the impact on the buyer of the letter the buyers received from the broker that told the buyers they should enter into a contract to lock in relying on contract rights, but is merely asking relief from the seller’s unjust enrichment.”).
the purchase price. The court wrongly concluded that the buyers did not "reasonably" rely on the letter because the contract contained terms stating that the contract superseded any and all other previous agreements. In another law review article, we demonstrated the unfairness of this type of conclusion in light of the psychological realities of the level of reading and likely comprehending of contract terms that consumers in fact have and how preventing a fraud or deceptive practices act claim on this basis creates a license to deceive. 

Perhaps the weakest point of the court’s analysis of the procedural unconscionable claim was when the court concluded that there may not have been a conflict between the contract terms and the letter since if the seller had not exercised its right to terminate the buyers could have bought the unit for the contracted for purchase price. If the termination right had been very narrow in scope there might be some validity to this statement. But because the contract clause broadly provided the seller with a right of termination, that right is in contradiction to the lock in statement promised in the letter.

A final critique of the Goodwin decision is whether courts should require evidence of “bad faith” (defined by the court as the seller using the limitation of remedy clause to “pick the deal” based on property valuation or better offers) to rule that the type of limitation of remedy clause in Goodwin is unenforceable. One can make a strong argument that an extreme limitation of remedy to the buyer when the seller is provided very adequate remedies to address their losses should be found to be unenforceable even when the seller is not trying to use the clause to “pick the deal.” The buyer will in a typical deal suffer a loss of out of pocket expenses and in some cases loss of expectation damages or consequential damages when the seller fails to close and terminates the contract, regardless of whether the failure to close is in bad faith or not. Loss of the right to specific performance is a major waiver of a right and, as noted earlier, should not be enforced when other remedies to the buyer are also waived but the seller retains important remedies.

The Washington Supreme Court in Torgerson v. One Lincoln Tower LLC, also ruled that a contract clause that clearly limited the buyer’s remedy to return of her own earnest money (while the seller’s remedy was retention of the earnest money) was enforceable and not unconscionable. The special and unique facts in Torgerson, however, better justify this ruling than in the Goodwin case. In addressing the procedural unconscionability claim, the court noted that the purchasers in Torgerson were real estate brokers who were marketing the sales of units in the building and that they negotiated for certain changes to the form contract (regarding the interior finish, color schemes, and due date and amount for the earnest money deposit). In addressing the substantive unconscionability claim, the court emphasized the very low security deposit paid by the

79 Torgerson, 210 P. 3d 318.
80 Id. at 325.
81 Id. at 318.
82 Some contracts, those created later, only limited buyers from obtaining consequential damages or punitive damages. Id. at 321.
buyers/brokers and the fact that the bulk of their security deposit would be paid seven
days before closing or even at the closing (the details on the security deposit provisions
are discussed below)\textsuperscript{83} and inferred that these buyers agreed to the extreme limitation of
their remedies in exchange for the low security deposits they were initially making and
had better opportunities to negotiate the contract than typical home buyers.\textsuperscript{84} Although
not expressly noted by the court, it would also be a fair inference that these buyer/brokers
were far more familiar with the terms of the developer’s form contract and more likely to
have a sense of the remedies they were giving up. The amount they initially deposited
was only $5,000 for each unit.\textsuperscript{85} The court assumed, perhaps correctly, that the brokers
agreed to the extreme limitation of remedy for the seller’s breach in exchange for the
buyers/brokers only initially depositing $5,000 of their own money as earnest money.
The normal earnest money deposited to estimate a seller’s damages for a buyer’s breach
is in the range of 5-10\% of the purchase price and here the $5,000 deposit is only 1.5\% of
the $332,000 purchase price for one buyer/broker and .37\% of the $1,318,000 purchase
price for the other buyer/broker. The brokers also, however, pledged the commissions
they would have earned at closing as part of their security deposit, thus increasing the
deposits to 5\% and 10\% of these purchase prices. Assuming that the commissions were
only for this deal (the case is not clear on this point\textsuperscript{86}) then the court would be correct to
point out the very small amount of money the buyers were depositing here (the rest of the
deposit apparently not being payable until closing of this deal) as justifying them having
very limited remedies upon the seller’s default. But if the assignment was of commissions
owed to these brokers for other deals under contract then this was valuable consideration
much more within the normal range (although not being paid up front as is typical) and
there would be a substantial imbalance in remedies.

