

Promises and Prices

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I. Prices in the Abstract	3
A. When prices are likely to rise	3
B. Evaluating price effects	6
II. Prices and Specific Individuals	8
A. Punitive damages (Amitabh)	9
B. Non-pecuniary losses (Ira and George)	10
C. Mitigation of damages (Theresa)	11
D. Consequential damages (Rick)	12
E. Sale to another buyer (Bithiah)	13
III. Prices in Noneconomic Analyses	14
IV. How Prices Get Dismissed	18
A. Impermissible choices	18
B. Default rules	19
C. Tacit understandings	28
D. Deductive logic	35
E. The entailments of a promise	42
F. The scope of contract law	47
G. Impermissible rationales	50
H. Cultural effects	59
V. Conclusion	68

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*Richard Craswell**

What sanctions should the law inflict on those who break their contracts? Would it matter if more severe sanctions were likely to cause prices to rise? What if most contracting parties prefer higher sanctions and higher prices, or what if they prefer lower sanctions and lower prices? And whatever the answer to these questions might be, *why do economists and philosophers think about these issues so differently?*

Of course, when I speak of “economists” I mean something closer to “most economists, though not necessarily all of them; and including the many lawyers (like me) who do not have advanced degrees but who use economics in their scholarship.” An analogous but even broader qualification should be presumed whenever I speak of “philosophers.” Indeed, on the issues I discuss here, many philosophers of a utilitarian or welfareist persuasion will be closer in spirit to my “economists” than they will be to other professional philosophers. So, too, will contractualist philosophers such as T. M. Scanlon.¹

However the two groups are defined, though, they bring very different perspectives to issues of contract theory. In particular, the two groups differ markedly in the relevance they assign to the effects that contract law can have on prices. In this essay, I try to illuminate these differences in two respects.

First, rather than analyzing prices in entirely theoretical

1. T.M. Scanlon, *What We Owe to Each Other* (Cambridge: Harvard University Press, 1998). Professor Scanlon’s views on remedies for breach of contract can be found in T.M. Scanlon, *Promises and Contracts*, in Peter Benson (ed.), *The Theory of Contract Law: New Essays* 86, 99–111 (Cambridge: Cambridge University Press, 2001).

terms (as economists typically do), section *II* discusses five concrete examples in which named individuals have particular reasons for caring about prices. This puts economics and philosophy on something closer to an even footing, since many analyses in philosophy similarly focus on the interests of individual parties.

Second, sections *III* and *IV* look more closely at various philosophers' analyses of contract law, to see exactly where the parties' reasons for caring about prices drops out of the analysis. This is not as easy as it might sound, for very few authors argue *explicitly* that prices shouldn't matter. Instead, non-economists who exclude prices from their analysis, they often do so merely by omission, or by adopting premises whose consequences are not immediately obvious: these are the steps that sections *III* and *IV* seek to illuminate. In doing so, I focus especially on recent work by Seana Shiffrin, for she is one of the few philosophers to discuss price effects at any length.² But sections *III* and *IV* also examine the work of other noneconomists, to show the variety of ways in which prices can end up being excluded.

Before proceeding, I must acknowledge my debt to Charles Fried's *Contract as Promise*.³ While I have disagreed with some aspects of that book,⁴ I have also learned a great deal from it,

2. Seana Valentine Shiffrin, *The Divergence of Contract and Promise*, 120 Harv. L. Rev. 708 (2007) [hereafter cited as Shiffrin, *Divergence*]. Her recent exchange with Steven Shavell is also instructive. Seana Shiffrin, *Could Breach of Contract be Immoral?* 107 Mich. L. Rev. 1551 (2009) [hereafter cited as Shiffrin, *Immoral*]; and Steven Shavell, *Why Breach of Contract May Not be Immoral Given the Incompleteness of Contracts*, 107 Mich. L. Rev. 1569 (2009).

3. Charles Fried, *Contract as Promise: A Theory of Contractual Obligation* (Cambridge: Harvard University Press, 1981).

4. Richard Craswell, *Contract Law, Default Rules, and the Philosophy of*

as well as from the legacy that (thirty years later) is now apparent. During the 1980s, just as I was beginning my own academic career, *Contract as Promise* sparked a remarkable interest among legal scholars in questions about the morality of promises (e.g., why are promises binding?), and also in questions about the relation between morality and law (to what extent do the moral aspects of promises limit the rules that contract law may legitimately adopt?). Under the latter heading, *Contract as Promise* also gave focus to some of the debates about the place of economics in contract theory (e.g., do the moral aspects of promises ever require that contract law depart from whatever rule would be efficient?). These questions have been central to contracts scholarship over the past thirty years. And those years would have been far less interesting if *Contract as Promise* had never been written.

I. Prices in the Abstract

A. *When prices are likely to rise*

I begin with the standard (and highly abstract) economic analysis. Suppose that we were considering whether to change contract law in some way that would increase (on average) the damages sellers had to pay if they broke their contracts.⁵ As this is an abstract analysis, I will not even specify which legal doctrine might produce this change, for the same economic analysis can be applied regardless. Thus, it will not matter (for

Promising, 88 Mich. L. Rev. 489, 517–23 (1989) [hereafter cited as *Craswell, Default Rules*].

5. I assume for simplicity that the seller is the party who might commit the breach, and who might therefore have to pay the higher damage awards. A similar analysis would apply to breaches by buyers, but the direction of the effect would be reversed – that is, subjecting *buyers* to higher sanctions for breach would *reduce* the price that *sellers* could charge.

present purposes) whether the increased damages result from more frequent use of punitive damages, or from abolishing the mitigation doctrine, or from changes in the way that nominally compensatory damages are measured (e.g., by more frequent awards of cost-of-completion damages), or even from narrowing the situations in which the seller's nonperformance would be legally excused.

The reason these doctrines can be lumped together, at least for purposes of abstract economics, is that each of these proposed changes would likely cause sellers' average liability costs to rise. As a result, economic theory predicts that each change would cause sellers' prices to rise as well. Indeed, in economic analyses of contract law, this prediction of higher prices has been standard for more than thirty years.⁶ To most economists, then, it will be entirely uncontroversial.

To be sure, there are a few conditions under which higher liability costs may not translate into higher prices. For one, as Bruce Ackerman famously emphasized,⁷ sellers will not be able to raise prices if both of the following conditions hold: if (1) marginal buyers of the product place no value whatsoever on the benefit of being able to collect a larger damage award; and if (2) sellers are unable to exit the market, or to otherwise reduce their total sales, in response to the increase in liability costs. Markets that satisfy both conditions are rare, and no

6. Steven Shavell, *Damage Measures for Breach of Contract*, 11 Bell J. Econ. 466 (1980) [hereafter cited as Shavell, *Damages*].

7. In the legal literature, this possibility was famously emphasized by Bruce Ackerman in 1971. Bruce Ackerman, *Regulating Slum Housing Markets on Behalf of the Poor: Of Housing Codes, Housing Subsidies and Income Redistributive Policy*, 80 Yale L.J. 1093 (1971). See also Richard Craswell, *Passing On the Costs of Legal Rules: Efficiency and Distribution in Buyer-Seller Relationships*, 43 Stan. L. Rev. 361 (1991) at 372–383, and the extensive literature cited there.

confirmed cases have ever been found. If such markets do exist, though, the analysis in this essay simply will not apply.

Another case where sellers might be unable to raise their prices involves sanctions limited to certain kinds of breaches – specifically, breaches that some sellers could entirely avoid committing *at no cost or sacrifice to themselves*. After all, sellers who entirely avoid such breaches will never be held liable, and thus will not have to worry about higher liability costs. And if avoiding those breaches is itself costless, these sellers will not have to worry about avoidance costs, either, so they can continue to operate at the same costs as before.

However, these conditions too will rarely be satisfied, if only because of the difficulty of defining any subset of breaches that sellers could costlessly avoid with certainty. Even if the higher sanctions were limited to, say, “willful” breaches, it is not clear that sellers can always succeed in avoiding what a court might later label a willful breach. It is even less clear that such liability can be avoided without incurring other costs.⁸

In short, it is not the case that every change in contract law will *necessarily* produce a change in sellers’ prices. In this essay, though, I will focus on the more usual situation where price effects are likely, for these are the situations in which economics and philosophy most typically diverge. More specifically, while economists and philosophers may agree that price effects will be present in a given case, they are apt to disagree about the normative significance (or insignificance) of those effects.

8. I discuss some of these difficulties in Richard Craswell, *When is a Willful Breach “Willful”? The Link Between Definitions and Damages*, 107 Mich. L. Rev. 1501 (2009) [hereafter cited as Craswell, *Willful*].

B. Evaluating price effects

I focus on the normative evaluation of price effects because, in economics, higher prices are not necessarily bad for buyers. True, higher prices leave buyers with less money, and that by itself may be undesirable. But buyers also get something in return for their money, when the accompanying legal change allows them to collect a larger remedy (on average) in the event of breach. And while some buyers might not consider that extra benefit to be worth the higher price, others might be quite happy to accept the combined package of a higher price and a larger remedy. This point is sometimes overlooked by judges, who leap to the conclusion that higher prices *must* leave buyers worse off, and who therefore treat the price effect as an argument against changing the legal rule.⁹ But this leap is unwarranted, without analyzing what it is that buyers get for the price they have to pay.

Indeed, there are a number of reasons why reasonable actors might sometimes prefer to pay a higher price for their contract, if doing so allows them to collect a more generous remedy in the event of a breach.¹⁰ For one thing, paying for such a remedy might get the buyer a more reliable product or service, if the larger sanctions give sellers more incentive to reduce the number of preventable defects.¹¹ And even for those defects

9. E.g., *Erich v. Menezes*, 21 Cal.4th 543, 981 P.2d 978 (1999) (refusing to allow buyers of a defective house to recover damages for emotional distress, in part because of the court's concern that increasing builders' liability "could increase the already prohibitively high cost of housing in California").

10. Oscar Wilde's *bon mot*, about the cynic who knows the price of everything and the value of nothing, surely ought to be quoted at some point in this essay. This is as good a place as any.

11. In the economics literature see, e.g., Lewis A. Kornhauser, *Reliance*,

that are not practicably preventable, paying for a higher remedy could give buyers additional insurance, which would be particularly valuable if private insurance is unavailable, and if the law's usual damage remedy provides less insurance than buyers want.¹² Higher prices might also correct for some kinds of imperfect information, if the higher prices reflected (as they might in a strict liability regime) the cost of risks that consumers would otherwise underestimate.¹³ And in any situation where enforcement of legal rules is less than perfect, buyers might prefer to pay higher prices (up to a point) to cover the extra penalties needed to increase deterrence.¹⁴

Of course, it is also possible for some (or even all) buyers to prefer *not* to pay higher prices, even if those higher prices come with more generous remedies for breach. Thus, when economists evaluate a proposed change in the law, they will

Reputation, and Breach of Contract, 26 J. L. & Econ. 691 (1983). For a less technical discussion, see Charles J. Goetz & Robert E. Scott, *Liquidated Damages, Penalties and the Just Compensation Principle: Some Notes on an Enforcement Model and a Theory of Efficient Breach*, 77 Colum. L. Rev. 554 (1977).

12. For economic analyses of this motive for paying a higher price see, e.g., A. Mitchell Polinsky, *Risk Sharing Through Breach of Contract Remedies*, 12 J. Legal Stud. 427 (1983). A less technical discussion can again be found in Goetz & Scott, *supra* note 11.

13. Steven Shavell, *Strict Liability versus Negligence*, 9 J. Legal Stud. 1, 3–6 (1980).

14. On punitive damages and deterrence generally, see A. Mitchell Polinsky & Steven Shavell, *Punitive Damages: An Economic Approach*, 111 Harv. L. Rev. 869 (1998); or Richard Craswell, *Damages and Deterrence: The Multiplier Principle and its Alternatives*, 97 Mich. L. Rev. 2185 (1999); and the extensive literature cited there. On the additional trade-offs involved when higher damages are used in contractual settings, where buyers may have to pay higher prices as a result, see Richard Craswell, *Damage Multipliers in Market Relationships*, 25 J. Legal Stud. 463, 478–90 (1996) [hereafter cited as Craswell, *Punitive Damages*].

usually want to determine just how many buyers would prefer to pay the higher prices, and how many buyers would prefer the opposite. By contrast, philosophers often seem to evaluate legal changes without worrying about the effect on prices, or about how many buyers would prefer a lower or higher price. Hence the question with which this essay began: why do economists and philosophers think about prices so differently?

