TWO FORMS OF FORMALISM IN CONTRACT LAW

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Formalism in contract interpretation has had many defenders and many critics. What lawmakers need, however, is an account of when formalism works and when it does not. This Article addresses that need by providing a general theory of contract exposition and differentiating between two forms of formalism in contract law. Formalities effect legal change by virtue of their form alone, thereby obviating interpretation. Examples include "as is," the seal, and sometimes contract boilerplate. Evidentiary formalism, in distinction, limits the evidence that goes into interpretation. Plain meaning rules are an example of evidentiary formalism. This Article provides a detailed analysis of each form of formalism, identifies when they are and are not likely to advance the goals of contract law, and discusses the optimal design of each type. It recommends legislative expansion of the number of contract formalities.

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INTRODUCTION

For well over a century, United States scholars and jurists have been debating the choice between formalist and contextualist rules of contract exposition. Oliver Wendell Holmes and Samuel Williston famously advocated interpreting contractual writings according to their plain meaning.[1] Arthur Linton Corbin, Karl Llewellyn, and a generation of legal realists criticized such formalism, arguing that courts should attempt to discern what parties' words meant in the context in which they

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1 *See* Oliver Wendell Holmes, *The Theory of Legal Interpretation*, 12 HARV. L. REV. 417, 420 (1899); 2 SAMUEL WILLISTON, *General Rules for the Interpretation or Construction of Contracts and the Parol Evidence Rule*, *in* THE LAW OF CONTRACTS §§ 601–62, at 1158–278 (1st ed. 1920).

were used.[2] Those antiformalist arguments influenced the drafting of both Article Two of the Uniform Commercial Code and the Second Restatement of Contracts.[3] The last decades of the twentieth century then saw a resurgence of formalism in contract law and scholarship. Under the banner of the "New Formalism," scholars marshaled economic analysis and empirical studies to argue that sophisticated parties often preferred formalism and that existing context-forward rules of interpretation stood in their way.[4] At the same time, other scholars and jurists continued to defend contextualist approaches.[5]

This Article does not take sides in the formalist-antiformalist debate. Too often the design question is framed as a simple choice between Willistonian formalism and Corbinite contextualism. Although that choice is central, it is not simple. In fact, one can distinguish two salient forms of formalism at work in contract law and a range of more and less formalist approaches to contract exposition. What lawmakers need are

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2 *See, e.g.*, ARTHUR LINTON CORBIN, CORBIN ON CONTRACTS: A COMPREHENSIVE TREATISE ON THE RULES OF CONTRACT LAW §§ 535–37, at 495–506 (2d ed. 1952). For ease of reference, the single-volume edition of Corbin's treatise is cited here, though the numbering and text are identical to that in the multi-volume edition. *See also* Arthur L. Corbin, *The Interpretation of Words and the Parol Evidence Rule*, 50 CORNELL L.Q. 161 (1965); K.N. Llewellyn, *On Our Case-Law of Contract: Offer and Acceptance I*, 48 YALE L.J. 1 (1938); K.N. Llewellyn, *On Our Case-Law of Contract: Offer and Acceptance II*, 48 YALE L.J. 779 (1939); Karl N. Llewellyn, *What Price Contract?—An Essay in Perspective*, 40 YALE L.J. 704 (1931).

3 *See, e.g.*, RESTATEMENT (SECOND) OF CONTS. § 202(1) (AM. L. INST. 1981) ("Words and other conduct are interpreted in the light of all the circumstances, and if the principal purpose of the parties is ascertainable it is given great weight."); U.C.C. § 1-303 (AM. L. INST. & UNIF. L. COMM'N 2022) (providing current rules for use of course of performance, course of dealing, and usage of trade); *id.* § 2-202 cmt. 2 (explaining the admissibility "of course of dealing, usage of trade and course of performance to explain or supplement the terms of any record stating the agreement of the parties in order that the true understanding of the parties as to the agreement may be reached").

4 For an early example, see Robert E. Scott, *A Relational Theory of Default Rules for Commercial Contracts*, 19 J. LEGAL STUD. 597 (1990). For a more recent example, see Ronald J. Gilson, Charles F. Sabel & Robert E. Scott, *Contract and Innovation: The Limited Role of Generalist Courts in the Evolution of Novel Contractual Forms*, 88 N.Y.U. L. REV. 170 (2013). For a critical overview, see David Charny, *The New Formalism in Contract*, 66 U. CHI. L. REV. 842 (1999). Perhaps the best-known judicial statement of the formalist position is Judge Kozinski's criticism of *Pacific Gas & Electric Company v. G.W. Thomas Drayage & Rigging Company*, 442 P.2d 641 (1968), in *Trident Center v. Connecticut General Life Insurance Company*, 847 F.2d 564, 569–70 (9th Cir. 1988). Judge Easterbrook has penned his share. *See, e.g.*, *Empro Manufacturing Co., Inc. v. Ball-Co Manufacturing, Inc.*, 870 F.2d 423 (7th Cir. 1989).

5 *See, e.g.*, Melvin Aron Eisenberg, *The Emergence of Dynamic Contract Law*, 88 CALIF. L. REV. 1743 (2000); Eyal Zamir, *The Inverted Hierarchy of Contract Interpretation and Supplementation*, 97 COLUM. L. REV. 1710 (1997). Courts in England have recently taken a sharply antiformalist turn, most significantly in *Investors Compensation Scheme Ltd. v. West Bromwich Building Society* [1998] 1 WLR 896. For a domestic example of judicial antiformalism, see *Teachers Insurance & Annuity Association of America v. Tribune Company*, 670 F. Supp. 491, 499 (S.D.N.Y. 1987).

not arguments for or against formalism writ large, but an understanding of when one or another type is likely to fail or succeed.

The word "formalism" itself has multiple meanings. When the subject is not interpretation, the word is commonly used in legal scholarship to describe a jurisprudential temperament that prefers rules over standards, favors deductive systems or conceptual analysis over consequentialist legal reasoning, would limit the discretion of judges when deciding cases, and would have legal rules operate independently of moral considerations, customs, and other nonlegal norms.[6] Formalism in this sense is often associated with Christopher Columbus Langdell's 1880 book *A Summary of the Law of Contract*.[7]

This Article is not about Langdellian formalism. It is about formalism in legal interpretation, or more broadly, legal exposition. In this context, "formalism" is generally understood to refer to an approach that limits the evidence adjudicators may consider when determining the meaning of legal actors' words and actions or that treats an act's legal effects as relatively context independent.[8]

This Article argues that there are two very different forms of such formalism at work in the law of contract. The first is the use of legal *formalities*, such as the seal, "as is," and "F.O.B." Properly understood, a formality works by obviating interpretation or relegating it to a subsidiary role. What matters is the words or symbols the parties use, not what those words or symbols mean. The second is *evidentiary formalism*. Evidentiary formalism limits the evidence decision-makers may consider when interpreting a text's meaning. Plain meaning rules are examples of evidentiary formalism. Whereas formalities, by conditioning legal outcomes only on an act's form, avoid interpretation entirely, evidentiary formalism constrains interpretation by limiting the evidence that goes into interpreting the act's meaning.