Notwithstanding that the result in Torgerson may have been appropriate (i.e. the
court was upholding a true bargain made between sophisticated parties), there is some
dicta in the case that is problematic. First, although the court noted that under
Washington law, a clause that unilaterally and severely limits the remedies of one side is
substantively unconscionable for denying any meaningful remedy,\textsuperscript{87} the court declined to
rule on whether the doctrine of unconscionability applies to real estate transactions in the
State of Washington.\textsuperscript{88} In addition, even when the court nevertheless analyzes whether
the contract remedy clause was unconscionable, the court states: “Here, both sides are

\textsuperscript{83} Id. at 322-323.
\textsuperscript{84} Id. at 322.
\textsuperscript{85} Id. The court does not clarify whether the commission relates to the sale of these two
units or other units they acted as broker on. If it is for other units that they would be owed
a commission on, then the earnest money adding up to 5\% of the purchase price for one
broker/buyer and 10\% for the other broker/buyer is in fact a significant sum of money
and the argument that there was no substantive unconscionability under the facts of this
case is less strong.
\textsuperscript{86} The court stated “the Buyers negotiated to pay the rest of the deposits in commissions
from their work as agents for the condominium development, and that money was due
only seven days prior to closing or at closing.” Id. at 322-23.
\textsuperscript{87} Id. at 323.
\textsuperscript{88} Id. at 324.
limited to the retention or return of deposits in case of breach.”—as if to say this is a remedy that is mutually beneficial to the non-breaching party and mutually detrimental to the non-breaching party. The court continues, “To be sure, the deposits come out of Buyers pockets; but at $5,000 and the promise of real estate commissions payable upon closing, the deposits are not so insignificant a sum as to foreclose legal action.” It is true that the non-defaulting buyer here will want his $5,000 money deposit back, but that is still only a return of the buyer’s own money (and the commission for work done on other deals is also just a return of the buyer’s own earned money). Only if the commission for this closing is something the seller would still have to pay to the buyer if the seller breaches the contract is it accurate to state that the buyer may be getting a meaningful remedy here with return of the commissions it has pledged to the seller.

A second category of dicta that is problematic in the Torgerson case relates to its treatment of possible UCC remedies protections. The court stated that just because case law in the state has adopted UCC law on the disclaimer of the warranty of habitability for construction contracts does not mean this court would extend UCC remedies protections to real estate contracts. Nevertheless, the court addressed remedies laws under the UCC, indicating that under the UCC, general remedies may be available where “circumstances cause an exclusive or limited remedy to fail of its essential purpose.” The court noted that commentary for this section of the U.C.C. states that parties are free to shape their remedies and “reasonable agreements limiting them are to be given effect.” Although the court refused to extend UCC remedial provisions to this real estate transaction, it proceeded to conclude that the remedies clause here would satisfy the UCC test. The court stated, “since Buyers get their deposits back, along with certain sums paid for improvements on the units, they are not left without ‘a fair quantum of remedy’ as is the concern of the UCC in a goods context.” This interpretation of the UCC remedial provisions is highly problematic since it provides that the grant of only rescission/restitution to the non-breaching party and potentially much greater remedies to the other breaching party is “a fair quantum of remedy.” The court fails to limit this dicta to the setting where the other party is also severely limited in its remedies or if the other party who has waived contractual remedy rights has been given other valuable consideration for this waiver.

Finally, the Torgerson court’s reasoning in its ruling that the contract remedies clause did not violate public policy is also flawed. The buyer correctly pointed out that when the buyer’s sole remedy for the seller’s default is return to the buyer of the earnest money or other sums paid by the buyer, this will encourage sellers to engage in more strategic defaults, and enforcing such a clause would be injurious to the public. In response, the court stated: “…the remedies limitations can cause either these Buyers or Sellers to bear the risk of the other party’s breach, depending on changes in the housing market… this agreed upon allocation of risk, which limits liability for both parties, does

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89 Id. at 323.  
90 Id.  
91 Id. at 324.  
92 Id.  
93 Id.
not violate public policy.” Again, the court treats the limitation of remedies as being comparable, but the buyer would have to experience a benefit greater than at least $5,000 plus transactions costs to benefit from a strategic default, while the seller would only have to benefit $1 plus transaction costs to benefit from a strategic default.

