

Unconscionability – Statutory Prevention of Unethical Business Practices

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ABSTRACT

This paper examines broadly the doctrine of unconscionability and analyzes to what extent business as well as consumer contracts in Malaysia do not preclude the possibility of unconscionability and unethical bargains. The commercial or business to business contracts look into the relationship in agency and franchising while the consumer contracts specifically relate to the sales of goods, consumer credit as well as sales and purchase of housing. These commercial and consumer contracts are commonly adhesion in nature and are getting more complex in the modern world. This paper would also suggest the statutory requirement of conscionable conduct in all its variation in both the formation as well as performance of commercial and consumer contracts generally. The variation of conscionable conduct refers to conducts that are fair and made in good faith or without undue influence, gross inequality or presumed dishonesty.

Keywords: Unconscionability, Unethical Business Practices, Business-To-Business Contract and Consumer Contract

INTRODUCTION

Conducts and bargains that are considered inequitable in contractual relationships have always become the subject of legal scrutiny as these situations suggest that contractual justice has been compromised. In order to deal with such a situation, special equitable rules such as unconscionability, good faith, undue influence, inequality of bargaining position and fair dealing have been developed. Despite the several rules available to deal with inequitable conduct, it will appear that the rule of unconscionability is of a wider application.

Unconscionability is understood by jurists as a doctrine used by the court of equity to correct men's conscience against conducts and bargains that are unconscionable. This understanding is derived from the judgments in several early

English cases including the *Earl of Oxford's Case* (1615), *Earl of Chesterfield v Janssen* (1751) and *Earl of Aylesford v Morris* (1873). Until now, inspiring writings and discussions have been made concerning the supposed or probable definition, description, criteria and application of the doctrine. Impliedly, it means that the uncertain nature of the doctrine does not deter its significance in promoting and achieving contractual justice; a prominent theory in contract law apart from the theory of freedom of contract.

In Malaysia, the doctrine of unconscionability is considered as still at its infancy but the awareness of the existence of this doctrine seems to be gaining ground. As diverse forms of businesses and relationships also exist in Malaysia, it is probable that the business as well as consumer contracts in Malaysia do not preclude the possibility of unconscionability and unethical bargains. There are two types of contractual relationships; contracts between businesspersons and contracts between businessperson and consumer. Both are the produce of human creativity to satisfy their wants and needs. In this paper, the commercial or business to business contracts look into the relationship in agency and franchising while the consumer contracts specifically relate to the sales of goods, consumer credit as well as sales and purchase of housing. These commercial and consumer contracts are commonly adhesion in nature and are getting more complex in the modern world.

This paper presents the new parameters of the doctrine of unconscionability in the law of contract. The new parameters will then be used to explain the possibility of unconscionable and unethical bargains in business and consumer contracts. This paper also suggests the statutory requirement of conscionable conduct in all its variation in both the formation as well as performance of commercial and consumer contract generally.

PARAMETERS OF THE DOCTRINE OF UNCONSCIONABILITY

Unconscionability is a prime element in contractual justice without which contractual justice cannot stand firmly as a theory in the law of contract. As a prime element in contractual justice, unconscionability should be placed as an essential doctrine in the law of contract. The modern law of contract is a marriage between common law and equity. Common lawyers prefer the test of reasonableness over fairness in the law of contract. This preference entails unconscionability although unconscionability is a creature of equity.

Inequitability connotes the unfair or unjust practice, which is against the contractual justice, while unethicality relates to the immoral practice. At a first glance, morality stands in a different ground from contractual justice but borrowing the word of HLA Hart (1961), justice is a specific idea within the general sphere of morality. Therefore, justice may sometimes collide with the other ideas of morality including ethics. The pursuit of achieving contractual justice is clear within the

doctrine of unconscionability and its parameters that include fairness, good faith and fair dealing, undue influence and, in certain circumstances, inequality of bargaining position and honesty are also concomitant to ensure an ethical bargain. Since the limits of unconscionability can be ascertained by these factors, the claim by Cooke and Oughton (2000) that unconscionability is devoid of real content, therefore, could not stand. The developments in the respective factors do not remove them from being part of unconscionability. Instead they will feed unconscionability.

Special position or disadvantage is not a pre-condition for unconscionability but its existence gives unconscionability the more reason to exist. It is particularly useful when the mechanism used to determine unconscionability is undue influence and gross inequality; less or of no use in good faith and fair dealing. The special disadvantage refers to the condition or situation of the party that makes his position more disadvantageous than other contracting parties in the same situation.

In order to allow a broader commercial application of the notion of special disadvantage, it is proposed here to adopt the view by the Federal Court of Australia in *ACCC v. Samton Holdings Pty. Ltd. and Others*¹ that special disadvantage can occur as a result of either situational disadvantage or constitutional disadvantage. It is ‘special’ because it adds to the disadvantage position and contributes to justify the conscionability of the commercial transaction among businesspersons. This means that the adaptation of special disadvantageous is according to the circumstances of each particular case and the use of reasonableness is necessary to substantiate a fair valuation of the case.