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6 *See generally* Richard H. Pildes, *Forms of Formalism*, 66 U. CHI. L. REV. 607 (1999) (describing the many meanings of "formalism"); Eric A. Posner, *The Decline of Formality in Contract Law*, *in* THE FALL AND RISE OF FREEDOM OF CONTRACT 61, 63–65 (F.H. Buckley ed., 1999) (describing ways in which Holmes can be viewed as a formalist); Cass R. Sunstein, *Must Formalism Be Defended Empirically?*, 66 U. CHI. L. REV. 636, 638–39 (1999) (describing the formalist attitude).

7 CHRISTOPHER COLUMBUS LANGDELL, A SUMMARY OF THE LAW OF CONTRACT (2d ed. 1880); *see, e.g.*, Thomas C. Grey, *Langdell's Orthodoxy*, 45 U. PITT. L. REV. 1 (1983).

8 *See, e.g.*, Sunstein, *supra* note 6, at 639 ("Formalism therefore entails an interpretive method that relies on the text of the relevant law and that excludes or minimizes extratextual sources of law."); Avery Wiener Katz, *The Economics of Form and Substance in Contract Interpretation*, 104 COLUM. L. REV. 496, 516 (2004); Lon L. Fuller, *Consideration and Form*, 41 COLUM. L. REV. 799, 802 (1941) (describing a "formal transaction" as one that "is abstracted from the causes which gave rise to it and which has the same legal effect no matter what the context of motives and lay practices in which it occurs"); Henry E. Smith, *The Language of Property: Form, Context, and Audience*, 55 STAN. L. REV. 1105, 1112 (2003) (treating an expression as "formal to the extent that its meaning is invariant under changes in context").

Because the difference between these two forms of formalism is commonly overlooked, the choice of where and how to adopt formalism has been treated as simpler than it is. The choice is not merely between more or less formalist rules of contract exposition. It is also between these two different forms of formalism, adjudicators should address the proper design of each, and should consider the relative advantages of each as compared to more contextualist approaches.

There are additional reasons why generic arguments for or against formalism in contract law oversimplify. Contract law addresses a remarkably broad range of transactions—everything from agreements between family members to long-term supply contracts between multinational corporations. And contract law principles apply even more broadly, from corporate governance documents to international treatises. The law properly applies different rules to different transaction types.[9] Moreover, the parties' legal relationship commonly depends on a variety of meaningful acts taking place at different times in the transaction. Although theorists tend to focus on formation, a theory should also address precontractual information sharing, precontractual agreements, modifications, waivers, repudiations, demands for adequate assurance, elections of remedies, and other acts that affect the parties' legal relationship. A theory of contract exposition should also be able to explain why courts apply different levels of formalism to these different types of contractual acts. Finally, contracts include different types of terms. Most saliently, whereas all contractual agreements include performance duties—duties whose violation will generate an action for breach—many also address the framework rules that govern legal enforcement.[10] Examples of such framework terms include conditions precedent, merger clauses, no-oral-modifications clauses, limitations on damages, and choice of law and forum clauses. It is not obvious that the same type or degree of formalism should apply to different types of terms.

This complexity means lawmakers do not need generic arguments for or against formalism, but an account of what type of formalism is likely to serve the law's purposes and when. This Article provides such an account. It first identifies the tools for contract exposition the law has at its disposal: formalities, evidentiary formalism, and nonformalist interpretation. It then examines what purposes formalist exposition can serve, in what conditions they work best, and when they are likely to fail.

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9 For more on this point, see HANOCH DAGAN & MICHAEL HELLER, THE CHOICE THEORY OF CONTRACTS (2017).

10 Compare Jody Kraus and Robert Scott's distinction between contractual ends and contractual means. Jody S. Kraus & Robert E. Scott, *Contract Design and the Structure of Contractual Intent*, 84 N.Y.U. L. REV. 1023, 1025–26 (2009).

Part I elucidates basic concepts in legal exposition: the distinction between interpretation and construction; the categories of mandatory rules, default rules, and altering rules; and a novel distinction between formalistic and interpretive altering rules, which sets the stage for that between formalities and interpretive formalism. Part II provides a more detailed analysis of contract exposition. It identifies six desiderata in the design of contract altering rules, formalist or otherwise: accuracy, knowability, low compliance costs, low adjudication costs, low relational costs, and social goals independent of party choice. Part II then discusses the too often overlooked difference between juristic and nonjuristic altering rules. Part III provides a detailed analysis of the two most salient forms of formalism in contract law. The first is the use of legal formalities, which obviate interpretation altogether. The second, exemplified by plain meaning rules, limits the evidence that goes into interpretation. Prior arguments for or against formalism in contract law have largely failed to recognize this distinction, leaving those theories incomplete. Part IV applies the analytic and normative framework developed in earlier Sections to draw lessons about formalism in contract law. It examines in detail the design of legal formalities; when evidentiary formalism is appropriate; the relational costs of contract formalism; and concludes with a legislative proposal: a model statute establishing new canonical contract formalities.

Two comments on the analysis that follows. First, legal theory is about both existing social practices and possible ones. As an exercise in contract theory, this Article is therefore about both the contract law we have and contract laws that might be. Theory of this type requires choices about what one keeps fixed and what one allows to vary. The analysis below treats as fixed, for example, the fact that parties' contractual obligations can be affected by both juristic and nonjuristic acts—though one can imagine a contract law that is purely juristic or purely nonjuristic.[11] This Article does not treat as fixed the so-called objective theory of interpretation. Because of an interest in contract exposition generally, this Article considers the full range of meanings contract interpretation might seek out—subjective and objective, contextual and acontextual, semantic and pragmatic, and so forth. These choices regarding what to keep fixed and what to vary are not given from on high. They reflect my theoretical commitments and the range of phenomena this Article wishes to explore.

Second, the two forms of formalism at work in contract law do not exhaust the ways legal exposition can be formalist. As this Article observes in Part III, in other areas of the law, formalism might be achieved

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11 *See infra* Section II.B.

by focusing on one type of meaning rather than another, which this Article calls "semantic formalism." And as this Article discusses in Part I, some rules of exposition impose requirements such as a writing, a signature, or notarization that might also be considered a type of formalism. The goal is not to catalog every possible sense of expositional formalism, but to identify and analyze two forms that are especially important in contract law: formalities and plain meaning rules. There remains more to say about the various forms of formalism in legal exposition writ large.