II. Prices and Specific Individuals

In sections *III* and *IV*, I explore in more detail some of the reasons why price effects drop out of many non-economic analyses. First, though, it will be useful to restate the economic analysis on a more human scale, focusing on the reasons why individual parties to a contract might themselves care about contract law's effects on prices. Otherwise, if the only reason for caring about price effects is a broad (and ill-defined) goal like "efficiency," the debate is likely to bog down in warring abstractions, with efficiency set against equally general and equally contestable principles such as respect for autonomy, or fidelity to commitments.

This focus on abstract goals like efficiency is sometimes encouraged by the fact that, when economists evaluate contract law, they do not limit their attention to the *price* effects of any particular rule. As we have just seen, most legal rules (in addition to affecting prices) affect other behavior as well, as when higher damage awards induce sellers to take extra precautions to reduce the likelihood of a breach. Moreover, these other effects will also be relevant to economists: possibly more relevant than the price effects themselves. After all, a change in price is partly a zero-sum transfer, as the buyer's loss from paying a higher price equals the seller's gain from receiving a high-

er price. Thus, for there to be any *net* change in overall welfare, that change will usually have to come from the other behavior that is affected, not just from the change in prices.

However, economists' focus on overall welfare (or on some other abstraction like efficiency) often ends up obscuring the actual effects of contract law on particular individuals, including any effect on the prices those parties pay. To bring those effects back to the foreground, this section presents five concrete examples, each involving a specific legal issue (punitive damages, nonpecuniary losses, the duty to mitigate, limits on consequential damages, and deliberate breaches). Each example also features one or more identified individuals with a particular reason for preferring lower prices and a less generous legal remedy.¹⁵ Sections *III* and *IV* will then show how these individuals' reasons drop out of most noneconomic analyses.

A. Punitive damages (*Amitabh*)

The first example features *Amitabh*, a buyer who is about to enter an investment contract. If the contract is not performed, the loss he suffers will be entirely financial, and can easily be measured. However, *Amitabh* cannot afford to suffer a financial shortfall just now, so he wants a seller who is willing to compensate all his losses in the event of a breach. In fact, he is even willing to pay a somewhat higher price for his contract (within reason, of course) in order to get that assurance.¹⁶

Apart from his current financial needs, though, *Amitabh's*

15. As noted earlier, similar examples could be constructed involving individuals who preferred *higher* prices and *more* generous legal remedies. I leave those examples as an exercise for the reader.

16. I am fully aware of the argument that real people do not think about contract damages in this way. See the discussion *infra* at note 64.

tastes are modest. He does not dream of untold wealth; nor does he buy lottery tickets, or bet on horses at long odds. He is therefore surprised when his seller offers to agree (for just a few dollars more) that, in the event of a breach, she will pay Amitabh a penalty equal to ten times the amount of his financial losses, thus giving him a spectacularly high return on his contract. Having no need for such a spectacular return, and preferring not to pay extra to get a chance at riches, Amitabh declines this offer. In other words, Amitabh would rather save by paying a lower up-front price, while giving up the right to collect a supracompensatory award in the event of a breach.

B. Non-pecuniary losses (Ira and George)

The second example features Ira and George, who are hiring a videographer to record their upcoming wedding. If the videographer botches the recording, they will not suffer any financial loss, but they will lose something of irreplaceable sentimental value. The couple therefore wants to be sure the videographer has a strong incentive *not* to botch the recording, and this leads them (initially) to want a contract under which the videographer must pay a substantial penalty if the recording is not successful.

When the videographer quotes a price to them, though, Ira and George reconsider. They realize that a monetary penalty for breach (even a large one) will not replace the lost recording. They also realize that a botched job by the videographer will not leave them with any greater financial needs – unlike Amitabh, in the previous example – while paying a high price for the recording would take money they could certainly use *now*, what with the cost of weddings these days and the expenses of starting a new household and so on. In the end,

they compromise on a moderate contract at a moderate price, which requires the videographer to refund double her fee if she fails to deliver the pictures. This double refund is far less than any truly compensatory measure of damages would be, meaning that it is less than the pictures are truly “worth” to the couple (by any plausible measure of worth). But the double refund is still large enough to make the videographer take her professional duties seriously, if she needs any prompting at all in that regard, and all consider it a reasonable compromise.¹⁷

C. Mitigation of damages (*Theresa*)

For a third example, suppose that the duty to mitigate were abolished, so breachers were held fully responsible even for losses that the nonbreacher could easily have avoided. One effect would be to increase sellers’ average liability costs, leading to higher prices for the reasons discussed above.

Now consider Theresa, a principled buyer who wouldn’t dream of trying to collect from a seller for losses she could have prevented herself. If the seller Theresa bought from *knew* that she held these principles, and if he were sure he could trust her to adhere to those principles even when push came to shove, he might then charge Theresa a lower price than usual, because his average liability costs would be less (as a result of Theresa’s diligent efforts to mitigate). But if the seller does not know Theresa, he is unlikely to reduce his price just on her own

17. For formal economic models of this trade-off, see Philip J. Cook & Daniel A. Graham, *The Demand for Insurance and Protection: The Case of Irreplaceable Commodities*, 91 Q.J. Econ. 143 (1977); Rickuel A. Rea, Jr. *Nonpecuniary Loss and Breach of Contract*, 11 J. Legal Stud. 35 (1982). A less technical exposition can be found in Alan Schwartz, *Proposals for Products Liability Reform: A Theoretical Synthesis*, 97 Yale L.J. 353, 362–67 (1988).

assertion that she always mitigates her losses.¹⁸ Instead, to get a lower price from this seller, Theresa will probably have to offer a contract in which she *binds* herself not to sue for losses that could have been mitigated – which is fine with her, since she doesn’t believe in suing for those losses anyway. Theresa therefore agrees to a lower priced contract that “imposes” on her a duty to mitigate.

D. Consequential damages (Rick)

As the previous example illustrates, price effects do not always affect all buyers equally, so buyer heterogeneity – the distribution of effects on different *types* of buyers – may have to be considered. Indeed, the issues posed by buyer heterogeneity can easily arise in almost any case involving consequential damages are at stake.

To make this more concrete, suppose that the limits on consequential damages, such as the rule of *Hadley v Baxendale*, have all been relaxed or repealed. More specifically, suppose that airlines are now legally liable for whatever losses their passengers suffer if the airlines’ flights are delayed. Some passengers have missed important business meetings; and these, let us assume, have collected appropriately large damages from the airlines, who have raised ticket prices to reflect this increased liability. Rick, however, is a college student taking a year off to travel around the Mediterranean on no particular schedule. Knowing that he will lose little if his flight out of

18. This illustrates a point that Dori Kimel has emphasized: while *promises* are often made to trusted acquaintances, legally enforceable *contracts* are likely to be particularly useful in dealings with strangers. Dori Kimel, *From Promise to Contract: Towards a Liberal Theory of Contract* (Oxford: Hart Publishing, 2003) 29–32.

Morocco is delayed, Rick buys a heavily-discounted ticket on Air Marrakesh which specifies that the airline will have no liability at all if the flight is delayed, and need only refund the ticket price if the flight is canceled. While this puts Rick at some risk that he might not reach his destination in time, he is not averse to spending a few more days in Morocco; and he has also learned (correctly) that Air Marrakesh has a good track record with relatively few delays or cancellations. Rick is therefore willing to take this chance, in the hope that the heavily-discounted fare will leave him with more money to spend during the rest of his travels.

E. Sale to another buyer (Bithiah)

The final example features Bithiah, a wealthy collector of art and antiques. Browsing in an antique store, she finds an oil painting that she likes and offers to buy it at its listed price of \$5,000. The store owner agrees, but tells her that he cannot let her take the painting just yet, because an old and valued customer who had also expressed interest in the painting is arriving the next day to look at it. The store owner explains that if his old customer wanted the painting, the owner would feel obliged to sell it to him, not only because of their long-time relationship (the customer was a friend of the owner's father), but also because the customer had hinted that he might pay significantly more than \$5,000.

The store owner then told Bithiah: "Of course, if he does decide to buy it, I'll give you back your \$5,000." When Bithiah looked unenthusiastic, the owner continued as follows:

Were you thinking of the painting as an investment? If so, I'll agree to hand over to you anything that my old customer pays above my original price of \$5,000. But in

that case, if I'm giving up any chance at the extra profits from my old customer, I'm going to want a higher price from you – say, \$5,500. In other words, (a) if you buy the painting for \$5,500, you'll either get the painting (if my old customer doesn't want it) or you'll get whatever my old customer pays above \$5,000. Or if you'd rather, (b) you can buy the painting for only \$5,000 – but in that case, all you'll get is your money back if my old customer decides to buy the painting.

After thinking it over, Bithiah decided she wasn't interested in speculating on the painting's resale value, so she agreed to option (b), buying the painting for the lower price of \$5,000. The next day, the old customer offered the store owner \$8,000 for the painting. The owner accepted that offer; gave the painting to his old customer; and gave Bithiah her \$5,000 back.

III. Prices in Noneconomic Analyses

In each of section II's examples, one of the contracting parties has what I take to be at least a potentially legitimate reason to prefer that the other party *not* be subjected to heavy sanctions for breach, in order to bring down the price that party is willing to charge. As the citations in that section illustrate, these reasons have often been analyzed by economists.

Most non-economic theorists, however, devote little or no attention to price effects. Charles Fried, in *Contract as Promise*, mentions them only once.¹⁹ Stephen Smith does only slightly

19. Fried (supra note 3) at 105–06 (noting that restricting lenders' remedies against defaulting borrowers might increase the lenders' costs and drive some of them out of business, thus potentially making borrowers worse off rather than better). I have stretched slightly to count this as a discussion of "price" effects, for Professor Fried never mentions the possibility that lenders, rather

better, mentioning them just twice in the 430 pages of his otherwise comprehensive book on contract theory.²⁰ And Dori Kimel, in a book that nicely advances Professor Fried's analysis in many respects, does not mention price effects at all.²¹

Moreover, even these few references to price effects all come in connection with doctrines or policies that, in these authors' view, should not be part of contract law in the first place. Professor Fried, for example, believes that price effects shed important light on the costs of the unconscionability doctrine – but he also believes that unconscionability is a dangerous and unwise intrusion into the promise-based rules of contract law.²² Similarly, Professor Smith believes price effects could shed light on contract law's efficacy in pursuing distributive goals – but he also believes contract law should not pursue that goal.²³ In other words, not one of these authors discusses price effects in connection with any topic that they believe *are* properly part of contract law – topics like the mitigation requirement, or the limits on consequential damages, or of the other issues in the examples in section II.

How is it, then, that some non-economists can so completely ignore price effects when it comes to contract law? The short answer, of course, is that these theorists believe they have good substantive reasons for disregarding price effects: reasons

than simply going out of business, might instead try to charge higher *prices*.

20. Stephen A. Smith, *Contract Theory* 129, 137 (Oxford: Oxford University Press, 2004) (arguing that contract law should not be used to pursue distributive goals, because any redistribution toward buyers will be undone by sellers' higher prices).

21. Kimel (*supra* note 18).

22. Fried (*supra* note 3) at 105–06.

23. Stephen A. Smith, *Contract Theory* at 129 and 137. Professor Smith makes the same point in each of these two passages, so I am being generous in counting it as two references.

that rest on normative criteria that do not depend on prices. Some of these substantive reasons will be examined at more length in section IV.

First, this subsection briefly mentions some non-substantive factors that may predispose economists and philosophers to think differently about price effects, without necessarily justifying either predisposition. For example, one obvious difference is that economists are *trained* to study prices, and most of their work involves markets in which prices play a central role. To a child with a hammer, everything looks like a nail; and the hammer of many economists is price theory.

By contrast, philosophers do not regularly study prices in the ordinary course of their profession. To the contrary, many noneconomists study legal doctrines other than contract law; and where those other doctrines are concerned, prices may indeed be irrelevant. For example, if the law increases the penalties for theft or trespass, that will not raise the prices that thieves or trespassers charge their victims, for thieves and trespassers do not charge prices in the first place.²⁴ Thus, price effects will not naturally be salient to scholars who think of remedies as a unified field of its own, whose principles apply to remedies for *all* wrongs across *all* legal contexts.

It may also be significant that, when philosophers do turn to contract law, they usually begin with the extensive literature that asks how promises can be morally binding. As David Hume noted long ago, there is something of a puzzle about how a promisor, merely by uttering certain words, can create a moral obligation where no obligation existed before.²⁵ Hume

24. I discuss this at more length in Craswell, *Passing On* (supra note 7) at 386–84.

25. David Hume, *A Treatise on Human Nature* [1739–1740] (Oxford: Ox-

had his own solution to this puzzle, of course, as do the many others who have written on the issue.²⁶ But what is significant for present purposes is that practically all of the solutions to this “puzzle” are independent of the price that the promisor charges. If a promise to deliver ten bushels of widgets for \$500 creates a moral obligation, so too (under most circumstances) will a promise to deliver the same quantity of widgets for \$450; and whatever explains the moral obligation in the first example will surely also explain the obligation in the second. In short, in the literature about *why* promises are binding, there has never been any reason for philosophers to pay particular attention to the promise’s price.

