On the Stickiness of Default Rules

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ON THE STICKINESS OF DEFAULT RULES

OMRI BEN-SHAHAR & JOHN A. E. POTTOW*

I. INTRODUCTION

It was once perceived, and still is commonly taught, that default rules in contract law must mimic efficient arrangements. Otherwise, these rules impose needless transaction costs upon parties who seek to opt out of them to reach more efficient positions.¹ In settings where these costs are high, parties might find themselves “stuck” in a default, unable to reach the outcome that they prefer.

The strong version of this account—that the only factor that can make an inefficient default rule stick is the direct cost of drafting a tailored provision—has been gradually reappraised.² It is by now recognized that factors beyond drafting costs might also cause parties to stick with an undesirable default rule; that is, parties might choose not to opt out of a legal default even when a better provision can easily be identified and articulated at a negligible drafting cost. While this “stickiness” of defaults has been identified before in

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¹ See, e.g., Charles J. Goetz & Robert E. Scott, Liquidated Damages, Penalties and the Just Compensation Principle: Some Notes on an Enforcement Model and a Theory of Efficient Breach, 77 Colum. L. Rev. 554 (1977); Robert E. Scott, Rethinking the Default Rule Project, 6 Va. J. 84, 94 n.4 (2003) (“[C]hoosing a default rule on the basis of some normative conception of fairness would be wrong, in the sense that it would not increase the amount of fair contracts in the world, but it would increase the amount of contracting costs.”).

discrete contexts, the purpose of this Article is to suggest that its pervasiveness may be even broader than previous accounts have predicted.

The core intuition is simple. In the presence of a default rule—or, more precisely, in the presence of a familiar and commonly utilized background provision, be it a common law doctrine, a business norm, or a boilerplate contractual term—a transactor might fear that proposing an opt-out from the default will dissuade his potential counterparty from entering into the agreement. The fear is that the counterparty will suspect that the proposer's decision to deviate from the norm and use an unfamiliar provision hides some unknown problem: in short, that it is a "trick." The counterparty, seeking to rationalize why the deviation was proposed, may construct a negative account and attribute some undesirable reason for the departure by the proposer. Depending on the plausibility of the imputed negative account, the counterparty will either exact an offsetting discount or avoid entering into the contract altogether.

Consider the following example. An author submits her manuscript to a publisher or a law review. Suppose the common practice (the "default") is for her to offer the manuscript on an exclusive basis. An author who opts out of the practice and offers to submit to multiple publishers concurrently may be viewed adversely, and her chances to publish the manuscript might be diminished. Aside from begrudging the negative direct value of having to compete against other publishers, a reviewer might make a host of negative inferences about the author: that she is insecure about the quality and the appeal of the manuscript, that she disregards editorial norms and is difficult to work with, perhaps even that the quality of the manuscript is inferior.

But what if the default is the opposite, and publishers allow and expect multiple concurrent submissions? How would a publisher view an author who opts out and offers exclusive submission of a manuscript? We argue that although there is positive direct value to avoiding competition with other publishers, a reviewing publisher might still make a negative inference about the proposal: that the author is desperate and does not think she can publish the manuscript elsewhere so is trying gimmicks, that the author is unpredictable and is difficult to work with, perhaps even that the study lacks timeliness and so the author sees no urgency to


4. For a discussion of the similarities between these terms, see generally Michael Klausner, Corporations, Corporate Law, and Networks of Contracts, 81 VA. L. REV. 757 (1995).
publication. In short, no matter what the default practice is, a proposal to opt out of it can raise a host of suspicions. Anticipating these suspicions, an offeror may adhere to the default and suppress any desire to deviate or experiment.

Opt-out proposals may differ widely in terms of the direct value to the offeree. Apart from the associated learning costs, a proposed opt-out can have positive, negative, or neutral "direct value" to the offeree. That is, some terms may have positive direct value to the recipient, meaning that, other things being equal, a rational offeree would pay to have the term included in the contract and adjust the price favorably. A seller's proposed warranty of satisfaction would be such an example. Similarly, it is easy to imagine terms whose direct value is negative to a recipient, such as a seller's proposed as is/no refunds condition. In theory, then, a deviant proposed term should be rationally priced by the counterparty, with either an upward or downward adjustment based on direct value.

But when an unfamiliar term is proposed, other things may not be equal. Due to the unfamiliarity of the term itself, its recipient may impose an effective penalty in the form of an additional, negative adjustment. Indeed, a principal claim of this Article is that the contractual phenomenon we might loosely refer to as "deviance avoidance" may even apply to proposals which, by the objective direct value of their content, should be seen as good for the counterparty, that is, when the departure from the default is genuinely favorable to the recipient of the proposal.

To be sure, not all default rules and terms are sticky. Many types of complex transactions are tailored term by term, and in those settings the content of untailored default rules plays little role. Stickiness, this Article argues, is more likely to be an impediment to opt-outs in situations where it is uncommon for other market participants to negotiate a tailored provision, that is, where the background rules and templates are well entrenched and commonly employed. Moreover, there are various other forces, apart from the one discussed here, that can render a default provision sticky, such as learning effects, network externalities, interpretive risk, and more. The purpose of this Article is neither to unbundle them nor


6. The argument is not that stickiness can be inferred from the existence of uniformity in the adherence to the background default—this would be a tautology. Rather, the argument is that the more prevalent the adherence of other contractors to the background default, the more costly it becomes for a party to propose a deviant term.

7. See Marcel Kahan & Michael Klausner, Standardization and Innovation in Corporate Contracting (or "The Economics of Boilerplate"), 83 VA. L. REV. 713 (1997) (discussing network externalities and learning effects); Ehud Kamar, A Regulatory
rank their importance. It is to suggest that the resulting stickiness from the combination of these and other forces may be more robust than often appreciated.

To explore the stickiness of default rules, this Article employs the following technique. It identifies and examines situations in which two sets of jurisdictions take opposite approaches with respect to the default rule they apply to a specific issue of contract law. In these situations, if the defaults are sufficiently divergent and if we assume that it is impossible for both default rules to be equally efficient, then we should expect (as our null hypothesis) that in one set of these jurisdictions—but not the other—parties will systematically opt out of the default more prevalently, particularly if the transaction costs involved are predicted to be low. If, instead, parties stick with the default in both sets of jurisdictions, regardless of that rule’s content, then such contracting behavior must indicate the additional costs associated with deviance avoidance.

The Article focuses on three examples. The first example looks at the rules governing the revocability of contractual offers. It shows that there is significant variance across jurisdictions in defining the right to revoke offers. It also shows that there were important changes to this doctrine within jurisdictions over time. But there is no evidence that opting out became more prevalent in one jurisdiction (or time period) based upon the content of the default rule regarding revocability. The second example looks at the rules governing the termination of employment contracts—the at-will versus for-cause doctrines—and again argues that there is no evidence of greater incidence of opt-out under one regime versus the other. Finally, a third example examines the drafting of boilerplate contracts in a specific sector: bond covenants. It discusses a study that demonstrates how surprise changes in the substantive legal interpretation by courts of terms in these contracts did not produce responsive redrafting.

Part II of this Article reviews the prior accounts of default stickiness that have developed the intuition underlying this analysis. Part III discusses the larger phenomenon of stickiness that can be pieced together with those prior accounts and offers additional conjecture regarding the mechanisms at work. Part IV presents the three examples of stickiness of default rules to support the claim that the problem of stickiness is pervasive. Part V concludes.
II. PRIOR ACCOUNTS OF STICKINESS

This Article is not the first to identify the stickiness of legal default rules in contracts, nor is it the first to argue that parties might sometimes leave contracts "economically incomplete" (that is, leave some contracts ungoverned by terms that are Pareto optimal), even when the direct transaction costs of identifying specific arrangements for some important contingencies are low. For example, Russell Korobkin conducted a series of experiments (discussed in more detail below) on first-year law students exploring whether the psychological phenomenon sometimes known as the "endowment effect" leads parties to attach disproportionate utility to legal default rules as the status quo. Korobkin hypothesized that the same cognitive bias that underlies individuals' preferences for maintaining the status quo with respect to physical items also generates a bias for legal defaults. If the legal default is perceived as an entitlement with similar attributes to, say, a coffee mug (the physical item used in many endowment effect experiments), then individuals will be less inclined to opt out of them. His findings do, indeed, lend support to the conclusion that human beings are cognitively disposed to prefer a default legal rule in contractual negotiations, irrespective of the content of that legal rule.

Korobkin also ran follow-up studies to probe further the apparent bias toward the status quo. For example, what happens when the default rule changes? Would status quo preferers seek out the old default rule (to return to comfortingly familiar territory), or would they prefer the new default rule (to remain passive in the face of an opportunity to opt out)? The data from his follow-up trials led Korobkin to conclude that it is the latter, for which he offers a cognitive bias explanation: the attractive role of inaction in the service of "regret avoidance" by decisionmakers. He calls this account the "inertia theory."

