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OOPS! THE LEGAL CONSEQUENCES OF AND SOLUTIONS TO ONLINE PRICING ERRORS

By Benjamin Groebner¹

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ABSTRACT

How can businesses conducting sales over the Internet protect themselves from the inevitability of pricing errors? Unlike the brick and mortar retailers' ability to catch a pricing error quickly, thousands of orders can be placed with online retailers before they detect the problem. When pricing errors do occur and contracts are formed, merchants are forced to choose between absorbing the resulting financial loss as an investment in goodwill or trying to invalidate the contracts under the doctrine of unilateral mistake.

To avoid binding contracts with customers at erroneous prices, online retailers should employ protective methods of contract formation that help prevent loss.

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INTRODUCTION

<1> With an estimated \$54.9 billion spent on U.S. retail e-commerce sales in 2003,² pricing errors that expose online retailers to considerable loss are inevitable. In 2003, experienced online retailer Amazon.com lodged 6,000 orders for a \$1,049 television incorrectly listed online for \$99.99 before the company detected and corrected the pricing error. Amazon.com could have been bound to 6,000 enforceable contracts with each television purchaser for a loss totaling over \$500,000 if its user interface designed for online contracting was not designed to minimize the company's exposure to this kind of risk. Instead, Amazon.com avoided considerable loss by being able to cancel the orders.³

<2> This article discusses the financial impact caused by Internet pricing errors and examines the methods online retailers use to limit liability. Two specific methods include: (1) controlling the method of contracting by designing a system that conditions contact formation on verification of the contents of a customer's order, and (2) resorting to the equitable doctrine of unilateral mistake.

The Risks and Costs of Pricing Errors

<3> All retailers experience pricing mistakes, but they can be more commonplace and much more harmful to online retailers. Many errors result from normal proofreading mistakes and software problems, but the probability of mistakes increases because many online retailers

change their prices more often than brick-and-mortar stores.⁴ Also, unlike brick-and-mortar retailers, online merchants execute sales automatically and therefore lose the added safety of having a human eye confirm the price.

<4> The Internet, with information spreading quickly, can compound the harm. Shopping "bots"⁵ like MySimon.com and Shopping.com, combined with chat rooms, emails, and bulletin boards, rapidly circulate news concerning good deals. This can result in a flood of orders and thousands of sales being processed before the retailer is able to recognize and correct the mistake. For example, in late 2001, Kodak offered a £329 digital camera for £100.⁶ At the time, legal experts argued that Kodak's automatic confirmation email formed legally binding contracts,⁷ and in the end, the company decided to honor the sales. The incident caused Kodak to suffer a loss of more than £2 million.⁸ In another instance, Buy.com agreed to a \$575,000 settlement after 7,000 customers sued the company after it refused to honor their orders for a \$164 Hitachi monitor, mistakenly marked down from \$588.⁹ Fortunately, companies can implement inexpensive measures to protect against this type of loss.

Using Protective Contract Formation Methods to Guard Against Pricing Errors

<5> Instead of relying on post-contractual strategies to mitigate loss, companies can implement simple proactive procedures to avoid the problems caused by pricing errors up front. As a first line of defense, creating special data monitoring systems or purchasing products that generate alerts when atypical shopping activities occur can help limit the frequency and effects of pricing errors.¹⁰ Since errors will inevitably slip through the cracks, less experienced online retailers could learn from the way Amazon.com has structured and conditioned its online purchasing process. It has saved the company millions by allowing Amazon.com to cancel orders on mistakenly priced products. In the spring of 2003, for example, the company's UK site, Amazon.com.co.uk, erroneously listed an iPaq Pocket PC for £7.32 instead of the normal £287 and successfully cancelled all the orders placed at the lower price by ensuring that a contract was not formed.¹¹

Using Terms and Conditions to Avoid Loss

<6> As the first level of protection, Amazon.com and other online retailers have successfully employed protective terms and conditions which they invoke to avoid honoring pricing errors.¹² Their websites include legal pages with disclaimers reserving the right to refuse to honor pricing errors. For example, Amazon.com's site lists its pricing policy under its Conditions of Use. It states that despite Amazon.com's best efforts, a small number of items may be mispriced and if an item's correct price is higher than their stated price, they will, at their discretion, either contact the purchaser for instructions before shipping or cancel their order with notification.¹³