I. LEGAL EXPOSITION

A large portion of the law of contracts comprises rules governing how parties' words and meaningful acts affect their legal relationship. These include, inter alia, rules that govern when a contract comes into existence, such as the rules for offer, acceptance, counteroffer, rejection, and agreement; rules for determining the scope of parties' contractual duties, rights, privileges, powers, and so forth; rules for contract modifications and waivers; rules for anticipatory repudiation and adequate assurances; and rules governing the remedies available for breach, such as rules for liquidating damages and for election of remedies.

This radical mutability of parties' legal relationship is among contract law's defining features. Sophisticated parties have enormous, though not unlimited, control over when contractual obligations attach, what those obligations are, the consequences of their breach, and even how their agreement will be construed and how they can alter their obligations going forward.

This Article uses the term *exposition* to refer to the process of identifying the nonremedial legal effect of people's words and meaningful acts.[12] Legal exposition is not limited to contracts. The above definition also captures statutory interpretation, constitutional interpretation, the interpretation of wills, the interpretation of deeds, and so forth. Although this Article focuses on contract exposition, elements of its analysis apply to these other areas of law.

The qualification "nonremedial" in this Article's definition is intended to exclude the determination of whether a person's words or

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12 In a previous publication, I followed Francis Lieber and used the term "exegesis." Gregory Klass, *Contracts, Constitutions, and Getting the Interpretation-Construction Distinction Right*, 18 GEO. J.L. & PUB. POL'Y 13, 16–17 (2020); *see* FRANCIS LIEBER, LEGAL AND POLITICAL HERMENEUTICS, OR PRINCIPLES OF INTERPRETATION AND CONSTRUCTION IN LAW AND POLITICS 64 (enlarged ed. 1839); *see also* Exegesis, MERRIAM-WEBSTER, https://www.merriam-webster.com/dictionary/exegesis [https://perma.cc/X8SR-9MFV]. "Exegesis," however, is commonly associated with writings. Contract-altering acts can also include oral words and nonlinguistic acts.

actions violate a duty-imposing law in a way that gives rise to a legal remedy or punishment. Interpreting a speech act to determine whether it is false, libelous, part of a criminal conspiracy, disclosure of a trade secret, or the like is not exposition in the sense the term is used in this Article. Possible nonremedial legal effects include changes to one or more persons' first-order duties, privileges, or powers. They might also include changes to the legal remedy should a violation occur, as distinguished from the applicability of that remedy because there has been a violation.

This Part identifies basic structural features of legal exposition in general, though the concepts are illustrated with examples from contract law. The next Part discusses distinctive purposes and features of contract exposition.

A. *Interpretation and Construction*

Legal exposition comprises two distinct activities: interpretation and construction.[13] Arthur Linton Corbin defines each as follows:

> By "interpretation of language" we determine what ideas that language induces in other persons. By "construction of the contract," as the term will be used here, we determine its legal operation—its effect upon the action of courts and administrative officials. If we make this distinction, then the construction of a contract starts with the interpretation of its language but does not end with it; while the process of interpretation stops wholly short of a determination of the legal relations of the parties.[14]

Interpretation identifies the meaning of some words or actions, whereas *construction* identifies their nonremedial legal effect. For example, it is one thing to determine that a reasonable person would understand an offer made over drinks to be a joke, another to determine whether the purported offer created the power of acceptance.[15] It is one thing to determine whether the parties agreed to liquidate damages for breach, another to determine whether the amount is a penalty and therefore cannot be awarded.[16] It is one thing to determine that the parties adopted a writing "as a complete and exclusive statement of the terms of

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13 For more on the differences between interpretation and construction, see Klass, *supra* note 12, at 16–17. For more on the history of the distinction, see Gregory Klass, A Short History of the Interpretation-Construction Distinction (June 6, 2024) (unpublished manuscript), https://papers.ssrn.com/abstract=4857430 [https://perma.cc/2FR4-3T3X].

14 CORBIN, *supra* note 2, § 534, at 492 (footnotes omitted).

15 *See, e.g.*, Lucy v. Zehmer, 84 S.E.2d 516 (Va. 1954).

16 RESTATEMENT (SECOND) OF CONTS. § 356 (AM. L. INST. 1981).

the[ir] agreement,"[17] another to determine what evidence they can therefore use to prove the terms of the contract and to what end. Rules of interpretation govern the identification of meaning, whereas rules of construction govern the determination of nonremedial legal effects. Legal exposition, as the term is used in this Article, comprises both interpretation and construction.

The word "meaning" in the technical definition of "interpretation" is intended to be capacious. It is a familiar fact, for example, that contracting parties' words and actions can have different types of meanings—intended and unintended, literal and implied, objective and subjective, and so forth.[18] This Article uses "interpretation" in the broadest sense possible, leaving unspecified the types of meaning legal interpretation might address.

B. *Rules of Construction: Mandatory, Default, and Altering*

Rules of construction divide into three types: mandatory rules, default rules, and altering rules.

A *mandatory rule* specifies a legal state of affairs that applies in certain circumstances no matter what legal actors say and do.[19] The Second Restatement, for example, observes that "[e]very contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement."[20] This is a mandatory rule: every contract comes with a duty of good faith that cannot be disclaimed. Laws governing marriage and fiduciary obligations contain many mandatory rules.[21] Though these legal obligations are voluntary, they are less mutable than are most contracts. Although some regions of contract law, such as

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17 *Id.* § 210 cmt. a.

18 *See infra* Section III.B.1 (discussing types of meaning that contract interpretation can address).

19 For a detailed discussion of mandatory rules in contract law, see Eyal Zamir, featuring Ian Ayres, *A Theory of Mandatory Rules: Typology, Policy, and Design*, 99 TEX. L. REV. 283, 302–10 (2020). The modification "in certain circumstances" is meant to capture the fact that the circumstances in which the rule applies might not themselves be mandatory. For example, existence of a contract is not mandatory, but if the parties choose to enter a contract, the duty of good faith is mandatory in the circumstances.

20 RESTATEMENT (SECOND) OF CONTS. § 205 (AM. L. INST. 1981). This is not to say that the parties cannot alter the specific requirements of that obligation through their words and actions. The point is only that they cannot escape the duty altogether.

21 *See, e.g.*, Unif. Premarital Agreement Act, § 10 (AM. L. INST. & UNIF. L. COMM'N 2012) (providing that marital agreement terms concerning child custody are unenforceable); Alexander Trukhtanov, *The Irreducible Core of Trust Obligations*, 123 L.Q. REV. 342 (2007); David Hayton, *The Irreducible Core Content of Trusteeship*, *in* TRENDS IN CONTEMPORARY TRUST LAW 47 (A.J. Oakley ed., 1996).

employment and landlord-tenant law, include a fair number of mandatory rules.[22] The general law of contract includes relatively few. This is another way of saying that contractual obligations are, generally speaking, highly mutable.