Even if one takes Korobkin's studies as consistent with a psychological attachment to default arrangements, the question

9. Id. at 611-12.
10. See, e.g., Jennifer Arlen et al., Endowment Effects Within Corporate Agency Relationships, 31 J. LEGAL STUD. 1, 6-7 (2002).
11. See Korobkin, supra note 8, passim.
15. Id. at 1586; see also infra notes 87-100 and accompanying text.
remains as to the strength and nature of this effect. Korobkin examined the preferences of individuals toward a favorable legal rule. He found that they would demand more to give up the rule when it was framed as a default legal entitlement than they would pay to acquire the rule when it was not framed as a default. But his studies that measure abstract pricing preferences when framing is manipulated may not fully capture the dynamic, interactive nature of contract negotiation. Consider in this regard the example of a written proposal in which a default term is crossed out (for example, an offer presented as a boilerplate contract with a standard clause explicitly and conspicuously altered and replaced by the opposite arrangement). Do recipients, following Korobkin's inertia theory, prefer to remain passive and avoid regret by accepting the penciled-in alteration as proposed by the offeror (as the "framed" status quo)? Or do they prefer to send back the offer with a counterproposal reverting to the crossed-out term (returning to the "default" status quo)? Korobkin's results tend to suggest that they prefer the latter, which strikes us as plausible. We are not sure, however, that this strategy reflects an exhibition of inertia. Inertia alone, it seems, cannot fully explain the attraction of default rules.

Taking an economic perspective, Lisa Bernstein offers another explanation for the attachment of parties to default rules, based on social norms and negotiation strategy. She explores the possibility that parties form adverse judgments when they encounter proposals to alter default norms in negotiating contracts. She further predicts that these "costs" to deviate depend upon the type of contract at issue. They are likely enhanced in situations where repeat interaction is required over the course of the contractual relationship:

Relational factors may also affect the cost of contracting around default rules. In transactional settings where informal norms are an important part of the parties' contracting relationship, a party may be reluctant to suggest varying a particulardefault rule even if the "direct transaction costs" are low and the variation would make both parties better off.

16. See Korobkin, supra note 12, at 1621; see also Korobkin, supra note 8, at 637-47.
17. Korobkin, supra note 8, at 637-47; see also infra notes 87-100 and accompanying text (discussing Korobkin's findings).
19. See id. at 71-72.
Bernstein believes such costs can be reconciled within the Coasian framework by arguing that costs (and also benefits) of opt-out cover a wider sweep than lawyers’ fees. Thus, implicit in Bernstein’s account is the idea that a party who varies a particular default rule is regarded by her counterpart as a more likely violator of the informal cooperative norms that discipline participants’ behavior and the idea that such a negative perception can be costly. As a consequence, deviant proposals are shied away from in the negotiation of long-term contracts.21

Taking a similar but more rigorous approach, economist Kathryn Spier indirectly touches upon the persistence of default contract terms in her theory regarding why some contracts remain “economically incomplete.”22 She models formally the signaling effects of bargaining proposals and demonstrates that uninformed parties may infer information from the content of a proposal made by more informed parties. A fear of adverse inferences may lead the more informed parties to forego proposing potentially surplus-enhancing terms when they negotiate their contracts.23

Illustrating her model, Spier uses a stylized example of a professional athlete negotiating his employment contract with a sports team.24 Even though the athlete might want an “injury clause,” that is, a specific provision guaranteeing some minimum level of compensation in the event of an injury, and even though he presumably would accept the commensurate downward wage adjustment that is actuarially appropriate for a wage guarantee (since he is more risk-averse than the team), he is nevertheless unlikely to propose such a provision in negotiations. This is because, predicts Spier, the athlete recognizes that the team may view his very request to include an injury clause as a signal that he has a greater than average tendency to become injured. If the team does read the proposal as such a signal, then it will adjust his wage by more than the average cost of an injury. Not knowing how injury-prone the athlete truly is due to the costly observability of this characteristic, but knowing that it is likely known (or at least more known) by the athlete as private information, the team would conclude that, other things being equal, it is the more fragile athletes who tend to benefit from injury clauses. Hence it would suspect that

21. Bernstein speculates that these forces may arise in certain short-term transactions as well. See Bernstein, supra note 18, at 71 (“Similar barriers to contracting around default rules are also present even in transactional settings where the parties do not have long-term business or social relationships and tend to think about the transaction in terms of their legal rights and duties.”).
23. Id. at 433.
24. See id.
those who ask for such clauses are more likely to be fragile, and it would draw an adverse inference from any such request. Regardless of the true probability of injury, and regardless of the presumably superior knowledge the athlete might have both of that probability and of his personal preference to forgo some wages to gain the insurance term, surplus-enhancing injury clauses might never get put on the negotiating table by athletes for fear of the negative message they could send.\textsuperscript{25}

A similar understanding of the strategic behavior of negotiating parties is developed in an important article by Jason Johnston.\textsuperscript{26} Critiquing the idea that default rules should be designed to induce the revelation of information (the "penalty default" paradigm),\textsuperscript{27} Johnston notes that strategic considerations in certain circumstances could make it undesirable for parties to propose deviations from background legal rules.\textsuperscript{28} He argues that it could conceivably be a superior strategy for a party to remain silent and accept a seemingly inefficient default arrangement, rather than propose a potentially efficient opt-out, if the very process of opting out effectively requires the revelation of valuable private information that can be exploited by the other party. For example, a shipper who highly values safe carriage of goods might be inclined to contract out of default rules of limited carrier liability and ask for higher liability coverage. But in so proposing such a high-insurance opt-out, she would reveal to the carrier her higher value attached to full performance of the contract and thus expose herself to having a greater share of her surplus extracted by the carrier through a price adjustment that would more than account for the greater liability.\textsuperscript{29} Facing this expropriation risk, the shipper might prefer to remain silent and accept the suboptimal

\textsuperscript{25} See id. Interestingly, injury clauses are apparently the norm in some professional sports' collective bargaining agreements (hockey) but not others (football). See Collective Bargaining Agreement Between the NHL and the NHL Players' Ass'n, art. 23.4 (June 26, 1997), http://www.nhlpa.com/CBA/PDF/CBA-1997.pdf [hereinafter NHL CBA]; Collective Bargaining Agreement Between the NFL Management Council and the NFL Players Ass'n, art. XII, § 2 (Feb. 25, 1998), http://www.nflpa.org/Media/main.asp?subPage=CBA+Complete#art12 [hereinafter NFL CBA]. The reader is invited to speculate why these different norms might have developed, which may have to do with the comparative prevalence and seriousness of injuries. It is possible that NFL players have a greater chance of experiencing major injuries than NHL players, and this increased risk led to differences in standard contract norms. In any event, the injury clause norms are mandatory rather than waiveable by contract, so not amenable to empirical analysis of opting out behavior.

\textsuperscript{26} See Johnston, supra note 3.

\textsuperscript{27} See id. at 616; see also Ian Ayres & Robert Gertner, Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules, 99 YALE L.J. 87, 91 (1989) (introducing the concept of "penalty defaults").

\textsuperscript{28} Johnston, supra note 3, passim.

\textsuperscript{29} Id. at 617.
liability coverage; the default arrangement will stick. Johnston uses this example to conclude that strategic behavior in forming contracts can be influenced by the content of the default rules. In other words, not only are default rules sticky, but some defaults are stickier than others. Under Johnston's argument, the limited liability default is stickier than an unlimited liability default because only with the former does an opt-out reveal the shipper's high idiosyncratic value of performance.

Johnston's argument was responded to by Ian Ayres and Robert Gertner, the original proponents of penalty defaults, who concede that strategic considerations could affect party conduct in moving out of default positions but disagree with the implication that these incentives could be asymmetric. Proposing an "irrelevance conjecture," Ayres and Gertner contend that any signal an informed party could choose to withhold in negotiating a contract could be effectively extracted through a screening proposal by the counterparty to force selection from a fixed menu of terms. Therefore, they conclude, rather than the content of a default rule making some gaps more inefficient than others due to asymmetric signaling, "those inefficiencies will be the same regardless of the initial gap filler." Johnston and Ayres & Gertner all agree, however, that strategic incentives influence contracting behavior in just the same way as direct transaction costs; all can undermine efficient tailoring.