<7> While ensuring customers assent to the terms and conditions, the online retailer must balance their legal and marketing objectives by managing the tradeoff between effective communication with the customer and a certain legal outcome. Terms and conditions merely posted somewhere within a company's website are called "browse-wrap" agreements and some courts refuse to enforce them unless customers validly and reliably assent to their terms.¹⁴ To strengthen the enforceability, some retailers employ "click-through" agreements to ensure the customer manifests assent – making the terms visible during the purchase and requiring the customer to click "I agree" to the terms, before being allowed to complete the purchase.¹⁵ Amazon.com has prioritized and elected a middle ground. Before completing a purchase, the checkout page foregrounds the contract formation and returns policy by describing them in plain language directly on the page. The customer also submits to Amazon.com's privacy notice and conditions of use by placing an order, but the information is only accessible by clicking on a link.

Controlling Offer and Acceptance to Avoid Loss

<8> The very best measure to avoid fulfilling erroneously priced orders, however, is to avoid the formation of unfavorable sales contracts. To use Amazon.com's purchasing structure as a

model, the principles of offer and acceptance can be employed to create a buffer of up to several days between Order placement and Contract formation. On the final Web Page before completing a purchase, Amazon.com states that "[w]hen you click the 'Place your order' button, we'll send you an e-mail message acknowledging receipt of your order. Your contract to purchase an item will not be complete until we send you an e-mail notifying you that the item has been shipped."¹⁶ This communicates that the buyer, by proceeding through the shopping cart system and placing an order, is making an offer that will form a contract only after vendor acceptance.

<9> Because acceptance usually comes in the form of an email sent to the customer, retailers should be careful with to avoid inadvertently forming a contract with automated order confirmation emails. As indicated above, Amazon.com informs customers that no contract exists until they receive an email confirming that their order is being dispatched. Amazon.uk.co has received criticism because its order confirmation email contained information on how "to cancel this contract"¹⁷ making it unclear whether it acknowledged the order or confirmed the contract. Arguably, the email served as an acceptance of the consumer's offer.¹⁸ Therefore, retailers should issue automatic order confirmation emails that explicitly state that the order is being processed and the offer will be accepted upon dispatch. This will ensure that retailers retain a safe harbor period during which they can detect pricing errors if orders suddenly and unexpectedly increase in volume.

Relying on the Equitable Doctrine of Unilateral Mistake

<10> In the event that online retailers fail to control the methods of contract formation and have formed contracts at the wrong price, companies can resort to the equitable doctrine of mistake instead of absorbing the loss. Unilateral mistake can be grounds for relief.¹⁹

The Equitable Doctrine of Unilateral Mistake Defined

<11> When online retailers make honest, good-faith pricing mistakes that result in huge losses to the benefit of opportunistic online shoppers, their mistake could be grounds for rescinding the unfavorable contract under the doctrine of unilateral mistake. One party's mistake can make the contract voidable when the mistake concerns a basic assumption on which the contract was formed and has a material effect on the agreement that is adverse to that party.²⁰ In addition, the adversely affected party must establish that either: (1) the effect of the mistake is such that enforcement of the contract would be unconscionable, or (2) the other party had reason to know of the mistake or his fault caused the mistake.²¹

Applying Unilateral Mistake to Online Retailers

<12> A retailer's mistake as to the price of an item might constitute a mistaken basic assumption and, depending on the degree, might materially affect the agreement., but there is no simple or mechanical way to predict the magnitude of pricing error needed to clearly establish material effect.²² A mistake as to the price by one party, however, is not enough. The adversely affected retailer must also show that enforcing the contract would be unconscionable or that the online shopper knew or should have known that the price was a mistake.²³

<13> An unconscionable contract is one which "no man in his senses, not under delusion, would make...and which no fair and honest man would accept..."²⁴ The contract, if enforced as formed, needs to cause hardship to the adversely affected party.²⁵ Among other things, courts will consider whether the sale would cause the retailer a loss, rather than merely earn a diminished profit.²⁶ Unconscionability, however, is not a set standard and therefore not a principle on which to rely.