From one perspective, it is arguable that because of the existence of special disadvantage of a party or the parties’ inequality, good faith should be an inherent factor. However, such argument means a direct importation of civil law’s concept of good faith in contracts to common law. Compared to good faith, the doctrine of unconscionability was brought to life at the common law jurisdiction. In spite of the ambiguities and diverse views in relation to its nature and scope, unconscionability has its root firmly ground at common law.

Presumed dishonesty in the sense of equitable fraud emphasizes on the existence of special position or disadvantage of a party contracting along with the unconscientious use of the power, or extortion or unfair advantage taken. This view is derived from the explanations of equitable fraud by Lord Selborne in *Earl of Aylesford v. Morris*² and of presumed dishonesty in the Halsbury’s law of Malaysia (2005). Therefore, the statement made by Gopal Sri Ram JCA in *Saad Marwi v Chan Hwan Hua & Anor* that “English equity jurisprudence does in fact recognize a wider doctrine of unconscionable bargains as a species of equitable fraud”³ is not followed. Rather, the existence of presumed dishonesty or equitable fraud shows,

¹ (2002) 189 ALR 76 at 92.

² (1873) LR 8 Ch App 484, 490-491.

³ [2001] 3 CLJ 98 at 114-115 (CA).

as stated in *The Earl of Chesterfield v Janssen*, the “intrinsic unconscionableness of the bargain.”⁴

Arguments against applying the doctrine of unconscionability to commercial transactions rest upon the issues of uncertainty as well as the financial impact upon business. Again, it should be noted that certainty requires that contractual duty will not arise outside the terms of the agreement. Apart from the question of certainty of contract, achieving contractual justice via unconscionability will result in greater efficiency in the contract by reducing the cost of avoiding non-compliance. For example, if ‘A’ knows that he can contract with ‘B’ and the law will protect him if ‘B’ behaves unconscionably, ‘A’ will be more willing to contract. The contract will not become more complicated, rigid or involving prolonged negotiation. The process of the contract will become more efficient.

In relation to the financial impact upon business, it would cause the business to be unduly stopped or terminated because of the finding of unconscionability. There is a truth in the argument if unconscionability is applied on the reasoning of inequality of bargaining position without considering whether there is gross inequality, in the circumstances. However, it is arguable that this claim is usually made by or on behalf of the stronger businesspersons or unscrupulous businesspersons to protect what they call as their legitimate business interests. The yardstick to determine the legitimate as opposed to the illegitimate seems to be based upon fairness and honesty, which in fact relates to good faith.⁵ It is also valid to claim that both parties in a contract can argue that they have their own separate legitimate business interests. In practice, it is unlikely that a commercial contract between businesspersons will be left absolutely undisturbed by law in cases where gross inequality of bargaining power occurs or lack of good faith and fair dealing and/or dishonesty are proven, unless the courts’ focus is only upon attaining freedom of contract.

Unconscionability as a ground to seek relief is very dependent on the independent factors causing unconscionability. This means that unconscionability by itself is not a basis of any specific relief. It is a doctrine describing the lack of quality of the transaction and the lack of that quality maybe caused by some independent factors as discussed above. If, for example, the unconscionability were because of unfairness, lack of good faith, lack of fair dealing, undue influence or gross inequality, one should go to those independent factors to seek relief. Therefore, the remedy for unconscionability will depend on the remedy that is available for the factors that caused that unconscionability.

⁴ (1751) 2 Ves Sen 157; 28 ER 82 at 101.

⁵ Conaglen is right when he notes legitimate interests as the basic concept for the duty of good faith but his argument is unsound when he want to unite other doctrines like duress, undue influence and unconscionable bargains under the concept of good faith using legitimacy as the reason: MDJ Conaglen ‘Duress, Undue Influence, and Unconscionable Bargains – The Theoretical Mesh’ (1999) 18 NZ Uni L Rev 509, 541.

POSSIBILITY OF UNCONSCIONABLE AND UNETHICAL PRACTICES

Business Contracts

Agency

There are many business contracts that are actually carried out by the agents on behalf of or representing the principals. These agents are recognised in law by reason of the creation of the partnership and employment agreement or by reason of necessity and holding out. The law of agency in Malaysia is prescribed in Part X of the Contracts Act, 1950 (CA). The statutory provisions generally regulate the appointment and authority of agents, duties of the agent and principal inter se, and effect of agency on contract with third parties. The CA, however, does not oust the expressly or impliedly agreed rights and duties of the principal and agent.⁶ This situation can be inferred as Part X of the CA is silent on this matter. It is also understood that the CA is not a Code and is a statute of general application; hence parties to contract are free to determine their agreed terms.

