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Unity and Pluralism in Contract Law

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CONTRACT THEORY. By *Stephen A. Smith.* New York: Oxford University Press. 2004. Pp. xxvi, 450. $35.

I. INTRODUCTION

It is a cliché of contemporary legal scholarship that, in the last few decades, the study of law has witnessed a vast proliferation of competing theoretical approaches. The old faith in the careful honing of doctrinal concepts and the essential usefulness of legal analysis has given way to a cacophony of competing theoretical sects.[1] Economists, moral philosophers, sociologists, historians, and others have stepped forward to offer the insights of this or that discipline as a new and superior path to legal enlightenment. Perhaps nowhere has this cliché been truer than in the realm of contracts scholarship, where, for a generation, the competing disciplinary approaches have been energetically proselytizing for their chosen theories. Hence, modern legal scholarship abounds with economic, philosophical, and sociological theories of contract law.

Most contracts scholars take one of two basic approaches. On one side stand those who, while acknowledging the usefulness of the new theoretical tools, remain unconverted to any of them. With lawyerly pragmatism, they remain skeptical of unifying theoretical enterprises. Human experience and the law are too complex for academic reductionism, they argue, and "a good gray compromise" of competing principles and policies[2] is the best that we can hope for. On

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1. *See generally* Richard A. Posner, *The Decline of Law as an Autonomous Discipline: 1962-1987*, 100 HARV. L. REV. 761 (1987) (chronicling the rise of interdisciplinary approaches to legal scholarship and the decline of doctrinalism).

2. *See* Jean Braucher, *Contract Versus Contractarianism: The Regulatory Role of Contract Law*, 47 WASH. & LEE L. REV. 697, 701 n.14 (1990).

the other side are those who declare that "theory works."[3] The problem with pragmatism, they assert, is that ultimately it fails to provide either illumination or concrete conclusions. We are left with little more than a series of ad hoc ipse dixits lacking coherence or justification. In contrast, rigorous theory of one sort or another offers the promise of real understanding. Obviously, both portraits are overdrawn, and individual scholars fall at different points along the spectrum between them. Nevertheless, the tension between pragmatism and theory explicitly or implicitly pervades much of contemporary contracts scholarship.

Into this discussion comes *Contract Theory* by Stephen A. Smith.[4] Published as part of Oxford University Press's Clarendon Law Series, Smith's book, despite its aggressively boring title, is a fascinating and important contribution to the current debates. Part textbook and part original analysis, Smith surveys most of the prominent contemporary theories of contract law and ultimately offers a detailed argument in favor of a unified theory built around the moral force of promising.[5] Smith is a legal philosopher by training, and he has a philosopher's faith in theory. Hence, *Contract Theory* squarely challenges the pragmatic approach to contract law. Smith admits that "[i]n the end . . . because there is little consensus as to the best theory of contract, studying contract theory mainly entails learning about competing theories" (p. viii). Nevertheless, he clearly believes one may hope for greater unity and precision than "a good gray compromise," and one of *Contract Theory*'s contributions is Smith's sustained discussion and defense of a set of criteria for winnowing out defective theories.

Ultimately, however, Smith's laudable desire for theoretical rigor ignores the possibility the pragmatic approach to contract law suggests: a principled reconciliation of competing approaches. Smith argues for an essentially unified theory. He seeks to defend his promissory approach by arguing for the wholesale rejection of competing alternatives, most notably reliance and efficiency theories. The "good gray compromise" school of thought, however, acknowledges that such outright dismissals are problematic. Most people have powerful intuitions that autonomy, efficiency, and corrective justice should all play important roles in our understanding of contract law. "Theory works" partisans rightly respond that such intuitions, by themselves, fail to provide us any way to coherently

3. *See* ROBERT E. SCOTT & JODY S. KRAUS, CONTRACT LAW AND THEORY (3d ed. 2004).

4. Professor of Law, McGill University.

5. Briefly stated, this is the theory that certain promises to perform some action create a moral obligation to act, for the breach of which the law should provide a remedy.

integrate those competing values. Smith's work graphically illustrates this quandary. His quest for theoretical unity leads him to make a series of problematic arguments dismissing efficiency theories. Indeed, in his drive to ground contract law in a single normative principle, he comes to the startling conclusion that many of what we think of as the core rules of the subject — such as those governing breach and damages — are not actually part of contract law at all. The difficulties Smith faces suggest that, rather than trying to unite all of contract law under a single normative principle, theorists should turn their attention toward providing a principled way of integrating competing approaches to contract in a single theory. As an example, I will present my strategy for reconciling the values of autonomy and efficiency into a single theory, while neither dismissing one approach nor falling into the trap of making ad hoc choices between them.

This Review proceeds as follows. I begin, in Part II by placing Smith's book in the context of the contemporary scholarly literature on contracts and detailing some of its main contributions. Next, in Part III, I turn to Smith's attempt to offer a theoretically unified view of contract law, outlining the arguments he uses to establish this unity and explaining why they are ultimately unpersuasive. Finally, in Part IV, I suggest that, in place of theoretical unity, contracts theorists should turn their attention to the possibility of a "principled pluralism" and put forward a set of arguments suggesting how this might be accomplished.

II. *CONTRACT THEORY* AND THE PRESENT SITUATION

The past three decades have seen a succession of ambitious books on the theory of contract law. Patrick Atiyah's magisterial *The Rise and Fall of Freedom of Contract* told a story of common law judges who labored, in vain, to construct a theory of contract law organized solely around the idea of party autonomy.[6] Grant Gilmore told a pithier, American version of this same tale in *The Death of Contract*, where he suggested that contract's days were numbered and it would soon subside into tort, which Gilmore insisted was the residual form of civil liability.[7] In response to these attacks, Charles Fried penned *Contract as Promise*, which insisted that a consistent theory of contract based on party autonomy is possible and provides the best interpretation of legal doctrine.[8] More recently, Michael Trebilcock has written *The Limits of Freedom of Contract*, which surveyed a

6. P.S. ATIYAH, THE RISE AND FALL OF FREEDOM OF CONTRACT (1979).

7. *See* GRANT GILMORE, THE DEATH OF CONTRACT (1974).

8. CHARLES FRIED, CONTRACT AS PROMISE (1981).

variety of problems in contract law and brought to bear the insights of twenty years of industrious law and economics scholarship.[9]

Smith's work is the latest volume in this conversation. Unlike the others, Smith sets out to provide a more or less comprehensive survey of contract theory. He is mainly successful, although his performance is not without faults. His treatment of economic theories is ultimately unpersuasive. In addition, there are some rather unaccountable absences in the book. For instance, Smith pays virtually no attention to the work of James Gordley and others seeking to articulate a neo-Aristotelian theory of contract.[10] Still, a student or scholar looking for a compendium of recent work on the philosophy of contract law is not likely to find a more detailed overview than *Contract Theory*. It is, however, much more than a mere summary of contemporary contract scholarship. It also offers a spirited defense of a much maligned theory in American jurisprudence: contract as promise.