<14> Alternatively, the adversely affected retailer needs to demonstrate that the online shoppers knew or had reason to know of the mistake.²⁷ The Restatement uses the language "reason to know" to communicate that the actor "has a duty to another" and "he would not be acting adequately in the protection of his own interests were he not acting with reference

to the facts which he has reason to know.” This requirement narrows the applicability of this remedy because the rescission is inequitable conduct requiring rescission unless the online shopper knows or at least suspects there is a mistake.²⁹

<15> What is known or should be known creates unique problems for online retailers because what a customer would suspect was a pricing mistake at a brick-and-mortar store might appear reasonable on the Internet. Internet retailers regularly offer legitimate deals that could seem to be too good to be true. In fact, some sites like Half.com focus on that very type of sale.³⁰ Super-deals, however, are not limited to liquidators. Regular retailers, like Amazon.com, often offer sales that are not typical for brick-and-mortar retailers. This makes it difficult to establish what exactly the customer had reason to know. To illustrate, in the Amazon.com and Kodak examples above, a £329 camera for £100 may not be so discounted as to give the customer reason to know while the £287 iPq for £7.32 might be enough cause the customer to suspect a pricing mistake.

<16> Rescinding the contract is the only available remedy under unilateral mistake; it is not a basis for reformation.³¹ This means that online retailers cannot require the customer to continue with the sale at the actual retail price. Instead, the retailer must cancel the customer’s order and re-offer the product at the actual price. Understandably, however, many customers might not elect to re-purchase at the full price after losing the bargain.

<17> Importantly, for some particular circumstances, courts have suggested they might refuse to order rescission. Courts have noted in dicta that the following factors may be relevant in deciding whether to grant rescission: whether other party has so detrimentally relied on the contract it would be inequitable to order rescission,³² will be prejudiced by rescission,³³ or cannot be returned to the status quo.³⁴ In addition, courts have refused to rescind contracts when the mistake resulted from the affected parties’ negligence or lack of due care.³⁵ One court even required that the mistake result from clerical, mechanical, or technical errors.³⁶

CONCLUSION

<18> To avoid significant losses caused by pricing errors, online retailers can employ a few inexpensive measures to protect their business. The retailer’s site should include in its terms and conditions a statement reserving the right to cancel orders and an explanation that the customer’s order only constitutes an offer, which the retailer can accept by either charging the customer’s credit card or by dispatching the product. For additional insurance, the customer should be required to assent to those terms by clicking “I Accept” during the checkout process. Finally, the retailer can condition contract formation on successful completion of certain steps by the retailer, such as confirming the availability of inventory or shipping the goods.

PRACTICE POINTERS

- Require customers to accept the terms and conditions before completing an order or highlight the terms and conditions during online purchase and again in email acknowledgment.
- Ensure that automated email response systems send acknowledgements that the order was processed, not confirmation emails stating that the order has been accepted.
- Create systems to automatically track sales trends and flag any unexpected increases in volume to allow verification of price before the sales are complete.
- Consider honoring the price error as a gesture of goodwill to foster customer loyalty.

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FOOTNOTES

1. Benjamin Groebner, University of Washington School of Law, Class of 2005.

Thanks to Jonathan Franklin and David Zapolosky for feedback on a draft of this

article.