Section 141(2) of the CA prescribes that the extent of an agent's authority is to do every lawful thing necessary for the purpose, or usually done in the course of conducting such business. It is clear that the guiding factor is what is lawful and necessary, which is subjective, or usually done in such business, which is objective. An agent, therefore, cannot act unlawfully. Section 24(e) of the CA prescribes that the consideration or object of an agreement is lawful, unless the court regards it as immoral, or opposed to the public policy. An agreement is unlawful when the court regards a particular consideration, which can be in the form of an act, abstinence or promise,⁷ or object of an agreement as immoral. Illustration (j) to section 24 shows an example of unethical or immoral behaviour of a solicitor. In that Illustration, a solicitor, A, promises to exercise his influence over B, his client, in favour of C who promises to pay him \$1,000 for the effort. Therefore, in relation to unlawful agreement, immorality in Malaysia is much wider than the common law notion and includes unethical bargains.

In addition to that, from the agency law perspective, Illustration (j) also shows that the solicitor who is the agent to the client promises to make secret profit out of the performance of his duty. Such conduct falls under the ambit of presumed dishonesty. In *TH Mahesan s/o Thambiah v Malaysia Government Officers' Co-operative Housing Society, Ltd* [1979] AC 374, it is a well settled law that an agent should not act dishonestly. In this case the director of a housing society who received a bribe entitled the principal to recover the amount of bribe and damages for the whole loss suffered by it as the result of the fraudulent transaction.

⁶ This rule is the same as common law, see AG Guest *Anson's Law of Contract*, p.543.

⁷ Section 2(d) of the CA.

In *Wong Mun Wai v Wong Tham Fatt and Anor* [1987] 2 MLJ 249, the court found that the first defendant failed in his duty as agent of the plaintiff when he sold the plaintiff's half share of land well below market value and when he failed to inform the plaintiff that he had sold it to the second defendant who was his wife. According to the court, the first defendant had a duty to act in good faith in protecting the interests of the plaintiff and could not use his position as agent to profit at the plaintiff's expense.

Both of the above cases show that unconscionable and unethical bargains could occur in agency. The agent's unconscionable and unethical bargains are implied in his equitable fraud or dishonest act of making secret profit or his lack of good faith in failing to give material information of the transaction to his principal.

Unconscionability is also a reason for estoppel to exist. According to Finn (1994), unconscionability in the specific field of equitable estoppel is used in the sense that "equity will prevent an unconscionable insistence on strict legal rights ... [and] are conditioned upon the explicit finding of unconscionable conduct in the person against whom they are invoked." It should be noted that estoppel claim would also exist in an agency by holding out. This principle is succinctly explained by Tan Sri Datuk Edgar Joseph Jr, SCJ in *Cheng Hang Guan & Ors. v Perumahan Farlim (Penang) Sdn. Bhd. & Ors.* [1994] 1 CLJ 19:

"The doctrine of "holding out", sometimes called apparent or ostensible authority, has been said to be based upon estoppel. Agency by estoppel arises where one person has so acted - and this he may do by allowing the agent to hold himself out as having authority as to lead another to believe that he has authorised a third person to act on his behalf, and that other, in such belief, enters into transactions with the third persons within the scope of his ostensible authority. The onus rests on the person dealing with the agent to establish real or ostensible authority... it would be unconscionable for a party to be permitted to deny that which, knowingly or unknowingly, he has allowed or encouraged another to assume to his detriment...."

Franchising

Franchising relationship is different from other forms of business relationships because it is a hybrid of several bodies of laws that make it a unique form of relationship. In Malaysia, complaints by the franchisors or franchisees on breach of a particular clause in the franchising agreement or any unfair practices in franchising can be brought to the Registrar of Franchises, the Malaysian Franchise Association or the court. The first two channels encourage mediation as an alternative form of dispute resolution. In fact, many franchising complaints are actually settled out of court because it is deemed that mediation will provide amicable resolution through innovative business arrangements (Miranda, 1997).

It is found that franchising is also open to unconscionable and unethical bargains due to its relational nature. Coratta (1992) reminds us that franchising is structurally vulnerable to conflicts, while Adams and Jones (1990) agree that franchising lends itself to a number of frauds and sharp practices. One of the measures apparently adopted by Malaysia in order to control these negative bargains is by prescribing the franchisors to provide disclosure documents so that prospective franchisees can have the full view of the franchise business. This requirement is impliedly a requirement of good faith and fair dealing. In other words, failure to provide such document and dishonesty in the disclosure is unconscionable.

According to Iglesias (2004), a certain degree of good faith is required in the relationship. The various views on the scope or meaning of good faith seemingly point to the duty to act fairly, honestly and reasonably to the other (Waddams, 1995; Steyn, 1997; Stack, 1999; and Peden, 2003). The requirement to act honestly is in fact available under section 29(1) of the Franchise Act 1998 (FA).

Caruso (2003) points out that franchising agreement was drafted by the franchisor and for the franchisor. The standard form agreements drafted by franchisors commonly include the franchisors' unilateral decisions rights, which equipped them with the ability to deal with contingencies during the performance of the franchise contract. Although the obvious reason behind this rights is to protect the franchisors' business interests and to maintain the uniformity of the system, franchisors must aware that such unilateral decision must be made "reasonably and with proper motive" and not arbitrarily.⁸ Else, it would be a sign of franchisors' unfair dealing and lacking in good faith for not considering the interests of the system as a whole.