Promissory theories of contract have not been popular in American scholarship. Under the influence first of Lon Fuller[11] and later of Grant Gilmore,[12] many American scholars have found reliance to be a more attractive basis than promise for explaining and justifying contract law. The promissory theory has been associated with the discredited "classical" view of contract, and for many scholars there is something suspiciously Willistonian about it. On this view, it is a theoretical mirage from which Corbin and section ninety of the *Restatement* have delivered legal thought. It is not without its partisans, most prominently Charles Fried.[13] Yet Fried's theory has gained few followers and even theorists that share the libertarian sensibilities behind *Contract as Promise* have criticized it.[14] Smith, on the other hand, concludes that a promissory theory provides the best

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9. MICHAEL S. TREBILCOCK, THE LIMITS OF FREEDOM OF CONTRACT (1993). See also JAMES GORDLEY, THE PHILOSOPHICAL ORIGINS OF MODERN CONTRACT DOCTRINE (1991), and ROBERT A. HILLAM, THE RICHNESS OF CONTRACT LAW (1997); both also deserve honorable mention.

10. *See* GORDLEY, *supra* note 9 (setting forth Gordley's argument that modern contract doctrine is best understood using the theories of late-scholastic philosophers); *see also* James Bernard Murphy, *Equality in Exchange*, 47 AM. J. JURIS. 85 (2002) (arguing for an Aristotelian theory of contract law). Smith does discuss Gordley's work in a single footnote in which he says: "[W]hile I cannot defend the claim here, it is suggested that insofar as Gordley's theory is meant to provide a positive justification for contractual obligations (rather than only a reason for *limiting* their scope), it disaggregates into a mixture of utilitarian and rights-based justifications." P. 52 n.16.

11. *See* L.L. Fuller & William R. Perdue, *The Reliance Interest in Contract Damages*, 46 YALE L.J. 52 (1936).

12. *See* GILMORE, *supra* note 7.

13. *See* FRIED, *supra* note 8.

14. *See* Randy E. Barnett, *Some Problems With Contract as Promise*, 77 CORNELL L. REV. 1022 (1992).

account of contract law. He thus offers a useful restatement and deepening of the argument in favor of contract as promise.

According to Smith, the most telling normative objection to promissory theories rests on the harm principle. Famously formulated by John Stuart Mill, the harm principle states that in a liberal society, the machinery of the state can be legitimately used to prevent harm to others but should not be used to enforce moral obligations whose violation do not result in harm.[15] Most promissory theories conceptualize promise breaking as an immoral act. The harm principle, however, suggests that the immorality of promise breaking is not a sufficient reason to mandate government enforcement of that promise. Smith's solution to this problem is what he calls an intrinsic view of promising (p. 74). Promises, he asserts, are intrinsically valuable because they create a special relationship between the promisor and the promisee. Promise breaking harms this special relationship by taking something intrinsically valuable to the promisee (the promise) and destroying it.[16] The advantage of such a view is that it transforms contract law from a species of mere morality enforcement into the forestalling of harm to another. Thus the harm principle is neatly sidestepped and can actually be invoked as a reason for enforcing promises.

Much of *Contract Theory* is taken up with a detailed application of various theories to different doctrinal areas.[17] He admits there are some areas where promissory theories offer only an incomplete and, in some sense, unsatisfactory account of the law.[18] He nevertheless concludes that his modified promissory theory offers the best interpretation of contract law. Hence, Smith's contribution to promissory theory is twofold: First, he offers a subtle new argument about promising that purports to avoid a key objection that has dogged such theories in the past. Second, he examines the application

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15. *See* JOHN STUART MILL, ON LIBERTY (1859).

16. In stark contrast to Smith's theory, Dori Kimel has recently argued that the legal enforcement of promises has precisely the opposite effect to the one posited by Smith. According to Kimel, legal enforcement actually undermines the trust that makes promising a valuable activity. *See* Dori Kimel, *Neutrality, Autonomy, and Freedom of Contract*, 21 OXFORD J. LEGAL STUD. 473 (2001); *see also* Anthony J. Bellia, Jr., *Promises, Trust, and Contract Law*, 47 AM. J. JURIS. 25 (2002) (responding to Kimel's arguments).

17. *See* pp. 167-208 ("Establishing Agreement: The Law of Offer and Acceptance"); pp. 209-244 ("The Kinds of Agreements that are Enforced: Formalities, Intention to Create Legal Relations, Consideration, and Estoppel"); pp. 245-268 ("The Kinds of Agreements not Enforced: Substantive Limitations on Enforceability"); pp. 269-314 ("The Content of the Contract: Interpreting and Implying Terms"); pp. 315-375 ("Excuses for Non-performance: Duress, Unconscionability, Mistake, Misrepresentation, Frustration, and Discharge for Breach"); pp. 376-386 ("Breach of Contract: The Puzzle of Strict Liability"); pp. 387-431 ("Remedies for Breach").

18. *See infra* Part III.C.3 (discussing Smith's admission that the concept of promising cannot account for certain doctrinal areas).

of promissory theories across a greater range of doctrinal topics and in greater depth than any prior legal philosopher.

III. UNIFYING CONTRACT LAW

The theoretical heart of *Contract Theory*, however, does not lie in its usefulness as a survey or as a restatement of the promise theory. Indeed, Smith's defense of promise rests less on his arguments about the function and importance of promising than on his approach to dealing with theories. The core of Smith's argument is a set of criteria for judging between competing theories of contract. These criteria offer an intriguing framework for dealing with the central issue in the philosophy of contract law: the brute fact of theoretical pluralism.

Contract theory suffers from an embarrassment of riches. Roughly speaking there are two main camps, one of which contains two significant subcamps. On one side sit the economic theories, which not surprisingly argue that contract law should be guided by notions of efficiency and welfare maximization. On the other side sit what Smith labels "rights-based" theories. These come in essentially two different flavors: those that see contract as properly focusing on compensating parties who detrimentally relied on the promises of others, and those that see contract as properly focusing on promising itself as an independent source of legal obligation.[19] Both the reliance and promissory theories (also called "autonomy theories") share an essentially ex post perspective. They both see contract law primarily as a way of compensating a disappointed promisee for harm to some entitlement. Their disagreement lies in how they account for the genesis and scope of the promisee's protected interest. Both, however, share the basic paradigm of corrective justice. In contrast, efficiency theorists take an essentially ex ante approach. Rather than focusing on the problems of entitlement and compensation, they look to the incentives that contract rules create for rational actors and then argue that we should adopt rules that generate economically efficient outcomes. The problem lies in the apparent incommensurability of these two approaches. Jody Kraus aptly summarizes the issue, writing:

> As normative theories, economic contract theories would seem to be logically incompatible with autonomy contract theories for the same reason that consequentialist moral theories are logically incompatible with deontological moral theories: The former claim that moral

19. One could also add so-called transfer theories, which conceptualize contracts as the voluntary alienation of rights. *See, e.g.*, Randy E. Barnett, *A Consent Theory of Contracts*, 86 COLUM. L. REV. 269 (1986); Peter Benson, *The Unity of Contract Law*, *in* THE THEORY OF CONTRACT LAW 118 (Peter Benson ed., 2001). Smith discusses these theories at some length, but ultimately dismisses them as unpersuasive because of their inability to explain how future performance can be explained in terms of a right held in the present. *See generally* pp. 97-103.