Yet another strand of contracts scholarship identifies the stickiness of default terms and suggests that externalities might be a cause. In a series of articles, Michael Klausner and Marcel Kahan discuss the network externalities of standard contract provisions that include "learning" and "networking" benefits. Learning benefits are the advantages that retrospective usage of an entrenched legal term (through judicial interpretation, legal service familiarity, and so forth) accord current users. These benefits arise wholly apart from the rule's intrinsic efficiency. Network benefits are the collective advantages shared among multiple contemporaneous (and

30. Ayres and Gertner recognized this obstacle to information-forcing opt-outs. See Ian Ayres & Robert Gertner, Strategic Contractual Inefficiency and the Optimal Choice of Legal Rules, 101 YALE L.J. 729, 741 (1992) (noting the possibility that contractual inefficiencies will persist even when contracting is costless and showing that these inefficiencies arise when the hidden characteristics of the more informed party are nonverifiable).
31. See Johnston, supra note 3, at 626-27.
32. See id. at 630-31.
33. See Ayres & Gertner, supra note 30, at 732-34.
34. See id. at 737-39.
35. Id. at 737.
36. See id.; see also Johnston, supra note 3.
37. See Kahan & Klausner, supra note 7, at 718-27; Klausner, supra note 4, at 772-825.
38. See Kahan & Klausner, supra note 7, at 718.
prospective) users of a term when it is widely proliferated.\textsuperscript{39} The quintessential example of such a networking benefit is telephone technology; a solitary telephone is of limited usefulness, but when everyone has one they become quite valuable.\textsuperscript{40} Similarly, a legal term, dispersed throughout a network, can create externalities—benefits that may be unrelated to the inherent value of the term itself (recall that Betamax was supposedly a superior product but everyone used VHS).\textsuperscript{41} Kahan and Klausner model under which conditions these learning and network externalities can distort the selection of legal rules and lead to suboptimal terms.\textsuperscript{42} Such situations provide yet another illustration of when defaults can become sticky.\textsuperscript{43}

Although these prior analyses offer differing perspectives regarding the stickiness of default rules, they all examine the same phenomenon. They each struggle to understand the true and full costs of deviating from the status quo that parties incur in forming their contracts, beyond the simple transaction costs of drafting. In the next section, this Article builds (modestly) upon a subset of these accounts—the Johnston-Spier-Bernstein signaling theory—to suggest that the scope of this stickiness problem is potentially broader and more prevalent than previously perceived.\textsuperscript{44}

III. THE COSTS OF DEVIATING FROM DEFAULT RULES: FEAR OF THE UNKNOWN?

In situations of contract formation by two arms-length parties, each actor forms opinions and expectations about the other party and the value she brings to the transaction through the filters of incomplete and asymmetric information. Anytime a relationship involves uncertainty about attributes of the partner, the process of entering into a contract is affected, and potentially obstructed, by information the parties infer about one another.

\begin{itemize}
\item \textsuperscript{39} See id. at 725-27.
\item \textsuperscript{40} See Klausner, supra note 4, at 772.
\item \textsuperscript{41} A typical example of these benefits is in insurance industry boilerplate, where wide proliferation of identical language allows insurance carriers to compare actuarial data. See, e.g., Michelle E. Boardman, Contra Proferentem: The Allure of Ambiguous Boilerplate, 104 MICH. L. REV. 1105 (2006).
\item \textsuperscript{42} See Kahan & Klausner, supra note 7, at 730.
\item \textsuperscript{44} This survey is not comprehensive. For example, Mark Roe has written about "semi-strong path dependence" and defaults. See Mark J. Roe, Chaos and Evolution in Law and Economics, 109 HARV. L. REV. 641, 648-52 (1996). And Claire Hill, for example, explored literature about the incentive of attorneys to draft contracts that resemble familiar and existing templates. See Claire A. Hill, Why Contracts Are Written in "Legalese," 77 CHI.-KENT L. REV. 59 (2001) (suggesting that nervous junior associates might prefer leaving boilerplate unaltered because "the form offers comfort").
\end{itemize}
Information can be gathered about partners in a variety of manners. The very terms of a proposed deal provide one such important source of information. These terms have an effect beyond their direct content value (that is, their direct worth to a fully informed recipient of the proposal). They additionally serve as potential indicators regarding unknown attributes of the proposing party. The athlete from Spier’s example\(^\text{45}\) solicits an injury clause (that guarantees some salary in the event of an injury) because, presumably, he would prefer compensation adjustment to self-insurance. The content of this term, that is, its full-information value, is negative for the recipient: it should compel an actuarial downward wage adjustment by the employer to compensate for the expected value of the insurance risk. But the proposed term has another negative effect, as Spier explains, which emerges only when the recipient is \textit{imperfectly} informed. This is the negative signal regarding the athlete’s privately known internal attributes and the related likelihood that he will become injured.

To see the full potential effect of the proposal to deviate from the default, consider the athlete example, but this time imagine a mirror version of Spier’s hypothetical. Spier’s signaling account suggests that while parties worry about terms that can generate negative signals (such as requesting an injury clause when the default is for exclusion of injury compensation), they should be more than willing to opt out when the inferred information is positive. In Spier’s example, because the default norm is for no injury insurance, an athlete would be disinclined to propose a deviation from this default, even if it were efficient, for fear of sending the adverse signal regarding his fragility. But what about the reverse scenario, in which the default arrangement or the norm is for the routine \textit{inclusion} of injury clauses? In such a circumstance, Spier’s signaling account suggests that some athletes should be eager to send the reverse signal. They would offer to \textit{waive} the default injury clause so as to signal \textit{positively} to the prospective employer their unobservable private attributes (that is, that they are especially hale), and they should accordingly demand a higher wage, augmented at least by the actuarial risk foregone by the employer relieved of such insurance liability. Therefore, opting out of the default should be likely to occur when the opt-out, as in this example, has positive direct content value and is consistent with a positive signal.

The policy prescription that follows from this signaling reasoning is to set default rules where positive signals, or at least no negative

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\(^{45}\) Spier, \textit{supra} note 22, at 433.
signals, will result as natural inferences from opting out.\textsuperscript{46} Indeed, building upon the asymmetric information-forcing effects of competing default rules, Johnston claims that the \textit{Hadley v. Baxendale} default rule of limited carrier liability stifles opt-out by shippers who fear the negative strategic consequences of seeking higher liability coverage. But a reversal of the \textit{Hadley v. Baxendale} default rule—to a legal baseline of unlimited carrier liability—would create an environment conducive to opt-outs, freeing shippers from some of the strategic motives that would otherwise impair them from private tailoring under the current rule.\textsuperscript{47}

There is an additional factor, however, that renders more difficult the task of setting default rules such that opt-out proposals will be immune from negative signals. If, say, one default rule (“no injury insurance”) generates a negative inference against parties who propose to opt out of it, it does not follow that the opposite default rule (“injury insurance”) will guarantee a positive inference. True, it is possible that parties might interpret waiver of a default injury clause positively (the athlete is injury-free), as Spier’s analysis suggests.\textsuperscript{48} Indeed, the direct content value of the term should force, other things being equal, an upward wage adjustment to compensate for the employer’s reduced risk of not having to provide disability insurance. But other things are not equal. A departure from the “norm”—a proposal to incorporate terms that are not the standard, default terms—may in and of itself raise suspicion. A negative account can also be constructed for the proposed deviation, notwithstanding its positive direct content value. Here, it could be that the deviation of waiving an injury clause would cause the employer to question the athlete’s commitment to the enterprise. (“Is he not going to be giving his all in each match? Is that why he thinks he will never be injured?”) It might even signal more generally to the employer that the athlete is prone to hyper-negotiate his contract and perhaps be the type of person who will hold out in future phases of the relationship to expropriate a disproportionate share of any surplus. As Bernstein notes, a proposal to tinker with the boilerplate terms may signal legalistic attributes and even litigiousness.\textsuperscript{49}

\begin{itemize}
  \item \textsuperscript{46} Ayres and Gertner argue that when the uninformed party can propose a “menu” of contracts, the content of the default rule becomes irrelevant. Ayres & Gertner, \textit{supra} note 30, at 739-41. Under their framework, the problem of negative signals is muted since it is up to the uninformed party to “screen” the information in a manner that does not leave the informed parties the option of remaining silent and hiding their information. \textit{Id.} at 739 n.33.
  \item \textsuperscript{47} See Johnston, \textit{supra} note 3, at 630. Presumably the current rule makes opt-out by carriers easier because their offering unlimited liability could signal reliability. Indeed, although a shipper likely has superior \textit{ex ante} knowledge about the damages from breach of the shipping contract, the carrier has superior knowledge about the likelihood of breach.
  \item \textsuperscript{48} Spier, \textit{supra} note 22, at 433.
  \item \textsuperscript{49} Bernstein, \textit{supra} note 18, at 71-72.
\end{itemize}
deviation is thus susceptible to more than one explanatory account, and one or more of those accounts may well be negative.

