DERECHO CIVIL

Capítulo 4

Alfredo Bullard
Gastón Fernández
(Editores)

PONTIFICIA UNIVERSIDAD CATÓLICA DEL PERÚ
FONDO EDITORIAL 1997
FACULTAD DE DERECHO

Primera edición: octubre de 1997

Diseño de Cubierta: AVA diseños

Derecho Civil Patrimonial

ISBN 9972-42-029-9

Impreso en el Perú - Printed in Peru

THE IMPACT OF CONTRACT LAW ON THE ECONOMY

Stewart Macaulay

I. Introduction.

A. Too often, we in the U.S. pay little attention to Peru. However, just this past month, an entire symposium in the Yale Law Journal,[1] the lead article and a lengthy comment in the Law & Society Review,[2] and an article in Social & Legal Studies[3] focused on underground or second economics "in formal legal systems" and the power of other-than-legal sanctions in economic transactions, particularly in highly successful Asian economies.

1. Article after article in both of the first two journals focused on Eastern Europe and the former Soviet Union and their transitions to some form of market economies.

2. However, article after article in all three journals also focused on Hernando de Soto's The Other Path.[4] Here, Peru came to stand for Latin

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1 See Symposium: The Informal Economy, 103 Yale Law Journal 2119-2436(1994). See, particularly. Arthur J. Jacobson. The Other Path of the Law, 103 Yale Law Journal 2213(1994).

2 See Jane Kaufman Winn. Law and Relational Practices in Taiwan, 28 Law & Society Review 193(1994): Frank K. Upham. Comment—Speculations on Legal Informality: On Winn's "Relational Practices and the Marginalization of Law," 28 Law & Society Review 233, 236-237 (1994).

3 See Lauren Benton, Beyobnd Legal Pluralism: Towards a New Aproach to Law in the Informal Sector, 3 Social & Legal Studies 223 (1994)

4 Hernando de Doto, The Other Path: The Invisible Revolution in the Third World (1989).

America, Africa and much of Asia as well as many African-Americans, Hispanic-Americans and Asian-Americans in the United States who survive in our second economy.

B. The Other Path contains several distinct parts. There is:

1. A description of the practices of many Peruvians in housing retailing and transportation most of which violate Peruvian law.

2. An analysis of how such transactions are successful standing apart from the official legal system—that is, the norms and sanctions that support long-term continuing relationships even when they are illegal.

3. A diagnosis of the problems with Peruvian law, at least as it stood when the book was written.

a. Here we read a devastating criticism of over-regulation and a neglect of its many costs and consequences;

b. He advocates deregulation to legalize much of what is now the informal, and often illegal, sector.

4. A prescription for a "revolution" that would encourage and focus all of the entreprencurial energy of the popular classes in Peruvian society—in essence. The Other Path is the "rule of law", so beloved by international monetary organizations.[5]

a. De Soto calls for protection of private property recognizing much of what is now property, in fact, although not in law.

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5 Udo Reifner remarks: "While in former times capitalist nations used priests, soldiers and merchants to convince less developed peoples to adhere to their system, we can now rely on the convincing forces of IMF, World Bank, BERD and other financial institutions where nations cue up to be accepted as members. Reifner, The Vikings and the Romans—Contract Law and Social Economy 6 (Paper presentad at the Conference on Perspectives of Critical Con tract Law, Tuusula, Finland, May 7 to 10, 1992).

b. He also calls for legal enforcement of contracts so that planning and risk taking would be encouraged.

(l) He finds that the tactics used by those in the informal sector now—such as establishing trust, maintaining valued long-term-continuing relations and the alike—are inefficient because they impose unnecessary costs on traders.

(2) He advocates legally enforceable contracts so that traders could rely on the legal system to insure performance at a lower cost than that involved in present practices.

(3) He writes as if legally enforceable contracts standing alone, would make trust and the sanctions of long-term continuing relations unnecessary in a truly modern economy.