A *default rule* specifies the legal state of affairs absent the right person's or persons' act or expression to the contrary.[23] Familiar contract examples include the revocability of an offer not relied upon,[24] the implied warranty of merchantability that attaches to a merchant's sale of goods,[25] and most rules governing damages for breach.[26]

Scholars often speak of default rules as "rules of interpretation" and commonly use terms like "default interpretations" or "interpretive defaults."[27] If one attends to the distinction between interpretation and construction, however, it is clear that a default rule is a rule of construction. It says what the *legal* state of affairs is when the parties have not expressed an intent one way or the other. As Corbin observes,

> [w]hen a court is filling gaps in the terms of an agreement, with respect to matters that the parties did not have in contemplation and as to which they had no intention to be expressed, the judicial process . . . may be called "construction"; it should not be called "interpretation."[28]

An *altering rule* specifies whose doing of what suffices to effect a change from an associated default.[29] A merchant selling goods, for example, can make their offer irrevocable for up to three months by expressing their intent to do so in a signed writing,[30] a seller can disclaim the implied warranty of merchantability by using words like "as is" or "with all faults,"[31] and parties can generally agree to liquidate or limit

22 For example, minimum wage laws and the mandatory warranty of habitability.

23 Scholars have paid considerable attention to the design of default rules. For an overview of design considerations, see Ian Ayres & Robert Gertner, *Majoritarian vs. Minoritarian Defaults*, 51 STAN. L. REV. 1591 (1999).

24 *See* RESTATEMENT (SECOND) OF CONTS. § 42 cmt. a (AM. L. INST. 1981).

25 *See* U.C.C. § 2-314(1) (AM. L. INST. & UNIF. L. COMM'N 2022).

26 *See* RESTATEMENT (SECOND) OF CONTS. §§ 346–52 (AM. L. INST. 1981).

27 A search of Westlaw's Law Reviews and Journals database on November 1, 2024, found 301 works using "default interpretation," "interpretive default," "default rule of interpretation," or a combination thereof.

28 CORBIN, *supra* note 2, § 534, at 494.

29 This term is taken from Ian Ayres's important work: Ian Ayres, *Regulating Opt-Out: An Economic Theory of Altering Rules*, 121 YALE L.J. 2032 (2012). *See also* Brett H. McDonnell, *Sticky Defaults and Altering Rules in Corporate Law*, 60 SMU L. REV. 383 (2007) (anticipating some of Ayres's points). In earlier work, I have discussed altering rules under the heading "opt-out rules." Gregory Klass, *Intent to Contract*, 95 VA. L. REV. 1437 (2009).

30 U.C.C. § 2-205 (AM. L. INST. & UNIF. L. COMM'N 2022).

31 *Id.* § 2-316(3)(a).

damages for breach by simply expressing their shared intent to do so.[32] More fundamentally, parties can take themselves from a default state, in which there is no contract between them, to one in which there is a contract by agreeing to an exchange.[33]

Every default comes with an altering rule, though it might not be expressly stated. To describe a legal state of affairs as a default is to say that some legal actor or actors might change it by saying or doing the right thing in the right way. Altering rules determine who must say or do what and how. Some altering rules specify the use of particular words or phrases, such as "as is." Others are more open-ended. Article Two of the Uniform Commercial Code, for example, provides: "A contract for sale of goods may be made in any manner sufficient to show agreement . . . ."[34] This rule requires only that parties express their agreement to the transaction, not that they do so in a specified way.

C. *Types of Altering Rules: Formalistic and Interpretive*

All altering rules share a tripartite structure. An altering rule provides that if (1) the right actors, (2) do the right type of act, then (3) a specified non-default legal state of affairs shall pertain. Consider the Article Two rule for firm offers. The default is that an offer is revocable.[35] Section 2-205 provides an altering rule:

> An offer by a merchant to buy or sell goods in a signed record which by its terms gives 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 . . . .[36]

This rule establishes:

(1) *the actor*: a merchant buyer or seller of goods;
(2) *the act*: a signed record assurance that the offer will be held open; and

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[32] *See* RESTATEMENT (SECOND) OF CONTS. § 356 (AM. L. INST. 1981) (regarding liquidated damages); *see also* U.C.C. § 2-719 (AM. L. INST. & UNIF. L. COMM'N 2022) (empowering parties to contractually modify or limit the remedy for breach).

[33] Some readers might find it odd to describe the no-contract state as a legal default. My goal is to provide a general theory of both the rules of contract formation and the rules that determine the terms of a contract. In that context, the no-contract state shows itself to be a default. In the antebellum South, enslaved people had no capacity to contract. *See* WILBERT E. MOORE, AMERICAN NEGRO SLAVERY AND ABOLITION: A SOCIOLOGICAL STUDY 99–101 (1971). For those enslaved people, the no-contract state of affairs was a mandatory one.

[34] U.C.C. § 2-204(1) (AM. L. INST. & UNIF. L. COMM'N 2022).

[35] *Id.* § 2-205.

[36] *Id.*

(3) *the effect*: irrevocability for the time stated or, if no time is stated, for a reasonable time, but in no case for more than three months.

This Article focuses on the second element of altering rules: the specification of acts sufficient to displace the default, which this Article calls *altering acts*.[37] Later Sections also touch on how the first and third components, actor and effect, can figure into the design of altering rules.[38]

Interpretation enters legal exposition by way of altering rules, which, again, are rules of construction. More specifically, interpretation commonly enters by way of an altering rule's specification of requisite altering acts and perhaps legal effect.

Consider again the Article Two rule for firm offers. Section 2-205 provides that to be effective, the merchant's act must satisfy three elements.[39] It must:

(a) "by its terms give[] assurance that it will be held open,"
(b) be in a record, and
(c) be signed.[40]

Determining whether the first element is satisfied—whether the right sort of assurance was given—requires interpretation, even if only to ascertain the literal meaning of the merchant's words.[41] By contrast, determining whether the second and third elements are satisfied—whether the assurance was in a record and whether it was signed—does not require interpretation. The first element requires that the offeror perform an act with the right meaning, whereas the second and third require that the act be of the right form.

Note that interpretation also figures into section 2-205's specification of legal effect. One must interpret the record to determine "the time stated." More generally, where there is more than one possible non-default term, legal effect commonly turns on the meaning of the altering act.

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37 Not all contractual acts are altering acts in this sense. Sometimes parties include language that affirms a default or even a mandatory term. Force majeure clauses are arguably an example, given the impracticability rule. *See* Farshad Ghodoosi, *Contracting Risks*, 2022 U. ILL. L. REV. 805, 818–20, 824, 840 (2022) (discussing whether force majeure clauses merely replicate the impracticability defense).