That the deviant term can be reconciled with more than one rationale does not mean that a negative version will necessarily eclipse a positive one. The claim here is more modest: the presence of a plausible positive explanation for a deviant term that should be costed favorably on its direct content value by a rational actor does not preclude the simultaneous existence of an alternative, less positive account. This possibility of multifaceted interpretation means that any recipient of a proposal can recast a term that is facially favorable into one that carries, regardless of its objectively positive content, an accompanying negative message about unobserved characteristics of the proposer.

When a negative inference is plausible, it will provide a basis for a negatively disposed recipient to rationalize the deviance adversely. The degree of plausibility is, of course, relevant, because the more intuitive the negative explanation, the stronger the negative inference.\(^5\) In strong enough cases, the negative message could conceivably outweigh the otherwise favorable value of a positive-cost term to the recipient. For example, if the concern of the athlete's non-commitment to the enterprise (even if never validly grounded) overshadows the actuarial benefit to the recipient team that should follow from waiving an injury clause, then the default injury clause might stick, even when inefficient. Indeed, in settings in which deviations are uncommon, it will become increasingly likely that the recipient will be disposed to construct or select a negative account, and hence default rules will be at their stickiest.

The inherent suspicion toward proposals to opt out may stem, as Bernstein suggests, from the adverse messages about the deviating party's treatment of relational norms—that she will be unlikely to resolve disputes in a collaborative and informal manner.\(^5\) Indeed, as Alan Schwartz posits, it might cue that the proposer is hyper-litigious.\(^5\) It might even be a negative signal in the traditional

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50. This may be related to the theory of “counterfactual reasoning,” where negative events possibly cause subjects to relive those events counterfactually, altering the most “mutable” characteristics, in feeling regret. Even positive events can trigger some counterfactual thinking when negative events are “very close to occurring.” Korobkin, supra note 12; see also text accompanying notes 93-108 (summarizing social psychological literature). Thus, the more plausible a negative account is, the more likely a deviant term is to trouble a recipient.

51. Bernstein, supra note 18, at 70-71.

economic sense used by Spier: a visible proxy for a specifically identified but unobservable attribute.\textsuperscript{53} Any of these explanations, of course, may overlap with a black box cognitive bias of preferring the status quo, as explored by Korobkin,\textsuperscript{54} or with a reluctance to forfeit accrued network benefits from using standardized terms, as discussed by Kahan and Klausner.\textsuperscript{55} But it could also be something broader and more diffuse than any of these fairly particularized grounds. It might be that parties' disinclinations toward deviance stem from a rudimentary fear of the unknown.

Pause to reflect on the commercial contracting setting. When a party does not know her counterpart well, she must always consider the risk of being exploited by an undesirable or opportunistic actor. There is consequently added comfort when that counterpart plays the game according to familiar patterns. Conversely, there is added concern when the counterpart's conduct is unfamiliar, different from what is ordinarily done. The asymmetric information regarding the counterpart's attributes makes parties seek out clues to ascertain these hidden traits, which are theoretically infinite in number, to reduce the information disparity and minimize uncertainty.\textsuperscript{56}

It is possible that these clues the parties seek out are both broader and looser than what economists traditionally refer to as "signals." In a strict signaling account, the party who is less informed uses an observation about the informed party's conduct to make a rational inference of the counterpart's unobserved type. The recipient of a proposal first identifies the unknown trait and then predicts that a person of a given type will be more likely to make the proposal that the counterpart made; the proposal is a signal for the unknown trait.\textsuperscript{57} In military parlance, the signal serves as a proxy for a "known" unknown: a situation in which the uninformed party knows the domain (the "distribution") of her ignorance.\textsuperscript{58}

In the contracting setting, however, it is additionally possible that the uninformed party does not even know what it is that she doesn't know; that is, the uninformed party may not be proactively seeking out a signal to serve as a proxy for a specified but unobservable characteristic. Rather, she may reactively regard a deviation from the

\textsuperscript{53} Spier, supra note 22, at 434.

\textsuperscript{54} See Korobkin, supra note 8, at 625-30.

\textsuperscript{55} Kahan & Klausner, supra note 7.

\textsuperscript{56} Cf. Karen Eggleston et al., The Design and Interpretation of Contracts: Why Complexity Matters, 95 NW. U. L. REV. 91, 109-10 (2000) (predicting that transactors are less suspicious of form contracts than highly tailored ones due to fears of the exploitation of private information more possible in highly tailored ones).

\textsuperscript{57} See, e.g., ERIC A. POSNER, LAW AND SOCIAL NORMS 18-20 (2000).

default as raising a red flag. It cues her to wake up and become concerned, even without a lucid understanding of what the relevant unknown characteristic worthy of concern is. She experiences fear of the “unknown unknown.” Such a deviant proposal causes her to think, “I don’t know what it is that I should know better about my counterpart, but something doesn’t look right.” This fear of the unknown may account for documented situations of contractual parties becoming “spooked” by unconventional terms. For example, in a study on Silicon Valley start-up ventures, Joseph Bankman found a dearth of (tax-efficient) partnership structures and a plethora of (tax-inefficient) stand-alone corporation structures. In offering an account based on the ability of corporations to confer compensation through the readily familiar tool of “stock options” (as opposed to partnerships’ less gainly tool of “partnership interests”), a surveyed venture capitalist observed, “Management gets spooked by [the unfamiliar tool of] partnership interests.” This led Bankman in turn to conclude, “in an atmosphere of trust, it might take only a few hours to explain the equivalence of corporate and partnership options or interests. In an atmosphere of distrust, an employee might feel reluctant to accept any explanation, however coherent.” Thus a prospective employee offered partnership interests instead of stock options, even if told the reason for doing so is tax-related, might nevertheless “get spooked” that such exotica portend something wrong.

The psychological underpinning for this suspicious tendency may find its roots in the phenomenon known as “ambiguity aversion,” or more formally, “source preference,” in the social psychology literature. One strand of this research explores the degree to which decisionmakers generally prefer “known” to “unknown” risks. As broad generalization, when presented with a choice between flipping a coin and having it land heads ($p = 0.5$) and drawing a red chip from

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59. See id.
61. Id. at 1751.
62. Id. at 1752; see also Klausner, supra note 4, at 821 (postulating that Bankman’s findings could be a manifestation of marketing externalities).
63. Another illustration of this might be in the diametric default rules concerning the right to sue under the automobile insurance schemes in New Jersey and Pennsylvania. Default coverage seems to predominate in both jurisdictions. See Kahneman et al., supra note 13, at 199.
an urn with ten chips of which between three and seven are red \( (p = 0.5) \), subjects tend to prefer the known risk of the coin toss, notwithstanding the equal probability of the chip draw, because it is of equal risk but it is less “ambiguous.” In other words, the source of its probability is more known. Secondary studies in this area explore various refinements, including, among other factors, the ability to mute the effect in noncomparative forced-choice environments, the sensitivity of the effect to the probability level of the underlying risk, and the framing effects of juxtaposing confidence-building and conference-shaking heuristics.

One of the dominant models explaining this behavior relies upon the concept of “comparative ignorance,” whereby decisionmakers tend to feel more anxious in situations where their adversaries (or even experimenters) are perceived to have more knowledge or competence in assessing the underlying risk probability. In a particularly relevant study, the data suggest that subjects seek to avoid, with increasing anxiety, situations in which the risk probability is known, situations in which the risk probability is unknown and unknowable by any party, and situations in which the risk is unknown but more likely to be known by another party (that is, escalating comparative ignorance). Considering these psychological findings, it could well be that the proposal of an aberrational term unsettles the recipient, who starts to focus on his comparative ignorance of the other party’s internal attributes. (“Why did she propose that? Normal people don’t put in that term. What is it about this person that I don’t know? What is it about this deal that she knows but I don’t?”) The more jarring (cognitively dissonant) the departure is from standard terms, the more salient the trigger will be that invokes comparative ignorance concerns. This is why the mere existence of a plausible negative account to the deviance is more important than its ultimate persuasiveness vis-à-vis a positive account; the existence of a negative possible explanation fuels the fear of the unknown and sets the recipient down a speculative path of worry regarding his counterpart’s private information.

68. See Fox & Weber, supra note 64.
70. See Fox & Tversky, supra note 65, at 587-88.
72. It is for this reason that if, by corollary, a deviation from the status quo can be accompanied by a credible explanation, the proposer may defuse or at least minimize the negative potential signal.
formal psychological model within the scope of this Article, we do offer this account as a further possible explanation for the ubiquity and persistence of default stickiness and the seeming avoidance of deviance in writing contracts.

