Client Alert.

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Online Businesses - Are your terms and conditions fair?

By Susan McLean and Alistair Maughan

Have you heard the one about the 5-year-old trader and the £50,000 losses? No, actually, it's not a joke…

Two recent cases in Europe indicate how courts across Europe will apply rules on the enforceability of online contracts. In one case, the UK High Court held that a man, who blamed his girlfriend's five year old son for running up £50,000 of losses in online spread-betting, was not bound by a provision in online terms and conditions that made him responsible for trades made on his account. The online operator had to bear the loss even though it's not clear what more it could have done and, to the extent that any "fault" existed, surely it was on the part of the careless online user.

The issue of enforceability of online contracts is a familiar one: how do online businesses ensure that their terms of trading form binding contracts with their customers? The consequences of failing to implement the correct procedures can be real – as the online spread-betting operator in the UK case described below found out to its (considerable) cost.

In Europe, various rules and regulations apply to online contracts depending on the country and sector (most countries' financial services regulators have issued particular regulations, for example). Typically, the rules in Europe target:

- the information which must be disclosed to online customers;
- cooling-off periods for online purchases; and
- the test of fairness (or otherwise) to be applied to online terms.

It has been left up to the courts to fill in the gaps by adjudicating on the procedures by which online contracts are formed in the first place and to interpret the fairness requirements. These two recent cases – one a UK case and the other a European Court of justice ruling on a Hungarian case – covered both the *formation* and *fairness* aspects of online contracting.

Spreadex Limited v Cochrane

Mr. Cochrane opened an online account with the online spread-betting company, Spreadex, in October 2010. As part of the account sign-up process, Cochrane was asked to "*read our U.S. based policy, Client Declaration, Customer Agreement, Risk Warning Notice and Order Execution Policy. Once read and understood, please click on "Agree" to signify your agreement to the terms*". Cochrane ticked to accept the terms.

Cochrane made a significant number of trades each month. By the beginning of May 2011, he had a credit balance of more than £60,000. On 2 May 2011, whilst staying at his girlfriend's house, he used his computer to make trades and this was witnessed by her five-year-old son "C". Cochrane explained the trades to C as a kind of "guessing game". Cochrane left his computer at his girlfriend's house for two days whilst visiting a friend. A few days later, Cochrane learnt that his account was £50,000 in debit. Cochrane claimed that C had run up the losses whilst "playing" on Cochrane's computer.

Cochrane explained the situation to Spreadex but Spreadex demanded payment of the losses and brought a claim for summary judgment relying on clause 10(3) of its 49 page Customer Agreement which provided "*You will be deemed to have authorised all trading under your account number*".

The High Court rejected Spreadex's application for summary judgment and held that clause 10(3) was not legally binding because (1) it did not form part of a binding contract between Spreadex and Cochrane and (2) it was an unfair term.

On the issue of formation, the Judge held that the online terms and conditions which Cochrane had accepted did not constitute a contract. For a contract to be formed under English law (whether online or offline), there must be offer, acceptance and consideration (*i.e.*, each party must obtain a benefit from the contract). The Judge held that there was no consideration. The online terms and conditions were so favourable to Spreadex (for example, Spreadex could refuse to accept bets, it could remove their online service at any time and it had the right to close or suspend an account at any time) that there was effectively no commitment from Spreadex.

On the issue of fairness, the Judge held that the contract had not been drafted in accordance with the good faith requirements under the Unfair Terms in Consumer Contracts Regulations 1999 and there was a significant imbalance in the parties' rights and obligations arising under the contract that negatively impinged on Cochrane's rights. As the terms were not fair, they were not legally binding on Cochrane. The Judge indicated in his judgment that if the clause had only made Cochrane liable for unauthorised trades where he had been negligent the provision may have passed the fairness test, but making him liable for all unauthorised trades under his account was not fair.

The Judge also said that Spreadex had not made sufficient effort to inform Cochrane of the clause. The Judge believed that it was unlikely that Cochrane would have reviewed all four of the documents referred to during the acceptance process and would have been "*close to a miracle"* if Cochrane had actually read clause 10(3) of the Customer Agreement, "*let alone appreciated its purport or implications*". In fact, the Judge believed that the 49-page Customer Agreement was an "*entirely inadequate*" way to seek to make the customer liable for any potential trades he did not authorise.