Courts in Florida have taken a different approach and have embraced the argument that a clause that limits the home purchaser to the remedy of return of the buyer’s earnest money upon seller’s default creates an illusory contract, permitting the seller to breach with impunity. Thus the court in Port Largo Club, Inc. v. Warren and Thomas, held that this type of clause was unenforceable and would permit the buyer to obtain the remedy of specific performance or benefit of the bargain damages, notwithstanding the limitation of remedy clause in the contract, when the seller breached the contract. The court stated that persons may limit their liability by contract “but such provisions must be reasonable to be enforced.” Because the court noted that this type of clause “renders the seller’s obligation wholly illusory and would permit him to breach with impunity” the court concluded that “such provisions are antithetical to the concept of fair dealing in the marketplace and will not be enforced by courts of law.” The court also stated that to obtain benefit of the bargain damages the breaching party must have breached in “bad faith” which the court initially defined as the opposite of “good faith” and later seemed to define as being without any “reasonable justification.” The court noted that the time-share units under contract had increased substantially in value and since the seller failed to provide reasonable justification for the failure to complete the closing, this failure to close was deemed to be lacking “good faith.”

The Florida Court of Appeals in Blue Lakes Apartments, Ltd. v. Gowing, Inc., similarly ruled that although parties to a contract may agree to limit their respective remedies and that those remedies need not be the same, the contractual provisions must be reasonable to be enforced. The court ruled that a contract clause that provides that the buyer’s sole remedy is limited to the return of the buyer’s earnest money while the seller’s sole remedy is limited to retention of the earnest money constituted a “heads-I-win, tails you lose approach to defaults…so rapaciously skewed as to be patently unreasonable.” The court also characterized this type of limitation of remedy clause as a subversion of contract that permits one party to breach with impunity, causing the

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94 Id. at 324-25.
96 Id.
97 The buyer did not obtain benefit of bargain damages in this case, though, because the buyer failed to provide evidence of the difference between the fair market value of the property on the date of the breach compared with the contract price.
98 Port Largo Club, Inc., 476 So. 2d at 1332.
99 Id.
100 Id. at 1333.
102 Id.
seller’s obligations to become wholly illusory while the buyer’s are quite real (the buyer had deposited 10% of the purchase price as its security deposit in this case). The court affirmed the trial court’s awarding of benefit of the bargain damages and did not require a showing of bad faith. In support of its similar conclusion that this type of limitation of remedy clause causes the seller’s obligations under the contract to be illusory in nature, the Florida court in *Ocean Dunes of Hutchinson Island Development Corp. v. Colangelo and Woodward*, noted that “return of one’s own money hardly constitutes damages in any meaningful sense.” The court in Ocean Dunes therefore ruled that because the contract provided no reasonable remedy for its breach, the equitable remedy of specific performance for the buyer ordered by the trial court was affirmed.

The court in *Idevco, Inc. v. Hobaugh*, also ruled that when the buyer’s sole remedy is return of their earnest money and the seller’s sole remedy is retention of the buyer’s earnest money this constitutes a lack of mutuality of obligation and causes the limitation of remedies clause to be void. However, in Idevco, it was the buyer who was in breach of contract not the seller. Consequently, the court affirmed the trial court’s order that the seller return the buyer’s earnest money deposit, but noted that when a default provision of a purchase agreement is invalid, the non-defaulting party (here the seller) is entitled to prove and recover its actual damages. The court in *Hackett v. JRL Development, Inc.* also ruled that the buyer in default would not lose their earnest money under a similar contract remedies limitation clause due to the clause being invalid for lack of mutuality of obligation, but the seller could still recover its actual damages from the breach if the seller properly pleads and proves actual damages. The trial court concluded that the remedy was reasonable because the buyer would also be entitled under other portions of the contract to interest earned on the security deposit in the event of the seller’s default (similar to the Utah District court’s ruling in the *Goodwin* case). The appellate court disagreed because the interest was earned on the buyer’s money, thus the seller had “no real obligation.” The court in *Terraces of Boca Associates, v. Gladstein*, also ruled that a similar contract limitation of remedies clause was invalid and unenforceable due to the unreasonable disparity in remedy alternatives available to