> justification is solely a function of consequences, while the latter claim that moral justification is independent of moral consequences.[20]

Without some way of choosing between these theories or otherwise reconciling them, contract theory is deeply incoherent. It lacks the ability to generate consistent normative or descriptive theories of the law.[21]

A. *A Theory About Theories*

The philosophy of contract law thus faces a thorny problem of normative pluralism. How are we to choose between competing approaches? To his credit, Smith tackles this problem head on. The first forty pages of *Contract Theory* consists of a careful elaboration of criteria for choosing between competing approaches. Smith takes an essentially interpretivist approach to the question. The purpose of contract theory, on this view, is not to provide us first with an ideal normative framework and only then offer concrete rules of law that flow from that framework. Rather, one takes contract law as it currently exists and seeks an explanation that renders it as coherent and intelligible as possible. According to Smith, this internal approach generates four concrete criteria by which to judge theories: fit, coherence, morality, and transparency. These criteria then form the heart of Smith's argument for rejecting efficiency theories of contract in favor of the rights-based approach.

1. *Fit and Coherence*

The concepts of fit and coherence are pretty straightforward. In order for a normative theory to make current law intelligible, it must generate concrete rules that more or less track current law. Suppose one was looking for a theory that rendered the Thirteenth Amendment's prohibition on slavery intelligible. Obviously, one could not use Aristotle's argument for the natural inferiority of some people and the justice of enslaving them to provide such a theory.[22] The legal rules Aristotle's theory suggest are simply too at odds with the rule set forth in the Thirteenth Amendment. By the same token, a theory that

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20. Jody Kraus, *Reconciling Autonomy and Efficiency in Contract Law: The Vertical Integration Strategy*, 11 PHIL. ISSUES 420, 420 (2001); *see also* Kaimipono David Wenger & David A. Hoffman, *Nullificatory Juries*, 2003 WIS. L. REV. 1115, 1138 (2003) (discussing the conflict between economic and moral theories in the context of tort law).

21. By "descriptive theory," I do not mean sociological type descriptions of legal practice or even traditional doctrinal accounts of contract law. Rather, I am referring to the process of interpreting the practice of contract law and rendering it internally intelligible. Accordingly, in this context, "interpretive" serves as a synonym for "descriptive."

22. *See* ARISTOTLE, THE NICOMACHEAN ETHICS, Bk. VII; ARISTOTLE, THE POLITICS, Bk. I, ch. ii-vii.

implied that contract law ought to provide a cause of action only against those who maliciously breach their agreements is too wide of the current law to render it intelligible.[23] Coherence is even simpler. A theory that generates contradictory conclusions obviously suffers from a basic problem of consistency. Smith also suggests that consistency requires that a theory rendering a particular body of law intelligible must account for the fact it is thought of as a distinct body of law. "More specifically," he writes, "to explain why contract law merits the title 'contract law', a good theory must show that *most* of the core elements of contract law can be traced to, or are closely related to, a single principle" (p. 13).

2. *Morality*

Smith subscribes to Joseph Raz's claim that the concept of law, as an analytic matter, always consists of a claim to authority.[24] Part of what we mean when we use the term "law" is the idea that one has an obligation to obey the law. This authoritative aspect of law is part of what differentiates its commands from those of a highway robber. Hence, any theory of law must also be in some sense a moral theory. It must purport at least to explain why the law is authoritative. This does not require that it necessarily be a good moral theory. Smith differentiates three different versions of the morality criterion. Under a very weak version, the theory must simply make an identifiable moral claim, even if it is clearly incorrect. For example, the Nuremberg laws passed by the Third Reich rested on theories of racial superiority and the legitimacy of anti-Semitism that are analytically identifiable as moral claims even if those claims are not themselves morally defensible. A middling version of the criterion asserts that a legal theory must contain a moral theory that is both analytically identifiable as a moral claim and also within the range of reasonable moral positions, even if ultimately mistaken. Finally, the strongest version of the moral criterion requires that the moral component of a legal theory be ethically correct.

3. *Transparency*

The transparency criterion has to do with the sorts of arguments judges offer when they expound the law. The claim is that judicial

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23. *See* RESTATEMENT (SECOND) OF CONTRACTS § 252(2) (1979) ("When performance of a duty under contract is due, *any* non-performance is a breach." (emphasis added)).

24. *See, e.g.*, JOSEPH RAZ, ETHICS IN THE PUBLIC DOMAIN: ESSAYS IN THE MORALITY OF LAW AND POLITICS 199 (1994) ("I will assume that necessarily law, every legal system which is in force anywhere, has *de facto* authority. That entails that the law either claims that it possesses legitimate authority or is held to possess it, or both.").

opinions are part of the legal data to be rendered intelligible. According to Smith:

> The transparency criterion evaluates contract theories according to how well they account for what may be called the 'legal' or 'internal' explanation of contract law. . . . That law is understood from the inside as transparent is clear: law-makers, and in particular judges, give public reasons for acting as they do and those reasons are presented as their real reasons. The report of a legal decision is not mere window dressing; it is meant to explain why the plaintiff did or did not win. (pp. 24-25)

Hence, any successful theory must fit not only the rules in the common law of contracts but also the arguments judges use to justify their decisions under those rules. For example, if judges consistently claim that damage awards in contract cases exist to compensate successful plaintiffs for harms they have suffered, then a successful theory must account for the fact not only that the law awards damages but also for the fact that damages are conceptualized as compensation.

B. *Dismissing Efficiency Theories*

While Smith analyzes efficiency theories under all four criteria, the transparency criterion proves decisive in his effort to reject those theories. To be sure, he is quite sympathetic to the traditional anti-utilitarian arguments that have been marshaled as moral objections to efficiency as a normative criterion.[25] On the other hand, Smith concedes that for an interpretive theory, even ultimately valid moral objections may be irrelevant. In order to satisfy the morality criterion in its least demanding form, all that is necessary is that efficiency theories make identifiably normative claims, which they clearly do. Smith even seems willing to concede that efficiency theories are among those that could be endorsed by reasonable people. Only under the strong version of the moral criterion would efficiency theories, according to Smith, suffer from a serious moral objection (p. 132). Broadly speaking, he concludes that the fit objections to efficiency theories are not compelling because he believes that economic analysis is so indeterminate that one could construct plausible efficiency arguments in favor of most important rules of contract law (p. 125).