38 *See infra* Sections II.A.3 (discussing the difference between formalities whose effects are defeasible and those whose effects are indefeasible) & IV.A.1 (discussing different rules depending on the responsiveness of parties to legal rules).

39 U.C.C. § 2-205 (AM. L. INST. & UNIF. L. COMM'N 2022).

40 *Id.*

41 Recall the observations that interpretation can aim at different types of meaning. *Supra* Section I.A; *see also infra* Section III.B.1. For present purposes, this Article is agnostic as to which type of meaning interpretation does or should address.

Interpretive components of an altering rule condition legal outcomes on the meaning of altering acts, such as whether an offer gave assurances it would be kept open. Application of an interpretive component requires interpretation of the parties' words and actions. *Formal* components of altering rules, in distinction, conditions legal outcomes on formal qualities of altering acts, such as whether an offer was in a signed record. These are facts that can be ascertained without interpretation.

Any given altering rule might have only interpretive components, only formal components, or a mix. This Article uses *formalistic* to describe altering rules that include only formal components in specifying altering acts and *formalities* to denote those altering acts. Consider section 2-319 of the Code: "[W]hen the term is F.O.B. the place of shipment, the seller must at that place ship the goods in the manner provided in this Article . . . and bear the expense and risk of putting them into the possession of the carrier."[42] According to this rule, the letters "F.O.B." together with the name of a place suffice to effect the legal change. No further inquiry into what the parties or their words meant is required. The rule is a formalistic one and "F.O.B." is a formality. The section 2-316 rule for "as is" and "with all faults" is another formalistic altering rule.[43] It provides that, *ceteris paribus*, the mere use of those words is enough to exclude all implied warranties. So too are the common law and statutory rules governing the legal effect of the seal.

This Article uses *interpretive* to describe altering rules with an interpretive component. A *pure interpretive altering rule* has no formal component. The Second Restatement, for example, defines an offer as any "manifestation of willingness to enter into a bargain . . . ."[44] This is a pure interpretive rule: it does not condition the existence of an offer on any formal qualities of the act, such as the production of a writing or signature or the use of certain words. Or consider the Restatement's rule for waivers: "It is immaterial how the promisor manifests his intention to fulfill the prior duty without the performance of the condition. Words of promise or waiver, though often used, are unnecessary; in many situations non-verbal conduct is enough."[45] This is another pure interpretive altering rule.

Altering rules that have both interpretive and formal components are *mixed interpretive altering rules*. The section 2-205 rule for firm offers is a mixed interpretive rule. It requires both that a merchant seller say

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42 U.C.C. § 2-319(1)(a) (AM. L. INST. & UNIF. L. COMM'N 2022) (citing *id.* § 2-504).

43 *Id.* § 2-316(3)(a).

44 RESTATEMENT (SECOND) OF CONTS. § 24 (AM. L. INST. 1981).

45 *Id.* § 84 cmt. e.

words with the right meaning—that the offer “by its terms gives assurances that it will be held open”—and that those words be in the right form—“in a signed record.”[46]

These distinctions result in the following typology:

Figure 1: Typology of Altering Rules

		Interpretive Component	
		Yes	**No**
Formal Component	Yes	mixed interpretive (UCC rule for firm offers)	formalistic (“as is,” “F.O.B.”, the seal)
	No	pure interpretive (generic rules for agreement)	

The majority of contract altering rules fall into the two boxes on the left: the legal outcome turns, in part or in whole, on the meaning of what parties say or do. This is why interpretation is so often central in contract cases. That said, contemporary contract law also includes formalities, and the final Section of this Article argues for adding more.[47]

Altering rules of any type might themselves be mandatory or default. New York’s requirement that all door-to-door sales contracts include specific language informing the buyer of the mandatory three-day cancellation period is mandatory.[48] Parties cannot contract around it. The rule that a written contract can be modified by an oral agreement, in distinction, is a default. Courts regularly give effect to no-oral-modification clauses.[49] If an altering rule is a mere default, it comes with a higher-level rule for how parties might change it. This Article does not provide a systematic analysis of altering rules for altering rules, though Section IV.B discusses one type: the rules governing integration of a contractual writing.

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[46] U.C.C. § 2-205 (AM. L. INST. & UNIF. L. COMM’N 2022).

[47] *See infra* Section IV.D.

[48] N.Y. PERS. PROP. L. § 428(1)(a) (McKinney 1989); Vom Lehn v. Astor Art Galleries, Ltd., 380 N.Y.S.2d 532, 542 (Sup. Ct. 1976) (finding that failure to provide notice of a three-day cancellation period rendered a contract voidable by a buyer at any time).

[49] *See* U.C.C. § 2-209(2) (AM. L. INST. & UNIF. L. COMM’N 2022); Elmsford Sheet Metal Workers, Inc. v. Shasta Indus., Inc., 477 N.Y.S.2d 391, 391–92 (App. Div. 1984).

D. *Summary*

Legal exposition involves two activities: interpretation, which identifies the meaning of what parties say and do, and construction, which identifies nonremedial legal effects. Rules of construction include mandatory, default, and altering rules. A mandatory rule says what the legal state of affairs is no matter what the relevant legal actors say or do. A default rule says what the legal state of affairs is absent those actors' contrary acts or expressions. An altering rule identifies what acts or expressions by whom suffice to effect a change from a default and what that change is. Altering rules can have interpretive and formal components. Interpretive components condition legal change on the performance of acts with the right meaning; formal components on the performance of acts of the right form. Formalistic altering rules have only formal components, pure interpretive rules have only interpretive components, and mixed interpretive rules have both formal and interpretive components.

II. CONTRACT EXPOSITION

This Part examines special aspects of contract exposition. It first identifies the criteria one should use to judge a rule of contract exposition as better or worse, as a success or a failure. It then examines the difference between juristic and nonjuristic altering rules, a distinctive feature of contract law that is especially important for an understanding of contract exposition.

A. *Six Design Goals*

This Section identifies six criteria for assessing rules of contract exposition: accuracy, adjudication costs, compliance costs, relational costs, knowability, and the promotion of social goals independent of the parties' intent.[50]

Accuracy. As courts regularly intone, "[t]he fundamental, neutral precept of contract interpretation is that agreements are construed in

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[50] For other lists of relevant criteria, see Katz, *supra* note 8, at 522–36; Eric A. Posner, *The Parol Evidence Rule, the Plain Meaning Rule, and the Principles of Contractual Interpretation*, 146 U. PA. L. REV. 533, 543–47 (1998).

accord with the parties' intent."[51] This is not to say that party intent always controls or that the terms of a contract always match the parties' actual or even apparent intentions and understandings. Default terms exist because parties sometimes do not have or properly express an intent one way or another; mandatory terms exist because the law sometimes refuses to give effect to their intent. When parties have different understandings of their words and actions, the law needs to pick a winner. And sometimes the law imputes an intent that might not be there, as when parties agree to a writing one or both have not read (the so-called duty to read).[52] That said, the parties' intent, subjective or objective, actual or imputed, is generally the starting point. Because contractual obligations are by and large chosen, or voluntary, obligations, contract law is designed to condition parties' legal obligations on, *ceteris paribus*, their intentions and understandings.