Importantly, this negative disposition toward deviant legal terms is not unique to default legal rules. A similar stickiness potentially exists when the default arrangement is embodied in a business norm (for example, cash on delivery) or in routine provisions of industry boilerplate (for example, closing terms of standard-form residential purchase and sale agreements). Indeed, notwithstanding the presence of a default legal rule, a norm may emerge under which transactors regularly opt out of the legal rule and create a stock commercial term that is the opposite. In such situations, the background norm, rather than the legal rule, would arguably become the relevant "default." For example, a default rule in shipping contracts of consequential damages in the event of breach (the Hadley rule) can be and often is readily reversed by a boilerplate disclaimer of liability and nominal cap on damages. In such situations, the stickiness likely applies with respect to the boilerplate term, not the common law backdrop against which it was developed. Thus the problem of stickiness may be even broader than a formal conception of "legal" defaults might suggest.

This understanding of stickiness also suggests that the frequency—and infrequency—of opting out will have a self-reinforcing quality. The less often opt-out happens, the more empirically prevalent the background default becomes. The greater empirical prevalence of the background rule will in turn increase the suspicious nature of any specific instance of deviation, which further in turn will weaken the incentive of any party to propose such a deviation in the first place. Conversely, the more common it becomes to propose opting out of a particular term, the less reason there will be for the recipient of the proposal to be suspicious, and so the norm

73. In these situations, where the parties' familiarity with the background arrangement is acquired through experience, the negative inferences attributed to deviance may be more severe. See Bernstein, supra note 18, at 70-71. But cf. Korobkin, supra note 12, at 1603-05.

74. One of Korobkin's experiments produced data that may be at odds with this intuition, suggesting that parties' status quo preference might be stronger to the underlying legal default rule rather than the opposite commercial norm. See Korobkin, supra note 12, at 1603-05. For reasons beyond the scope of this Article, methodological constraints in Korobkin's law student experiment may limit the generalizability of his findings, and these ones especially. For a more detailed critique of Korobkin's methodology, see Guy Rub, The Grounds for the Stickiness of Contractual Default Rules 34-43 (Aug. 2004) (unpublished thesis) (on file with author).

against private tailoring should weaken. In these latter situations, not only will parties be less inclined to penalize the proposed opt-out under consideration, but they also will be more amenable to having discussions about the content of the underlying term itself. It will get placed "on the table." In other words, an equilibrium in which few if any opt-outs occur is possible, but it is by no means unique. If some parties "fluctuate," by experimenting with deviant provisions, then instances of deviation will become less rare and the suspicion against them will subside. 76 There may even be a critical mass threshold depending on the term and the parties.

In this regard, one of the interesting results from Korobkin's status quo bias experiments are the data that he does not analyze. Korobkin's principal experimental design involves a hypothetical bargaining over the terms of a delivery contract. In the relevant baseline trial (Trial 1), he analyzes an impossibility excuse, that is, a contractual term that releases the delivery service from liability for breach if external circumstances make fulfillment of the contract impossible. 77 To test the presence of a status quo bias, Korobkin assigns subjects to two conditions. In the first condition, subjects are told that the default legal rule is for such an impossibility excuse and asked how much the delivery service should demand to waive the legal rule. 78 In the second condition, subjects are told that there is no impossibility excuse in default law and asked how much the delivery service would pay to secure it. 79 Strictly Coasian economic actors should price the term the same way (to waive it if they have it by default or to buy it if they do not), but Korobkin finds a status quo bias based on the different mean prices between the two conditions ($188,000 in the first to waive and $56,000 in the second to buy, with a p < 0.01). 80

To explore further an "inertia theory" explanation, Korobkin conducts Trial 2, in which he alters the experiments, telling subjects in the first condition that while the default rule is for an impossibility excuse, that rule is actually a new legal development and that previously there was no such excuse (he does so to test the effect of learning benefit externalities). 81 In the second condition, he reverses, with no impossibility excuse again being the default, but a newly created one. 82 He still finds "inertia" in the differing mean

76. See Korobkin, supra note 12, at 1605-08 (giving an example of a rapid shift from a no-opt-out equilibrium to a common-opt-out equilibrium).
77. Id. at 1590-92.
78. Id. at 1591.
79. Id.
80. Id. at 1591-92.
81. Id. at 1599-1600.
82. Id. at 1600.
ON THE STICKINESS OF DEFAULT RULES

prices for waiving/buying the term ($139,000 versus $31,000, with a \( p < 0.001 \)). Moreover, in Trial 3 (to test the preference of legal rules versus commercial norms), he makes the first condition that the default legal rule is for an impossibility excuse but that there is a routine commercial practice of waiving the rule, and the second condition the reverse. Yet again, a “status quo bias” trend persists in the mean prices ($63,000 versus $20,000, with a \( p < 0.05 \)).

Korobkin’s interesting studies focus on within trial differences between conditions. What are more interesting for the present analysis are the among trial differences across conditions. While we do not have the data to analyze the variance, the falling price offers of the first condition from Trial 1 to Trial 2 to Trial 3 ($188,000 to $139,000 to $63,000) support the intuitions of this Article, namely, that a norm that is less entrenched becomes more susceptible to deviation and hence permits parties to exact less of a penalty for alteration. In Trial 1, subjects were told of a default legal rule and asked to deviate from it by waiver; they demanded a high price. In Trial 2, they were told of a default legal rule, but that that rule was a newly created one; they demanded less. In Trial 3, they were told that the default “rule” was in name only and was systematically departed from; they demanded still less. The default rule thus became less sticky in strength as its “pedigree” diminished.

In conclusion, if default rules are indeed stickier than previous accounts suggest (as we believe), then there may be ramifications for legal policymaking. For example, policymakers should arguably place even more emphasis on setting accurate defaults, because departure costs might be higher than previously thought. As for the effect on penalty default rules, however, there are more complex considerations. On the one hand, the premise that parties will easily opt out of them to avoid the penalty may be more difficult to defend when there is widespread stickiness that stifles tailoring. On the other hand, harsh enough penalty defaults can overcome the stickiness effect, and once that effect is overcome, the increased prevalence of deviation will, in and of itself, attenuate the stickiness of the default rule even further.

83. Id. at 1601-02.
84. Id. at 1603-04.
85. Id. at 1604-05.
86. Id. at 1591.
87. Id. at 1599-1600.
88. Id. at 1603-04.
89. Professor Klausner notes that legal “menus” of multiple options from which one must be affirmatively selected can help overcome the power of “focal points” upon which parties can fixate and become stuck. Klausner, supra note 4, at 800-01.
90. Similarly, in the second condition, the price fell from Trial 1 to Trial 2 to Trial 3 by $56,000 to $31,000 to $20,000. See id. at 1606 tbl.2.C.
Another policy implication of the stickiness conjecture has to do with the design of standard forms. Many de facto default provisions appear not in the Uniform Commercial Code or in industry regulations but rather in boilerplate forms that are distributed by trade groups and nonprofits to industry participants, often with no charge. Once these circulated forms achieve enough popularity, they may themselves become “sticky”; that is, it may be difficult to adopt competing forms with different terms. This suggests that the drafters of popular forms have more power than is perceived. They can implement terms that are one-sided without leaving adversely affected parties a realistic opportunity to opt out. Associations that coordinate these forms may therefore create antitrust concerns even if there are no apparent transaction costs to opting out of their forms. Thus, the stickiness problem raises issues regarding the influence of the organizations that draft standard forms. It may justify closer social scrutiny of the terms they promulgate.

IV. EXAMPLES

This Part identifies instances in which a default rule varies, either across jurisdictions or over time. It argues that the absence of noted differences in the degree of opt-out under these varying circumstances provides evidence of stickiness.

A. Revocability of Offers

Before her offer has been accepted, an offeror may suffer a change of heart. Market prices could change, she could receive better proposals to deal, or she might discover something about the offeree. Various reasons could underlie her desire to revoke. Under the traditional common law, offers were historically revocable anytime prior to acceptance. In fact, this rule was not even a default provision from which the offeror could opt out: it was impossible to make irrevocable offers by mere statement of intent. Under classic contract law, a statement by the offeror that an offer was irrevocable for a given length of time—the so-called firm offer—lacked legal effect.


92. This concern is separate from the political economy concerns of how these forms are produced. Cf. Alan Schwartz & Robert E. Scott, The Political Economy of Private Legislatures, 143 U. PA. L. REV. 595 (1995).

93. Dickinson v. Dodds, (1876) 2 Ch.D. 463, 472 (Ch.).

94. See, e.g., Routledge v. Grant, (1828) 130 Eng. Rep. 920 (Bing.) (stating that a promise to keep an offer open for a fixed period is not binding absent consideration by the offeree). By corollary, a promise not to revoke supported by independent consideration was enforceable as forming an independent contract unto itself.
Modern common law gradually eroded the immutable revocability rule. Likely recognizing that it may be in the interest of offerors to issue irrevocable offers (and that it is surely in the interest of offerees to receive irrevocable offers), the law came to permit offerors to stipulate an offer’s irrevocability. Dispensing with the requirement of independent consideration, the law’s reasoning shifted to focus on reliance by the offeree, not economic consideration of the deal, to justify allowing the promise not-to-revoke to become binding.95 Codifying this understanding, section 2-205 of the Uniform Commercial Code enables merchants to make offers irrevocable for up to three months.96 Thus, under Anglo-American law, revocability is now a default rule, subject to virtually costless alteration. Offers are revocable anytime prior to acceptance, but an offeror may opt out of this default simply by stating that the offer is firm.