In contrast, Smith believes the transparency criterion provides a reason for rejecting efficiency theories regardless of one's opinion as to their moral defensibility or the strength of the analytic connection between law and morality. According to Smith, "arguably [the] most

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25. *See* pp. 127-32; *cf.* RONALD DWORKIN, *Is Wealth a Value*, *in* A MATTER OF PRINCIPLE 237 (1985) (arguing that wealth maximization is a normatively unattractive criterion for the law). For a more sophisticated set of arguments against efficiency norms than those offered by either Smith or Dworkin, see JULES COLEMAN, MARKETS, MORALS, AND THE LAW 67-153 (1998).

important objection to efficiency theories of contract law is that they regard contract law as non-transparent, as hiding its own foundations" (p. 132). Smith acknowledges that judges sometimes consider the effects their rulings will have, but insists this reasoning is inconsequential. Mainly, when judges and litigants make arguments in contract cases, he asserts, they do not claim that damages are necessary to deter future actors. Rather, they argue about what the parties are entitled to as a matter of justice. In other words, legal reasoning is always an ex post attempt to establish what rights litigants are entitled to, while economic reasoning is always an ex ante attempt to gauge future reactions to incentives created now. Accordingly, Smith concludes that "[t]here is virtually no point of contact . . . between the legal explanation and the efficiency based explanation" (p. 133). It is not that judges and lawyers employ less sophisticated versions of the arguments made by law and economics scholars. Rather, their arguments are of a fundamentally different kind.

This disjunction between legal arguments and economic arguments, according to Smith, leaves efficiency theorists still interested in offering an interpretive view of contract law with one of two untenable reactions to the transparency argument. First, they can argue that the arguments made by lawyers and judges are basically insincere, a mere screen that obfuscates the real reasons for their decisions. Smith dismisses this possibility by arguing that "to successfully explain a self-reflective human practice, such as the law, one of the things that must be explained — that must be made intelligible — is how that practice understands itself" (p. 134). Hence, the smoke-screen vision of legal reasoning fails as an interpretive theory precisely because it fails to offer any explanation of a key phenomenon. The second alternative for efficiency theorists, according to Smith, is to assert that the law pursues efficiency, without legal actors knowing about it, through some invisible-hand or evolutionary mechanism. The problem with this approach, according to Smith, is that it still fails to explain why legal actors choose to justify rules in the way they do. Furthermore, given the sophistication of judges and lawyers, Smith finds it implausible that they could be systematically mistaken about the nature of the enterprise in which they are engaged.

C. *The Failure of the Effort to Dismiss Efficiency Theories*

Economic theorists could respond to Smith's arguments in a number of ways. Some of them would no doubt simply brush aside the transparency objection as meaningless. They would argue that they are concerned with finding the optimal rules for contract law as it should be, rather than finding some interpretation of contract law as it is. In a sense, this response simply concedes Smith's point. These

theorists would agree with him that their theories are simply about different things. Even within the interpretive criteria that Smith sets up, however, it is by no means obvious that economic theories can be so easily dismissed. First, Smith's transparency argument conflates two aspects of ex post reasoning. Once these two aspects are untangled, the import of the ubiquitous ex post reasoning one sees in judicial opinions becomes less telling than Smith believes. Second, judicial reasoning is considerably less hostile to economic arguments than Smith suggests. Finally, rights-based theories underdetermine the content of certain rules that economic theories account for quite well. As a result of this problem, Smith is forced into making the rather implausible claim that certain well-established features of contract doctrine, such as the rule in *Hadley v. Baxendale*,[26] are not actually part of contract law at all.

1. *The Two Forms of Ex Post Reasoning*

Smith is correct to observe that much of judicial reasoning is backward looking and focuses on the question of who is entitled to what as a matter of pre-existing rights. It hardly follows from this fact, however, that the basis of the law is the enforcement of pre-existing moral rights. Judges are primarily concerned with determining the rights the law confers on particular parties. The source judges use to determine these rights is generally not some body of pre-existing moral entitlements, but rather the pre-existing body of law. When a judge rules that A has no good breach of contract claim against B because their agreement was not memorialized as the Statute of Frauds requires, she is making a statement about the contours of A and B's legal rights. She is not, however, necessarily making a statement about the moral foundations of the Statute of Frauds.

There is no reason that efficiency theorists must reject the notion that judges should decide cases according to pre-existing rules, nor do they question the basic belief that someone who holds a legal entitlement has a legal right to that entitlement. Economic theories of law are not attacks on the rule of law per se. Rather, they are explanations for why the law takes one shape rather than another. For example, one might argue that the expectation measure of damages should be chosen over the reliance measure because it provides proper incentives for disappointed parties to bring suits and for potential breachers to take the optimal level of precautions to avoid those suits. There is nothing about the ex ante shape of this argument, however, that precludes one from also affirming that the disappointed promisee of a breached contract has a legal right to her expectation damages. In

26. 156 Eng. Rep. 145 (Ex. 1854).

short, one may believe that ex ante arguments provide the best account for particular legal rules while also believing that ex post analysis should be used to determine whether a particular person has a particular entitlement under those rules.

Judicial decisions are mainly concerned more with the application of pre-existing law to concrete facts than with the application of normative theories to particular legal rules. Hence, it should not surprise us to find that most legal discussions center around arguments over the scope of pre-existing rights. That, after all, is what the parties to a lawsuit are litigating. It is important to remember, however, that these are pre-existing legal rights. It hardly follows from the fact that judges are mainly concerned with these pre-existing legal rights that that the law itself is best understood as enforcing pre-existing moral rights. The preponderance of judicial cases are not about the normative foundations of the law but about the application of the law — regardless of its normative foundations — to particular cases. This is what accounts for the preponderance of ex post arguments in the judicial opinions. Tellingly, when judges do discuss the normative foundations of the law, they use ex ante arguments with greater frequency than Smith suggests.

2. *The Transparency of Economic Reasoning*

It is simply not true that common law judges eschew the ex ante perspective as completely as Smith implies. For example, in criticizing the California Supreme Court's decision to adopt a "soft" version of the parol evidence rule,[27] Judge Alex Kozinski wrote:

> [The California Supreme Court's decision] casts a long shadow of uncertainty over all transactions negotiated and executed under the law of California. As this case illustrates, even when the transaction is very sizeable, even if it involves only sophisticated parties, even if it was negotiated with the aid of counsel, even if it results in contract language that is devoid of ambiguity, costly and protracted litigation cannot be avoided if one party has a strong enough motive for challenging the contract. While this rule creates much business for lawyers and an occasional windfall for clients, it leads only to frustration and delay for most litigants and clogs already overburdened courts.[28]

Note that Judge Kozinski's objections take an almost exclusively ex ante approach, resting on the incentives that the rule creates for litigation and the increased transaction costs it places on parties as they attempt vainly to bargain around it. This kind of argument is not confined to contemporary judges whose judicial opinions have been

27. *See* Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co., 442 P.2d 641 (Cal. 1969) (Traynor, J.).