2. U.S. Census Bureau, *United States Department of Commerce News*, at <http://www.census.gov/mrts/www/current.html> (last visited, May 7, 2004).
3. Candace Heckman, *A 36-Inch TV Just \$99? Judge Sees the Big Picture; Court Rules Customer A Victim Only of Price Error By Amazon*, *Seattle Post-Intelligencer*, Jan. 29, 2003, at A1.
4. Bob Tedeschi, *Mixed-up Prices Pose Dilemma: Lose Customers or Money*, *Chi. Trib.*, Dec. 27, 1999, § 4, at 2 (citing an Internet pricing study conducted by Professor Erik Brynjolfson at the Massachusetts Institute of Technology's Sloan School of Management).
5. A shopping "bot" is a website that will search multiple online retailers for a given product and will return the best prices. See www.mysimon.com and www.shopping.com.
6. Mathew Broersma, *Amazon Mis-priced iPacs: No Sale*, *ZDNet UK* (Mar. 19, 2003), at <http://news.zdnet.co.uk/business/0,39020645,2132174,00.htm> (last visited Apr. 4, 2003).
7. *Id.*
8. Lawrence H. Hertz, *Don't Get Trapped into Honoring Online Pricing Errors!*, 4 No. 7 *E-Com. L. Rep.* 6 (2002).
9. *Id.*
10. Alexei Oreskovic, *The Price Isn't Right*, *unlimitedNet*, June 7, 2001, at <http://www.unlimited.co.nz/unlimited.nsf/0/B333D06B92AAF897CC256A630072620C?OpenDocument> (last visited May, 9, 2004) (The author refers to TeaLeaf Technology for products that will help detect and eliminate pricing errors).
11. Broersma, *supra* note 5.
12. See, e.g., Daniel Thomas, *Amazon Pricing Blunder a Warning to Business*, *Computer Wkly.*, Mar. 27, 2003, at <http://www.computerweekly.com/articles/article.asp?liArticleID=120474&liArticleTypeID=1&liCategoryID=2&liChannelID=20&liFlavourID=1&sSearch=&nPag> (last visited Apr. 4, 2004); see also Hertz, *supra* note 7.
13. See <http://www.amazon.com/exec/obidos/tg/browse/-/508088/qid=1076974207/sr=1-3/103-5417578-3987036>
14. See, e.g., *Specht v. Netscape Comm. Corp.*, 306 F.3d 17 (2d Cir. 2002); Christina L. Kunz, et al., *Browse-Wrap Agreements: Validity of Implied Assent in Electronic Form Agreements*, 59 *Bus. Law.* 279 (2003) (The authors of this article posit that vendors should ensure assent and the enforceability of their terms by using four elements: (1) The user is provided with adequate notice of the existence of the proposed terms; (2) The user has a meaningful opportunity to review the terms; (3) The user is provided with adequate notice that taking a specified action manifests assent to the terms, and; (4) The user takes the action specified in the latter notice.
15. Christian L. Kunz, et al., *Click-Through Agreements: Strategies for Avoiding Disputes on Validity of Assent*, 57 *Bus. Law.* 401 (2001).
16. This language is only available by ordering a product and proceeding through the check-out process.
17. See Thomas, *supra* note 10.
18. *Id.*
19. See Arthur Linton Corbin, *Corbin On Contracts* §§ 608 et seq. (1960).
20. *Restatement (Second) of Contracts* § 153 (1979).
21. *Restatement (Second) of Contracts* § 153(a)-(b) (1979).

22. See, e.g., *Donovan v. RRL Corp.*, 27 P.3d 702, 716-17 (Cal. 2001) (held that although the parties had entered into a contract for the sale of a vehicle, it could be rescinded on the basis of unilateral mistake and because the error was in the price term of the contract it was significant and was a mistake as to a basic assumption and has a material effect adverse to the mistaken party. When the seller mistakenly contracted to sell the vehicle for \$12,000 less than the intended retail price, and the court concluded that made the mistake material).
23. Restatement (Second) of Contracts § 153(a)-(b) (1979) (This article will not address the possibility that the customer's fault caused the mistake. That would require an unusual set of circumstances – i.e. where a customer hacked into the company's website and changed the price in an effort to defraud the company, and even then it would be limited to that single customer).
24. *Gill v. Waggoner*, 828 P.2d 55, 58 (Wash. Ct. App. Div. III 1992).
25. E. Allen Farnsworth, *Farnsworth On Contracts* § 9.4 (2d ed 1998).
26. See, e.g., *Alaska Int'l Constr. v. Earth Movers*, 697 P.2d 626, 629-31 (Alaska 1985) (enforcing the contract would not be unconscionable because the mistake was small compared to the size of the project and would not cause the bidder to lose money).
27. Restatement (Second) of Contracts § 153 (1979).
28. Restatement (Second) of Contracts § 153 (1979) (comment e).
29. See *Ostman v. St. John's Episcopal Hosp.*, 918 F. Supp. 635, 646 (E.D.N.Y. 1996).
30. See www.half.com.
31. See *Matter of ENSTAR Corp.*, 604 A.2d 404, 413 (Del. 1992).
32. See *Florida Ins. Guar. Ass'n, Inc. v. Love*, 732 So.2d 456, 457 (Fla. Ct. App. 1999).
33. See *A.A. Metcalf Moving & Storage Co., Inc. v. N. St. Paul-Maplewood Oakdale Sch.*, 587 N.W.2d 311, 318 (Minn. Ct. App. 1998).
34. See *Cameron v. Bogusz*, 711 N.E.2d 1194, 1198 (Ill. App. Ct. 1999); *Fleming Co., Inc. v. Thriftway Medford Lakes, Inc.*, 913 F. Supp. 837, 843 (D.N.J. 1995).
35. See *Fleming*, 913 F. Supp. at 843.
36. See *Nat'l Mut. Ins. Co. v. Voland*, 653 A.2d 484, 489 n.9 (Md. Ct. Spec. App. 1995).

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