It was decided in *Zapatha v Dairy Mart* that franchise agreement is unconscionable if the clause is worded obscurely. In a case study from the Franchise Unit of the Ministry of Entrepreneur and Cooperative Development (MECD), the franchisee complained that the franchisor has breached the territorial right that had been given to the franchisee according to the franchise agreement. The franchisor had unilaterally decided to open another franchise outlet at a location within an area where territorial right has already been given to the franchisee. The territorial right as provided in their franchise agreement is as follows:

"Within a diameter of 5 km (for the purpose of measurement from point to point, proper road way available at the point of agreement shall be used); or in a "taman" (housing area) with approximately 300 houses; or under special circumstances, the territory shall be agreed by the franchisor, franchisee and affected parties...."

⁸ *Bonfield v Aamco Transmissions, Inc.* 708 F Supp 867 (ND 111 1989).

The franchisor argued that no breach occurred because he interpreted the given territorial right as including all with the usage of the word 'or' in accordance to the agreement. This means that the franchisor had unilaterally interpreted the word 'or' as conjunctive and not disjunctive. The Registrar of Franchises agreed with him. However, it can be claimed that the clause on territorial right in the franchise agreement above was obscurely worded due to the use of the words 'or' and 'special circumstances'. Such clauses are unconscionable. There is an unfair advantage taken out of the inequality bargaining power and special disadvantage of the franchisee. It is the business concept dependence that causes the franchisees to succumb to the terms of agreements drafted by the franchisor. Such abuse is related to gross inequality.

Other examples of gross inequality by the franchisors include the unconscionable and unethical practices of franchisors who receives some economic benefit or secret rebates from the designated third party supplier on top of any payment received from franchisees;⁹ franchisor restricts certain franchisees from selling certain products or offering certain services that are sold or offered by competing franchisees at other location; and franchisor only allows selected franchisees to sell products or offer services at promotional price. In fact, section 20 of the Franchise Act 1998 (the FA) marks the latter two examples of discriminatory actions as an unfair franchise.

Consumer Contracts

Sale of Goods

The buying and selling of goods is the most common transaction that everyone will get involved in almost on a daily basis. This is the fact of a market economy. Hence, contract of sale of goods is the most fundamental kind of contract for consumers. According to Professor Atiyah (1991), the contract of sale of goods is a consensual transaction based on an agreement to buy and an agreement to sell. Despite it being consensual, consumers-purchasers are often at the weaker bargaining position. Evelyn (1982) points out that this situation is due to the operation of the principle of freedom of contract and growing complexity in the market.

Unconscionable practices in the sale of goods could exist within the method of dealings and the transactions. In a plain contract law term, these are known as the procedural and substantive process. The method of dealings in either conventional retail or direct selling would invite unconscionability arguments whenever the process at the procedural stage is tainted by the unfairness caused by undue influence or gross inequality.

The direct distribution method or direct selling, which includes the door-to-door plan, party plan, multi-level marketing plan and pyramid plan, is increasingly

⁹ *Jirna Ltd v Mister Donut of Canada Ltd* (1973) 40 DLR (3d) 303.

becoming a significant distribution channel within Malaysia's total retail enterprise system.¹⁰ As opposed to the conventional distribution method, direct selling occurs whenever the direct seller or retailer initiates contact with the potential customer instead of waiting for customer coming to him.

In direct selling that involves family members and friends as the consumers, most transactions are made to preserve their personal relationship. This ethical issue is intertwined with the doctrine of unconscionability when the will of the buyer is dominated by the seller to make unwanted purchases that enables the seller to gain unfair advantage.

Many multi-level marketing (MLM) plans are pyramid plans if they sell opportunity rather than product. While it is clear that pyramid selling is a fraud, many people are still lured into the trap set under the pyramid plan until they are too late to discover the truth.¹¹ The disguise of the pyramid scheme can be unmasked by the unconscionability doctrine via the good faith doctrine and unfair dealing.

There are a number of statutes which have been enacted which protect the consumer interests in Malaysia. These are found in the Sale of Goods Act 1957 (SGA) and the Consumer Protection Act 1999 (CPA). The SGA followed the obsolete English statute that is the English Sale of Goods Act 1893. The English statute has been replaced by the Sale of Goods Act 1979 (SGA 1979) and had incorporated some changes to the provisions. It is worthy to note that if some of the provisions in the SGA 1979 have been criticized by writers,¹² what more of the 'obsolete' Malaysian SGA.

A study in Hong Kong shows that unconscionability does occur when a seller insert terms that are so unfair that can be regarded as unconscionable.¹³ Likewise, unconscionability could occur in Malaysia via the standard form agreement between the seller and buyer. These terms are usually designed to protect the seller only against certain liability.