28. Trident Ctr. v. Conn. Gen. Life Ins. Co., 847 F.2d 564, 569 (9th Cir. 1988).

somehow tainted by law and economics scholarship. Consider Judge Danaher's dissent in the famous case of *Williams v. Walker-Thomas Furniture Co.*[29] In that case, Judge Skelly Wright held that a cross-collateralization clause in a sales contract was potentially unconscionable because of unequal bargaining power. In his dissent, Judge Danaher reasoned:

> There are many aspects of public policy here involved. What is a luxury to some may seem an outright necessity to others. Is public oversight to be required for the expenditures of relief funds? A washing machine, e.g., in the hands of a relief client might become a fruitful source of income. Many relief clients may well need credit, and certain business establishments will take long chances on the sale of items, expecting their pricing policies will afford a degree of protection commensurate with the risk.[30]

Judge Danaher's defense of the traditional rule that courts will not examine the adequacy of consideration is based on explicitly ex ante reasoning. There is no discussion of the ex post rights of the defendant in the case, but rather an analysis of how the incentives the rule creates will impact the availability of credit and capital for the very poor.

Nor is such reasoning confined to recent judicial decisions. In 1854, Baron Alderson issued his opinion in the famous case of *Hadley v. Baxendale*.[31] The opinion stated a two-part rule governing consequential damages in breach of contract cases. The first part of the rule is that a plaintiff can recover only those damages that were reasonably foreseeable to the breaching promisor. The second part of the rule is that where the plaintiff has specifically communicated to the defendant that certain consequences will flow from a failure to perform, the defendant becomes liable for those consequences, even if they otherwise would not be reasonably foreseeable. Baron Alderson justified the rule thus:

> [I]f these special circumstances were wholly unknown to the party breaking the contract, he, at the most, could only be supposed to have had in his contemplation the amount of injury which would arise generally, and in the great multitude of cases not affected by any special circumstances, from such a breach of contract. For, had the special circumstances been known, the parties might have specially provided for the breach of contract by special terms as to the damages in that case; and of this advantage it would be very unjust to deprive them.[32]

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29. 350 F.2d 445 (D.C. Cir. 1965).

30. *Id.* at 450 (Danaher, J., dissenting).

31. 156 Eng. Rep. 145 (Ex. 1854).

32. *Id.* at 151.

Note that Baron Alderson's ex ante reasoning here is quite subtle. Simple efficiency theories of damages tend to focus on how to induce efficient performance and breach of obligations.[33] Baron Alderson, however, employs what Richard Craswell has called "second-generation efficiency," which asks what effect rules have on the contracts that are negotiated.[34] Thus, Baron Alderson justifies the specially communicated rule in terms of the incentives it creates for the parties at the time of negotiation. To be sure, some of the language of justice remains, but the argument nevertheless explicitly looks to the incentives to negotiate that the rule creates.

3. *Underdetermination and Line Drawing*

The rule in *Hadley v. Baxendale* illustrates the third problem with Smith's attempt to dismiss economic theories: the promissory theory he espouses underdetermines certain rules. Economic theorists can neatly explain the holding in the case in terms of incentives and information.[35] When parties enter a contract they have imperfect information about the other party's situation, which can result in inefficiencies. For example, it is efficient for the promisor to take any precaution to avoid breach of his promise that is less than the value of that promise to the promisee. At the time of contracting, however, the promisor may not know the value of the promise to the promisee. Indeed, during negotiations the promisee has incentives to conceal the true value of the potential promise in order to get a better price. As a result, the promisor may take inefficiently few precautions to avoid breach. As Baron Alderson suggested, however, limiting the promisee's damages to those that are reasonably foreseeable creates incentives for parties to negotiate around this problem. Because the promisee cannot recover damages for losses that are in effect invisible to the promisor at the time of breach, this rule gives the promisee an incentive to disclose this information when negotiating. Once the hidden information is communicated, the promisor has an incentive to take the efficient level of precautions to avoid breach because he will be liable for the full amount of the promisee's damages.

Although he does not address the economic justifications offered for the rule in *Hadley*, Smith is generally critical of economic theories of damages. His main objection is that no single rule can create

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33. *See, e.g.*, RICHARD POSNER, ECONOMIC ANALYSIS OF LAW 117-20 (4th ed. 1992) (discussing the theory of efficient breach).

34. *See* Richard Craswell, *Two Economic Theories of Enforcing Promises*, *in* THE THEORY OF CONTRACT LAW 19 (Peter Benson ed., 2002).

35. *See* Ian Ayers & Robert Gerner, *Filling the Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87, 101-04 (1989) (discussing the holding in *Hadley* as a penalty default rule).

efficient incentives for all parties to a contract. Hence, while expectation damages may create efficient incentives for parties choosing whether or not to breach their contracts, they create inefficient incentives for those choosing the extent to which they should rely on the promises of others.[36]

Smith himself, however, does not provide a satisfying account of the rule in *Hadley*. The rights-based approach, he argues, implies that contract damages are explainable in terms of corrective justice. "This explanation is consistent, in broad terms," he argues, "with the principle that victims of breach have a right to compensatory damages" (p. 412). Beyond this, however, Smith seems to deny that his account of contractual obligation has any concrete implications for damages rules. Rather, he argues that it is unnecessary for a theory of contract law to explain the remoteness rule in *Hadley* (or any other rule regarding contract damages). "[T]he answers [to these questions]," he argues, "will not tell us anything special about contractual obligations" (p. 427). He offers two reasons for why this is so.

Smith's first claim is that the rule in contract damages does not actually exist. Rather, he denies that there is any distinction between the foreseeability or remoteness rule applied in torts[37] and the rule applied in contracts, arguing that any apparent differences can be accounted for in terms of different factual circumstances (pp. 426-27). While he cites an English case in support of his position,[38] as a doctrinal matter his claim is at least doubtful.[39] Smith's doctrinal reformulation, however, is less important than his second reason.

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36. Pp. 410-11. Smith does not, however, deny that it is logically possible to come up with a socially efficient measure of damages. He simply believes that it is virtually impossible to identify it:

> [I]n theory it might well be that the expectation measure is produces the most efficient aggregate behavior (if it could be proved, say, that the breach decision overwhelms all others). But making the necessary calculation is complex to say the least. I doubt that such a calculation has or even could be attempted. As was true [for other economic issues] the relevant quantitative data is not available.

Id.

37. *See* Palsgraf v. Long Island R.R., 162 N.E. 99 (N.Y. 1928) (stating the remoteness rule in tort); *cf.* Hadley v. Baxendale, 156 Eng. Rep. 145 (Ex. 1854) (stating the remoteness rule in contract).

38. H Parson (Livestock) Ltd. v. Uttley Ingham & Co., 1978 All. E.R. 525 (C.A.), Q.B 791, *cited at* p. 427 n.54.

39. For example, it is a well established rule that generally speaking one cannot recover for emotional distress as a result of a breach of contract. *See, e.g.*, Rubin v. Matthews Internment Corp., 503 A.2d 694 (Me. 1986) (emotional distress damages generally not recoverable in contract); Moffet v. Kan. City Fire & Marine Ins. Co., 244 P.2d 228 (Kan. 1952) (same). In contrast, such damages are not too remote in the tort context. *See, e.g.*, Samms v. Eccles, 358 P.2d 344 (Utah 1961) (allowing recovery in tort for intentional infliction of emotional distress); Rubbish Collectors Ass'n v. Siliznoff, 240 P.2d 282 (Cal. 1952) (same).