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103 Id.
104 The court did mention that the seller had sold the property to a third party but noted this in the context of answering why the trial court did not award specific performance. The court also mentioned the purchase price of the seller’s sale of the property to a third part in the context of affirming the trial court’s calculation of benefit of the bargain damages. *Id.* at 709.
106 *Id.* at 440.
108 *Id.* at 489.
109 *Id.*
111 *Id.* at 603.
112 *Id.*
the seller and buyers\textsuperscript{114} and therefore the buyers in breach were entitled to the return of their deposit. The court in this case did not address whether the seller could potentially recover its actual damages instead.\textsuperscript{115}

In light of these Florida cases it appears that a clause limiting the buyer’s sole remedy to return of its earnest money but allowing the seller the remedy of retention of the buyer’s earnest money, will not be enforced under Florida law. However, there are two Florida cases that may have taken a less protective approach. The court in Greenstein v. Greenbrook, Ltd. and Florida Housing Capital Corp.,\textsuperscript{116} enforced a limitation of remedy clause that prohibited both parties from bringing a claim of specific performance for the other party’s breach ruling that this was mutual and reasonable.\textsuperscript{117} Although the court focused on the portion of the remedies clause that provided for the mutual agreement relating to specific performance, the clause also stated that the buyer’s “full and complete settlement of all claims against Seller” in the event of the seller’s default was refund of all monies paid to the seller by the buyer and the seller’s remedy was retaining the moneys paid to the seller by the buyer as liquidated damages.\textsuperscript{118} The court failed to address this fact except in a footnote where it stated that they have not decided whether the buyer in an action for damages upon seller’s default would be limited to the return of his deposit where seller’s default was shown to be in bad faith. However, the court then cited to a prior Florida case that did allow recovery beyond return of buyer’s earnest money where there was a finding of bad faith by the seller. Although unclear, it may be the case that this court is indicating it will enforce this type of limitation of liability clause unless there is a showing of bad faith (indeed in the Port Largo case in the same district the court ruled three years later that to obtain benefit of the bargain damages in that case there needed to be a showing of bad faith).\textsuperscript{119}

The second Florida case with a less protective approach was Developers of Solamar, LLC v. Weinhaus and Gudac.\textsuperscript{120} The contract in Solamar included an exception to the limitation of the buyer’s remedies in the event of the seller’s willful breach of the contract. In light of this, the court concluded that this default clause did not fail for lack of mutuality of obligation in that the buyer could seek his actual damages if the seller had willfully failed to perform. As such the seller could not have breached the terms of the contract “with impunity.”\textsuperscript{121} While this is accurate, an argument could still be made, as raised earlier, that whether the seller breached for a cause beyond its control

\textsuperscript{114} The limitation of remedy clause in this case was even more unfair than the paradigm clause since it not only limited the buyers’ sole remedy to return of their earnest money, it also granted the seller the right to choose between retaining the earnest money as liquidated damages or pursuing an action at law for actual damages or pursuing equitable remedies. \textit{Id.} at 1303.

\textsuperscript{115} \textit{Id.}

\textsuperscript{116} Greenstein v. Greenbrook, 413 So. 2d 842 (Fla. Dist. Ct. App. 1982).

\textsuperscript{117} \textit{Id.} at 843.

\textsuperscript{118} \textit{Id.} at 842.

\textsuperscript{119} \textit{Id.} at 843 n. 4.

\textsuperscript{120} Cates v. Heffernan, 18 So. 23d 13 (Fla. Dist. Ct. App. 2009).

\textsuperscript{121} \textit{Id.} at 16.
or with impunity, the buyer’s losses exist in both situations and if the seller has reserved more meaningful remedies for a buyer default a court might find no real remedy to the buyer in such circumstance to be so imbalanced as to be an unreasonable limitation of liability or unconscionable.