It is also true that economists and philosophers differ in the kind of contract or promise that they take to be the standard or typical case. Economists, of course, routinely analyze commercial dealings between parties with economic motives: parties for whom price is an important consideration. By contrast, as Barbara Fried has pointed out, philosophers who write about promises often focus on informal promises between friends or family members. Since informal promises rarely involve the payment of any price at all, it is not surprising that no analysis of price effects has emerged from that literature.²⁷

In short, there are many reasons why economists and philosophers might be *disposed* to devote more or less attention to price effects. However, careful theorists do not rely merely on

ford University Press, 2000) at 332–36.

26. Including, of course, *Contract as Promise* (supra note 3) at 14–17.

27. Barbara H. Fried, *What’s Morality Got to Do With It?* 120 Harv. L. Rev. Forum 53, 55 n.13 (2007). Professor Fried adds: “[T]hat people generally must pay for what they get in arm’s-length deals is, in my view, one of the chief reasons to be skeptical of claims that the moral obligations imposed by gratuitous promises and those imposed by commercial contracts converge.”

their own dispositions to decide whether to consider price effects (or anything else). Instead, many philosophers rely on one or more substantive arguments that could justify them in disregarding price effects. Section IV surveys seven of those substantive justifications, collecting them all in one place for what I believe is the first time. It will no doubt be clear that I do not find many of these justifications persuasive, given my roots on the economists' side of the divide. But the aim of section IV is as much to catalog these arguments as it is to criticize them. If we can be clear about what the arguments *are*, we should then be better able to debate their merits.

IV. How Prices Get Dismissed

Suppose, then, that we have a case in which greater remedies for breach would trigger higher prices. Suppose also that some contracting parties would prefer not to pay those higher prices, perhaps for one of the reasons discussed in section II. As we have seen, economists would place a great deal of weight on these individuals' reasons for not wanting to pay a higher price. Why might noneconomists differ?

A. Impermissible choices

The first argument offers the most direct challenge to the relevance of price effects. The premise of this argument is that there are some choices we simply do not allow individuals to make, no matter how much they might want to, and *no matter how good a price* they could get. For example, no state allows contracts of personal slavery, regardless of how high a price the slave might get.²⁸ Many states also refuse to enforce paid ges

28. For the possible application of this prohibition to other personal serv-

tational surrogacy agreements – and again, this prohibition applies regardless of the price the surrogate receives.²⁹ In economics, these are sometimes referred to as “merit goods.”³⁰

Of course, many of these prohibitions are controversial, and I will not address those controversies here. Instead, I will merely note that these arguments for an outright prohibition are relatively rare, and are almost never invoked in for garden-variety issues like those in the examples in section II. Nobody argues that contracting parties should not be allowed (at any price) to agree to extra mitigation requirements, for example, or to stipulate to damages that are less than fully compensatory. To understand how price effects disappear from non-economic analyses of *these* issues, we will have to look further.

B. Default rules

The prohibitions discussed in the previous subsection were *mandatory* rules: rules that deny the parties the option of entering certain kinds of contracts. Much of contract law, though, consists of *default* rules: rules that parties are allowed to “opt out” of if they wish. If the law adopts a particular damage rule for parties who have not specified otherwise, but if it allows parties to specify otherwise if they want to, then the rule is merely a default rule.

Because default rules leave parties free to choose their own terms and prices, they may be easier to justify than the mand-

ice contracts, see Randy E. Barnett, *Contract Remedies and Inalienable Rights*, 4 Soc. Phil. & Policy 179 (1986); and Nathan B. Oman, *Specific Performance and the Thirteenth Amendment*, 93 Minn. L. Rev. 2020 (2009).

29. E.g., *In the Matter of Baby M*, 109 N.J. 396, 537 A.2d 1227 (1988).

30. Richard A. Musgrave, *The Theory of Public Finance* 13–15 (New York: McGraw-Hill, 1959). Of course, for products or contracts that we prohibit, merit “bads” might be a more accurate label.

atory rules discussed above. For example, Seana Shiffrin has written critically about small remedies for certain breaches, and her criticisms might have been used to support a mandatory rule, under which no parties would be allowed to contract for those remedies, no matter how favorable a price they got.³¹ Professor Shiffrin's actual position, though, is only that the law should not adopt various smaller remedies *as a default rule*. In other words, she argues that the law should not presume from the contract's silence that the smaller remedies were intended. Instead, she supports the opposite default rule, in which contracts would be presumed to come with relatively generous remedies, unless the parties explicitly specified otherwise.³²

1. *Choosing a default rule.* Though it may not be obvious, this is one of the points at which price effects sometimes disappear from noneconomic analyses of contract law. Specifically, if we are looking at those parts of contract law that are merely default rules, it can easily seem as though there is no need for us to be concerned about Amitabh, or Theresa, or any of the other parties in section II. After all, even if we adopt a default rule with a very generous remedy, which leads sellers to charge a high price, the Amitabhs and Therasas of the world can avoid that price simply by opting out of the default rule: they can stipulate to a less generous remedy, which should bring down the seller's costs and (hence) result in lower prices.

In other words, as long as Amitabh and the others are free to negotiate their own package of prices and remedies, it might

31. Professor Shiffrin frames the question by asking whether "a mere implicit price break *could* morally compensate for a nonconsensual deliberate breach." Seana Shiffrin, *Could Breach of Contract be Immoral?* 107 Mich. L. Rev. 1551, 1558 n.27 (2009) [hereafter cited as Shiffrin, *Immoral*].

32. *Id.* at 1568.

seem that there is no reason for scholars to choose a particular package for them, or to advise them about what package they should prefer. More precisely, scholars (or practicing lawyers) who advised *private parties* would still have to worry about price effects, since private parties are the ones who decide when to opt out of the law's default remedies, and to decide what to negotiate for instead.³³ However, most legal scholars see themselves as advising judges or legislators rather than private parties. And since public lawmakers (in a default-rule regime) are not the ones who ultimately choose the remedy or price, it might seem as though these scholars could justifiably ignore any price effects.

While this is an attractive position, it is incomplete in one respect, for it fails to address how the law's default rules should be chosen. That is, why should the default rule be a generous remedy, which puts the burden of opting out on buyers like Amitabh and Theresa, if they want a lower price? Why not instead make the default remedy very low, thus placing the burden of opting out on any buyers who want higher prices and more generous remedies? To be sure, if the cost of opting out is very small, having to do so may not be very *much* of a burden on the Amitabhs or Therasas. But what if the cost of opting out would be equally small for parties who prefer a higher price and a more generous remedy? Why should the Amitabhs and Therasas be the ones to bear *any* burden?

In other words, default rules present a sort of formal symmetry that defeats any easy normative conclusion. Typically, the law has more than one default rule it could choose, and *any*

33. For an argument that much law-and-economics analysis could be better understood as directed at the choices made by contracting parties, see Avery Wiener Katz, *Taking Private Ordering Seriously*, 144 U. Pa. L. Rev. 1745 (1966).

of the possible choices will leave *some* parties with the burden of opting out, however heavy or light that burden might be. To find some reason for choosing one of the possible defaults over another, we need some way of getting around that apparent symmetry.

Of course, over the last three decades or so – roughly, in the years since *Contract as Promise* was written – economists have developed an extensive analysis of factors that might argue for one default rule rather than another. Not surprisingly, perhaps, the economic analysis of default rules also depends heavily on what I am calling price effects. The following subsection briefly summarizes that analysis, so that we can later see just where the non-economic analyses depart from it.

2. *Default rules in economic analysis.* Economists do not all think alike on the topic of default rules (or on any other topic, of course). Indeed, one scholar recently questioned whether the law ever uses certain kinds of default rules, in a debate that reflects deeper differences over how the concept of a “default rule” should even be defined.³⁴ That said, here is how *I* see the economic analysis of default rules, and I do not believe my account to be far from the mainstream.

This account begins by distinguishing two bases on which default rules might be chosen.³⁵ So-called “majoritarian” default rules are chosen to minimize the number of parties who

34. Eric A. Posner, *There Are No Penalty Default Rules in Contract Law*, 33 Fla. St. L. Rev. 563 (2006). For a contrary view, see Ian Ayres, *Yah-Huh: There Are and Should Be Penalty Defaults*, 33 Fla. St. L. Rev. 583 (2006). For the record, I believe Professor Ayres’s definitions to be the more useful.

35. The distinction was formalized by Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 Yale L.J. 87 (1989), though some of the basic concepts date back even earlier. Ayres and Gertner also coined the labels “majoritarian” and “penalty” default rules.

will want to opt out of the rule, since opting out of a rule typically takes at least some time and effort (including, perhaps, the cost of paying a lawyer to draft the opting-out language). These opt-out costs can be minimized if the law picks a default rule that mimics what most parties would agree to anyway, for that way most parties will not have any reason to opt out. More precisely, *if the cost of opting out is the same for all parties*, the aggregate opt-out costs can be minimized by picking the default rule that the greatest number of parties would prefer (hence the “majoritarian” label). If, instead, the cost of opting out varies across different parties – as might be the case if some parties had easier access to lawyers, for example – then aggregate opt-out costs can be minimized only by weighting the number of parties who would want to opt out according to the actual cost that each of those parties would have to incur.³⁶

Default rules can also affect other costs, though, including the various costs that will be felt if one or both parties misunderstand the legal effects of the contract they have entered. “Penalty” default rules aim to reduce these latter costs by inducing some parties to spell out their intended agreement clearly and explicitly. What gives this inducement its force is the threat that, if the parties fail to be sufficiently explicit, they will be governed by a default rule chosen deliberately to be unattractive – in other words, a penalty.

To be sure, if this threat succeeds in inducing a great number of parties to make their contracts more explicit (thereby opting out of the penalty), that will maximize rather than minimize the aggregate opt-out costs. But those extra opt-out costs may be worth it, on balance, if being more explicit up front causes one or both parties to be better informed about what

36. *Id.* at 114–15.

they have agreed to.³⁷ For example, the rule of *Hadley v. Baxendale* might well increase aggregate opt-out costs, if it induces lots of buyers to provide full information to their sellers about just how much the buyers will lose in the event of a breach. But that information might on balance be worth the extra transaction costs, if (say) it enables sellers to adjust their level of precautions in light of the extra information they now have.³⁸

Penalty default rules raise another issue involving the precise way in which the “penalty” should be unattractive to the parties. Penalty defaults are meant to act as a threat, to induce the parties to be more explicit, but sometimes one side’s threat is the other side’s bonus. (Imagine a default rule that said “If the parties do not specify a damage measure, the buyer must pay the seller ten million dollars.”) In such a case, a choice may have to be made about which way to “slant” the default rule,

37. *Id.* at 97–100. As Ayres and Gertner note, being more explicit might also reduce subsequent litigation costs, by making it easier for a court to tell what the parties actually agreed to. This potential benefit of being more explicit is, at bottom, the same as what Lon Fuller long ago described as the “channeling” function of legal formalities. Lon L. Fuller, *Consideration and Form*, 41 Colum. L. Rev. 799, 801–03 (1941); see also Curtis Bridgeman, *Default Rules, Penalty Default Rules, and the New Formalism*, 33 Fla. St. L. Rev. 683 (2006). For a modern analysis of these costs and benefits, see Robert E. Scott & George G. Triantis, *Anticipating Litigation in Contract Design*, 115 Yale L.J. 814 (2006).

38. Ayres & Gertner (*supra* note 35) at 101–04. The now-extensive literature on *Hadley v. Baxendale* as a default rule includes, among others, Jason Scott Johnston, *Strategic Bargaining and the Economic Theory of Contract Default Rules*, 100 Yale L.J. 615 (1990); Barry E. Adler, *The Questionable Ascent of Hadley v. Baxendale*, 51 Stan. L. Rev. 1547 (1999); Ian Ayres & Robert Gertner, *Majoritarian vs. Minoritarian Default Rules*, 51 Stan. L. Rev. 1591 (1999); Lucian Arye Bebchuk & Steven Shavell, *Information and the Scope of Liability for Breach of Contract: The Rule of Hadley v. Baxendale*, 7 J. L. Econ. & Org. 284 (1991); and Eric Maskin, *On the Rationale for Penalty Default Rules*, 33 Fla. St. L. Rev. 557 (2006).

meaning which party should be the one to suffer the penalty if the contract is not made explicit. On this issue, a common recommendation is to slant the penalty against whichever party is most likely to be aware of the law's default rule, since the threat of a penalty will have little or no effect on anyone who doesn't know that the threat exists.³⁹ Thus, in settings where only one of the parties is likely to know the default rule – as might be the case in contracts between businesses and consumers, for example – the threat will probably be most effective if the default rule is chosen to be unattractive to the party who is better informed about the law.