Unfair Terms in Consumer Contracts

All countries in the EU are required to implement the Unfair Terms Directive (93/13/EEC) on unfair terms in consumer contracts ("Unfair Terms Directive"). This directive protects consumers from unfair terms used by suppliers in two ways: firstly, it requires that suppliers draft in plain and intelligible language (the so-called "transparency test"); secondly, it applies a test of fairness to the substance of most terms (the "fairness test"). The Unfair Terms Directive also gives a list of terms which may potentially be unfair.

The Unfair Terms Directive has been implemented in the UK in the Unfair Terms in Consumer Contracts 1999. Under the Unfair Terms in Consumer Contracts Regulations 1999, "unfair" contract terms are not binding on a consumer. A contractual term which has not been individually negotiated is considered unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract to the detriment of the consumer.

Nemzeti Fogyasztóvédelmi Hatóság v Invitel Távkőzlési Zrt.

No, we don't know how to pronounce it, either.

This case arose when a Hungarian court asked the ECJ for a ruling on the Hungarian implementation of the Unfair Terms

Directive. Back in 2008, Invitel, a fixed-line telephone network operator in Hungary, varied its terms and conditions to include a term which required consumers using money orders to pay additional fees. This led to a flood of complaints and, eventually, to the highest court in Europe.

The core problem was that a Hungarian statute gives consumers a right to terminate if the supplier unilaterally varies the contract charges. This is actually a mandatory provision of local law but the ECJ still found that the supplier must state this right in the consumer contract in plain and intelligible language, and any failure to do so should be taken into account by a national court when determining whether a term of a consumer contract is unfair.

The main elements of the ECJ's findings were that:

- a consumer must be given the opportunity to examine all the contract terms and their effects;
- any supplier must always draft in plain and intelligible language;
- suppliers must always inform consumer of any mandatory statutory or regulatory provisions which may set out a supplier's rights to vary fees and/or which provide a consumer with a termination right in these circumstances.

The ECJ's decision is consistent with an earlier decision from January 2012 in a different Hungarian case in which it ruled that, in relation to a consumer contract, a national court in the EU has a duty (not merely a right or power) to assess the fairness of a term even if the consumer has not challenged the fairness of that term. If the national court considers a term to be unfair, it must not apply it unless the consumer wants it to be applied.

CONCLUSION

Although the *Spreadex* case is clearly unusual, it is a useful reminder that companies providing products or services online need to be very careful when drafting their terms and conditions to ensure that those terms are enforceable against consumers.

DRAFTING TIPS

- Try to make the contracting process as straightforward as possible (*e.g.*, are multiple sets of terms and policies necessary? Can all relevant issues be contained in one set of terms and conditions?).
- Make the terms easy to read – this applies to the format as well as the wording itself (*e.g.*, don't make the wording too small or too closely printed).
- Try to limit the length of any terms and conditions to something manageable (a consumer is more likely to read 5 pages than 49 pages – particularly if scrolling through terms online).
- Ensure that your contracting terms are binding (in particular, that they are not drafted with such little commitment on your side that it could be argued that there is no consideration).
- Avoid making your terms and conditions unreasonably one-sided. Whilst protecting your organization, try to make the provisions as reciprocal as possible, bearing in mind the responsibilities of each party.
- Draft your terms and conditions in language which is as clear and simple as possible – avoid legal or technical jargon wherever possible.
- Bring any unusual or onerous terms to the attention of the consumer.

- If your organisation operates globally, before using any standard terms and policies in respect of your European operations make sure that you review those terms and policies in light of the local implementation of the Unfair Terms Directive and other applicable laws. What works in the U.S. or in other jurisdictions may not meet the requirements of applicable UK or other European consumer laws.

Contact:

Susan McLean
44 20 7920 4045
smclean@mofo.com

Alistair Maughan
44 20 7920 4066
amaughan@mofo.com

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