C. My paper will focus on this last factor—the role of contract law in market economics particularly that of the United States, simply because I know it the best.[6]

D. However, insofar as I am critical of de Soto's claims for contract law, I do not want to be misunderstood as being critical ofso much that I admire in The Other Path.

II. What is the received model of the role of contract law in market economics?

A. There are some common elements of the classic model of the functions of contract:

1. One version of the functions of contract law suggests that in a state of nature we are all selfish.

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6 See Stewart Macaulay. Non-Contractual Relatins in Business: A prelimnary Study 28 American Sociological Review 55 (1963): Stewart Macaulay. Elegant Models, -Empirical Pictures, and the Complexities of Contrat, 11 Law & Society Review 507 (l977); Stewart Macaulay, An Empirical Wiew of Contract, l985 Wisconsin Lay Review 465.

a. Law supports needed interdependence by coercing us to honor obligations to others.

b. Ideally, it should make no difference whether we perform or breach a contract because legal action would take away any harm resulting to the other party.

2. The supposed historical story is that we begin by trading within real *communities.*

a. Capitalism breaks this up, and we become alienated strangers.

b. The legal system supplies a king of synthetic community based on rights and duties enforced by courts.

3. The model also makes many *assumptions* about planning, performance of obligations and dispute resolution—all in terms of legal rights:

a. First, it is assumed that business people carefully plan relationships in light of legal requirements and the possibilities of nonperformance.

(1) They must spell out every thing because parties will perform only to the letter of a contract, if they go that far.

(2) Indeed, if parties do not plan and spell out everything, they are fault and responsible when they fail to receive what they expected from the bargain.

b. Second, it is assumed that contract law is a body of clear rules so that it can facilitate planning and the performance of contracts.

(1) It provides format channels so that we know the right way to proceed to produce desired legal results.

(2) It provides default rules so that parties can save transaction costs.

(a) Unless they wish others terms, they can rely on the law to fill in standard provisions.

(b) This avoids the costs of negotiating about possible contingencies.

(c) Finally, the model assumes that contract litigation is a primary means of determining breach and, directly o indirectly, resolving disputes.

B. This classic model has an illustrious history.

1. We find traces of it in Shakespeare's The Merchant of Venice.

a. Antonio has breached a contract, and, under its terms, he owes Shylock a pound of flesh.

b. Several characters search for a way out, but those representing the establishment argue that the economy of Venice depends on certain and predictable legal enforcement of contracts.

c) There is a way out, but remember that it involves claiming to enforce the letter of the contract.

2. We can find in Max Weber's assertion that capitalism and increasing "formal rationality" go together. David Trubel[7] tells us that:

a. Weber argues that only a truly formal system of law can be calculable.

b. Substantive ends lead to particularistic decisions. Such decisions make it difficult for people to know in advance the outcome of legal questions.

(1) Formal justice, thus, enhances individual opportunities, promotes self-determination and helps ensure individual freedom.

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7 David M. Trubek, Reconstructing Max Weber's Sociology of Law, 37 Stanford Law Review 919 (1985). See, also, David M. Trubk, Max Weber's Tragic Modernism and the Study of Law in Society, 20 Law & Society Review 573 (1986).

(2) Perhaps paradoxically, Weber also argued that formal thought in law may actually defeat the intent of transacting parties, benefit those with power and wealth, and, in fact, may be an impossible ideal to carry out.

III. How well does this classic model of the role of contract law fit an empirical picture of contract in the United States and elsewhere? It certainly is an overstatement.[8]

A. The North American story offers a complex picture.

1. Sometimes the classical model tracks well with an empirical picture.

a. Business people do engage in elaborate planning, and the contract is a blueprint for their performance.

(1) They do what they've agreed to do, no more and no less.

(2) Typically, these area lawyer-controlled transactions, involving such things as the sale of a major building or a business or the licensing of intellectual property.

b. When disputes arise, sometimes business people litigate to final judgment, the loser appeals, and we get an appellate opinion applying the Uniform Commercial Code or general principles of the common law contract.