Other legal systems, however, have different revocability defaults. In Germany, for example, the default rule is opposite from the Anglo-American one (as it is in Switzerland, Portugal, and Brazil, to name a few other places).97 Unless otherwise stated explicitly, offers are irrevocable during the time in which the offeror may expect an answer under ordinary circumstances, or for such other time as specified in the offer.98 Again, this is only a default—opting out is possible. Indeed, it is very simple. All an offeror needs to do to recapture the power of revocation is add sufficiently clear language, such as, “this offer is revocable at any time prior to its acceptance.” Under the German practice, the use of terms like freibleibend (“without engagement”) or widerruflich (“revocable”) would suffice to reverse the irrevocability default and make the offer fully revocable.99

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96. U.C.C. section 2-205 states the following:

  An offer by a merchant to buy or sell goods in a signed writing which by its terms give assurance that it will be held open is not revocable, for lack of consideration, during the time stated or if no time is stated for a reasonable time, but in no event may such period of irrevocability exceed three months . . . .


99. FOSTER & SULE, supra note 98, at 384; see also P.D.V. MARSH, COMPARATIVE CONTRACT LAW: ENGLAND, FRANCE, GERMANY 63 (1994); BGB § 145 (“Whoever offers to another to enter a contract is bound by the offer, unless he has excluded being so bound.”).
Since it is impossible that both the Anglo-American revocability rule and the German irrevocability rule are equally efficient (indeed, they are diametrical), we should expect that opt-out will occur in one of these jurisdictions more prevalently than the other. In fact, given the polar nature of this rule (either revocable or not), we would expect opting out to be commonplace in one of the countries, readily detectable to the outside observer. This is especially so because the direct costs of opting out—either adding a freibleibend recital in Germany or signing on the firmness of the offer in the United States—are practically zero. And yet, surprisingly, such prevalent opt-out does not appear. In Germany, other than in discrete past periods of severe economic trouble and hyperinflation during which the freibleibend exception became for a time (unsurprisingly) widely used, it has been uncommon for offerors to opt out of the irrevocability default. German commentators do not find this result surprising. They describe their practice of keeping offers irrevocable as a “superior system.” As leading German comparativists note in so concluding, “[E]xperience shows that [the irrevocability] results are practical and equitable; the offeree can act with assurance in the knowledge that his acceptance will bring about a contract.”

Similarly, there is no detectably robust pattern of opt-out under the Anglo-American revocability default. In general, offers are made in a revocable, nonbinding fashion. Some limited empirical scholarship explores this trend. One such study examines opt-out practice within the construction industry. It finds that tendering subcontractors do not opt into an irrevocability regime when making their bids. Nor do general contractors request those bids to be

100. Benefits from defining the revocability term surely exist. Indeed, offer irrevocability is one major type of precontractual liability. There is now a burgeoning body of literature on the value of precontractual liability, both in terms of distribution effects and in terms of efficiency. See, e.g., Lucian Arye Bebchuk & Omri Ben-Shahar, Precontractual Reliance, 30 J. LEGAL STUD. 423 (2001); Richard Craswell, Offer, Acceptance, and Efficient Reliance, 48 STAN. L. REV. 481 (1996); Avery Katz, When Should an Offer Stick? The Economics of Promissory Estoppel in Preliminary Negotiations, 105 YALE L.J. 1249 (1996).

101. Proving that a specific practice does not exist is, of course, a difficult task. We neither offer such proof nor intend to suggest that the opposite conclusion is unprovable. We merely report our impression based on numerous informal conversations with practitioners and European law professors, as well as a survey of the empirically oriented literature.

102. See MARSH, supra note 99, at 63.


104. Id.; see CASEBOOKS ON THE COMMON LAW OF EUROPE, supra note 97, at 205.
irrevocable. Both subs and generals alike seem content with the revocability default of their legal system.

To be sure, business negotiators often do use firm offers in the course of a sales transaction in the United States, such that an offer “on the table” may be deemed by section 2-205 of the Uniform Commercial Code to be irrevocable. Indeed, one survey of general counsels of large firms and conglomerates found that a majority both make and receive firm offers regularly in their contracting practices. The methodology in this study, however, is unfortunate, because the respondents were expressly asked to consider as a firm offer any “promise to buy or sell at a fixed price over a period of time . . . not given in exchange for any promise or other payment by the offeree.” Thus while such offers might have been technically irrevocable in the eyes of the Code, we cannot be certain that the respondents actually considered them irrevocable in any meaningfully behavior-affecting manner. On the contrary, in other parts of the same survey, these respondents indicated that even binding promises were often jointly renegotiated. So it is not clear that we have reliable data indicating an opt-out norm favoring firm offers, even within the subset of large firms and conglomerates. (Interestingly, even if we did read these data to indicate such a norm, we see its prevalence vanish when we move from large conglomerates to smaller firms.)

The reluctance of parties to opt out of the revocability default can be further evidenced when the default rules change over time within a given jurisdiction. Such an example also exists in the specific context of bid revocability. In this legal domain, an “interpretive shock” occurred when a long-standing default rule of common law was reversed regarding reliance upon an outstanding offer.

107. Id. at 26 (alteration in original).
108. See id. at 22-23; see also Note, Another Look at Construction Bidding and Contracts at Formation, 53 Va. L. Rev. 1720, 1734 (1967) (surveying offerors who proclaimed “[o]ur word is our bond and our reputation paramount”).
109. Firms that reported using firm offers all had annual income exceeding $500 million. See Weintraub, supra note 106, at 27-28. Smaller firms did not report using firm offers. Id. These results could show that with large firms the stakes of deals are larger and more likely to offset any cost of altering defaults. Large firms are also more likely to have credible reputations and hence get more mileage from making firm offers because the offeree must rely on the offeror not to welch in ascribing value to the offer’s “firmness.”
110. This rule is related to, but conceptually distinct from, the revocability of an offer. It does not alter the baseline revocability rights of an offeror; rather, it pertains to an estoppel based upon (reasonable) counterparty reliance.
Baird Co. v. Gimbel Bros., 111 allowed a bidder to revoke its (presumptively revocable) bid at any time before acceptance, even after the recipient’s pre-acceptance reliance. This rule was effectively abolished in 1958 by California Supreme Court Justice Traynor’s decision in Drennan v. Star Paving Co. 112 What happened to the default norm after this interpretive shock? If post-reliance revocability were efficient, we should have expected a contracting shift back to the old status quo by express stipulations of revocability in offers. Otherwise, if it were inefficient, we should have seen prevalent opt-in prior to the Drennan decision. But we lack data to suggest that anything actually changed after this decision in the way parties solicited or submitted bids.113 To be sure, it is risky to draw conclusions from this particular area of contracting since many of the parties’ motivations are influenced by extralegal norms, reputation bonds, and informal accommodations. Nevertheless, this appears to be an illustration of the disinclination parties have to opt out of defaults, even when those defaults change.

Some of the theories discussed earlier in this Article are consistent with these observed patterns of opt-out infrequency. For example, in some particular contexts the trend can probably be explained by the parties’ adherence to informal norms that regulate the legitimacy of revocation.114 But this explanation only goes so far. When the legal default changes, it usually does not coincide with a change in the norms of negotiations. Thus, we would expect opt-out and a return to the old revocability default, the one that is consistent with the parties’ expectations. It is also hard to imagine what network benefits or interpretive advantages could explain this default entrenchment. This is why we offer our further account as a plausible explanation: deviating from the revocability default under either regime may cause the offeree to suspect the value or the