Viewed in these terms, penalty default rules have much in common with mandatory disclosure laws, like the truth-in-lending rules or various product labeling requirements.⁴⁰ (Another common label for penalty defaults is “information-forcing rules.”⁴¹) All of these increase transaction costs in one respect, by inducing parties to spend more time disclosing information in advance of a sale. On this view, penalty defaults make sense under the same broad conditions that mandatory disclosure laws make economic sense – that is, if but only if the benefits of disclosing the extra information are worth the costs of having to communicate it.⁴²

39. Ayres & Gertner (supra note 35) at 98–99.

40. This similarity is emphasized in J.H. Verkerke, *Legal Ignorance and Information-Forcing Rules*, University of Virginia Law & Economics Working Paper No. 03–4 (2003).

41. Robert E. Scott, *A Relational Theory of Default Rules for Commercial Contracts*, 19 J. Legal Stud. 597, 609 (1990).

42. Verkerke, supra note 40; see also Richard Craswell, *Taking Information Seriously: Misrepresentation and Nondisclosure in Contract Law and Elsewhere*, 92 Va. L. Rev. 565 (2006); and Omri Ben-Shahar & Carl E. Schneider, *The Failure of Mandated Disclosure*, University of Chicago Olin Working Paper No. 516 (2010). Much of the vast literature on procedural unconscionability

This analogy to mandatory disclosure laws may also shed light on a less-frequently studied question, about exactly what should have to be disclosed (and where, and in what format) before a party will be deemed to have opted out of a penalty default rule. As Rip Verkerke has emphasized, inserting a line of fine print in a boilerplate contract is unlikely by itself to produce the hoped-for informational benefits. As a consequence, it might sometimes (or even often) make sense to require a more prominent disclosure before the parties can be said to have successfully opted out of the penalty. But this recommendation too, like the case for penalty defaults themselves, works only when the benefits of more prominent disclosures exceed the likely costs.

Indeed, the issue of what the parties must do to opt out of a default is really just the flip side of another question that has not been as frequently studied: the question of what should count as a “gap” for purposes of determining whether there is any space in the contract for a default rule to fill. On the view I have presented here, a “gap” cannot be defined solely by reference to the semantic properties of the contract itself. Instead, on this view a “gap” exists in just those cases where the parties, in terms of the completeness and prominence of their disclosure, have fallen short of *whatever we decide they ought to do* in order to opt out of that particular default rule. To answer one question (what should be required to opt out?) is to simultaneously answer the other question (what should count as a gap?), because in economics they are the same question.⁴³

and on the “battle of the forms” is also relevant here.

43. As Professors Ayres and Gertner put it: “By establishing the necessary and sufficient conditions for contracting around a default rule, contract law simultaneously defines when contracts have obligational gaps.” Ian Ayres &

To summarize, the economic analysis of default rules can be seen as taking economists' concern with price effects and extending that concern over the entire population of buyers and sellers. Some buyers, like Ira and George and Amitabh, will prefer small remedies and low prices; other buyers will prefer the opposite; and still others will prefer something in the middle. By choosing a default rule rather than a mandatory rule, the law allows all of these buyers to get their preferred contract, as long as they are willing to bear the cost of opting out. However, the law cannot be similarly neutral in deciding *which* default rule to select, since every possible choice will inflict opt-out costs on a different set of buyers.

Economists, characteristically, try to make this choice by looking at the aggregate costs faced by all of the possible buyers or sellers, across an entire population of sellers and buyers. This means that economists must also attend to all the ways in which buyers differ from one another – including some assessment of which buyers would prefer to pay a higher price for a more generous remedy, and which buyers would not, for that is what determines which buyers will want to opt out of any given default rule. This is why price effects remain central to economic analysis, even when the rule being analyzed is merely a default rule.

By contrast, most noneconomic analyses continue to pay little attention to questions about which price packages would be preferred by which sellers or buyers, at least when we are talking about mere default rules. The remaining sections explore this omission in more detail, to see some of the ways in which philosophers might justify one default rule over another

without caring which buyers would want to pay for that default.

C. *Tacit understandings*

Here is a different reason why price effects might be disregarded by noneconomists. As we have just seen, if the parties to a contract have explicitly agreed to some combination of price and remedy, most scholars would then see no reason for conducting their own analysis of price effects, for that would be second-guessing the parties' decision. But perhaps price effects can also be disregarded even in cases where the parties' contract was silent on the issue, *if the parties nevertheless had a tacit agreement or understanding* about what price and remedy they were agreeing to. In other words, this argument holds that agreements can sometimes be tacit rather than explicit – and that in either case, the terms of the actual agreement should prevail over (and thus eliminate any need for) any economic analysis of price effects.

To put the argument more precisely, theorists in this camp begin with the premise that contracts should be interpreted, where possible, to match the intention of the contracting parties. They then add an additional premise: that the relevant “intentions” are not necessarily limited to those that were consciously in the parties' minds. Instead, a party's intentions (on this view) may include many things that were not consciously considered: things that were only implicitly understood, or things that “went without saying.”⁴⁴ Lon Fuller put the point as follows, in a passage that is often quoted:

It is ... plain that there is a psychological state which can

44. Brian Langille & Arthur Ripstein, *Strictly Speaking – It Went Without Saying*, 2 *Legal Theory* 63 (1996).

be described as a ‘tacit assumption’ that does not involve a consciousness of alternatives. The absentminded professor stepping from his office into the hall as he reads a book ‘assumes’ that the floor of the hall will be there to receive him. His conduct is conditioned and directed by this assumption, even though the possibility that the floor has been removed does not ‘occur’ to him, that is, is not present in his mental processes.⁴⁵

And those scholars who do not quote Professor Fuller are sure to quote this similar passage from Wittgenstein:

Someone says to me, “Show the children a game.” I teach them gaming with dice, and the other says, “I didn’t mean that sort of game.” Must the exclusion of the game with dice have come before his mind when he gave me the order?⁴⁶

Wittgenstein’s answer, and that of many contract theorists, is that the exclusion of gambling could have been “intended” even if it never consciously came before the speaker’s mind.⁴⁷

Now, to be sure, many of the theorists who take this view are concerned mostly with rebutting claims that contract law

45. Lon L. Fuller, *Basic Contract Law* 666–67 (Minneapolis: West Publishing, 1947).

46. Ludwig Wittgenstein, *Philosophical Investigations* 33 (G.E.M. Anscombe trans.) (Oxford: Oxford University Press, 4th ed. 1972).

47. Theorists who share this view (in various forms, and to varying degrees), include Charles Fried, *Contract as Promise* (supra note 3) at 86–89; Langille & Ripstein (supra note 44); Stephen Smith, *Contract Theory* (supra note 20, 23) at 297–314; Randy E. Barnett, *The Sound of Silence: Default Rules and Contractual Consent*, 78 Va. L. Rev. 821, 874–94 (1992); and Adam Kramer, *Common Sense Principles of Contract Interpretation (and how we’ve been using them all along)*, 23 Ox. J. Leg. Stud. 173 (2003).

“imposes” certain doctrines, against the will of the contracting parties. For example, implied excuses such as frustration or impracticability have been described by some as having nothing to do with the parties’ intentions – as they surely do not, if “intentions” are limited to those factors the parties consciously thought of.⁴⁸ However, those doctrines might seem less of an external imposition, if they could be characterized as something that the parties implicitly intended all along. And while all acknowledge that the line between “tacitly intended” and “externally imposed” is a thin one,⁴⁹ the tacit agreement theorists usually argue that many of the law’s implied terms are in fact better understood if they are seen as merely carrying out the parties’ tacit understandings.

My interest here, though, is not in whether tacit understandings are “externally” imposed, but rather with the relation between tacit understandings and price effects. The possibility of tacit understandings does not inevitably make price effects irrelevant, for a careful analysis of price effects might help us understand what different parties are likely to assume. Stephen Smith puts the point as follows:

A significant part of the shared or “public” understandings about agreements is comprised of understandings

48. See *Davis Contractors* [1956] A.C. 696 (H.L.) (per Lord Radcliffe) at 728 (there is “something of a logical difficulty in seeing how the parties could even implicitly have provided for something which, *ex hypothesi*, they neither expected nor foresaw”).

49. As Charles Fried puts it, “there is a vaguely marked boundary between interpreting what was agreed to and interpolating terms to which the parties in all probability would have agreed but did not.” *Contract as Promise* (supra note 3) at 60. As Jody Kraus has helpfully shown, some of my earlier criticisms of *Contract as Promise* failed to respond to this distinction. Kraus (supra note ?) at 715–30.

about what should, morally, happen – these understandings, in turn, are to a significant extent grounded in, or influenced by, ideas of fairness and efficiency. In short, one of the things that “goes without saying” in many contexts is that the arrangement should be fair and efficient.⁵⁰

In keeping with this suggestion, I have argued that courts who attempt to identify industry customs (one possible form of tacit understanding) are often influenced by their view of the economic merits of whatever custom a party alleges to exist.⁵¹

Nevertheless, the scholars who emphasize the role of tacit understandings are almost never economists, so (as noted earlier) these scholars almost never actually discuss price effects in their analysis. And while it is also true that these scholars rarely try to justify their disregard of price effects, it is not hard to imagine an argument that might do so. All that is needed are two premises: (1) that the parties in fact *have* a tacit understanding on some point, whose terms can be known without economic analysis; and (2) that tacit understandings should be enforced, because they are part of the parties’ actual agreement. Grant these premises, and it follows that the dispute should be settled by reference to the terms of the tacit understanding, rather than by reference to anything an econ-

50. Smith (*supra* note 20, 23) at 303; a somewhat similar argument is made in Randy E. Barnett, *The Sound of Silence: Default Rules and Contractual Consent*, 78 Va. L. Rev. 821, 907–09 (1992) [hereafter cited as Barnett, *Silence*]. Professor Barnett prefers to refer to economic analysis merely as “evidence” of what the parties actually (if tacitly) consented to, but it is not clear that anything turns on this label.

51. Richard Craswell, *Do Trade Customs Exist?* in Jody S. Kraus & Steven D. Walt (eds), *The Jurisprudential Foundations of Corporate and Commercial Law* 118 (Cambridge: Cambridge University Press, 2000).

omist might say about price effects.

However, both of these premises are open to challenge. For one, even if a tacit understanding does exist, and its terms have been identified, it does not follow inevitably that the terms of that understanding should always be enforced. To the contrary, if many parties aren't aware of that tacit understanding, it might make sense to enforce only those terms of the tacit understanding that have explicitly been pointed out to the other party. In other words, it might make sense to adopt what economists would call a penalty default, to encourage greater disclosure to the party who is less-informed. And since tacit understandings are defined to include beliefs that the parties are not consciously aware of, the possibility that one party might benefit from explicit disclosure is very real.

Second, and perhaps more important, it will often be difficult to tell whether the parties in any given case actually *have* a tacit understanding on any given issue, or to tell what the terms of that understanding are. For example, Stephen Smith suggests that most parties tacitly accept contract law's excuse doctrines (mistake, frustration, and discharge for breach), so none of those doctrines is truly filling a "gap" in the parties' agreement.⁵² He acknowledges, though, that he has no evidence to support this assertion, describing his view as "one that I can really only report, not defend."⁵³ And while he may of course be right, it seems to me an unlikely coincidence that contracting parties – most of whom are not lawyers – should have tacitly internalized so much of the legal doctrine that Professor Smith seeks to justify.⁵⁴

52. Smith (*supra* note 20, 23) at 297–306.

53. *Id.* at 302.

54. Compare Thomas Scanlon's more skeptical view:

Nor does it help that other theorists have been equally quick, on equally little evidence, to find a tacit understanding in favor of whatever rules *those* theorists sought to justify. For example, Charles Fried has asserted that most people tacitly agree that the other party will be entitled to expectation damages if they fail to perform; and they also tacitly agree that the other party will be permitted to elect rescission as a remedy if she prefers.⁵⁵ And Randy Barnett has argued that most people's commonsense understandings include a rather detailed tacit agreement about the availability of specific performance. According to Professor Barnett, most people tacitly agree that (a) specific performance is the generally available remedy for failure to perform, except when (b) the promised goods are readily available from other suppliers, or when (c) the seller's cost of performance has gone up substantially.⁵⁶

One reason I am skeptical of such claims involves the nature of the issues for which a tacit understanding is asserted. Lon Fuller's example, involving the floor outside a professor's office, involved an issue on which near-unanimity could be expected, since no professor would want a hallway without a

[W]hen, for example, I try to determine whether a promise to do x obligates a person to do x even at the cost of y – it seems clear to me that I am engaging in moral reflection, not an inquiry into what the accepted rules of our social practice of agreement-making are. ... [W]hile a social practice of agreement-making *could* shape the content of particular obligations arising under it in this way, I am unable to identify any such limitations built into our particular practice of promising.