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8 Roberto Mangabeira Unger in Lay in Modern Society: Toward a Critisism of Social Theory 12-13 (1976), remarks:

By tightening or relaxing the strictness of the premises, by making them more or less complex and therefore more or less faithful to the social reality we want to apprehend, we are able to control the balance between simplicity of expla nation and descriptive fidelity.

The more we lean toward the former (simplicity), the greater the danger that our inferences will fail to apply to any world in which we are actually interested. The more we tend to the latter (descriptive fidelity), the highter the risk that our conjectures will degenerate into a series of propositions so qualified an complicated that we are just as well off with our commonsense impressions. Whether simpicity or faithfulness to fact is emphasized will depend on the particu lar purpose for which we choose between them.

(1) Often these are *power imbalance* situations.

(a) The cases may involve franchises, big firm-small firm transactions for transactions involving a regulated industry that has little flexibility.

(b) The weaker seeks the power of the law to offset its lack of power in the market.

(2) Also there are *salvage situations* that result form disasters and situations on the edge of bankruptcy.

(a) Long-term continuing relationships now are over because it is likely that one of the parties will not continue in business.

(b) Sometimes these are but failed attempts to settle where bargaining positions hardened or there are suspicions of bad faith and fraud.

c. Indeed, during the last decade or two, our Wisconsin Business Disputes Project has found that there has been an increase in contracts litigation involving major corporations.

(1) The relational glue that held transactions together melted in the great economic dislocations of the past few decades.

(2) Today many economic transactions involve great sums of money, and so the potential results of litigation can look worth its high costs.

2. Sometimes, instead of pure contract law, transactions rest on *legally guaranteed security interests.*

a. If, for example, an airlines fails to pay for a Boeing 747, Boeing can take back the aircraft and sell it to another airline, all through legal procedures.

b) Of course, the value of repossessing goods is problematic—if the used aircraft market is soft, recovering a 747 may benefit Boeing very little; the threat of losing the use of the aircraft, however, may induce the airline to exert great efforts towards performing its obligations.

c. My colleague, the great legal historian Willard Hurst celebrates the role of lawyers in the 19th century as "social inventors".

(1) Lawyers "contrived or adapted institutions (the corporation), tools (the railroad equipment trust certificate), and patterns of action (the reorganization of corporate financial structure or the fashioning

(2) Hust views these social inventions as critical for the economic development of the United States.

(3) We can analyze such transactions in contract terms, but usually there are legal structures and prescribed forms and procedures as well as a simple agreement. Much more than contract is involved.

3. However, very often, the classical model is far from the reality of American business. This particularly true in transactions among manufacturing firms.

a. The practices.

(1) Business people do not plan in detail or they plan (often on standardized forms) and then they ignore the plan as they perform in accordance with engineering rather than legal standards.

(2) When attention is paid to formal planning and contract law, often the purpose is to ward off the results that would otherwise be imposed by law and turn obligations and performance back to informal means. Freedom of contract is freedom to have no contract!

(a) In the automobile industry, manufacturers usually deal with suppliers under **blanket order purchasing.**

i.This process features flexible quantities and often flexible pricing.

ii. It is an arrangement designed to be changed to track changes in the future.

(b) The key provisions make sure that the supplier has no legal rights against the manufacturer but that the supplier will be responsible for product liability claims brought by consumers.

(3) Parties work to avoid disputes or settle those that occur with reference to rights and the threat of court proceedings.

(a) Instead of rights, they talk of solving problems and seeing the other's position.

(b) Contracts are modified greatly during performance, but often any formal procedures for modification are ignored.

(4) Even when litigation is considered or used, there is great pressure to settle.

b. Explanations for these less-formal practices: (contract law is not needed, and its benefits often do not outweigh its very high costs).

(1) **Formal contract is not needed** because transactions rest on trust, power, the sanction system of long-term continuing relations or some blend of all of these factors.

(a) These are the very factors that de Soto finds holding together business transactions in the Peruvian informal sector.