The importance of accuracy provides a familiar argument for majoritarian defaults. A default that matches the preferences of most parties is more likely to reflect the intentions of any given party or parties. Accuracy is also a core design goal of altering rules, which serve first and foremost to identify when parties intend something other than the default. Contract altering rules succeed when they enable third-party adjudicators to accurately identify parties' intent.

Although accuracy is an obvious design goal, theorists disagree on how much weight to give it. Alan Schwartz and Robert Scott, for example, argue that sophisticated risk-neutral firms do not much care about accuracy: "A risk-neutral party cares about the mean of the interpretation distribution but not the variance."[53] So long as interpretive errors are as likely to benefit as to harm the firm, the cost of those inaccuracies will, in the long run, even out. From the perspective of a risk-neutral firm, "it is good enough that courts get things right on average."[54]

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51 Greenfield v. Philles Recs., Inc., 780 N.E.2d 166, 170 (N.Y. 2002). For defenses of this goal, see Lawrence M. Solan, *Contract as Agreement*, 83 NOTRE DAME L. REV. 353 (2007); E. Allan Farnsworth, *"Meaning" in the Law of Contracts*, 76 YALE L.J. 939 (1967). This Article uses "intent" in this Section almost as broadly as it uses "meaning." The legally relevant intent might be subjective, objective, or imputed. And depending on the issue to be resolved, an adjudicator might look at the parties' joint intentions, one party's communicative intent, one or both parties' intent to achieve a certain end, the parties' intent to undertake a legal obligation, one party's intent to perform, and so forth.

52 *See* RESTATEMENT (SECOND) OF CONTS. § 23 Ill. 7 & cmt. e (AM. L. INST. 1981); Heller Fin., Inc. v. Midwhey Powder Co., 883 F.2d 1286, 1292 (7th Cir. 1989) ("[I]t is no defense to say, 'I did not read what I was signing.'").

53 Alan Schwartz & Robert E. Scott, *Contract Theory and the Limits of Contract Law*, 113 YALE L.J. 541, 576 (2003).

54 *Id.* at 577.

Schwartz and Scott's argument does not succeed on its own terms. In any case, it has among its premises not only that firms are risk-neutral, but also that the primary goal in enforcing contracts between them is to maximize the joint gains of trade.[55] This is hardly the only function contract enforcement might serve, whether for contracts between firms or for contracts among other sorts of parties. A theorist who considers the purposes of contract law to include enforcing parties' moral obligations, achieving just outcomes, or supporting the culture of making and keeping agreements, for example, is likely to attach greater value to interpretive accuracy than do Schwartz and Scott. To state the obvious: the value of interpretive accuracy depends on the reason or reasons for enforcing contracts.

Limiting adjudication costs, compliance costs, and relational costs. Even if accuracy is valuable, it does not follow that adjudicators should always do everything in their power to achieve it. The costs of perfectly accurately identifying the parties' intent might be higher than either society or the parties wish to pay. Those costs come in three forms.

First are the costs of *adjudication*, both to the parties and to society. Flipping a coin to decide a dispute is cheap but highly inaccurate; a trial in which both sides are represented by counsel and introduce testimony and other evidence is likely to be more accurate and will also be more costly.

Second are the out-of-pocket costs to the parties of *complying* with an altering rule. Formal components can be more or less expensive to produce. It is cheaper to generate a writing than it is to generate a notarized writing. Interpretive components can also affect the cost of compliance. Rules of interpretation that permit less evidence of context, for example, might drive up the costs of drafting, as it takes more effort to draft a writing whose words alone unambiguously capture one's intent.

Finally, satisfying an altering rule can sometimes negatively affect the parties' extra-legal *relationship*. Saying one wants a legal protection, for example, can erode extralegal forms of trust. Although relational costs can be viewed as a type of compliance cost, it will be useful in the analysis that follows to separate them out.

Knowability. Contract law is both backward-looking and forward-looking. After a possible breach, it serves to resolve disputes and provide relief to non-breaching parties. Earlier in a transaction, it helps parties structure their relationship and coordinate their behavior to achieve their individual and shared goals. Contract law's forward-looking functions require that parties be able to know their legal obligations. More specifically, parties must be able to predict the legal effects of their words

55 *Id.* at 556 ("The contract law of commercial parties is about efficiency.").

and actions. A flip of a coin is not only relatively inaccurate but is also highly unpredictable—its results unknowable. Altering rules are generally preferable to the extent they produce knowable outcomes.[56]

Other social interests. Although contract law is designed to enforce chosen obligations, that need not be its only purpose. A law of contract might also seek to support the moral practice of making and keeping agreements, to protect vulnerable parties and prevent harm to third parties, to guide parties to valuable forms of relationships, to promote fairness, whether between the parties or in society as a whole, and so on.

The salience of other social interests is most obvious in mandatory rules. Generic mandatory rules, such as the unconscionability defense, the public policy defense, and the penalty rule, reflect social interests that do not depend on, and might run contrary to, one or both parties' intent. So too mandatory rules for specific types of contracts, such as minimum wage, antidiscrimination, and workplace safety laws.

Defaults can also be chosen to advance broader social interests. Defaults tend, to one degree or another, to stick. Parties who, all things considered, might prefer a non-default legal state of affairs sometimes fail to opt out of the default. Or parties who are unsure might use the default as a guide. Setting the default at a socially preferred outcome is therefore likely to result in more parties ending up there.[57]

Altering rules too can be designed to promote social interests. Defaults stick because of the costs of opting out. An altering rule can be designed to increase those costs, thereby impeding departures from a socially preferred default.[58] Alternatively or in addition, an altering rule might employ a shibboleth to separate out sophisticated from unsophisticated parties. Or the rule might require the performance of a socially productive act to achieve a non-default state of affairs.[59]

B. *Guidance: Juristic and Nonjuristic Altering Rules*

Ian Ayres has suggested another criterion for assessing altering rules. Ayres likens altering rules to software interfaces.[60] "An altering rule in essence says that if contractors say or do this, they will achieve a

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56 Schwartz and Scott, for example, emphasize the value of knowability. Schwartz & Scott, *supra* note 53, *passim*.