Smith's second, and more philosophically interesting, justification for not accounting for the rule in *Hadley* is that it is not actually a rule of contract law at all and hence need not be explained by a complete theory of contract. Rather, he argues, "[t]he justification and meaning of remoteness is a general question for the law of obligations" (p. 427). Smith makes this move for at least two reasons. First, he argues, consistent with his view of promising as creating a uniquely valuable entitlement where none existed before, that the infringement of a contractual right through breach is analogous to a misappropriation of — or negligent damage to — property (p. 104). Just as these wrongs are not considered part of property law, Smith claims that "non-performance should not be regarded as part of contract law" (p. 104). Second, and more tellingly, he claims that "[a]s for remedial rules, the promissory account [of contract] has nothing special to say about how remedies for breach of contract should be classified."[40] This sort of shifting of the boundaries of contract law to save the promissory theory from embarrassment has been done before. Charles Fried, for example, denied that contract law had anything to do with those legal default rules whose content could not be determined by his promise principle.[41]

There is a *deus ex machina* quality to this argument. The fundamental problem is that Smith and Fried do not provide any arguments for defining the scope of contract law independent of the promise theory itself. Without such a theory-independent argument, a vicious circularity arises, with the theory of explanation being used to define what is to be explained and then citing its ability to explain this limited domain as evidence of the theory's success. To take an extreme example, it is as though one set out to explain the phenomena of "games," and first argued that "games" were those social interactions between two people over an eight-by-eight board with thirty-two pieces that conform to the rules of chess. Having made this move, the ability of the rules of chess to explain these particular social interactions would then be taken as evidence that the rules of chess constitute a successful theory of games!

IV. THE POSSIBILITY OF PRINCIPLED PLURALISM

The apparent failure of Smith's project of unification does not mean that we are left inevitably to "the good gray compromise of competing principles." It should, however, lead those who believe that "theory works" to re-examine an important insight provided by theory

40. P. 104; *cf.* Richard Craswell, *Contract Law, Default Rules, and the Philosophy of Promising*, 88 MICH. L. REV. 489 (1989).

41. *See* FRIED, *supra* note 8, at 69.

skeptics. The lure of pragmatism in contract law lies in the fact that most lawyers and judges have powerful intuitions that there are several legitimate values at stake in the law. Autonomy, welfare, and justice are all in play, and most people believe all of these things matter to some degree. If, as *Contract Theory* suggests, a unified theory resting on an exclusive commitment to a single normative principle is unlikely to succeed, theorists ought to turn their attention to whether it is possible to integrate these competing values in a principled way. Indeed, in the absence of a compelling unified theory, the alternative to a principled integration would be the perpetual exercise in ad hoc balancing that the "theory works" partisans wish to avoid. What follows sketches an approach to such a principled integration. Articulating a complete theory of contract law is beyond the scope of this Review. I do believe, however, that a successful theory will ultimately need to take the form of something like this: Contract law ought to be understood in terms of a two-tiered ordering of autonomy and efficiency. Both values ought to be pursued, but where they conflict, autonomy should act as a "trump" value.

A. *Contract Law and the Priority of Liberty*

John Rawls has argued that the first principle of justice is that "each person is to have an equal right to the most extensive scheme of equal basic liberties compatible with a similar scheme of liberties for others."[42] For Rawls, the principle of equal liberty enjoys priority over other concerns. Hence, while one may limit basic liberties in the name of liberty itself, one cannot limit basic liberties in order to secure other goals, such as distributive justice or increased levels of welfare. Rawls offers a variety of arguments for this privileged position for liberty,[43] many of which have been subject to criticism,[44] but the most compelling argument rests on the notion of self-determination.[45] Human beings in a liberal society have competing conceptions about what constitutes the ultimate good or where ultimate values lie. In ordering such a society, it follows that the most important concern should be to preserve the ability of people to choose and pursue a conception of the good. This is what the priority of liberty allows them to do. Its priority is justified precisely because it serves, in a sense, to

42. JOHN RAWLS, A THEORY OF JUSTICE 53 (rev. ed. 1999).

43. *See, e.g.*, *id.* at 130-39.

44. *See, e.g.*, Kenneth Arrow, *Some Ordinalist-Utilitarian Notes on Rawls' Theory of Justice*, 70 J. OF PHIL. 245 (1973); H.L.A. Hart, *Rawls on Liberty and Its Priority*, *in* READING RAWLS 230 (Norman Daniels ed., 1975).

45. My interpretation of Rawls' priority principle follows Robert S. Taylor, *Rawls's Defense of the Priority of Liberty: A Kantian Reconstruction*, 31 PHIL. & PUB. AFF. 246 (2003).

protect citizens' access to ultimate values by guaranteeing them a sphere in which to work out their own conceptions of the good.

This argument is useful for contract theory because it prioritizes liberty without necessarily committing itself to any outright hostility toward competing values. For example, it is still permissible to pursue increases in social welfare under this theory, so long as such pursuits do not threaten equal liberties. Hence, we seem to have at least an initially plausible reason for choosing efficiency in one sphere (those areas where liberty is not implicated) while placing emphasis on autonomy in another sphere (those areas where liberty conflicts with other concerns). The theory's value lies in its ability to provide principled reasons for using autonomy as a criterion some of the time and using efficiency at other times. This tracks the intuition at the heart of the pragmatic approach by acknowledging that apparently competing values both have legitimate claims. It does not commit us, however, to a "good gray compromise of competing values," but rather provides us reasons for consistently ordering those values.

Rawls, like most political philosophers, has little interest in private law and apparently even less knowledge of the intricate rules with which a legal theorist must cope. Hence, *A Theory of Justice* doesn't provide any concrete discussion of contract law other than to affirm that "freedom of contract as understood by the doctrine of laissez-faire [is] not [a] basic [liberty]."[46] There are no arguments as to why this is so, and one suspects that Rawls is simply eager to demonstrate that his concept of the priority of liberty is different from the more libertarian liberalism of the nineteenth century. As I shall argue below, however, this is an imaginary bogey man, as there is no a priori reason to believe that including freedom of contract in the catalog of basic liberties leads inevitably to the laissez-faire capitalism Rawls clearly rejects. Other than this unhelpful swipe at freedom of contract, it looks as though the Rawl's priority of liberty, despite its apparent theoretical usefulness, is at too high a level of abstraction to be jurisprudentially useful. As Charles Fried observed in a slightly different context:

> The picture I have . . . is of philosophy proposing an elaborate structure of arguments and considerations which descend from on high but stop some twenty feet above the ground. It is the peculiar task of law to complete this structure of ideals and values, to bring it down to earth; to complete it so that it is seated firmly and concretely and shelters real human beings against the storms of passion and conflict.[47]

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46. RAWLS, *supra* note 42, at 54.