(b) While he labels them as inefficient transaction costs, and prescribes formal contract law instead, North American business seems to disagree:

i. Arthur Okun, the economist, speaks of "auction" vs. "consumer" markets.[9]

ii. Economists like auction markets involving fungible goods, because here is where price competition brings all of the benefits

9 Arthur Okun, Prices and Quantities: A macroeconomic Analysis (1981). Okun says that consumer markets are often held together by an "invisible handshake"

promised by their theories. If I can fly either American or United Airlines from Chicago to New York, I'll pick the one with the lower fare, all other things being equal.

iii. Consumer markets come where goods are not standardized; where running changes may be needed; where it is hard to find substitutes quickly if anything should go wrong; or where continuing service will be needed to keep machinery operating.

—These are characteristics of much sophisticated production today.
—Here is where we find trust reinforced by relational sanctions.

(2) The cost of contract litigation outweigh its potential benefits in many transactions.

(a) One type of cost is what the German sociologist, Nicklas Luhmann calls crossing "thematization thresholds."[10]

i. If one talks in terms of trust and cooperation, he will prompt a response based on compromise.

ii If one talks legal rights, he is asking for a fight. There is a law of physics: "lawyers attract lawyers!"

(b) The benefits of American contract law seldom outweigh its high tangible financial costs:

1. Contracts litigation is an expensive game of chance. Many potential litigants must conclude that they cannot afford to roll the dice. **When others fail to perform promises, aggrieved parties cannot be sure that they will win a contracts lawsuit.** Contract law is not predictable and certain; it is not formally rational in a Weberian sense.

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10 Niklas Luhmann, Communication About Law in Interaction Systems, in K. Knorr-Cetina and A.V. Circourel, de., Advances in Social Theory and Methodology (1981). Luhmann says "It takes a certain amount of courage to openly confront the other with the question of whether he is actuallly in the right. The comfortable consensus that can normally be assumed in linving and acting together will be shattered".

a. American law often states contracts doctrine in hard-to-apply **qualitative** standards. (In Weber's terms, it is "substantively rational").

(1) For example, it asks has there been a "material failure of performance"?

(2) Has the other party "substantially performed"?

(3) Has his response to the defaulting party's problems "waived" exact performance?

(4) Was the default excused because it was caused by "the occurrence of a contingency, the nonoccurrence of which was a basic assumption of the contract"?

b. **Competing rules** generate uncertainty. American contracts doctrine often produces on rule almost matched by a counterrule.

c. Also, contract litigation often turns on hard-to-prove facts. Justifiable expectations may be dashed on the burden of proof, the parol evidence rule or the statute of frauds.

d. Furthermore, clauses commonly buried in form contracts may block legal protection of actual expectations. (In theory, this is a matter of free choice; in practice, such provisions enter the contract by subterfuge).

(1) Seller's forms usually disclaim all consequential damages, limit buyer's remedies to replacement and repair, and excuse performance when it becomes difficult because of any event listed on a long menu of contingencies.

(2) Buyers' forms may allow them to cancel-contracts-for-convenience, paying only the seller's actual out-of-pocket costs of performance.

(3) Sometimes courts will allow plaintiffs to avoid such clauses. However, at a minimum, such clauses increase uncertainty and add to the costs of writing briefs and arguing to avoid summary judgment.

3. Moreover, we know that usually the courts will not put aggrieved parties in the position they would have been in had their contracts been performed—**even when they win their lawsuit**. American contract law is a misrepresented product.

a. The primary remedy will be damages.

(1) American courts order people to perform promises only in certain types of case such as real estate transactions. (That is, specific performance is rare).

(2) Damages calculated in a monetary equivalent to performance is the ordinary remedy.

(3) However, other policies limit damages in American law.

(a) Contract damages must be foreseeable and proved with reasonable certainty.

(b) Often it is hard to satisfy these rules.

(c) This means that courts often will not protect all of a person's reasonable expectations.

b. A successful plaintiff may get an award of expectation damages, **but she must deduct the costs of winning the suit from her ultimate recovery**.

(1) Absent statutes to the contrary, successful plaintiffs in the American system must pay their own lawyers' fees and hourly fees are very high.