T. M. Scanlon, *Promises and Practices*, 19 *Phil. & Pub. Aff.* 199, 215–16 (1990).

55. *Contract as Promise* (supra note 3) at 118; for a further discussion, see Kraus (supra note ?) at 719–20 and n.99.

56. Barnett (supra note ?) at 183 and 196 n.59.

floor. The same may be true of Wittgenstein's example, at least for respectable families in his era.⁵⁷ By contrast, the availability of specific performance is something on which different parties are apt to have different preferences, *once any price effects are taken into account*. Indeed, price effects almost always introduce substantial diversity or heterogeneity across buyers, thus making unanimity unlikely. That is, even if all buyers would like the idea of specific performance (or any other remedy) *if they could get it for free*, buyers are much more likely to hold different views about just how much they are willing to pay for that remedy.

By contrast, the normative goals of the "tacit understanding" argument usually require not just that each individual have *some* tacit understanding, but that most or all contracting parties have *the same* tacit understanding, for otherwise we would have no basis for claiming a tacit *agreement*.⁵⁸ Thus, when theorists posit that most buyers have *the same* tacit understandings on any moderately complex issue, those theorists almost have to be (tacitly?) disregarding price effects.

57. As a naive baby boomer who was raised on board games like *Monopoly*, and who thus saw nothing wrong with "gaming with dice," my initial reaction to Wittgenstein's hypothetical was rather different.

58. Among tacit agreement theorists, Randy Barnett is a notable exception on this point, for he is willing to consider the possibility that different parties have different preferences and/or different understandings of the terms of their tacit agreement. Significantly, Professor Barnett is also willing to consider all of the factors that economists would consider relevant in selecting a default rule, including (for example) the use of penalty default rules to better inform parties who are less legally sophisticated than others. Barnett, *Silence* (supra note 50) at 885–93.

D. Deductive logic

The next argument relies not on tacit understandings, but rather on the rules of logic. Specifically, it has been urged that some remedies – including some remedy/price packages that some buyers might prefer – can nevertheless be excluded on grounds of logical inconsistency, because they are inconsistent with the premise that the parties’ contract was binding.

This argument is most often made in connection with what might be called a “deliberate” breach,⁵⁹ when a seller breaches one contract to sell to another buyer (as in section II’s example involving Bithiah and the painting). The argument begins with the premise that the original contract transferred *ownership* of the painting to Bithiah, for only by transferring ownership can a contract have any force at all (or so the argument runs). And if Bithiah now owns the painting (the argument continues), a breach by the seller would deprive her of what is actually her own property. Thus, in any system that respects property rights, the remedy for breach must logically be high enough to deter the seller from breaching without Bithiah’s consent, for otherwise the contract would not have succeeded in transferring full property rights to Bithiah.

Examples of this argument are easy to find. Here is Peter Benson’s version (the italics are mine):

The idea that the formation of a contract entails a transfer of non-physical possession at the moment of agreement *implies, in turn, a general entitlement in prin-*

59. I set aside here the challenges facing any attempt to rigorously define a “deliberate” breach. For a discussion of that issue, see Craswell, *Willful*, *supra* note 8.

principle to expectation damages for breach of contract. On this basis, when the law seeks to put the plaintiff in the position that he or she would have been in had the contract been performed, it simply ensures that, at the remedy stage, the plaintiff obtains in fact what he or she acquired in right at the moment of agreement. Expectation damages protect and, as it were, give back to the plaintiff something that already belongs to him or her.⁶⁰

And Daniel Friedmann has argued similarly:

Suppose that in consideration of \$300 D undertook to transfer to P, within 6 months, certain shares. After 5 months, when the price of the shares reaches \$1000, D reneges. If we assume that the contract was valid *so that it vested in P the right to the promised performance*, it follows that P would be entitled either to specific performance (the value of which is \$1000) or to the substitutionary remedy of damages, which will be based upon the value of the promised performance, namely \$1000.... To claim that the contract was binding, *i.e.* that P was entitled to D's performance, and yet that recovery can be confined to P's expenditure (\$300), *is a contradiction in terms*.⁶¹

In short, these authors are able to conclude that the proper

60. Peter Benson, *The Idea of a Public Basis of Justification for Contract*, 33 Osgoode Hall L.J. 273, 324 (1995).

61. Daniel Friedmann, *The Performance Interest in Contract Damages*, 111 L.Q. Rev. 628, 637–638 (1995) (footnotes omitted). For a broadly similar argument in favor of expectation damages, see Kimel, *supra* note 18, at 93 (“If a promise is binding, it invariably creates an entitlement in the promisee”).

remedy for breach of contract should be specific performance or expectation damages (at the least). Moreover, they are able to reach this conclusion without having to consider whether any buyers actually *want* that remedy, and without considering the price that buyers would have to pay. If their logical argument can truly do this much, then these theorists have strong reasons for disregarding prices.

However, this is more than logic alone can do. Even if we stipulate that Bethiah's contract must have transferred *some* ownership rights, we still need to interpret the contract to find out what rights were actually transferred. For example, Bethiah might have received the absolute right to block any breach by the seller; or she might have received merely the right to get her money back, which is what she contracted for in the example in section II. If Bethiah explicitly agreed to such a limited remedy, we can then say that the contract transferred to her not the ownership of the painting itself (as Professors Benson and Friedmann seem to assume), but merely the ownership of a right to *either* the painting *or* to the return of her purchase price, with the election between these to be made by the seller. And if we interpret the original contract as transferring only the hybrid combination of rights (the painting *or* some small quantum of damages), there is then no logical inconsistency in awarding her the small quantum of damages.⁶²

In other words, all that Professors Benson and Friedmann have really shown is that remedies for breach should involve expectation damages in a purely formal, tautologous sense.⁶³

62. Seana Shiffrin makes two other objections to this interpretation of the contract. I discuss these objections later in this section, and again in section IV.G.

63. Similar criticisms have been made by Jody S. Kraus, *Philosophy of*

They have shown that the remedy must logically match *whatever rights we decide that the contract has transferred*, for to do otherwise would indeed be a contradiction in terms. That is, if we decide that a contract transferred X, but if we then award some other value Y, that should logically force us to revise our decision about precisely what the contract had transferred. The problem, though, is that this purely logical analysis does not tell us how to decide whether the contract in fact transferred X or Y. In other words, formal logic cannot tell us how to decide whether any given should be read as transferring (a) the absolute right to all revenues from the painting, or as transferring (b) only a conditional right to the painting *if* the older customer didn't offer more for it. Since neither interpretation is truly self-contradictory, neither can be ruled out by formal logic alone.

At this point, then, we must return to the arguments discussed in earlier sections. For example, Professors Benson and Friedmann could say that their preferred interpretation is merely a default rule, so if Bethiah or anyone else actually prefers a smaller remedy (for a lower price), they are free to opt out of the default. But since neither author explicitly considers the price-related reasons why a buyer might want to opt out of such a default, neither author explains (or even asks) whether the law instead should choose the opposite default rule, in which those buyers who preferred a *larger* remedy would be the ones who would have to opt out.

1. *Buyers who don't want to speculate.* Are there other bases

Contract Law, in Jules Coleman & Scott Shapiro (eds), *The Oxford Handbook of Jurisprudence and Philosophy of Law* 747–49 (Oxford: Oxford University Press 2002); and by Daniel Markovits, *Contract and Collaboration*, 113 *Yale L.J.* 1417, 1499 (2004).

for choosing between these possible default rules? For example, does it matter if most buyers think of themselves as buying just “a painting,” rather than buying a complex set of options? Seana Shiffrin has pressed this point:

[P]arties typically come together to contract for performance not as a sophisticated, disguised way to exchange currency or to perform a veiled arbitrage dance. They contract for performance because goods and service are themselves the ends at least one party seeks. Putting aside middlemen contracts (e.g., insurance contracts, futures contracts, hedge contracts, and other contracts whose primary purpose is to allocate risk), the goods and services are not mere waystations for further economic exchanges.⁶⁴

This might be interpreted as a majoritarian argument: an argument that most parties (or most parties in certain kinds of contracts) want and/or tacitly expect that their contract will transfer *all* rights to the painting. There might also be an argument for a penalty default, if most buyers (in certain kinds of contracts) didn't know that their contract gave them only limited rights in the painting, and if most sellers did know and could easily inform buyers of those limits. Of course, to make either of these arguments, an economist would want to know just how many buyers needed this additional information, as well as how many buyers would actually prefer a more generous or a more limited remedy; and the latter question, about what various buyers would prefer, cannot be answered without attention to price effects. But in other contexts, Professor Shiffrin seems willing to accept economic arguments for

64. *Id.* at 1565.

choosing default rules,⁶⁵ and that might be true in this passage as well.

Notice, though, that whenever it is true that most buyers are contracting “for performance,” rather than for some option involving further economic exchange, that fact taken by itself may argue against the large remedies that Professor Shiffrin prefers. After all, Bethiah (in the example in section II) agreed to a smaller remedy precisely because she was not interested in the painting as an investment vehicle, so she didn’t want to pay a higher price up front just to be able to get a greater share of the profits if another buyer offered a higher price. If Bethiah *had* wanted to speculate on those gains, she then would have had a strong reason for insisting on a large remedy, for a large remedy would let her block the seller from breaching unless he agreed to share those gains with her – and the seller, knowing this, would likely charge a higher price. All else equal, then, buyers who are not interested in such speculation should be more likely to want to pay a smaller price for a smaller remedy, not a larger price for a large one.

2. *Remedies and universalizeability.* Professor Shiffrin also makes another argument that might be read as an attempt to deduce buyers’ preferences, either by formal logic alone or (perhaps) by invoking ethical principles as a constraint. This argument begins with the observation that breaching and paying damages cannot be recommended as a response to *every* contract, for in that case buyers would never get the goods or services they contracted for, and this would be an absurd result. For example, if Bethiah knew for certain that the owner’s other customer would buy the painting, it would be pointless for her to enter a contract whose only remedy was to refund

65. See section IV.F *infra*.

her purchase price. By contrast, the opposite practice (performing rather than paying damages) *could* be universalized as a response to every contract, without logical inconsistency or any other obvious problem. Professor Shiffrin thus concludes that the practice that is universalizable (performing) must be the one that is morally required. In other words, even if some buyers would prefer smaller remedies and lower prices, those preferences can be disregarded because they conflict with the logical (?) or moral requirement of universalizeability.

However, this use of universalizeability puzzles me. I cannot read universalizeability as a *logical* requirement, for it does not seem to me to be logically inconsistent for Bethiah to prefer a lower price and a smaller remedy, even though she admits that she would prefer a different remedy (or no contract at all) if she knew the seller was going to breach. Moreover if universalizeability is to have any significance, it surely must apply only to choices that are similar in some relevant way.⁶⁶ And a contract with a 10% chance of breach is, in ways that matter to buyers, a different contract than a contract with a 99% likelihood of breach, just as a lottery in which every ticket is a winner poses a different gamble than a lottery in which only one ticket will win. And while it is true that the first kind of lottery would be pointless, since every ticket would pay only its face value, what does that have to do with anyone's attitude toward the second kind of lottery? As Professor Shiffrin does not develop this argument at any length, I will not pursue it here.

66. Discussions of this issue in the philosophy literature include Don Locke, *The Trivializability of Universalizability*, 77 *Phil. Rev.* 25 (1968); and Alan Gewirth, *The Non-Trivializability of Universalizability*, 47 *Australasian J. Phil.* 123 (1969).

E. The entailments of a promise

A different argument, which Professor Shiffrin does develop at length, challenges whether any contract can legitimately be read as leaving the seller free to choose between either performance *or* the payment of damages. On her view, such a contract would fail to qualify as a *promise*, so it would therefore (?) be illegitimate to adopt this reading of the contract as the default interpretation. In other words, this argument rules out certain price/remedy combinations that buyers might prefer, if the combination in question would be inconsistent with the very idea of a promise.