111. James Baird Co. v. Gimbel Bros., Inc., 64 F.2d 344 (2d Cir. 1933).
113. Two studies from that era demonstrate an almost irrelevance of revocability law in the construction industry. See Franklin M. Schultz, The Firm Offer Puzzle: A Study of Business Practice in the Construction Industry, 19 U. CHI. L. REV. 237, 259-61 (1952) (finding that only half of general contractors even asked for firm offers from their subcontractors notwithstanding it being in their obvious interest to do so and that even then many said they would allow their subcontractors to back out of bids); Note, supra note 108, at 1733, 1739 (finding that the U.C.C. firm offer law had little relevance, as most sub bids to general contractors were oral, and that bids that were written were not treated differently by the generals; finding also that notwithstanding laxity toward firmness of sub offers, a strong norm of reliance existed, with ninety-two percent of generals believing that subs should be bound after reliance on their bids by the general). Note that the Chicago study found some industry-specific trends: manufacturers of basic building materials worried about potential firmness of written offers and expressly drafted their bids to preclude firmness. See Schultz, supra, at 264. This could be explained by the risk of multiple parallel bids by such offerors that could strain capacity if all were accepted.
114. See id.
integrity of the deal by introducing a fear of the unknown. Against a well entrenched backdrop of irrevocability, an offeror who explicitly secures for herself the power to retract might be perceived as an unreliable “fly-by-night,” one who might even retract from a finalized agreement. Her commitment to the transaction could be questioned, and with it, the willingness of the offeree to rely upon the offer and pursue the deal. By contrast, against a rich backdrop of revocability, an offeror who explicitly waives her power to revoke may not necessarily enjoy the converse effects of perceived added reliability and sense of commitment. Instead, the offeree might still construct an unfavorable explanation. He might question whether the offeror chose to confer an irrevocable option to him because the offeror had no other potential partners knocking on the door. Or he might worry that there were other market participants who became aware of some problem with the offered deal or with the reputation of the offeror. Since there are multiple dimensions of “unknowns,” it is plausible that an uninformed offeree could make inferences along one of the dimensions that yield a negative signal. Anticipating the potential for the opt-out to provoke this negative inference, the offeror is more likely to stick to the default practice.

B. The Duration of Employment Contracts

Another situation that reveals the stickiness of defaults is employment contracting, or more specifically, the legal provisions that govern the duration of the employment relationship in nonunion labor agreements. In almost all jurisdictions in the United States, the baseline common law default rule is employment at will, 115 that is, either party may terminate the relationship at any time, without having to display a good cause for the termination act. Parties can of course vary this default rule and enter into a more restrictive arrangement that limits the set of causes that can give rise to unilateral termination. Yet, other than in the union context, in which collective bargaining agreements highly formalize the negotiations process and subject it to a unique set of rules, such systematic opting out does not seem to occur. On the contrary, in a survey-based study published in 1995, J. Hoult Verkerke found that only fifteen percent of nonunion employers opted out of employment at will by expressly according just-cause protection in their employment contracts. 116 To
reach this conclusion, Verkerke had to make broad generalizations (for example, aggregate employment handbooks and express written contracts together), but his data are nonetheless instructive on an important American trend. Even more tellingly, one third of his respondents used no contracting at all, relying solely upon default common law and statutory rules to govern their employment relationships.\textsuperscript{117}

Within the category of “at-will” arrangements, however, U.S. jurisdictions vary along a continuum of employee solicitude. That is, although “employment at will remains the default rule for indefinite term employment contracts,”\textsuperscript{118} Verkerke also finds that “[t]he strength of the at will presumption varies substantially across jurisdictions.”\textsuperscript{119} The presumption varies across jurisdictions because states differ in their judicial opinions interpreting contract doctrines such as good faith and implied contracts.\textsuperscript{120} Effectively, then, the at-will default rule exhibits some variance across states.

Verkerke compares two jurisdictions to see if employers in a more “liberal” state, such as California, evince a greater pattern of opting out of default common law by contract than employers in a “stricter” state, such as Virginia.\textsuperscript{121} Assuming, for hypothesis only, that the liberal rule is more efficient, he offered the following prediction:

Employers in California should, therefore, be inclined to contract out of the state’s comparatively attractive default rule at a lower rate than will Virginia employers. Virginia firms that fail to contract receive that state’s stringent, and thus comparatively unattractive, at will default. In contrast, California employers will get a more relaxed version of the at will presumption that more closely approximates the life-cycle just cause default.\textsuperscript{122}

Verkerke’s data suggest that the predicted pattern of opting out does not occur: there is no statistically significant relationship

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\textsuperscript{117} Verkerke, supra note 116, at 867. This finding seemed to correlate significantly with firm size: the smaller employers relied on default law and avoided contracts significantly more than their larger counterparts (almost half of them did not reduce their employment relationships to writing). Conceivably this difference in contracting reflects the heightened pinch of transaction costs for smaller firms.

\textsuperscript{118} Id. at 863.

\textsuperscript{119} Id. at 848. Most jurisdictions in Verkerke’s estimation have actually settled on adopting “an intermediate approach.” Id.

\textsuperscript{120} Id. at 844.

\textsuperscript{121} Id. at 881. More specifically, Verkerke treated “more liberal” as following most closely a just-cause animated “life cycle” rule in employment jurisprudence. Id. at 848-50.

\textsuperscript{122} Id. at 881. Verkerke expressly rejected an information-forcing “penalty” default analysis in employment contracting. Id. at 885.
between state and contractual choice. In both jurisdictions, employers were sticking with no contracts about one-third of the time. In other words, the content of the default rule did not seem to goad Virginians to write employment contracts any more than Californians. The status quo was thus highly sticky, even on a matter of such seeming importance in the employment setting as the dischargability of employees.

Verkerke's findings have been subsequently interpreted as an illustration of asymmetric signaling, following the Spier/Johnston accounts of stickiness. Invoking this explanation for the failure to opt out of the default employment rules shown by Verkerke's data, Walter Kamiat contends that "an employee who seeks an enforceable just-cause provision in the employment contract confronts a serious signalling problem regarding the quality of the employee's likely work." Again, a plausible negative account can be constructed to explain the employee's solicitation of just-cause protection in the mind of the employer. ("Was she fired before? Does she predict trouble with an at-will relationship?") Anticipating that such a conclusion might be drawn from his findings, however, Verkerke dismisses signaling as an explanation in his analysis. He argues that any signaling effect of seeking just-cause protection would likely be symmetric. That is, if the signal of seeking a Pareto-optimal just-cause dismissal provision conveys negative messages about the seeking party's prospective conduct under the contract (here, the employee's work ethic), then the response to the signal ought to convey a similar and offsetting negative signal (here, the employer's stinginess in refusing to allow such an efficient just-cause provision). Competitive market forces would permit the disappointed employee to seek employment from another employer who offered, or at least did not respond hostilely to, such a proposed just-cause term. Thus, any negative signal from an employee seeking just cause would be

123. Although beyond the scope of this Article, Verkerke actually does find one difference in his logit analysis for Michigan, id. at 881, and he offers a possible explanation. Id. at 868.

124. Interestingly, Verkerke offers some crosstabulation data that could suggest a normative preference for at will as opposed to just cause when examining the subset of employers who did sink the transaction costs to write contracts in these two jurisdictions. Id. at 881.

125. A signaling argument is indirectly supported by the frequency of just-cause provisions in collective bargaining agreements. If the relative rarity of just-cause contractual protection for nonunion employees is explained by the negative signal that a request for such a term would send, then by corollary, the muting or masking of a signal that is conveyed by a bargaining unit of a union rather than an exposed, individual employee might explain why the term gets proposed (and accepted) more in the unionized employee context.


cancelled out, in Verkerke's estimation, by the employer's equally negative signal by refusal to accede.

Even leaving aside assumptions regarding bargaining power, it is not clear that a signaling explanation can be so easily dismissed. To say that the signals cancel each other out misses somewhat the nature of signaling effects. Rather than neutralizing each other, it is equally plausible that the employee's and the employer's concerns about negative inferences will compound one another in a vicious cycle, with the employee worrying about the employer's propensity to discharge summarily by insisting on at will and the employer worrying about the employee's work ethic by insisting on just cause.¹²_error\textsuperscript{8} Error can sometimes accrue rather than cancel. Thus, regardless whether one believes that Verkerke's employment contracting pattern data tell a story about negative signaling, they certainly do tell a story about sticky defaults in the nonunion labor market.