The SGA displaced the unfavorable principle of *caveat emptor* by having the principle of *caveat venditor* via the inclusion of implied terms in sale transaction. However, section 62 of the SGA allows the contracting parties to contract-out or exclude the implied terms if they wish. On one hand, the sanctity of contract is being observed by law. On the other hand, the consumers are being treated unfairly. Whether or not unconscionability exists depend upon the existence of the parameters of unconscionability in a particular case. It can be argued that the chances that

¹⁰ See DSAM 'What is Direct Selling?' at <<http://www.dsam.org.my>> as at 2/12/2008.

¹¹ Pyramid schemes scam: Colombians have lost hundreds of millions of dollars in pyramid schemes that are collapsing around the country-14 Nov 2008, 7:10am by ONENEWS at <<http://tvnz.co.nz/view/page/411366/2308292>> as at 2/12/2008.

¹² See Roger Tan Kor Mee 'The Need to Amend Sections 13 and 14 of the Sale of Goods Act 1979' [1990] 2 CLJ xviii.

¹³ The Law Reform of Hong Kong (February 1990) "Report on Sale of Goods and Supply of Services [Topic 21]" at <<http://www.hkreform.org>> as at 20/11/2008.

unconscionability might occur would be greater when the statutory protection is chosen to be excluded by the sellers. Unscrupulous sellers could then easily employ tactics that allow them to sell more goods without violating the SGA.

For instance, section 16(1)(a) of the SGA provides that there is an implied condition that goods must be fit for the particular purpose for which the goods are acquired. In *Frost v Aylesbury Dairy Co. Ltd* [1905] 1 KB 608, the seller was held liable for the typhoid-infected milk that caused death to the buyer. If in similar case a seller contract-out the implied term that the goods sold is on 'as is' basis, relying on the SGA will not assist the consumer. The consumer would need to seek the protection of the CPA where section 6 of the CPA prohibits any contracting out in the agreement. However, Geraint Howells, et. al. (2007) apparently points out there could be ways or tactics undertaken by sellers to undermine such statutory protection. These tactics could be in the form of less direct approaches relating to the time when those terms have to be complied with, such as a term that openly seek to say that the obligations as to quality or fitness only apply prior to installation, or a term deeming the consumer to have been made aware of defects relevant to the acceptable quality standards.

The melamine scandal involving melamine added to food products is meant to make it appear that it has higher protein content than what it actually contains. Malaysian law does give protection to consumers against unsafe goods via section 23 of the CPA. In addition to the CPA, the authorities should consider the law on labeling of the product. The weak labeling law caused melamine can be subsumed under other instances. The harm would only be known after the goods are consumed or after the ingredients are scientifically tested, which is a waste of both time and money. It should be made clear that the reason for a better law is to protect the consumers against the unscrupulous practice of manufacturers and sellers.

Consumer Credit

Contracts for consumer credit involve moneylending, hire-purchase, pawnbroking and banking. It appears that consumers entering into these borrowing and lending transactions often faced informational disadvantages and unwarranted consequences if the transaction fails (McBride, 2003). These transactions are also frequently characterized by unconscionable and unethical practices which are harsh, unjust or contain unfair terms.

i. Moneylending

Moneylending activities in Malaysia are regulated under the Moneylenders Act, 1951 (MA). The MA was patterned after the English Moneylenders Act 1900 which was enacted to curb the increasingly unconscionable practices of moneylending particularly in the case of unsecured loans. Section 21 of the MA empowers the

court to reopen a moneylending transaction where the Court is satisfied that the interest charged is excessive and that the transaction is harsh and unconscionable or substantially unfair.

Prior to the MA, it was held in *Chait Singh v. Budin b. Abdullah*¹⁴ that a presumption of unconscionability occurred in a moneylending transaction with a good collateral security which the defendant, an illiterate farmer, had to provide to the plaintiff because the interest charged was at a rate of 36 per cent per annum.¹⁵ It is understood from the case that an excessive interest and the special position of the party led to the presumption of unconscionability. Using the new parameters of unconscionability, the moneylenders had actually dealing unfairly and gaining unfair advantage by way of gross inequality between the parties.

Section 21 of the MA is said as underutilized due to lack of legislature guidance and conservatism of both the courts and legal profession (Cheong May Fong, 2005). It is submitted that evidence of excessive interest alone for moneylending transaction could invoke unconscionability. The term ‘excessive’ implies that the interest charged to the borrower is not just high but also unconscionable. The issue of excessiveness cannot be separated from unconscionability. It should be noted that excessiveness differs among judges as it is subject to government policy, overseas market and seasonal condition (Peden, 1982; Ford and Ford, 1985). Other evidence such as special position of the parties only gives it a greater reason for law to protect the borrowing party.