47. Charles Fried, *The Artificial Reason of the Law or: What Lawyers Know*, 60 TEX. L. REV. 35, 57 (1981).

At this point what is needed is a concept that will act as a bridge from the abstraction of the priority of liberty to the "thickets of the law."[48]

Promissory theories are useful here because some share the same liberal assumptions as Rawls's argument. For example, Fried also envisions a society where citizens pursue differing visions of the good life. Indeed, what Fried calls the "first principle of liberal political morality" reads very much like Rawls's priority principle: "[W]hatever we accomplish and however that accomplishment is judged, morality requires that we respect the person and property of others, leaving them free to make their lives as we are left free to make ours. This is the liberal ideal."[49]

Promising is valuable precisely because it allows us to enlist the help of others in pursuing our vision of the good without impermissibly imposing our will on them. We can enlist their help because promising allows us to commit ourselves morally in ways that invite the trust and confidence of others. "To renege is to abuse a confidence he [i.e. the promisor] was free to invite or not, and which he intentionally did invite. To abuse that confidence now is like (but only *like*) lying: the abuse of a shared social institutions that is intended to invoke the bonds of trust."[50] Such an abuse, according to Fried, violates the liberal ideal. Obviously, the validity of this argument is controversial. It does, however, suggest that providing a remedy for the breach of a promise can be traced back to the priority of equal liberty. Such a remedy protects people from the violation of the rights that they gained when others promised to perform on their behalf. To do otherwise would be to allow a promisor to treat a promisee as a mere means to his own ends. It would deny in effect that the disappointed promisee is a being entitled to choose his own vision of the good free from the illegitimate manipulation of others.[51] Hence, promising provides a way of enlarging the scope of the freedom available to all, and contract law, which ultimately provides a remedy for the breach of promises, protects the rights created by that enlarged sphere of liberty.

I am not offering a brief for Fried's theory or other promissory theories. I find them ultimately unpersuasive for many of the same reasons I find Smith's theory unpersuasive. Fried's ambition is theoretical unity; therefore, he, like Smith, must deny the claims of competing approaches and stretch the concept of promising in implausible ways in order to account for much of contract doctrine.

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48. *See* ROBERT BOLT, A MAN FOR ALL SEASONS 67 (1962).

49. *See* FRIED, *supra* note 8, at 7.

50. *Id.* at 16.

51. *Cf.* IMMANUEL KANT, GROUNDING FOR THE METAPHYSICS OF MORALS 35 (James W. Ellington trans., Hackett Publ'g Co., 1981) (1785).

Fried is useful not because his is a complete theory of contract, but because he provides a link between the lexical ordering provided by Rawls and something close enough to contract law that we can use it to provide the beginnings of a legal theory. Fortunately the priority (rather than the exclusivity) of liberty relieves us of the need to trace all rules of contract law to a single source. We can have pluralism without incoherence.

The priority of liberty has some concrete implications for contract law. It suggests that, by and large, promises ought to be enforced in some way. It also suggests that the scope of obligations should at least track the intentions of promisors. Translated into doctrinal terms, this means that autonomy ought to provide the primary basis for specifying the rules of contract formation and interpretation. This does not, however, necessarily mean that there should be no limitations on freedom of contract. Contrary to the fears of Rawls himself, acknowledging the basic liberty to contract does not automatically commit one to the dreaded "doctrine of laissez-faire." It does mean, however, that limitations on contractual freedom, such as those in the doctrines of consideration, capacity, and unconscionability, need to be justified in terms of preserving equal liberty. The priority of liberty does not mean that there are no restrictions of personal freedom. It simply means that those restrictions must be justified with reference to the concept of liberty rather than with reference to welfare, distributive justice, or some other value.

For example, Lon Fuller's famous claim that the doctrine of consideration serves to channel the intention of parties and ensure that legal obligations represent deliberate decisions suggests that consideration can be plausibly seen as a way of ensuring that contract enforcement more closely tracks the deliberate exercise of liberty.[52] In other words, the restriction on contractual freedom represented by the doctrine of consideration can be justified in terms of liberty itself. Contractual disabilities based on infancy or diminished capacity likewise serve to ensure that legal obligations arise from truly autonomous decision making. Similar arguments could be employed to justify various forms of unconscionability, particularly so-called procedural unconscionability.[53] All of these arguments are open to dispute. The important thing is to see that the priority of liberty provides a context in which these debates can occur, as well as giving us some sense of what sorts of criteria we should use. A visceral

52. *See* Lon L. Fuller, *Consideration and Form*, 41 COLUM. L. REV. 799 (1941).

53. *See* Dori Kimel, *Neutrality, Autonomy, and Freedom of Contract*, 21 OXFORD J. LEGAL STUD. 473 (2001) (arguing that limitations on the freedom of contract can serve to advance a perfection notion of liberty).

hostility to laissez-faire, however, does not constitute a good objection to the priority of liberty since the principle contains resources for justifying restrictions on freedom of contract.

Liberty alone, however, is not a sufficiently powerful concept to specify all of the rules of contract law. In particular, much of contractual doctrine is specifically concerned with how to resolve contract disputes in the absence of any overt choice on the parties' part. For those committed to a unified theory of contract, this poses a serious embarrassment to autonomy-based approaches.[54] If one conceptualizes liberty as a superior value, however, rather than as an exclusive value, there is no objection to employing welfare considerations in specifying rules where liberty is not directly implicated. Thorny issues remain, of course, about the scope of liberty's domain. In particular, determining the precise scope of what has or hasn't been decided by the parties can be difficult. The mere fact of contractual silence cannot necessarily be taken as absence of any intention on a particular point. Communication is inevitably nested in a social context that carries a host of implicit assumptions that must hold for any explicit communication to be intelligible. Lon Fuller provided a typically pithy example: If an absent-minded professor walks out of his office, he may not consciously be thinking that the floor of the hallway will be there, but the floor's presence is necessarily an implicit assumption of his actions.[55] In the same way, contracting parties implicitly assume much about their transactions that must be taken into consideration to give force to their intentions. As Fried put it:

> It is a truism in the philosophy of language that in interpreting a person's words we are not guessing at the hidden but determined content of some list of meanings in the speaker's head. Rather our concerns particularize, render concrete, inchoate meanings. . . . Yet at some point it becomes necessary to say not that this is what the speaker meant but rather that this is what the speaker might have meant had he thought of it.[56]

Once even the implicit intentions of the parties are exhausted, however, the value of liberty no longer has a dog in the fight.[57] There is no objection at this point to employing arguments derived from

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54. *See generally* Richard Craswell, *Contract Law, Default Rules, and the Philosophy of Promising*, 88 MICH. L. REV. 489 (1989).

55. *See* LON L. FULLER, BASIC CONTRACT LAW 666 (1st ed. 1947) ("The absent-minded 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 conscious mental processes.").

56. FRIED, *supra* note 8, at 60 (footnote omitted).

57. *Cf.* Jody S. Kraus, *Philosophy of Contract Law*, *in* THE OXFORD HANDBOOK OF JURISPRUDENCE AND PHILOSOPHY OF LAW 687 (Jules Coleman et al. eds., 2002).

considerations of welfare, and efficiency arguments can enter our theory of contract with full force. Indeed, one of the great theoretical virtues of efficiency is that it can provide arguments that yield relatively determinate answers in precisely those areas where autonomy theories have difficulty providing concrete conclusions. When faced with a well-established rule like that in *Hadley v. Baxendale*, Smith was forced to resort to a variety of ultimately unpersuasive stratagems to avoid the embarrassment created by the fact that the promissory theory fails to yield any determinate answers on the question. On the other hand, the economic theory of an information-eliciting penalty default accounts for the rule quite nicely.