57 *See* Ayres & Gartner, *supra* note 23, *passim*.

58 *See* Ayres, *supra* note 29, *passim*.

59 Such altering rules are an analog of what Omri Ben-Shahar, David A. Hoffman, and Cathy Hwang call "nonparty defaults." Omri Ben-Shahar, David A. Hoffman & Cathy Hwang, *Nonparty Interests in Contract Law*, 171 U. PA. L. REV. 1095, 1098 (2023).

60 *See* Ayres, *supra* note 29, at 2039–42, 2063–66, 2068–71.

particular contractual result."[61] Ayres's understanding of altering rules as instructions suggests another criterion for their success: guidance. Just as a word processing program should provide clear instructions for how to change the default margins, so too the law should instruct parties on how to get the legal outcomes they wish. Ayres argues that altering rules that do not "give guidance about either the non-default options or the mechanisms for achieving them" are characteristic of "'immature' regimes where the accretion of precedent has not provided judicial disclosure guidance about particular mechanisms that are sufficient to achieve particular alternatives."[62]

Ayres, thinking like an economist, conceives of altering acts as acts intended to achieve legal outcomes. Such a conception is akin to what German legal theorists term a "Rechtgeschäft," or *juristic act*:

> The juristic act . . . is a declaration of private will directed at the realization of a legal effect, an effect that follows on the authority of the legal system because it is willed. The essence of the juristic act is found in the fact that a will directed at the realization of the legal effect is confirmed, and that the legal system issues a judgment, in recognition of that will, that gives legal effect to the desired legal arrangement.[63]

A juristic act is one that can be translated into a sentence that begins, "I/we hereby determine that," followed by a proposition describing a legal change, such as "We the Congress of the United States hereby enact that" or "I hereby determine that upon my death, my property shall be distributed as follows." Although Anglo-American legal theorists have paid limited attention to the category of juristic acts,[64] they are as common as are legal powers. The category includes legislative votes, executive orders, judicial decrees, marriage licenses, formal wills, and transfer deeds. All are expressions of the speaker's intent to change the legal state of affairs by the very expression of that intent.

A *juristic altering rule* is an altering rule that includes among its components the performance of a juristic act. The Model Written Obligations Act, for example, provides: "A written release or promise hereafter made and signed by the person releasing or promising shall not be invalid or unenforceable for lack of consideration, if the writing also

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61 *Id.* at 2036.

62 *Id.* at 2053.

63 1 MOTIVE ZU DEM ENTWURFE EINES BÜRGERLICHEN GESETZBUCHES FÜR DAS DEUTSCHE REICH 126 (J. Guttentag 1888) (Ger.) (author's translation).

64 An important exception was John Henry Wigmore. *See* 5 JOHN HENRY WIGMORE, A TREATISE ON THE ANGLO-AMERICAN LAW OF EVIDENCE IN TRIALS AT COMMON LAW § 2401, at 238–39 (2d ed. 1923) (describing the category of "jural acts"). The idea of a juristic act is essential to Wigmore's account of the parol evidence rule. *See id.*

contains an additional express statement, in any form of language, that the signer intends to be legally bound."[65] The model rule is a juristic one, as it requires the signer's "express statement . . . that the signer intends to be legally bound."[66] Similarly, Section 21 of the Second Restatement provides that "a manifestation of intention that a promise shall not affect legal relations may prevent the formation of a contract."[67] Yet another example can be found in judicially created rules for the enforcement of preliminary agreements.[68] It is not uncommon during negotiations for parties to memorialize their agreement to some material terms with the expectation that they will continue to negotiate others. If negotiations later break down, the question can arise whether their preliminary agreement created a duty to negotiate in good faith. In a foundational case, Judge Leval described the default and altering rule:

> There is a strong presumption against finding binding obligation in agreements which include open terms, call for future approvals and expressly anticipate future preparation and execution of contract documents. Nonetheless, if that is what the parties intended, courts should not frustrate their achieving that objective or disappoint legitimately bargained contract expectations.[69]

This too is a juristic altering rule. Whether the preliminary agreement is legally binding turns on whether the parties manifestly intended it to be.

The above examples concern the existence *vel non* of a contract. There also exist juristic altering rules for certain contract terms. Parties can decide what law shall govern their agreement, for example, by agreeing to a choice of law clause. A choice of law clause expresses the parties' intent to select a governing law by the very expression of that intent. The same is true of other terms that concern not the substance of the parties' agreement, but how it will be enforced. Examples of such framework terms include choices of forum, liquidated damages, limitations on consequential damages, integrations of writings, and arbitration provisions. Parties can adopt such terms by expressing their intent to make that legal change. The relevant altering rules are, in other words, juristic ones.

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65 *An Act to Validate Certain Written Transactions Without Consideration, and to Make Uniform the Law Relating Thereto*, *in* HANDBOOK OF THE NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS AND PROCEEDINGS OF THE THIRTY-FIFTH ANNUAL MEETING 584, 584 (1925).

66 *Id.*

67 RESTATEMENT (SECOND) OF CONTS. § 21 (AM. L. INST. 1981).

68 For a more detailed discussion of the rule for preliminary agreements, see Klass, *supra* note 29, at 1480–87.

69 Teachers Ins. & Annuity Ass'n of Am. v. Tribune Co., 670 F. Supp. 491, 499 (S.D.N.Y. 1987).

That said—and this is crucial—many contract altering rules do not require that parties express or manifest an intent to effect the associated legal change. They are *nonjuristic*.

Consider the most fundamental of contract altering rules: the rule for formation. In the United States, "[n]either real nor apparent intention that a promise be legally binding is essential to the formation of a contract."[70] The rule is expressly *nonjuristic*. Corbin explains:

> There seems to be no serious doubt that a mutual agreement to trade a horse for a cow would be an enforceable contract, even though it is made by two ignorant persons who never heard of a legal relation and who do not know that society offers any kind of a remedy for the enforcement of such an agreement.[71]

Restatement formulations do not always capture everything in a rule's application, and some scholars have argued that, in fact, U.S. contract law sorts for parties' contractual intent.[72] Moreover, the black letter rules in England and other common law countries are that an intent to contract is necessary.[73] That said, there is no question but that the altering acts that generate contracts need not express or themselves evince the parties' intent to effect a legal change. Implied-in-fact contracts prove the point. Consider a Second Restatement example:

> A, on passing a market, where he has an account, sees a box of apples marked "25 cts. each." A picks up an apple, holds it up so that a clerk of the establishment sees the act. The clerk nods, and A passes on. A has promised to pay twenty-five cents for the apple.[74]

Here there is no "declaration of private will directed at the realization of a legal effect."[75] There is not even an express agreement. There are merely two nonverbal, but in context, meaningful acts—holding the apple up and a nod in response—that together establish that an agreement has been reached. That is enough to create a contract.