Professor Shiffrin introduces the argument by paraphrasing (and criticizing) the somewhat weak commitment that is presumed by contract law's current default rules:

It is out of bounds to say: "I solemnly promise to do X, but I may fail to do so if something better comes along; moreover, if it does, you can only expect X's market value from me, although you may need to enlist the help of others to pry it out of my clenched fist. Further, let us now declare that should I fail, it will not be the sort of thing deserving of moral reprobation so long as eventually you are made whole monetarily. Moreover, it is not the sort of thing you may be upset with me over or view as showing my bad character."⁶⁷

Such a "commitment" will indeed strike many as bizarre, though (as Barbara Fried has noted) that may be at least partly due to the loaded language that is used.⁶⁸ Professor Fried also

67. Shiffrin, *Divergence* (supra note 2) at 728.

68. "[W]hat is troubling about the behavior of the promisor here is pre-

points out, importantly, that it is unclear in this example whether the buyer knew all along that he was getting such a severely limited commitment, or whether this was sprung on him after the contract had already been signed.⁶⁹

I will set those issues aside, though, to focus on Professor Shiffrin's own objection to this commitment. She is not merely claiming that the buyer is getting a bad deal, for if that were her claim she would have to say something about the price the buyer is being charged. At a low enough price, and for a buyer who doesn't care that much about X in the first place, even the grudging commitment described by Professor Shiffrin might be an attractive deal. But if we ignore the price issue – or, what amounts to the same thing, if we assume that stronger commitments could have been obtained elsewhere *for the same price* – then of course this scenario will seem bizarre, for it gives us no reason why the buyer would have agreed to such a deal.

As I said, though, Professor Shiffrin is not criticizing this arrangement merely on the grounds that it gives the buyer a bad deal. Instead, her charge is that this seller is committed to so little that his commitment cannot even qualify as a promise. Her passage continues as follows:

This is not a full-fledged promise. Its elaboratory remarks defy the language of its opening gambit. They clarify that it is not a promise at all Rather, it seems to be the statement of an intention to act, along with an acknowledgment that the statement will, in this context, render the utterer susceptible to one sort of lia-

cisely the fact that for no reason he feels impelled to taunt the promisee with the limited nature of his commitment. We naturally and rightly feel that only a complete jerk would do that." B. Fried, *supra* note 27, at 60 n.29.

69. *Id.* at 56.

bility at the hands of another. But there is no commitment by the utterer to *do* anything at all. Although one can declare within a promise some of the conditions under which the promised performance may not occur, those conditions cannot coherently extend so far as to include any situation in which the promisor has a change of heart or entertains a better offer.⁷⁰

Now, to be clear, the arrangement that Professor Shiffrin describes (and which current law presumes, more or less) does not leave the seller completely free to behave as he likes, for failing to perform will now subject him to the loss of whatever small damages the law awards. The arrangement she describes thus represents a commitment of some sort, in the sense that it leaves him with fewer options than he would have had if he had not agreed to this arrangement. What it does not represent, according to Professor Shiffrin, is a *promise*.

While it might be possible to challenge Professor Shiffrin's definition of a promise, I will accept her definition here, at least for the sake of argument. I therefore also accept the implications of that definition: (1) that a promise must come with remedies of at least a certain minimal size, which is to say that (2) a promise cannot leave the party who made it free to choose between performing and paying damages. In other words, a true promise must not involve certain combinations of (low) price and (small) remedy, because those combinations fall short of what defines a promise.

But what follows from this stipulation that some commitments are not promises? Without more, all we have is a terminological point, whose only effect is on what we *call* those

70. Id. at 728-29.

commitments.⁷¹ As I said, I am willing to accept Professor Shiffrin's terminology, so I will stop using the word "promise" to refer to the preferred arrangements of Rick, or Theresa, or Ira and George. Instead, for convenience (and for want of a better label), I will refer to these as "demi-commitments."⁷²

The key question, though, is what follows from this terminological stipulation? Professor Shiffrin does not show, or even attempt to show, that demi-commitments are in any way inferior to "real" promises. Nor does she argue that the law should reserve its enforcement powers for real promises, while refusing to enforce mere demi-commitments. (An argument made by others will be discussed in the following section.) For example, as long as Rick or Theresa or Ira and George have explicitly agreed to a demi-commitment, by explicitly agreeing to accept a less stringent remedy, I do not read Professor Shiffrin as imposing legal enforceability at all. As discussed earlier, her argument seems to be only that the *default* interpretation of a contract (one that is silent on the issue) should not treat it as a demi-commitment, which would put the burden of specifying otherwise on those who prefer a stronger promise.⁷³ Instead, Professor Shiffrin prefers that the stronger promise be the default interpretation, thus putting the burden of specifying otherwise on those who prefer a mere demi-commitment.

71. Later in her article, Professor Shiffrin raises other objections that are not merely terminological; and some of those exceptions might apply to this example as well. These other objections deserve their own analysis, which I provide *infra* in sections IV.G and IV.H.

72. As Barbara Fried points out, some of these may be known by more familiar labels, such as "option contracts" or "non-recourse loans" or "pay or play" clauses. Fried (*supra* note 27) at 59.

73. See the text *supra* at note 32.

And now we are back on familiar ground, with the question of which group of buyers should get to have their preferred package as the default package. Specifically, we are back to the challenge created by the formal symmetry of default rules: why should the burden of stating their wishes explicitly be placed on those who want demi-commitments, rather than on those parties who want full-fledged promises? That position puts a great deal of stress on the difference between promises and mere demi-commitments, while the moral relevance of that difference has yet to be established.

Of course, there may well be economic grounds for choosing one default rule over another. For example, if we thought that most buyers preferred a full-fledged promise, even with the higher price such a promise might command, that might give us a majoritarian argument for making a full-fledged promise the default. Or if we thought most buyers didn't know that sellers' contracts were mere demi-commitments, and if most sellers did know this (and could easily inform buyers), that might give us a penalty-default argument for making a real promise the default. But each of these arguments, to be convincing, would have to make some effort to assess just how many buyers did know what they were getting, or how many buyers would actually prefer one form of commitment over another. In other words, each of these arguments depends, at least implicitly, on an unspoken judgment about price effects.

F. The scope of contract law

Others have suggested that the definition of a promise is not merely a stipulation about terminology, but is instead a substantive distinction with moral and policy significance. These scholars have suggested that mere demi-commitments

either should not be enforced at all; or – what is not quite the same thing – they should not be enforced under the rubric of contract law.

Consider a recent exchange between Michael Pratt and Dori Kimel. Professor Pratt gives us the example of Rudy, a self-employed electrician who is also “an eccentric, earnest, solitary sort who takes pains to minimize the moral claims others have on him.”⁷⁴ When a customer, Eliza, asks if Rudy will *promise* to fix her electric problem, he replies that he is uncomfortable making promises to his customers, so he prefers to make business commitments “by contract alone, leaving the morality of promising out of the picture entirely.” Eliza tells him that she would be satisfied with an exclusively legal commitment, so they draw up a contract that includes the following language:

[T]he commitments expressed herein are exclusively contractual. We intend hereby to bind ourselves contractually to make the payments and to perform the acts specified, but we do not intend to bind ourselves morally to do so: these are contractual undertakings, not promises.⁷⁵

Here, too, we have a document that clearly is meant to *commit* the seller to something (Rudy will now be liable for damages if he fails to fix the electric problem). Nevertheless, if the document is taken at its face value, Rudy’s commitment cannot be taken as a *promise*, for by design it does not commit him to any of the moral obligations that come with promising. It is, in other words, a mere demi-commitment.

74. Michael Pratt, *Contract: Not Promise*, 35 Fla. St. L. Rev. 801, 807 (2008).

75. *Id.* at 808.

Professor Shiffrin's position, as we have seen, is that (at the very least) Rudy and Eliza should have to state their wishes explicitly before the law will enforce this nonpromissory arrangement. It is also possible, though, to argue that such demi-commitments should not be enforceable at all *as part of contract law*. After all, if one believes that contract law is mostly concerned – or, better yet, exclusively concerned – with enforcing promises, then commitments that are not promises would seem to have no place in contract law. On this view, if demi-commitments are to be enforced at all, they would have to be enforced under some other doctrinal label – possibly tort law; possibly a newly-created Law of Demi-Commitments.⁷⁶

Indeed, this may be the position of Dori Kimel, at least for some demi-commitments. Responding to Professor Pratt, Professor Kimel describes Rudy's demi-commitment as “oxymoronic ... inasmuch as contractual undertakings *are*, in certain ways, promises.” He concludes that a party “cannot” enter a contract while meaningfully declaring herself to be making no promise.⁷⁷ And while Professor Kimel stops short of declaring that Rudy's commitment should therefore be unenforceable under contract law, his description of that commitment as “oxymoronic” suggests that such a conclusion would not be unthinkable.

Of course, even if Professor Kimel believes that Rudy's demi-commitment should not be enforceable *under contract law*, nothing in his position would preclude that same commit-

76. Compare the suggestion of Charles Fried (and many others) that some reliance-based obligations should indeed be legally enforceable, but under tort law rather than contract law. *Contract as Promise* (supra note 3) at 24.

77. Dori Kimel, *The Morality of Contract and Moral Culpability in Breach*, 21 King's L.J. 213, 220 (2010).

ment from being enforced under some other body of law, where the complaint “but it’s not a promise!” would have no force. As Jody Kraus has noted, one of the ways that economists and philosophers differ is that economists are rarely concerned with preserving contract law as a distinctive doctrinal area of its own, while (some) legal philosophers care intensely about these doctrinal boundaries.⁷⁸ Thus, the fact that some writers attach great significance to the question of whether demi-commitments are promises could be seen as just one more reflection of this difference between economists and philosophers.

In my view, though, these debates about the status of demi-commitments also illustrate two larger differences between economists and philosophers. First, when non-economists treat demicommitments as somehow inferior to real promises, they do so without ever considering any price effects that might come with the demi-commitment. To cite one more example: If the electrician, Rudy, dislikes being under a moral or promissory obligation, he might well charge a higher price if his customers demanded (or if the law imputed) a moral commitment as well as a legal one. This possibility went unmentioned, and apparently unnoticed, by *every one* of the non-economists cited above.

78. Kraus (supra note ?) at 699–700. For some arguments in favor of taking the law’s doctrinal boundaries seriously, see Smith (supra note 20, 23) at 103–05. On the other side, a typical economists’ position (which I share) can be found in Ian Ayres, *Empire or Residue? Competing Visions of the Contractual Canon*, 26 Fla. St. L. Rev. 897, 898 (1999) (“Our first response to someone’s impassioned suggestion that a particular area is or is not contractual should be ‘Who cares?’ or perhaps more precisely ‘Why should we care?’ ... Essentialist debates about what is contract are not only semantic in the most pejorative sense of the word, but may divert attention from what is really at stake.”).

Second, if theorists are able to exclude all demi-commitments from the very definition of contract law, this is another instance of avoiding merely by stipulation the complexities that arise when buyers and sellers differ among themselves in their willingness to pay higher or lower prices. That is, a theorist who excludes demi-commitments from his field of study can then stop worrying about electricians like Rudy, or about couples like Ira and George, or about any other “eccentrics” who are willing to settle for smaller remedies in order to get lower prices. Instead, parties with those preferences can all be relegated to some other body of law – quite possibly to a body of law that doesn’t even exist yet – where they will be somebody else’s problem.

G. Impermissible rationales

In these final two sections I discuss two further arguments advanced by Seana Shiffrin, both of which are new additions to the literature on default rules. Her first objection starts from the premise that the rationale for legal rules – including, presumably, the rationale for any default rule – must not be unacceptable to a virtuous moral agent. Her second objection is that some default rules, perhaps especially those that enforce mere demi-commitments, might have long-term effects on cultural attitudes toward commitments generally.

These are important arguments, in part because they avoid some of the problems with earlier discussions of default rules. That is, the earlier literature sometimes assumed (if only implicitly) that morality, if it required anything at all from a default rule, required only that the default rule not be inconsistent with the parties’ moral obligations. This posed a problem: since default rules, by definition, are those that leave parties

free to opt out of whatever the rule requires, how could a mere default rule ever be *inconsistent* with a moral obligation? As a result, various writers (myself included) argued that many moral theories placed no constraint at all on the permissible content of a default rule.⁷⁹

Professor Shiffrin has now introduced two other ways in which morality might constrain the content of a default rule. Even when the default rules do not require any behavior that is overtly inconsistent with morality, morality might nevertheless constrain the *justifications* that could be offered for that rule. Alternatively, or in addition, morality might also constrain the content of a default rule because of the possible long-term effects on *moral character generally*. The first of these objections is discussed below; the second in section IV.H.