(2) Contingent fees may be used in the U.S., but they may take from thirty to sixty percent of a recovery or even more in some cases.

(3) The cost awarded to a victorious plaintiff may not include the full amount of the experts' fees necessary to make a case and prove damages.

(4) We award interest on judgments to compensate for loss of the use of the funds, but the statutory amount often fails to reflect the market rates when the plaintiff recovers a judgment.

4. We also must remember that people fail to perform contracts because they are broke.

a. Filing or winning a contracts action may lead to the defendant's bankruptcy rather than to satisfaction of a judgment based on the expectation interest.

b. The risk of bankruptcy can become a bargaining tool for the weaker party; its creditor risks ending the business if it asserts its full claim in a legal action and this may mean that it will recover only a fraction of what it is owed.

5. All of these factors together prompt may aggrieved parties to swallow their losses and do no more than refuse to deal with the breaching party again.

6. Other aggrieved parties give up claims in exchange for negotiated settlements at lower amounts.

B. Stories elsewhere:

1. Studies in Great Britain,[11] France[12] and several Scandinavian countries[13]find similar patterns of the use and nonuse of contract law.

2. The **Asian experience** seems very different from our classical

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11 See Hugh Beale and Anthony Dugdale, Contracts Between Businessmen, 2 British Jounal of Law & Society 45 (1975).

12 See Edward H. Lorenz, Flexible Production Systems and the Social Construction of Trust, 21 Politics & Society 307 (1993)

13 See Britt-Mari Blegvad, Commercial Relations, Contract, and Litigation in Denmark: A discussion of Macaulay's Theories, 24 Law & Society Review 397 (1990).

model, and we must remind ourselves of the highly developed successful Asian economics when we claim too much for conventional notions of the functions of contract law. Here we find a number of features at least analogous to those found by de Soto in the Peruvian informal sector.

a. Business contracts turn on trust based on dealing with an extended family and long-term continuing relationships.[14]

b. A written contract is but a starting point for negotiations at best; you must consider the interests of your trading partner and share benefits and burdens; you don't assert rights, although you may assert power, if you do it the right way.

c. The Japanese pattern of business influenced, if not controlled, by a government bureaucracy.

d. Okke Braadbaart, after studying vegetable marketing in Java, points out: "Personal relationships often develop between

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14 Compare De Soto, The Other Path 163-165 (1989) where he argues that such relational sanctions and trust are high cost and inadequate for modern development. Perhaps the Peruvian and the, say, Taiwanese situations describe by Winn, supra, note 2, differ. Nonetheless, we can point to remarkable economic success that rests on just the mechanisms that de Soto finds inefficient and inadequate.
For studies about squatter settlements in Hong Kong that describe similar practices but offer a very different analysis from that of de Soto, see Alan Smart, The Informal Regulation of Illegal Economic Activities: Comparisons between the Squatter Property Market and Organized Crime, 16 International Journal of the Sociology of Law 91 (1988); Alan Smart, Invisible Real Estate: Investigations into the Squatter Property Market, 10 International Journal of Urban and Regional Research 29 (1986); Alan Smart, The Squatter property Market in Hong Kong, 5 Critique of Anthropology 23 (1985).
The classic stydy of a squatter settlement and its production of other-than-state law is, of course, Boaventura de Sousa Santos, The Law of the Oppressed: The Construction and Reproduction of Legality in Pasargada, 12 Law & Society Review 5 (1977).

representatives of firms cooperating closely over a longer period. These ties are of strategic value in recurrent crisis management."[15]

C. Look at the areas of the world where there is little or no functioning formal rationality standing behind transactions.

1. Consider international trade in areas controlled by no national legal system.

a. Sometimes this rests on a private arbitration system.

b. However, even when there is no state law and no arbitration possible, if the potential gains area great enough, firms do invest and produce.

c. In some areas, lawyers and others work to build "self-enforcing" structures that substitute for legal enforcement of contracts. In Erich Schanze's words: "the theory of self-enforcement implies that in the course of the anticipated project life, breach by one party will be prevented by the fact that in any stage of the investment process the ongoing, 'working relationship' makes the parties to the agreement better off than breaching."[16]

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15 Okke Braadbaart, Business Contracts in Javanese Vegetable Marketing, 53 Human Organization 143, 144 (1994).