It should be noted that other states have also embraced the concept that an illusory promise can cause a contract or clause in a contract to be unenforceable, albeit in different factual contexts. The court in Reeves v. Memorial Terrace, Ltd., laid out this law in a case where the terms of the contract made the buyer’s promise to purchase illusory. The court in Reeves, noted that for a contract to be enforceable, it must be supported by valid consideration (i.e. a mutuality of obligation) and that consideration can consist of an exchange of promises. “However, if a promise fails to actually bind a party because he retains the option to terminate the transaction in lieu of performing it, then the promise is illusory and is not valid consideration...Therefore, when illusory promises are all that support a purported bilateral contract, there is not contract.”

Although there is no direct power to terminate the agreement at any time in our paradigm situation, we argue that when the remedies upon breach are merely return of the buyer’s earnest money, the seller has created a power to terminate the agreement at any time making the seller’s promises of performance illusory.

In summary, home-buyers are more likely to be protected from grossly unfair limitation of remedies clauses in Florida than in other states for two reasons. The first is the different legal standard they apply to limitation of liability clauses than do other jurisdictions. Florida courts will not enforce limitation of remedy clauses when they are shown to be “unreasonable” while other courts require that such clauses be at the far higher standard of “unconscionable” to be unenforceable. Second, Florida courts better recognize the “non-remedy” nature of the “remedy” of returning to the non-breaching party their own money and find contracts that provide this as the sole remedy to be illusory in nature; thereby allowing the courts to not enforce the clause. Viewing such clauses as creating an illusory agreement has also enabled Florida courts to not enforce the clause when the buyer has breached and relegate the seller to actual damages rather than the liquidated damages amount when the liquidated damages amount was higher.

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122 See generally RESTATEMENT (SECOND) OF CONTRACTS § 77 (1981) Comment: a. Illusory promises “Words of promise which by their terms make performance entirely optional with the ‘promisor’ do not constitute a promise” and illustration 1 “A promises B to act as B’s agent for three years from a future date on certain terms; B agrees that A may so act, but reserves the power to terminate the agreement at any time. B’s agreement is not consideration, since it involves no promise by him.”


124 Id.

125 Id. See generally RESTATEMENT (SECOND) OF CONTRACTS § 77 (1981) and cases noted there.
In light of the results from the two empirical studies described in Section I and the Remedies Experiment detailed in Section II, the approach of requiring that limitation of remedy clauses be reasonable to be enforced makes much more sense than the approach of applying the very difficult to meet unconscionability test. The unconscionability test makes sense when there has been a true bargain between parties who understood what was agreed to. When this has not occurred, courts still engage in this fiction in order to further the goal of certainty of contract and to encourage parties to not enter into contracts when they do not understand what they are agreeing to. But in light of the widespread use of highly unfair limitation of remedies clauses evidenced in the two empirical studies, the likely lack of bargaining over such clauses in light of the profound lack of consumer understanding of them as evidenced in the Remedies Experiment (with participants being overly optimistic that they still had remedies available to them notwithstanding clear to language to the contrary—clear at least to a lawyer), it is imperative that courts take this reality into account and apply the Florida approach or other protective approaches described in Section IV.

IV. Legal Reforms to Address the Problem of Dysfunctional Contracts

There are four law reforms we propose to reduce the problem of dysfunctional contracts (i.e. contracts where the professional seller’s form limits the seller’s liability for its breach of the contract to return of the buyer’s earnest money and reserves to the seller far more significant rights in the event of the buyer’s default such as retention of this earnest money).

(a) Modify the Unauthorized Practice of Law Rules

Entering into a contract to purchase a home is the single largest and most important transaction that most consumers will enter into, and such contracts typically cover, in a highly technical fashion, a myriad of legal issues that can arise both before the closing and after. Yet it is the practice in many states for homebuyers to not be represented by an attorney who will review and propose changes to the form contract to protect the buyer’s expectations and goals, as is more commonly done in Illinois and a

126 See Odd Man Out, note 15, at n. 4(95% of the 132 Columbus home buyers surveyed said that their house was the most valuable asset they owned).