1. *What transparency requires.* Professor Shiffrin does not believe that contract law should enforce morality *per se*, but she does believe that contract law should not make it difficult for citizens to develop their moral capacity. Moreover, “moral capacity” (in this context) is not meant to be neutral between all the various moral views that citizens might hold, any more than it is meant to be neutral between moral and amoral views about promising. To the contrary, Professor Shiffrin believes that liberalism presupposes that citizens have developed certain substantive moral capacities, and among these capacities is a “mastery and appreciation of promissory norms.”⁸⁰ And for Professor Shiffrin, as we have already seen, a correct under-

79. Craswell, *Default Rules* (supra note 4) at 511–28.

80. Shiffrin, *Divergence* (supra note 2) at 714. Continuing her exclusive focus on promises (as she has defined them), Professor Shiffrin does not discuss whether a liberal society might also benefit if its citizens “mastered and appreciated” the norms embodied in demi-commitments.

standing of promissory norms includes the proposition that deliberate breaches are immoral, at least when the parties have not explicitly stipulated that such breaches will be permitted.

Now, the belief that deliberate breaches are immoral does not itself justify prohibiting those breaches (according to Professor Shiffrin), for that would be to enforce morality for its own sake. Instead, what Professor Shiffrin requires is that the legal system not adopt rules whose *justifications* would be inconsistent with citizens' legitimate moral beliefs, for that too would interfere with their development of the required moral capacities, including (presumably) their internalization of the correct promissory norms. She summarizes this by saying that legal rules and their justifications should be "capable of being known and accepted by a self-consciously moral agent."⁸¹

Professor Shiffrin then argues that this requirement precludes some legal doctrines that permit or encourage deliberate breaches, because the rationale for those doctrines could not be accepted by anyone who believes (and, in her view, believes correctly) that such breaches are immoral. The problem, as she sees it, is that the rationale for these doctrines usually treats efficient breaches as being *good* – either (1) so good as to be morally justified, all things considered; or at least (2) good in the weaker sense of being immoral, but still worthy of being encouraged by contract law, because contract law has purposes other than morality. To Professor Shiffrin, position (1) is out of bounds because it would be flatly inconsistent with the beliefs of, and therefore could not possibly be accepted by, any moral agent who correctly believes that such breaches are immoral. And even position (2) is problematic for a moral agent, for it holds that contract law should encourage people to do

81. *Id.* at 712.

things that conflict with that agent's fundamental moral commitments. As Professor Shiffrin puts it:

A virtuous agent can surely accept that there may be good aspects to wrongful breach on certain occasions. Yet, if such breach is indeed, all things considered, wrong, a virtuous agent cannot accept the economic benefits of breach as constituting a sufficient, or even a partial, contributory justification for the law's content.⁸²

In this section, I am not concerned with whether Professor Shiffrin is right that some breaches of contract are immoral, without regard to any price effects, so I will take that premise to be true. Instead, in this section I discuss what follows from that premise – and, in particular, what follows from it for the law's choice of default rules. That is, even if a virtuous agent could not accept a rationale that presupposed that efficient breaches were good, could a virtuous agent nevertheless accept a rationale for permitting efficient breaches as a default rule?

It might seem as though the answer is obvious: surely a moral agent who could not accept the rationale for efficient breach itself would be similarly unable to accept the rationale for any default rule that permitted (much less encouraged) efficient breach. But this conclusion is too hasty, for it ignores the other possible rationales for default rules, including the ways in which default rules might legitimately accommodate the views of *other* citizens.

2. *Default rules and transparency.* Consider the economic rationales for default rules that were described earlier in sec-

82. Id. at 732. On the question of whether (and how) this differs from enforcing the agent's moral beliefs directly, see id. at 733 n.47.

tion IV.B. To make the analysis more concrete, suppose (for now) that lawmakers decide to adopt a majoritarian default rule for certain kinds of contracts; and suppose that nearly everyone knows what the law is, so there is no need for a penalty or “information-forcing” default. Then, faced with the question of what the majoritarian default rule should be, suppose the lawmakers conduct an extensive survey of the parties who will be subject to this rule. Suppose this survey finds that most parties, because of price effects, actually prefer to have only moderate sanctions for breach, leaving the other party free to elect between performing or paying damages. In other words, suppose the survey shows that most parties prefer mere demi-commitments.

Now, if this survey is accurate, Professor Shiffrin’s virtuous agent may have good reason to object to the rationales that his *fellow citizens* appear to be using. However, the *legal system’s* rationale (when it adopts its default rule) will be one step removed from the rationale employed by any of the citizens who responded to the survey. That is, the legal system’s rationale in this case will not be, “We adopt moderate sanctions as the default rule because that’s what most citizens seem to want, *and we think they are right to want it.*” (The italicized clause would indeed be unacceptable to Professor Shiffrin’s virtuous agent.) Instead, the legal system’s rationale in this case will be more like this: “We adopt moderate sanctions as the default rule because, rightly or wrongly, that’s what most citizens seem to want, *so this default rule will minimize aggregate opt-out costs.*” The question, then, is whether minimizing aggregate opt-out costs is a rationale that a virtuous agent could accept, even if some of those costs involve his fellow citizens opting out (or not) for what he considers immoral reasons. Can a virtuous

moral agent be that tolerant of his misguided fellow citizens?

In my view, a virtuous moral agent can and should be. Recall that even Professor Shiffrin is willing to permit efficient breaches as long as the parties who want them have shouldered the costs of stating that preference explicitly in their contract.⁸³ But this returns us to the symmetry problem: As long as we permit both types of contract (those with high penalties and those without), *somebody* will have to bear the costs of being explicit. How, then, can a virtuous agent adopt the *NIMBY*-like attitude that he and those who think like him should be exempt from these drafting costs, and that it should always be the *other* citizens who have to state their preferences explicitly?

The case is, if anything, even stronger if the lawmakers instead select a penalty default rule. That is, suppose this time the lawmakers' survey reveals that most parties prefer a very large penalty for breaches by buyers (just as Professor Shiffrin would like). But suppose the survey also shows that (1) most buyers have no idea what they are responsible for if they breach, while (2) most sellers are repeat players who know exactly what the law provides. As a result, suppose the lawmakers adopt a default rule that is deliberately unfavorable to sellers – “buyers can breach whenever they like and pay no more than minimal damages” – precisely in order to encourage sellers to opt out of this default, with suitable requirements about just how explicit sellers must be to do so.⁸⁴

In this case, the default rule again diverges from what the

83. See the text and note *supra* at note 31.

84. For examples of such proposals in various business-to-consumer settings, see Ayres & Gertner (*supra* note 35) at 98–100; and Victor P. Goldberg, *An Economic Analysis of the Lost Volume Retail Seller*, 57 S. Cal. L. Rev. 283, 294–97 (1984).

virtuous agent would himself find acceptable. But in this case, the *rationale* for the default rule is even farther removed from the virtuous agent's reasons for disapproving of some deliberate breaches. That is, in this example the lawmakers' rationale is: "We adopt minimal sanctions as the default, even though we (and most citizens in our survey) agree that minimal sanctions are not ideal. But we still make minimal sanctions the default presumption, *in order to encourage more explicit disclosure by sellers.*" Surely this rationale, with its focus on greater disclosure to parties who are not well-informed, contains nothing that would be unacceptable to a virtuous agent.

To be sure, Professor Shiffrin does not directly address this question; but what she says on other issues suggests that this rationale should indeed be acceptable. For example, Professor Shiffrin acknowledges that a virtuous agent could accept justifications based on "distinctively legal" normative arguments.⁸⁵ And while it is not entirely clear what motivates this exception, or how it is to be defined,⁸⁶ "distinctively legal" might include goals such as "minimizing the aggregate costs of opting out of the law's default rules," or "informing less-sophisticated parties about the legal effect of their contracts."

It may also be relevant that Professor Shiffrin does not object, at least in principle, to writing requirements like the Statute of Frauds or the Parol Evidence Rule.⁸⁷ As was noted earlier, these requirements have much in common with penalty defaults, for they too threaten parties who fail to comply with

85. Shiffrin, *Divergence* (supra note 2) at 733–36.

86. Professor Shiffrin defines it only as "a moral argument whose range is specifically tailored to the special, normatively salient properties of law and its appropriate content and shape." *Id.* at 733.

87. *Id.* at 752.

a result that is intended to be unattractive. (In the case of the Statute of Frauds and the Parol Evidence Rule, the threat is to treat as legally unenforceable a contract that both parties intended to be binding). The purpose of the threat is also similar to the purpose of a penalty default, for in both cases lawmakers hope to induce parties to “opt out” of the threat by putting their contract into a particular *form*, in the belief that that form will be easier for subsequent courts to evaluate.⁸⁸

Indeed, and in keeping with this reading, Professor Shiffrin has herself relied on something that is very like a penalty default or information-forcing rationale. At one point during her exchange with Steven Shavell over the moral implications of “incomplete” contracts, she addressed Professor Shavell’s argument that efficient breaches of a snow removal contract might not be imoral at all, as long as the contract was silent on the question of whether performance was required even when it had become inefficient (say, because the removal equipment was inoperable). Professor Shiffrin responded as follows:

[T]he risks and costs of equipment failure are more salient to the promisor than to the promisee; after all, the maintenance of his equipment falls under the promisor’s control, and he would seem more aware of the likelihood of failure and the frailty of the equipment. One might presume for those reasons that he bears default responsibility for performance in this contingency, *or at the very least, that he bears responsibility for drawing attention to the issue*. It seems reasonable to expect the promisor to perform unless he raises the issue [in advance] and makes special arrangements to

88. Ayres & Gertner (supra note 35) at 123–25; see also note 37 supra.

counteract the promisee's reasonable expectations of performance.⁸⁹

In other words, Professor Shiffrin accepts that it may be justified to have a default rule that is unfavorable to the better-informed party – the snow removal firm, who has more control over the outcome and to whom the issue is more salient – in order to encourage that party to raise the issue explicitly.

To be sure, in this example the information-forcing default *increases* the damages for nonperformance (by denying the removal firm a legal excuse), so Professor Shiffrin has other reasons for supporting this default. But the arguments Professor Shiffrin invokes in this passage can point in either direction – for either larger or smaller damage awards – depending on the circumstances. For example, suppose the question were whether consumers should have to pay large damages for canceling a contract just a few hours after they entered it (assuming the contract was silent as to damages, and assuming that the seller had already and legitimately relied on the contract). In many such cases, consumers might not know what the default rule was; and the seller might be in a better position to predict and deal with any effects of cancellation on her schedule, thus making this issue more salient to the seller than to the consumer.⁹⁰ Indeed, this is the classic economic rationale for a penalty default rule. If a virtuous agent could accept this rationale in the snow removal case described above, then he should also be able to accept this rationale in the consumer case described here.

In short, this is yet another case where price effects, and the

89. Shiffrin, *Immoral* (supra note 2, 31) at 1561 (emphasis added).

90. See Goldberg (supra note 84).

resulting differences across different buyers, should matter. Once price effects are taken into account, it is very likely that some buyers *will* prefer mere demi-commitments, even while others might prefer full-fledged promises. In that case, economists will want to select the default rule by asking how many (and which) buyers will want to opt out, and what transaction costs will have to be borne by those who do opt out, even those who opt out for what we are taking to be an immoral reason. To make price effects irrelevant, then, it has to be argued that transaction costs borne by those who opt out for immoral, price-related reasons can justifiably be ignored, leaving the state to look only at the transaction costs borne by those who act morally. That premise seems to me to be difficult to justify.

H. Cultural effects

I now turn to one final argument that Professor Shiffrin supplies, which stands on a different footing than some of the others. This argument accepts economists' concern with the actual consequences of default rules, but criticizes that analysis for being unduly narrow, by leaving out one of the most important effects that any default rule might produce. Specifically, this argument worries that some default rules (or their commonly-accepted rationales) may produce *cultural* effects. As Professor Shiffrin puts it,

[T]he culture and practices facilitated by law should be compatible with a culture that supports morally virtuous character. Even supposing that law is not responsible for and should not aim to enforce virtuous character and interpersonal moral norms, the legal system should not be incompatible with or present serious

obstacles to leading a decent moral life.⁹¹

Professor Shiffrin's concern is that, if the law's default rule makes it very easy for parties not to keep their promises, that may make it hard to sustain a moral culture in which promise-keeping is valued. In a worst-case scenario, this could lead to a downward spiral in which habits of promise-keeping gradually grow weaker and weaker, until eventually promises become worthless. And even if that worst case never arrives, we might still object to even a small decline in the moral culture that supports promise-keeping. Thus, even if one default rule was superior to another in (say) its effect on aggregate opt-out costs, we might still prefer a different default rule that produced fewer adverse cultural consequences.⁹²

Moreover, if this argument has merit then it might be able to supply the missing justification for some of the arguments I discussed in earlier sections. For instance, if long-term cultural effects were likely to result only from default rules that fell short of being promises, that could explain why Professor Shiffrin was so concerned to emphasize that the law's current default obligation is a mere demi-commitment, and is not a promise at all. On this view, the failure to qualify as a promise would have more than merely terminological significance, for it might also be a good predictor of long-term cultural effects.