The doctrine of unconscionability is a practical tool to overcome the problem of illegal moneylending. The illegal moneylenders often charged exorbitant interest rate and use intimidating methods of recovering the loans in cases of non-repayment by the borrowers. Contract by the illegal or unlicensed moneylender is unenforceable under section 15 of the MA. Section 15 implies that consumers need statutory protection against unconscionable practices of illegal moneylenders. The effect of unenforceable contract is found in the CA. Unenforceable contract is void and any person who has received any advantage is bound to restore or compensate the person from whom he received it.¹⁶

Statutorily, unlicensed moneylender is different from exempted moneylender. In *Kok Swee Chin v. General Factoring and Credit Sdn Bhd*,¹⁷ credit companies granted exemption from the MA can charge any rate of interest they wish and operate from anywhere they like. This practice, of course, could lead to unconscionability. In *Aseam Credit Sdn Bhd v Eminent Avenue Sdn Bhd*¹⁸ the Court of Appeal seemingly

¹⁴ (1918) 1 FMSLR 348.

¹⁵ S. 17A of the MA prescribes the interest for secured loan is not more than 12% p.a. and for unsecured loan is not more than 18% p.a.

¹⁶ Ss. 2(g) and 66 of the CA.

¹⁷ [2004] 6 CLJ 101 HC.

¹⁸ [2008] 1 CLJ 12.

place a strict application of section 2A of the MA, unlike *Kok Swee Chin's* case, in order to ensure that the interest of the borrowers is protected. A mere letter from the Ministry promising an exemption is not valid. The companies claiming being exempted from the MA must show that the exemption has been gazetted. The decision in *Aseam's* case shows that statutory provision prevails in courts. The case also gives a subtle reminder to the authority that unconscionable practice could occur in moneylending transactions if the authority giving the exemption to the credit companies overlooked the requirements for exemption or failed to oversee the activities of these credit companies.

ii. Pawnbroking

The conventional pawnbroking business is governed under the Pawnbrokers Act 1972 (PA). The dealings in pawnbroking could confusedly become a moneylending if the pawnbrokers received money or deposit from members of the public in return of a higher interest to attract the depositors and then use the deposits to finance their pawnbroking businesses. However, in *Yeep Mooi v Chu Chin Hua & Ors*¹⁹, the contention that the depositor was a moneylender was set aside by Salleh Abas FJ as the depositor's main business was as a seamstress, not moneylending. The court also found that the pawnshop owner, upon receiving the deposits from 41 persons including the appellant, was carrying on a borrowing business illegally. The transactions were void and unenforceable. The appellant, nevertheless, was allowed to recover her money after the court agreed that she had placed her money on deposit in good faith without ever suspecting that the transaction was unlawful by any other law.

In pawnbroking transactions, consumers who wished to get quick and convenient source of credit without much formality would pawn their valuable belongings at a price that is usually low than the actual price of the goods. However, the common problem faced by consumers is the high interest rate. The rate of interest of 24% per annum allowed under the law continues to be rather high²⁰ as the loans given out are more than covered by the value of the collateral. According to Salleh Abas FJ in *Yeep Mooi's* case:

"It is true that pawnbroking business is still required to satisfy the need of the poor; but surely the system as we have today lends itself to their oppression. The interest charged is exorbitant, in the region of 24% per annum despite the fact that the loan is accompanied by the pledge of articles usually far in excess of the loan it advances.... In practice because the high rate of interest which keeps on accumulating, the

¹⁹ [1960] 1 LNS 169.

²⁰ Pawnbrokers (Control & Licensing) Regulation 2004; PU(A) 317/2004, regulation 17.

pawner is unable to find money to redeem the article as it becomes more expensive to do so than buying a new one. And so the article remains unredeemed and the loan unpaid, thereby giving right to the pawnshop to sell the article to satisfy its loan and keep the excess proceeds.”²¹

It should be noted that by using the word “oppression” in the learned judge’s statement above, it implies that charging 24% per annum enables the pawnshop owner to gain an unfair advantage by manipulating the inequality of bargaining position of the pawner. This is a clear instance of unconscionable practice which needs to be reconsidered by the legislature. In fact, the interest rate charged is higher than what is chargeable under the MA.

Another common complaint is that gold objects when pawned are not weighed and hence the weight of which is not recorded in pawn ticket or receipt. Subsequently, any complaints by consumers that the pawnshop owners had skimmed gold from the objects could not be verified. This dishonest and unethical practice is meant to obtain unfair advantage over the pawner. Such an act is also classified as unconscionable.

It is also unlawful for a person to pawn or attempt to pawn an article belonging to other person without his knowledge or consent. The PA clearly prohibits this unethical practice under section 28. Although the PA is silent in addressing that a particular practice could become unconscionable, it is still understandable that the PA protects the consumers from unconscionability by ordering the delivery of a pawned article that has been lost or dishonestly obtained or acquired to the owner.

iii. Hire-Purchase

Sale credit such as the hire-purchase contracts does not fall under the Moneylenders Act. Hire-purchase is a contractual arrangement whereby the owner agrees to let his goods for a stipulated period and payment arrangements to the hirer who may opt to return the goods and terminate the contract, or purchases the goods on the completion of the required periodic payments. A simple hire contains no such option. A hire-purchase agreement that involves consumer is governed by the Hire-Purchase Act 1967 (HPA).