128 See supra note 11 for examples of states that permit brokers to fill in form purchase contracts. When brokers are permitted to fill in form purchase contracts (a task which is arguably incident to their role in helping to bring the buyer and seller together), it is in the broker’s interest to not have an attorney review and approve the contract since the attorney may raise points that delay the deal or even cause the deal to not go through. Consequently, brokers are not likely to encourage the buyer to hire an attorney at this stage (unless they would have liability if they did not). Based on data collected in an empirical study in Columbus, Ohio 59% of homebuyers interviewed indicated that they did not hire an attorney to represent them. See also Odd Man Out, supra note 15.
few other states. One important reason for the prevailing practice of home buyers relying on brokers for assistance rather than lawyers is that in many states the rules on the “unauthorized practice of law” permit brokers to fill in standard form purchase and sale contracts and do not require that only attorneys can do so. It is thus customary for real estate brokers to use the standard form contract prepared by the developer, fill in the blanks of the form contract, such as the purchase price, loan numbers, and closing date, but not provide legal advice on the contract. Some courts have permitted this, it appears, due to a failure to appreciate the important rights that can be eradicated through contract that a well-trained attorney would identify and address but a broker would not. But some courts, such as the Supreme Court of New Jersey, have expressed an appreciation for the important rights and obligations that are created in a real estate purchase agreement, but concluded that since there is no evidence of how the public is in fact harmed when not represented by an attorney, they would not prevent brokers from

129 See Navigating Attorney Approvals, supra note 127, at n. 39 noting eleven states where there is case law on the use of attorney approval clauses in residential deals.

130 Another important reason is that some attorneys fail to properly review the purchase agreement with the buyer as they should, causing home buyers to justifiably not see any value in spending the money to hire an attorney. The homebuyers in the empirical study in Columbus, Ohio provided two main reasons for choosing not to hire an attorney: (i) the costs for the attorney (with some expressing it would be a waste of money) and because other persons in the transaction performed the role of or obviated the need for a lawyer. See Odd Man Out, note 15, at 472.

131 See supra note 11.

132 See Id. on brokers being permitted to fill in form contracts and cases therein which also clarified this did not include giving legal advice; See also Pope County Bar Ass’n v. Suggs, 624 S.W. 2d 828, 829 (Ark. 1981) (“the broker shall not give advice or opinions as to the legal rights of the parties, as to the legal effects of instruments to accomplish specific purposes or as to the validity of title to real estate.”); and State ex rel. Wright v. Barlow, 131 Neb. 294, 296 (1936)(permitted to act as an amanuensis but not provide advise or counsel as to the legal effect and validity of legal instruments).

133 See Chicago Bar Ass’n v. Quinlan and Tyson, Inc., 34 Ill. 2d 116, 120-21 (1966)(the court distinguished filling in blanks on a deed or other document that affects title to real estate which have “many points to consider” with filling in blanks [such as the date, price, name of the purchaser, location of the property, date of giving possession, and duration of the offer] or making appropriate deletions to conform to the facts, in a purchase and sale contract that is customarily used in the community, since such services “require no more than ordinary business intelligence and do not require the skill peculiar to one trained and experienced in the law.”) It is hard to understand why the court understood how “filling in some blanks” can be more complicated than it appears in a deed affecting title, but not in a contract form that affects the parties rights and obligations between each other.

134 See In re Opinion No. 26 of the Comm., 139 N.J. 1323, 1345, 1351 (1995). The court also noted the cost savings to the homebuyer when the broker fills in the form contract as contrasted with the buyer paying to have an attorney do so.
assisting home buyers in the use of a form purchase contract. Furthermore, when attorneys fail to spot problems with how a transaction is structured and documented and fail to negotiate for changes to reduce these problems, or fail to inform their client of these problems, their clients justifiably see no added value in hiring an attorney and only see the added costs in doing so.