Outside the United States, additional, more tentative evidence for the stickiness of labor defaults can be marshaled. This is done by considering a country, such as Canada, that has different labor default rules. In contrast to the American legal baseline of employment at will, Canada (at least in its most populous province of Ontario) effectively employs a common law default of dismissal only for cause.¹²_error\textsuperscript{9} The Canadian experience is complicated somewhat by the statutory overlay upon the common law of the Employment Standards Act (ESA), which prescribes certain employee-protection terms that cannot be waived by contract.¹³

Nevertheless, the overall structure seems to be the reverse of the American system. To be sure, describing the employment baseline in Canada as just cause is an apt, but not perfect, analogy, because employers technically retain ultimate discretion to terminate an employee's job unilaterally for any nondiscriminatory reason. But the just-cause rule can be seen as the effective default in Canada, because notwithstanding their nominal rights to dismiss an employee unilaterally, employers are required to pay "termination" or "notice" payments if they choose to dismiss an employee without just-cause.¹³\textsuperscript{1} These default common law termination entitlements of an employee may be raised or lowered by contract as employers and employees see fit. The ESA,

¹²8. Kamiat shares this critique of Verkerke's conclusions. Kamiat, supra note 126, at 1962 n.15.
¹³0. Id. § 5.
¹³1. Id. § 61 (stating that an employee dismissed without notice and cause is entitled to minimum payments under the common law). These payments vary widely and case-by-case, based upon factors such as duration of employment. See John-Paul Alexandrowicz, A Comparative Analysis of the Law Regulating Employment Arbitration Agreements in the United States and Canada, 23 COMP. LAB. L. & POL'Y J. 1007, 1029-30 (2002).
however, sets a minimum level of termination benefits below which private parties may not contract out, that is, a mandatory norm at the lower extreme.\(^\text{132}\) Thus, although employees can contract out of just-cause protection (or, more specifically, contract to waive their termination entitlements at common law), their range of waiver gets truncated by a statutory floor.\(^\text{133}\)

As a generalization, then, it is fair to say that Canada follows the reverse legal default from the United States: an effective rule of termination for just cause. Being a default rule, employees are free to request or agree to greater or fewer termination benefits as inclined. If the American at-will rule were more efficient, one would expect Canadian employees to offer and Canadian employers to seek waivers of the just-cause protections to the maximal extent allowed by the ESA in return for higher compensation.

Here, we were able to collect only anecdotal impressions from Canadian labor lawyers, but they consistently suggest the same trend of prevalent “noncontracting” that exists under the American experience. In the words of one Canadian lawyer:

> Although there is certainly a trend that we advise our [employer] clients to try more to reduce employment conditions to contract—and we are starting to see a bit more of that—the vast majority don’t have any contracts at all—but they are] relying on the statutory and common law entitlements. In fact, most ‘contracts’ for employment consist entirely of a one-page offer letter saying, “Congratulations, please report to your first day of work on this day at this pay.”\(^\text{134}\)

Further consistent with the American data, the Canadian anecdotal experience of labor lawyers is that if any trend exists, it is that larger, more sophisticated companies are the most likely employers to draft contracts for employment, with the smaller ones relying upon default law.\(^\text{135}\)

While it could, of course, be a comparative socio-legal phenomenon—that the Canadians are simply “different” in their

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\(133\). To be clear, though, all of these termination benefits in Canada are for dismissal “without cause.” By contrast, if an employer meets a relatively stringent test for dismissal “for cause,” then the notice benefits need not be paid under either the common law or the ESA; they are effectively forfeited. See id. at 5-6. “Cause,” under the common law, is again highly contextual and varies from employee to employee, depending on numerous factors. See id. at 5.

\(134\). Telephone Interview with Nadine Côté, Associate, Torys LLP, in Toronto, Can. (Feb. 2, 2005).

\(135\). Id.
legal preferences from their American counterparts—we just as easily can conclude that there is an explanation finding its roots in the reluctance to deviate from the standard legal default. Moreover, it cannot simply be a story of transaction costs, because a one-page letter in Canada can just as effortlessly become a one-and-a-quarter-page letter, with a further sentence setting by contract the termination benefits. Yet, just as with the American experience, we see a persistent stickiness of the default rule.

C. The Stickiness of Boilerplates

Another example of the stickiness phenomenon is found in the drafting of boilerplates. Complex transactions are often governed by industry-standard boilerplate terms, which vary little, if at all, across contracts. What happens when the default interpretation of such a boilerplate term changes, say, as a result of an external interpretive shock? For example, what happens if an unexpected court ruling interprets a standard term in a different (or, if possible, completely opposite) way from the traditional understanding? Does the new interpretation stick, or will parties redraft the boilerplate term to return to the original intended meaning?

A recent example arose in the context of sovereign bond contracts, as discussed in a working paper by Stephen Choi and Mitu Gulati.

Studying the restructuring consent terms of sovereign bond contracts (the provisions that determine what fraction of the creditors must approve a change in the credit terms), the authors identify a large sector of the market that traditionally used one type of provision, a “unanimous consent” clause. This clause requires, as its name implies, the approval of all creditors for a workout refinancing. In a landmark event in 2000, a sovereign debtor was able to modify a contract with a unanimous consent clause without, in fact, acquiring unanimous approval from the bondholders by invoking another provision in the contract. This shocked the market—doubtless, it

136. There is actually some weak evidence for this. In the telephone interview of Nadine Côté, Ms. Côté said that there is a “social justice” sense behind the minimum employment standard for termination benefits under the ESA, and that the no-contracting-out provision has been likened in case law to being similar to a prohibition against contracting out of a speed limit: its absence would be flatly inconsistent with deep norms of public policy. Id.


138. See Gulati & Choi, Boilerplate Contracts, supra note 137, at 5.

139. See Choi & Gulati, Contract as Statute, supra note 137. The complementary provision, known as “exit consent,” applied to early payment terms. The 2000 court decision was an “interpretive shock” because it allowed the (non-unanimous) exit consent
shocked the creditors who held unanimous consent clause bonds.\textsuperscript{140} Did the surprised creditors immediately insist upon amendments to their bonds to shore up the unanimous consent protection that they thought they had? Did issuers who drafted subsequent bonds revise the language of the contract to clarify that unanimous consent is required for modification?

No. Choi and Gulati found that, although many investors initially grumbled about this new interpretation, there was no massive opt-out of the new default and no redrafting of the boilerplate language in the contracts.\textsuperscript{141} The default text of the boilerplate remained the same. The default, even when its legal content changed by \textit{deus ex machina}, remained sticky. The empirical tests conducted by Choi and Gulati indicate that the use of the default boilerplate is "a reflection of the standardized nature of such terms and the 'stickiness' inherent in changing such terms."\textsuperscript{142} Specifically, they argue that the lack of immediate shift back to the pre-shock arrangement provides evidence for the stickiness hypothesis (or the "lock-in" effect, as they call it in this context).\textsuperscript{143}

Interestingly, Choi and Gulati also found a secondary effect: although no country changed its boilerplate language initially, there was, eventually, a follow-up effect, but only after three years. After this substantial time lag, a renegade country, Mexico, went out on a limb and altered the consent term to match expressly the meaning that the court applied. This departure from the old boilerplate language opened the floodgates, where other countries felt it was acceptable, then, to redraft their consent clauses.\textsuperscript{144} This follow-up provides support for the shifting nature of deviance costs mentioned above. Once those costs are borne by "a pioneer," future opt-outs produce less anxiety as instances of deviance become familiar. In such circumstances, the stickiness norm will erode and the opportunity widens for innovation and surplus enhancement through private legal tailoring.

V. CONCLUSION

Imagine the following scenario. You are looking to buy a new component for your computer (say, a wireless router). You log onto

\textsuperscript{140} See Choi & Gulati, \textit{Contract as Statute}, supra note 137.

\textsuperscript{141} \textit{Id}.

\textsuperscript{142} \textit{Id.}; see also Barry Eichengreen, \textit{Restructuring Sovereign Debt}, \textit{J. ECON. PERSP.}, Fall 2003, at 75.

\textsuperscript{143} Choi & Gulati, \textit{Contract as Statute}, supra note 137.

\textsuperscript{144} \textit{Id}.
eBay and type the model number into the search bar. To your delight, hundreds of items are auctioned. They are all very similar in description and are sold by sellers of varying reputations. You are getting ready to bid on one of these routers, the maximal value of which to you is $50, when you notice that one of the offers is a bit different. This offer is identical in every respect to the others—the same router model, the same description, the same shipping costs—but it includes an additional element. In a conspicuous fashion, the seller announces that the winner of the auction will receive, apart from the router, a handsome prize: a box of fancy chocolates. Indeed, in the auction page, the seller includes a picture of chocolate. Will you bid more than $50 for this auction? Will you bid less?

This Article posits that it is very plausible to expect that you will bid less than $50, even if you like chocolate. True, the direct value of this auction is increased by bundling the router with a non-zero value chocolate. But there is also an indirect effect on the valuation, which may be negative. You have never seen anything before like this on eBay—nobody who sells computer parts bundles them with chocolate. While the bundling itself does not provide any direct indication that something might be wrong with the router, the fact that this deviation is so uncommon may raise your suspicion that the seller is trying to trick you, and other potential buyers, into a transaction that you will later regret. The bundling of chocolate into the transaction, being such an unfamiliar practice, may scare you away by raising a host of “unknown” worries you had not originally perceived. So while there is nothing wrong with such bundling—in fact, it should increase the value of the sale to the buyer—it may never be offered.

This same intuition underlies the thesis of this Article. It is sometimes cheap and desirable to offer terms that differ from the default rules or the standard terms used in the market. But the proposal of new and otherwise unfamiliar terms may also raise suspicions and scare away potential counterparties. Default rules and the standard boilerplate terms may stick more than we think, and more than they should.

145. We reject melting and other nuisance costs—that is another type of stickiness.