16 Erich Schanze, Regulation by Consensus: The Practice of International Investment Agreements, 144 Journal of Institutional and Theoretical Economics (JITE) 152, 166 (1988). See, also, Erich Schanze, Constructive Jurispru dence in Mining Agreements: Institutional Innovation and Practical Drawbacks, in Gunther Jaenicke, Christian Kirchner, Hans-Joachim Mertens, Eckard Rehbinder, and Erich Schanze, eds., International Mining Investmen: Legal and Economic Perspectives 161 (1988); Terence Daintith, Mining Agreements as Regulatory Schemes, in the same book; Terence Daintith, The Design and Performance of Long-Term Contracts, in Terence Daintith and Gunther Teubner, eds., Contract and Organisation: Legal Analysis in the Light of Economic and Social Theory 164 (1986); Wolfgang Streek and Philippe G. Schmitter, Community, Market, Statate—and Associations? The Prospective Contribution of Interest Governance to Social Order, I European Sociological Review 119(1985).

2. Western businesses have invaded the former Soviet Union.

a. My colleague, Dr. Kathryn Hendley, is here and will tell us about this laboratory wherein many theories about the relationships between law and the economy are being tested.

b. My point is only that a market economy is developing despite the absence of a formal law of contract that is in place and working.

(1) Indeed, in 1992, the New York Times ran an article with the title: "The Art of a Russian Deal: Ad-Libbing Contract Law".[17]

(2) Deals turn on mutual benefit and trust. If they break down, the attitude is "we've made money in the interim, and if the deal stops, O.K." "We'll dance together until the music stops."

(3) Instead of state contract law, business people privatize law enforcement and pay off what the Russians call their "mafia" or hire private guards for protection.[18]

V. What is needed for a free market system to work? We can identify two important factors: Business needs what Karl Llewellyn called "reckonability" (not complete certainty, and not the power to go to the limit of legal behavior) plus **trust.** A combination of factors produces sufficient reckonability and security.

A. Note the trust inherent in all levels of business transactions in the U.S., which usually works through reputational sanctions, cultural norms about performing one's promises,[19] or a combination of these factors.

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17 Louis Uchitelle, The Art of a Russian Deal: Ad-Libbing Contract Law, N.Y. Times, Jan. 17, 1992, at AI, cols 3-4.

18 Michael Specter, U.S. Business and the Russian Mob: Some Hire Guards: Others Tougth It Out, N:Y: Times, July 8, 1994, at Cl, cols 3-5.

19 cf. Edward H.Lorenz, Flexible Production Systems and the Social Construction of Trust, 21 Politics & Society 307 (1993).

B. There are ways of handling those situations where promises might not be performed.

1. Catalog selling through credit cards. (Bad debts are expected and discounted).

2. Certain types of transactions run by a relatively effective property security system.

3. Firms can offer hostages: one buys stock in the other, with, perhaps, a seat on the board of directors or one firm builds a factory next to the factory of its major supplier. Default on a contract is thus given very high costs.

4. Contract litigation exists at the margins of this process.

C. Our Business Disputes Project found that businesses were litigating contracts increasingly over the past few decades.

1. However, when studied the auto industry we discovered that their experience with contract litigation prompted them to work hard to build structures to avoid it.

2. Private firms offering dispute resolution services have grown as have other forms of alternative dispute resolution.

VI. What is the contribution of contract law to a degree of reckonability and trust. (Elegant Models!)

A. It may symbolize that there should be a very good excuse or *pacta sunt servanda.*

1. Taken as a whole, statute and case law yields this message:

a. Contract law reinforces norms that exist in business culture about perfor ming promises.

b. It also suggests that there are excuses, but simple mistakes are not enough.

2. However, we can ask how these messages are *communicated* to the relevant *audience.*

a. **Lawyers** read these messages in cases and statutes.

b. But how does the law's stories get to the broader society or to those who make and perform contracts?