Based on the results from the Remedies Experiment it is clear that most consumers, even if they carefully read the limitation of remedy clause in the contracts presented to them, will not understand what rights they have waived and will not know to bargain for the clause to be revised or to bargain for an attorney’s fees clause to be added to the contract. One way to address this major problem is to change the unauthorized practice of law (“UPL”) rules to not permit brokers to fill in the blanks of a purchase and sale agreement, which should lead more buyers to seek out an attorney to assist them with this. The forms could be required by state law to state at the top that this legal document will have a major impact on the buyer’s rights and obligations and that the buyer should consult with an attorney before signing the agreement. States could go even further and require that prospective home buyers hire an attorney to review and advise them on the purchase and sale agreement before the buyer can be bound by the agreement (such as requiring an attorney review/approval clause). In light of the results from our Attorney Survey which reflected, among other things, that in 1-10% of the deals a major dispute arises between the parties after the contract is signed, and that the contract language is likely to have an essential impact on the rights and obligations of the parties relevant to this dispute, there is now empirical support for the proposition that homebuyers are clearly harmed when they are not represented by a well trained attorney. We therefore propose a companion rule to the change in the UPL laws that we proposed that would mandate use of an attorney by a home purchaser. The UPL rules should also require that only attorneys who have undergone special training and additional licensing for this type of representation can represent buyers of homes related to this area of practice. This would better ensure that home purchasers receive real value if they are required to hire an attorney to protect their interests.

(b) Enact Legislation That Prohibits Remedies Clauses That Limit Buyers’ Remedies to Return of Earnest Money and Create Safe Harbor Rules Based on Mutuality of Remedy and True Bargaining

Unfortunately, even if assisted by very able counsel, such attorneys might not be successful in negotiating for revisions to the typical limitation of remedies clauses used by developers, especially if it happens to be a seller’s market. Because of this, even with a reform of the UPL rules, state legislators should consider legislation that prohibits

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135 Id.
136 Indeed, as noted in Section II, many participants appear not to recognize the possibility of recovering benefit of the bargain/expectation damages or consequential damages, and expressed skepticism that this is a loss that a buyer could ever recover.
137 Only 35% of the attorneys in the Attorney Survey rated themselves as successful in negotiating over highly problematic or highly unfair terms in a professional seller’s purchase contract form greater than 50% of the time.
the one-sided type remedy clauses focused on in this article. The question then arises what would be an acceptable limitation of remedy clause under the statute (i.e. examples of “safe harbors”). For example, is it adequate protection to enforce limitation of remedy clauses but create a “bad faith” exception to enforcement when the developer is breaching to take advantage of property appreciation in value? We do not think so for reasons articulated earlier. What if the limitation of remedies clause permits the buyer her out of pocket expenses, but at a very low or nominal figure, should that be enforceable? It is difficult to anticipate and address each possible scenario that can arise, and a goal besides protecting buyers is to create rules that are both clear in scope and that permit true bargaining to occur. To accomplish this, safe harbors could be created based upon the concept of mutuality—so if the remedies clause is truly mutual this would be a safe harbor. An example would be mutual liquidating damages (seller retains 5% of the purchase price if buyer breaches and buyer is entitled to 5% of the purchase price if seller breaches) or mutual rights to specific performance, provided the seller can provide marketable title or reserving to both parties all rights and remedies available at law or in equity. We advocate creating legislation that prohibits the type of limitation of remedy clause focused on in this article (where the buyer’s sole remedy is return of the buyer’s earnest money, even with interest on it) but also creates safe harbors based on specific examples of acceptable mutual remedies. Any limitation of remedies clause used that does not fit within the parameters of what is expressly prohibited or expressly permitted as a safe harbor would then be judged by a court as enforceable or not under a test that asks the court to determine if the limitation of remedies clause under the circumstances of that case was “reasonable” or not (the Florida approach). A major factor in this determination could be if the clause was truly bargained over, with the buyer being represented by an attorney, and being presented with the choice between accepting a limitation of remedies that is not mutual but that they can agree to in exchange for certain valuable consideration (such as a reduction in the purchase price) or the right to decline this other valuable consideration and enjoy a mutual limitation of remedies clause instead.