Closer to hire-purchase arrangement that does not fall under the HPA is a lease arrangement. In *Credit Corporation (M) Bhd v KM Basheer Ahamed KM Maghdoom Mohideen & Anor*²², the appellant leased a photostat copier machine under a lease agreement to the respondents. The respondents suffered business

²¹ [1960] 1 LNS 169 at 174-175.

²² [1985] CLJ (Rep) 94.

losses occasioned by defects in the machine and as a result of this stopped payments of the monthly instalments. The appellant repossessed the machine and claimed the whole amount of the monthly rentals unpaid as per schedule to the lease arrangement, storage and custody charges. The Federal Court judges held that Clause 9 of the agreement that placed the respondents' liability to continue paying the rentals notwithstanding the occurrence of any defect in the machine is clearly one-sided in terms and unconscionable in effect.²³ The appellant had committed a breach of a lease in failing to dispose of the machine by means of a bona fide sale.

Like the MA, section 33 of the HPA also empowers the court to re-open transaction that is harsh and unconscionable. This position implies that unconscionable practices could occur in hire-purchase arrangements. However, as pointed out by Cheong May Fong (2005), section 33 is also underutilized by the courts. Despite this finding, the doctrine of unconscionability is still a relevant doctrine to control unconscionable and unethical practices in hire-purchase transactions. In *Chong Seng Yong v Credit Corp. (M) Bhd*, the purpose of enacting section 16(1) and regulation 3(1) on the formality of repossession "was to provide protection to hirers against harsh and unconscionable practices of certain owners who are without scruples."²⁴

According to Yap Kon Lim (2003), complaints are common on repossession fees and storage fees. The fee varies from hirer to hirer and from circumstance to circumstance and totally beyond the borrower's control. Section 16A allows these fees to be charged to the hirer who fails to return goods after 21 days has lapsed as per notice in the Fourth Schedule of the HPA. This means that hirers are often placed at disadvantage positions because of the inequality of bargaining positions between the hirers and owners. However, the practice of charging repossession and storage fees would only become unethical and unconscionable if owners of goods are charging excessive fees to the hirer. In other words, the owners of goods abused their stronger or superior bargaining position and caused the bargains as no longer reasonable and fair.

iv. Sale and Purchase of Housing

The Housing Development (Control and Licensing) Act 1966 (HDA) is a piece of social legislation to protect house purchasers in their relationship with housing developers.²⁵ It is raised in *Kheng Soon Finance Bhd v MK Retnam Holdings Sdn Bhd; Bhagat Singh, Surain Singh & Ors (Intervenors)* that those who entered into

²³ 1985] CLJ (Rep) 94 at 96.

²⁴ [1982] CLJ 428 at 430.

²⁵ *Energoprojek (M) Holdings v PP* [1996] 4 CLJ 571 at 575.

contract in contravention of the HDA is illegal as it infringes public policy.²⁶ In other words, it is unethical for the party to go against the HDA and it is a sign of lack of good faith that a party is imposing contractual terms in contravention of the HDA. Such situation leads to unconscionability.

In *Alexander John Shek Kwok Bun v Rich Avenue Sdn Bhd & Anor*, the court acknowledged that the use of standard agreements in this day and age has eroded the basic principle of freedom of contract. The court viewed that it is “duty bound to be vigilant to ensure that consumers are not being burdened with unconscionable terms.”²⁷ In this case, the plaintiff is required to pay the entire full purchase price before he can get vacant possession of the property. On the face of it, this is a reasonable term. However vacant possession is defined as not including the connection of water and electricity supply to the property. Nor does it mean that the plaintiff can take physical possession of the property until such time that the certificate of fitness is issued by the appropriate authorities. In short, what it means is that the plaintiff is obliged to fulfill his obligation by paying the entire purchase price without the reciprocal obligation on the part of the defendant in delivering vacant possession of the property. Not only that there is no timeline in which the defendant is required to connect the water and electricity supply to the property, there is also no timeline set out in the agreement for the defendant to obtain the certificate of fitness from the appropriate authorities for the property. The court held that these terms are absurd and among others stated that these standard form terms are unconscionable as ordinary consumers are being burdened by these terms.

Unconscionable practice was also found in *Tan Yang Long & Anor v Newacres Sdn Bhd*²⁸ where the standard form terms prescribed that no matter how long delivery is delayed, no damages need be paid until the day when the building is completed and vacant possession is delivered. This standard form term was held unconscionable as the defendant is urging the plaintiff to wait indefinitely without knowing when completion will take place.

STATUTORY REQUIREMENT OF CONSCIONABLE CONDUCT

Gopal Sri Ram JCA acknowledged in *Saad Marwi v Chan Hwan Hwa & Anor*²⁹ that many Malaysians are still vulnerable in matters of commerce and that statutory protection afforded to Malaysian consumers is still insufficient. In Malaysia, unconscionability is known through the term ‘unconscionable transaction’. This term is found in section 16(3) of the Contracts Act, 1950 (the ‘CA’) and the above-

²⁶ [1996] 4 CLJ 52.