B. Perhaps it is enough that to business people contract litigation symbolizes trouble, negative publicity, turning matters over to lawyers and losing con trol as well as diversion from profitable and enjoyable activities. "The hassle factor".

1. Business people may not need to know very much in detail about the law or the contract litigation system. (In some measure, perhaps the negati ve views of lawyers, held by so many, helps deter some from breaching contracts or crossing Luhmann's "thematization threshold" and talking rights instead of sweet cooperation.)

2. Udo Reifner suggests: "Law in market societies is a useful lie because economy needs to reduce complexity in order to be able to give ans wers where they are needed.[20] It may be enough that people **think** that they know what a court would do even when their lawyers would see doubts and questions.

C. Contract law may provide a vocabulary for negotiation—asserting an excuse vs. in your face.

1. One who asserts a plausible excuse may be less morally suspect than one who refuses to perform because it now is in his self-interest.

2. Conflicting claims of right at least open the possibility for some

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20 Udo Reifner, The Vikings and the Romans—Contract Law and Social economy 5 (Paper presented at the Conference on Perspectives of Critical Contract Law in Tuusula, Finland, May 7 to 10, 1992.

middle ground as contrasted with an expression of pure power and rejection of the interests of a trading partner.

VII. So What? (This is the first song on Miles Davis' classic album *King of Blue*; speakers should remember it!) What do we gain by an empirical picture of the contract system in action?

A. Are theories useful tools or are they ideologies in the service of power?

1. We might want to improve the cost/benefit ratio involved in the contract system if we wanted to make it easier to litigate and gain a declaration of rights plus adequate legal remedies.

a. Instead of taking this as a blanket overall policy, we might want to focus on those situations where a market economy really needs formal legal contracts which are readily enforceable.

b. If we try to seek formality and full enforceability too broadly, we may find that we will need broader laws of excuse and bankruptcy or we may be wasting effort to provide tools that never will be used.

2. We might, to the contrary, seek to recognize and legitimate compromise as the goal of the legal system and devise procedures to attain such ends.

a. Perhaps high cost barriers and uncertain payoffs are part of the best of all possible systems. (This is the Dr. Pangloss position!)

(1) People will litigate only important cases involving significant sums of money where there is a need for an authoritative declaration of rights.

(2) Otherwise people are given strong incentives to share losses, consider the interests of the other side, and work out solutions involving future business dealings.

b. To a large extent, this is the situation in international business

transactions, and its success should caution us about claiming too much for contract doctrine and litigation.

c. Of course, insofar as we see contract law as helping to empower the weak, we will be unhappy with bargaining in the shadow of the law.

(1) The Pangloss position rests on acceptance of the power positions of the parties; by definition, settlements do not bring the powerful to their knees.

(2) We might want to carve out special areas, as we have in my state, where we have different rules—we have an elaborate consumer protection and franchise legislation designed to give these weaker parties more bargaining power.

3. In the limited subset of cases where rights realization is important, we may want to create and perfect structures that will offer predictability and greater chances of gaining performance.

a. We can decide openly how far contracting should rest on anything that might be called choice and how far private govts should be able to impose liability in the guise of contract.

b. We can move from a rather simple correlation between Weberian formal rationality and market economics, to questions about how to gain trust and sufficient, but not total, security of transactions.

B. We should be able to ask about reform in the service of what interests? And we can face the transition costs of reform.

C. A modern economy can exist despite a substantively rational contract law. Perhaps we can remember that Shakespeare, in the Merchant of Venice, had Portia find a way not to give Shylock his pound of flesh.

1. In form, she just enforced the contract; in substance, Shylock was tricked and did not get the benefit of his bargain because of her sophistry. Others probably were deterred from claiming a

pound of flesh or, perhaps, they provided in their contracts that they could take all the necessary blood as well.

2. Shakespeare, however, never tells us whether Portia´s attack on the rule of law injured the economy of Venice. Somehow, I suspect that it did not.