(c) Replace Substantive Unconscionability Test With a “Reasonable Limitation of Remedy” Test in the Home Purchase Context

Although legislation is preferable to pure judicial response to the problem of dysfunctional contracts since legislation can more clearly and comprehensively address the problem than court decisions can, if legislatures fail to enact protections, then courts need to better protect home purchasers from highly unfair limitation of remedies clauses. Courts should replace the near impossible to meet test of substantive unconscionability with the test of whether the limitation of remedy clause under the circumstances is “reasonable.” Courts could look to factors such as mutuality and true bargaining articulated above in determining whether the clause is reasonable or not. All courts already engage in a test of reasonableness in enforcing liquidated damages clauses and so applying a reasonableness test in the context of limitations of remedies would not be unprecedented (also, as previously noted, courts in Florida already apply this approach to limitation of remedy clauses).
(d) Enact Legislation Requiring Attorney’s Fees to the Prevailing Party When Enforcing Rights in the Context of a Home Purchase Agreement

The reform of requiring attorney’s fees to the prevailing party in a lawsuit to enforce the home purchase agreement is critical because without it, even if the home buyer would have a valid claim for meaningful damages against a breaching seller, the buyer will unlikely be able to afford litigating the claim. This is because the costs of proving one’s case in litigation are typically very high. As noted in Section II, 71% of the participants in the clearly unfair condition and 76% in the vaguely unfair condition mistakenly believed there were no laws of remedies that would prevent their recovering their attorneys’ fees for handling the litigation to enforce the contract. They did not realize that this right must be in the contract or in a statute for them to recover on this. Yet, as noted in Section I, only 14% of the contracts in the Condo Contracts Study contained an attorney’s fees provision to the prevailing party in the event of a lawsuit to enforce the agreement. In light of the foregoing, states should enact legislation to require that this type of clause be added to the form purchase agreements used so that all buyers will have this right and realize they have this right if a dispute arises and they later carefully review the contract to see their rights.

Conclusion:

The results from the Condo Contract Study reflect that the vast majority of form contracts used by condominium developers in the jurisdiction examined contain a limitation of remedies clause that is completely one-sided, patently unreasonable, and that causes the seller’s obligations under the contract to be illusory in nature unless “saved” with an implied “bad faith” exception. Yet based on a review of relevant case law, it appears that many courts will still enforce this type of clause when it is clearly provided for and therefore presumably bargained for. But in order to bargain for a contract term one must at least understand it. Consequently, this article examined how well laypersons in fact understand this prevalent type of limitation of remedy clause by assigning one group to a fair remedies clause condition (where both parties have reserved all rights and remedies under the law in the event of a breach), a second group to a clearly unfair remedies clause (where the buyer’s sole remedy in the event of seller’s breach is return of the buyer’s own earnest money and the seller’s remedy, in the event of the buyer’s breach, is retention of that earnest money), and a third group to a vaguely unfair remedies clause (where the buyer’s sole remedy is limited to return of buyer’s earnest money but the clause does not expressly state this occurs in the case of the seller’s breach). The results of this Remedies Experiment reflected a profound misunderstanding of the impact of the two unfair remedies clauses with, for example, 64% in the clearly unfair condition and 68% in the vaguely unfair condition mistakenly believing they could still seek specific performance if the seller breached the contract and 54% in the clearly unfair condition and 60% in the vaguely unfair condition mistakenly believing that they could recover certain out of pocket expenses in the event of the seller’s breach. These results,

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138 See supra note 18.
139 See supra Section III for a discussion of case law.
140 Id.
and the others detailed in Section II, demonstrate that courts truly engage in a fiction when they presume that consumers understand clearly worded limitation of remedies clauses (clear at least to attorneys and judges) and therefore conclude that these clauses should be enforced because they have been bargained for. In light of this reality, we argue that home purchasers need greater protections than they currently enjoy and identify four areas of legal reform to better protect such home purchasers: (i) revise the unauthorized practice of law rules to mandate attorney review and approval of home purchase contracts, further requiring such attorneys to be specially trained and licensed for this type of representation, (ii) enact legislation that prohibits remedies clauses that limit buyers’ remedies to return of earnest money and create safe harbor rules based on mutuality of remedy and true bargaining in the home purchase contract, (iii) replace the substantive unconscionability test with a “reasonable limitation of remedy” test in the home purchase context for limitation of remedy clauses, and (iv) enact legislation requiring attorney’s fees to the prevailing party in the context of enforcing rights in a home purchase agreement.