91. Shiffrin, *Divergence* (supra note 2) at 719.

92. I thus follow Liam Murphy in giving an instrumental or consequentialist interpretation to Professor Shiffrin's argument. Liam Murphy, *Contract and Promise*, 120 Harv. L. Rev. Forum 10, 11–12 (2007). In other words, if the law imposed only weak penalties for breach – *but if, somehow, all citizens continued to regard every promise as a sacred commitment* – I take it that Professor Shiffrin's objection would no longer apply. Professor Shiffrin herself frames the argument not in terms of consequences but in terms of what is required for moral agency, but my comments in the text should apply to either version.

Similarly, if long-term cultural effects arise only from the law's *default rules* (and not, for instance, from the contracts that parties actually sign), that could explain why Professor Shiffrin is willing to accept deliberate breaches as long as those breaches are permitted by express contractual language, rather than being permitted by a default rule.

However, the key question under this argument is when these cultural effects are likely. They cannot be predicted by theory alone, for there is nothing logically inevitable about any of these consequences. There are many cultural habits that persist without legal encouragement (tipping, for one), just as there are other cultural habits that seem to have fallen by the wayside (writing thank-you notes?), so either outcome is clearly possible. And while tipping and thank-you notes might be considered trivial, we face the same indeterminacy when it comes to cultural habits connected with promise-keeping. After all, even if a legal system did nothing to enforce promises, it would not be *impossible* for a citizen to maintain his own moral standards in spite of the law's laxity ("Even though the law does not enforce promises, there's no reason I should stoop that low"). But theory alone cannot tell us *how many* citizens will be able to do this. It is fundamentally an empirical question.⁹³

Indeed, viewed in these terms the argument is not unlike similar arguments that have been made about the cultural effects of other legal rules. Consider the contemporary debates

93. While Professor Shiffrin at one point disavows making an empirical claim, I take her merely to be disavowing any claim that we have enough evidence to *answer* these questions empirically. Shiffrin, *Divergence* (supra note 2) at 741 (referring to the "the almost comic difficulties in adducing persuasive evidence and examples").

over who should be allowed to marry. It is sometimes argued that, if the government were to permit or “approve of” heterosexual marriages, that might somehow cheapen or degrade the relationships enjoyed by committed same-sex couples. (Or vice versa, as the argument of course is more usually made.) Here too, the “cheapening” effect is not logically compelled, for nothing about a law permitting one kind of marriage *necessarily* implies anything at all about the value of other marriages. But cultural attitudes are not formed by logical implication alone, so there is no way to rule out these effects purely as a matter of theory. It is, again, an empirical question.

An even closer parallel might be found in debates over what is sometimes called “commodification.” That is, one argument against allowing certain things to be sold on the open market – babies, for example, or sexual relations – is that a widespread practice of market sales might change (and not for the better) the way that many people view those items. For instance, if there were a standard market price for babies (with predictable adjustments for various attractive or unattractive features), that might lead some parents to think of their children as fungible financial assets, thus altering the culture of parenting in what would surely be undesirable ways.⁹⁴

Indeed, even in contexts where no monetary sales have been permitted, similarly undesirable effects might still be produced by the government’s acceptance of certain *rationales* for its actions. For example, if the government is deciding whether

94. See generally Margaret Jane Radin, *Contested Commodities* (Cambridge: Harvard University Press, 1996). Related though slightly different accounts can be found in Elizabeth Anderson, *Value in Ethics and Economics* (Cambridge: Harvard University Press, 1993); and in Joseph Raz, *The Morality of Freedom* (Oxford: Oxford University Press, 1986) at 345–57.

to build a dam that would flood a mountain gorge, and if (in the course of doing a cost-benefit analysis) government analysts translate the scenic beauty of the gorge into some quantity of dollars, that might lead some citizens to think of scenic beauty only in financial terms, thus destroying any sense of awe or reverence that the gorge might previously have inspired.⁹⁵ Of course, here too there is no imperative that *requires* citizens to alter their view of nature just because of the government's use of cost-benefit analysis. As an empirical matter, though, it is possible that they might.

How, then, should we judge the likelihood that undesirable cultural effects will follow from any particular default rule? Lacking empirical evidence, Professor Shiffrin suggests that we sit back and “ponder how human moral agents nurture and maintain their habits and dispositions of moral agency.”⁹⁶ When I ponder this question, though, I find myself more skeptical than she is.

Yes, it seems initially plausible to think that a market for babies might lead parents to look on their children in a different and much less loving way. On the other hand, puppies are regularly sold by pet stores on the open market, with no apparent consequences for the love and affection they receive. Works of great literature can also be bought and sold for money, with (so far as I can tell) a similar lack of negative effect.⁹⁷

95. Discussions of this point include Richard H. Pildes & Elizabeth Anderson, *Slinging Arrows at Democracy: Social Choice Theory, Value Pluralism, and Democratic Politics*, 90 Colum. L. Rev. 2121 (1990); and Cass R. Sunstein, *Incommensurability and Valuation in Law*, 92 Mich. L. Rev. 779 (1994).

96. Shiffrin, *Divergence* (supra note 2) at 741.

97. For similarly skeptical views about the inevitability of commodifying effects, see Scott Altman, *(Com)modifying Experience*, 65 S. Cal. L. Rev. 293 (1991); and Eric Mack, *Dominos and the Fear of Commodification*, in John W.

And in the case of same-sex marriages, there seems to me no reason at all to think that their legalization in certain states has devalued heterosexual marriages in any of the ways that critics feared.⁹⁸

Instead, I suggest that these cultural effects are almost always attributed to practices *that are already disapproved of* by the person who predicts the cultural spillover. For example, nobody really objects to selling works of literature for money; and because of this lack of objection (or so I would claim), nobody predicts that allowing such sales will “commodify” our attitude toward literature. The debates over same-sex marriage make a similar point. Nobody says, “I’d be all for same-sex marriages, if only they didn’t have the effect of cheapening heterosexual relationships.” Instead, the cheapening effect is predicted only by those who disapprove of same-sex marriages on other grounds.

I do not mean that these predictions are necessarily dishonest or in bad faith, any more than I believe that supporters of same-sex marriages (like myself) act in bad faith when they predict no adverse cultural effects. Instead, I think we typically expect other people to more carefully distinguish the implications of practices we believe to be desirable (“Just because the government lets some other couple marry, that needn’t imply anything about the value of *your* marriage”), for if enough people are careful in this way then the adverse cultural effects will be small. But when it comes to practices that we already disapprove of on other grounds, we typically are quicker to

Chapman & J. Roland Pennock (eds.), *Markets and Justice: Nomos xxxi* (New York: NYU Press, 1989) at 157.

98. Some of the available evidence is discussed in *Perry v. Schwarzenegger*, 704 F. Supp.2d 921 (N.D. Cal. 2010).

assume that there is less reason for people to be so careful in parsing the implications of the practice, and therefore more reason to predict adverse cultural effects.

Consider more closely the “cultural spillover” argument for prohibiting same-sex marriages. This argument might be expressed in three steps:

- (1) Heterosexual marriages are fragile, in the sense that they can be adversely affected by the mere presence of other kinds of marriage.
- (2) Couples in heterosexual marriages deserve to be protected from this fragility, even if the only way to protect them is by prohibiting same-sex couples from marrying.
- (3) The loss to same-sex couples, if they are not allowed to marry, is small.

But these three steps are not independent, for those who believe that prohibiting same-sex marriages would have few costs (step 3) are, as a result, likely to believe that the value of protecting heterosexual marriages will surely exceed any cost to same-sex couples (step 2). Similarly, those who believe that prohibiting same-sex marriages would have little cost are also likely to believe that heterosexual marriages, even if they are not excessively fragile, are at least *sufficiently* fragile (step 1) to justify such a low-cost, protective step. By contrast, those who believe that a great deal would be lost if same-sex couples were barred from marrying (step 3) are likely to be much more demanding when it comes to steps 1 and 2 as well.

Professor Shiffrin’s cultural argument about promising has a similar structure, even though its political valence is of course very different. That is, Professor Shiffrin sees the culture of promising as fragile, in the sense that it can be threatened if the state so much as adopts a particular default rule, allowing par-

ties to create a demi-commitment without requiring explicit language to that effect. She also, apparently, believes that those who prefer demi-commitments would lose little from the opposite rule, either because she thinks any parties who prefer a demi-commitment can easily create one by using express language (the default rule argument), or perhaps because she just isn't focusing on demi-commitments here (the argument that contract law is concerned only with *promises*). But any scholars who are more concerned with parties who prefer demi-commitments will likely see matters differently, and require more evidence that the culture of promising is quite so fragile.

By contrast, suppose someone proposed instead to ban *any* enforcement of demi-commitments, even when the parties had explicitly agreed that this was the relationship they wanted (as with Rudy and Eliza in section IV.F, and as with all of the examples in section II). In other words, suppose we were considering a not a mere default rule, but a mandatory rule against demi-commitments. Cultural arguments could easily support a mandatory ban, for permitting parties to *explicitly* enter into demi-commitments (and to enforce those commitments in court) could itself undermine the culture of real promises, in all the ways that Professor Shiffrin fears.⁹⁹ Indeed, some experimental evidence suggests, albeit tentatively, that explicit language drafted by the parties may have a *greater* effect on beliefs and attitudes than would a mere default rule adopted by the legal system.¹⁰⁰ The difference, though, is that a mandatory

99. Hence Barbara Fried's skepticism about whether Professor Shiffrin can remain committed to allowing parties to opt out of her preferred default rules. Fried (*supra* note 27) at 56.

100. Compare Russell Korobkin, *The Status Quo Bias and Contract Default Rules*, 83 *Corn. L. Rev.* 608 (1998); with Russell Korobkin, *Inertia and Preference in Contract Negotiation: The Psychological Power of Default Rules and Form*

ban would impose greater costs on any parties who had reason to prefer a mere demi-commitment, including those who had price-related reasons. Most theorists, therefore, before they would support a mandatory ban, would want more evidence that the culture of promising was *sufficiently* fragile to justify such a step.

Notice, though, that these evidentiary concerns do not go away even if we are considering a mere default rule. True, a large-remedy default rule could be opted out of by any parties who preferred a weaker demi-commitment, and in many cases the cost of opting out would be small. But there is still the symmetry problem: a small-remedy default could also be opted out of by any parties who preferred a stronger form of commitment, and in many cases those opt-out costs will be small as well. Moreover, there may also be symmetry on the cultural dimension. That is, if one concern is that a small-remedy default might adversely affect the culture of promising, the equal but opposite possibility is that a large-remedy default might adversely affect the culture of demi-commitments. True, both of these are highly conjectural effects (and necessarily so, given the lack of authoritative evidence on either). But the significance of each possibility will depend, in part, on how much we value these two institutions: not just on how much we value promises, but also on how much we value demi-commitments. And since one advantage of a demi-commitment is that it is apt to come at a lower price, scholars who fail to consider price

Terms, 51 Vand. L. Rev. 1583 (1998). The first study examined the effect on attitudes of the law's default rules; the second analyzed the effect of "standard form" language drafted by one party to opt out of the default rule. At least in the setting of this experiment, the standard form language had the greater cultural effect.

effects are likely to miss this advantage as well.

V. Conclusion

My interest in these topics lies mostly in the constraints that morality might (or might not) place on the use of economics to reform or improve contract law. That is, I am not interested in constructing a theory that would “explain” or justify current contract law, for I do not start with the premise that current law *is* justified.¹⁰¹ Moreover, when I consider ways in which current law might be improved, my inclination is to think of “improvements” in terms that economists would, such as better service or more reliable products or lower costs. I am not, however, indifferent to morality (or so I would like to think). Thus, if the moral aspects of promises do put limits on the improvements the law may pursue, this is something I want to know.

In this essay, I have tried to set out the reasons why many of the non-economic theories seem unpersuasive to me. No doubt I am influenced by my own blinders; and no doubt there is an equally long (or longer) list of reasons why my own arguments have not been persuasive to many non-economists. But that is all the more reason why the debate should continue.

101. I discuss this position at more length in Richard Craswell, *In That Case, What is the Question? Economics and the Demands of Contract Theory*, 112 Yale L.J. 903, 904–07 (2003).