There are, of course, objections that can be put forward against employing efficiency or welfare arguments to fill out a theory of contract. One might argue that while liberty properly enjoys a superior position, where it is not implicated one should turn to considerations of fairness or distributive justice rather than efficiency. Efficiency, after all, is indifferent to who enjoys the benefits of society's enlarged pie. On the other hand, we may have important ethical reasons for preferring some particular group — such as the poor or the virtuous. The problem with this approach is that so long as there is substantial contractual freedom, such attempts at distributive justice are likely to be ineffective because, generally speaking, parties will contract away from such rules if they are economically inefficient.[58] Of course, one might be able to achieve such goals through contract law by limiting the ability of parties to bargain away from the desired distributive outcomes. The problem with this solution is that it violates the priority of liberty. Remember, within this theory liberty may only be limited to secure expanded liberty for all, not in the interest of other concerns such as efficiency or distributive justice. It does not follow, of course, that one cannot pursue such other concerns; one simply cannot pursue them through contract law. Hence, one might be able to employ the taxing and spending power to distribute wealth to deserving constituencies without violating the theory of contract I am proposing here.

The idea that distributive justice is best pursued through transfer payments is a common argument among law and economics scholars.[59] It is important to realize, however, that the economic reasons offered for this preference are quite different from the ones I offer above. The economic argument asserts that distributively attractive but inefficient rules should be eschewed in favor of taxing and spending because

58. *See* Alan Schwartz & Robert E. Scott, *Contract Theory and the Limits of Contract Law*, 113 YALE L.J. 541 (2003).

59. *See, e.g.*, A. MITCHELL POLINSKY, AN INTRODUCTION TO LAW AND ECONOMICS 119-124 (2d ed. 1989) (arguing that equity is best pursued through taxing and transfer payments rather than legal rules governing the interactions between private parties).

adopting efficient rules coupled with transfer payments increases aggregate welfare while achieving the same distributive goals. The argument from the priority of liberty, however, does not hinge on the maximization of aggregate welfare. Indeed, if it did then one would not be able to prefer liberty over efficiency when the two conflicted. Rather, the argument against employing fairness or distributive justice as a secondary value in place of efficiency flows from the priority of liberty itself, because practically speaking such goals can only be pursued in contract law by violating the priority of liberty.

B. *The Vertical Integration Strategy*

The approach sketched in the previous paragraphs is no more than an outline of a theory of contract. There are obvious gaps and plausible objections. It does, however, provide a useful model of how one should approach the problem of theoretical pluralism. Ultimately, the argument above is an example of what Jody Kraus has called "the vertical integration strategy." The vertical integration strategy deals with the problem of conflict between consequential and rights-based theories by ranking values hierarchically. In place of pragmatism it "contemplate[s] . . . that both approaches may be combined as logically distinct components of a united theory."[60] There are several ways this might be done. One could argue, for example, that one approach is foundational to the other approach. Daniel Farber, for example, has proposed an argument along these lines, claiming that in the context of contracts governing commercial transactions, a respect for autonomy leads for a rule aimed at maximizing efficiency.[61] Alternatively, one could argue for the lexical superiority of one value over another value. My argument takes this form. I do not claim that efficiency can be derived from respect for autonomy or vice versa. Rather, I simply offer an argument for why when the two values conflict, one should be chosen over the other.

Regardless of the form taken, the vertical integration strategy offers the best hope for a satisfying and coherent theory of contract. So long as philosophers of law focus on a quest for a single master value that explains all of contract law, their arguments are likely to run into the same problems that, despite his ingenuity and subtlety, afflict

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60. Jody S. Kraus, *Reconciling Autonomy and Efficiency in Contract Law: The Vertical Integration Strategy*, 11 PHIL. ISSUES 420, 422 (2001).

61. *See* Daniel A. Farber, *Economic Efficiency and The Ex Ante Perspective*, *in* THE JURISPRUDENTIAL FOUNDATIONS OF CORPORATE AND COMMERCIAL LAW 54 (Jody S. Kraus & Steven D. Walt eds., 2000). Like the theory that I offer in the text, Farber draws on the philosophy of John Rawls in making his arguments. Farber, however, focuses on a different part of Rawls' work, arguing that behind Rawls' famous veil of ignorance parties in the Original Position would choose a regime of commercial law that aimed at the maximization of efficiency.

Smith's *Contract Theory*. The vertical integration strategy, in contrast, responds to the pragmatic insight, acknowledging that competing values of autonomy, efficiency, and justice all have their place in contract law, without falling into the trap of ad hoc balancing between them.[62]

V. CONCLUSION

Stephen Smith has produced an impressive and important book. It provides a detailed and nearly comprehensive introduction to contemporary theories of contract law. Perhaps more importantly, it makes important original contributions both to the theory of promising and contracts and to the larger issue of how scholars should adjudicate between the claims of competing theories of the law. Despite these considerable virtues, however, Smith's book is flawed by the fact that it leaves largely unconsidered an important possibility for contract theory: a principled integration of competing normative approaches. To illustrate this, I offer an argument based on Rawls's principle of the priority of liberty as one way in which autonomy and efficiency could be held together in a single theory. My argument is an example of the vertical integration strategy, which I believe is ultimately the most fruitful direction in which philosophers of contract law could move.

62. Kraus offers a second strategy for reconciling autonomy and efficiency, which he labels the "horizontal independence" strategy. *See* Jody S. Kraus, *Legal Theory and Contract Law: Groundwork for the Reconciliation of Autonomy and Efficiency*, 1 SOC. POL. & LEGAL PHIL. 385, 390-422 (2002). The heart of this argument is the claim that autonomy and efficiency theories are actually theories about different things. Thus, Kraus offers the not entirely plausible argument that efficiency theorists are primarily concerned with explaining the outcomes of cases, while autonomy theorists are primarily concerned with explaining the arguments that judges use. *See generally* Kraus, *supra* note 57. The problem with this approach is at least twofold. First, it is open to the same objection that can be leveled against Smith's anti-economic transparency argument, namely that judges actually do employ ex ante reasoning quite regularly in their opinions. Second, and more importantly, the "horizontal independence" strategy does not respond to the pragmatic insight, namely the powerful intuition that as a normative matter autonomy, efficiency, and other values are all important. When economic theories are reduced to intellectual constructs for predicting case outcomes they lose their normative force and become little more than instrumentally useful descriptive assumptions. *Cf.* ALEXANDER ROSENBERG, PHILOSOPHY OF SOCIAL SCIENCE 74-79 (1988) (discussing instrumentalism in economics). In other words, the horizontal independence strategy, as formulated by Kraus, does not acknowledge the intuition that efficiency is a normatively — as opposed to purely descriptively — important concept.