²⁷ [2008] 7 CLJ 754 at 774 and 775.

²⁸ [1992] 3 CLJ (Rep) 666; [1992] 1 CLJ 211.

²⁹ [2001] 3 CLJ 98.

mentioned section 21(2) of the MA and section 33 of the HPA. However, the existence of these statutory provisions does not caused unconscionability to be known as a recognized doctrine of its own.

According to section 16(3) of the CA, the notion “unconscionable” is a circumstance that could lead to the presumption of undue influence. The importance of the notion is also overshadowed by other tests of undue influence, namely the domination of will and the gain of unfair advantage. Applying the new parameters of unconscionability to all forms of contract would certainly lead to a clearer understanding of the doctrine of unconscionability. It would be very enticing to suggest a separate section for unconscionability in the CA. However, suggesting a separate section for unconscionability in the CA would ultimately lead to restructuring the whole CA. This is because the appropriate place for a section on unconscionability is only in Part III of the CA but Part III is already tied up to the notions of consent and consideration.

It is important to note that section 16(3) is limited to unconscionability arising from domination of will and it should remain that way. However, in order to make sure that section 16(3) will not be the dominating concept in unconscionability, it is pertinent to have an illustration. The illustration will show the limit of section 16(3) of the CA that it is limited to unconscionability arising from domination of will. The other broader parameters of unconscionability should be developed, evolved and recognized by courts to apply within the general law of contract.

For a specific law of contracts such as franchising and consumer contracts, the legislature should transform conscionability into a recognised duty and become mandatory in common clauses in the agreements. The followings are several alternative methods to achieve this purpose apart from revising section 16(3) of the CA:

i. Unconscionable Bargains as Implied Terms

The statutes could provide a format for unconscionable bargains as implied terms. They can follow this method as in sections 14 to 17 of the SGA, Part V and VIII of the CPA and section 7 of the 1967 Act that have implied conditions and warranties in every agreement.

ii. Requirement to Avoid Unconscionable Bargains in Prescribed Common Clauses

The statutes could provide the duty to avoid unconscionable bargains as a requirement of prescribed common clauses. They can follow this method as in section 11 of the HDA whereby the parties have to follow the conditions prescribed by the government in the sale and purchase of houses. The statutes can impose the

duty to avoid unconscionable bargains as conditions to be explicitly prescribed in each and every agreement.

iii. Requirement to Avoid Unconscionable Bargains as Mandatory Clause

The statutes could directly include the requirement to avoid unconscionable bargains as mandatory clause. The definition of unconscionable bargain is according to this paper submission. As a result, the parameters of unconscionability become mandatory in every agreement.

iv. Requirement Not to Contract Out

As it is a duty for the parties to avoid unconscionable bargain, any parties to the agreements cannot contract out these implied terms. It is also recommended that the statutes could include some illustrations to the provisions. The illustrations should highlight the common forms of unconscionable and unethical bargains in the transactions.

It is deemed that all the above ways of dealing with unconscionable and unethical practices require the intervention of law. The legislature can follow the above recommendations on transforming conscionability into a recognized duty.

CONCLUSION

Unconscionability is the situation whereby the contract is entered into, negotiated or obtained by a party who lacks conscience for justice. In the situation where there is no fair dealing negotiated, no good faith between the parties, inequality where there is abuse of position or unfair advantage taken or undue influence, the contract becomes unconscionable. The contract is a bargain, so when the bargain is unconscionable it becomes unconscionable bargain. Thus, unconscionable bargain is the result of all these factors.

Conscionability does not mean fairness; as in achieving conscionability of a contract, the courts may not necessarily determine whether the contract is fair or not but whether it is conscionable or not. For example, 'A' who has no knowledge of the deposit of gold below his land sells his land to 'B' who has knowledge of the deposit. 'A' sells to 'B' RM 3 million whereas it could reach RM 8 million. 'B's concealment is not fraud (*caveat emptor*). His act of concealment is also considered conscionable because he has invested some amount of money to investigate the land before buying, which 'A' did not. The transaction between 'A' and 'B' is conscionable so far as the parties are considered at arm's length and there is no duty to disclose. When there arise a duty to disclose, either imposed by common law such as in insurance and partnership or statutorily such as in the

FA, the conscionability at the procedural stage is supported by the requirement to deal fairly, reasonably and honestly or in other words in good faith.

After a review of the cases which reflect quite a positive attitude on the part of the judges on unconscionable bargain by applying several equitable rules such as fairness, the speed and expediency of changes that are required may be too slow mainly because judges only contribute towards formulating new laws as when cases come to them. Moreover, some difficult decisions that are too rigid and not favorable to the idea of contractual justice cannot be removed under our current system of *stare decisis*. So, this obviously leaves us with the most effective option to expedite reform of the law through legislative intervention by the Parliament.

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