This is not to deny that parties often enter contracts manifestly intending to alter their legal relationship. When two companies negotiate, draft, and execute a merger or acquisition agreement, they express their

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70 RESTATEMENT (SECOND) OF CONTS. § 21 (AM. L. INST. 1981).

71 CORBIN, *supra* note 2, § 34, at 53.

72 *See, e.g.*, Randy E. Barnett, *Some Problems with Contract as Promise*, 77 CORNELL L. REV. 1022, 1029 (1992); Randy E. Barnett, *A Consent Theory of Contract*, 86 COLUM. L. REV. 269, 313 (1986).

73 For detailed discussions, see Klass, *supra* note 29, at 1443–60; PRINCE SAPRAI, CONTRACT LAW WITHOUT FOUNDATIONS: TOWARD A REPUBLICAN THEORY OF CONTRACT LAW 71–101 (2019).

74 RESTATEMENT (SECOND) OF CONTS. § 4 cmt. a, illus. 2 (AM. L. INST. 1981).

75 MOTIVE ZU DEM ENTWURFE EINES BÜRGERLICHEN GESETZBUCHES FÜR DAS DEUTSCHE REICH, *supra* note 63, at 126.

shared intent to enter a contract. The same is true when a homeowner and homebuyer execute a contract of sale, or when a software user clicks an HTML button indicating their agreement to an unread end user license agreement.[76] The point is that the expression of that intent is not required. The basic formation rule is not a juristic one.

Many other contract altering rules are similarly nonjuristic. The *Hadley* rule entails that sharing information about probable losses in case of breach can increase recoverable damages.[77] The rule is an altering rule: the performance of an act with the right meaning changes the measure of damages. It does not, however, require a juristic act. The sharing of information suffices. Or consider Section 2-313 of the Code, which provides that any affirmation of fact, description of goods, or sample or model made by the seller that is part of the basis of the bargain is enough to create a warranty. "It is not necessary . . . that the seller use formal words such as 'warrant' or 'guarantee' or that he have a specific intention to make a warranty . . . ."[78] Post-formation altering acts can also be nonjuristic. A party waives a condition on their obligation merely by expressing an intent to perform despite its nonoccurrence.[79] And a party can commit anticipatory breach simply by stating they will be unable to perform, regardless of whether they know or appear to know that the statement constitutes a repudiation.[80]

The prevalence of nonjuristic altering rules in contract law distinguishes contracts from constitutions, statutes, regulations, oaths of office, deeds, wills, and many other power-conferring laws. Although contract law gives parties the power to intentionally effect legal change, it rarely requires that they express that intent. Although a juristic act can be sufficient to effect a contractual change, it is rarely necessary to do so.[81]

What does all this mean with respect to guidance? Ayres's comparison of altering rules to instructions is clearly correct with respect to juristic altering rules. Because juristic altering rules aim to give persons the power to effect legal change when they wish, they are like instructions. And like instructions, they succeed when they provide users clear guidance regarding how to achieve the outcome a user desires.

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76 *See* Tess Wilkinson-Ryan, *Intuitive Formalism in Contract*, 163 U. PA. L. REV. 2109, 2127 (2015) (providing empirical evidence that consumers believe themselves to be legally bound by unread terms to which they have manifested assent).

77 *See* Hadley v. Baxendale (1854) 156 Eng. Rep. 145; RESTATEMENT (SECOND) OF CONTS. § 351 (AM. L. INST. 1981).

78 U.C.C. § 2-313(2) (AM. L. INST. & UNIF. L. COMM'N 2022).

79 RESTATEMENT (SECOND) OF CONTS. § 84(1) (AM. L. INST. 1981).

80 *Id.* § 250.

81 I have argued that this distinctive feature is essential to understanding the reasons for contractual liability. Gregory Klass, *Three Pictures of Contract: Duty, Power and Compound Rule*, 83 N.Y.U. L. REV. 1726, 1727–34 (2008).

Guidance can be less relevant to the success of nonjuristic altering rules. When the goal is to condition legal outcomes on an act that is not intrinsically legal—entering into an agreement, making a representation about the quality of the goods, expressing an intention to perform despite the nonoccurrence of a condition—the altering rule should not be understood as a set of instructions for effecting a legal change. Because a nonjuristic altering rule does not assume the parties intend to effect a legal change, there might be no expectation that the parties will use the rule instrumentally. Though knowability of outcomes remains an important consideration in the design of such rules, guidance may not be essential to their success.

C. *Summary*

Rules of contract construction can be evaluated along six dimensions: whether the rule enables third-party adjudicators to accurately identify parties' intentions; the costs of adjudication under the rule; the costs to parties of complying with the rule; the rule's impact, if any, on parties' relationships; the knowability of legal outcomes; and whether the rule advances other social goals. Altering rules can also be designed to give guidance to parties on how to achieve the legal results they wish. Providing such guidance is important to the success of juristic altering rules; it is not essential to the success of nonjuristic altering rules.

III. TWO FORMS OF FORMALISM IN CONTRACT LAW

Scholars and jurists commonly describe contract formalism as if it were just one thing. Parts I and II have provided the materials for a more complex account. In fact, the law of contracts contains two very different forms of formalism: formalities and plain meaning rules. This Part describes each in greater detail. Part IV draws lessons for legal design.

A. Formalities

A *formalistic altering rule* conditions legal change solely on the formal properties of what the parties say and do, as distinguished from the meaning of those acts. A *formality* is an altering act that satisfies a formalistic altering rule. As this Section discusses, examples of formalities include the seal, "F.O.B." plus the name of a place, "as is" in a contract for the sale of goods, and boilerplate language that is automatically given the same legal effect in different transactions. A formality effects a legal

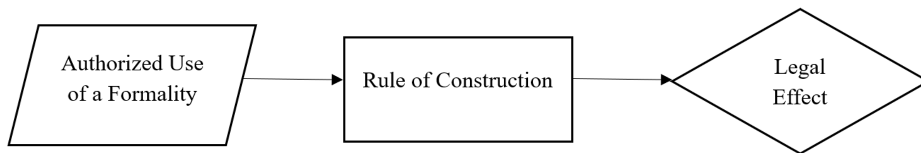
change solely by virtue of its formal qualities, as distinguished from its meaning.

1. Formalities and Formalism

Legal formalities are familiar creatures. Ian Ayres calls them "passwords"; Charles Goetz and Robert Scott refer to them as "invocations"; and Karl Llewellyn terms them "formal acts."[82] In Rudolf von Jhering's canonical explanation, "[L]egal formalities relieve the judge of an inquiry *whether* a legal transaction was intended, and—in case different forms are fixed for different legal transactions—*which* was intended."[83]

The process of exposition under a formalistic altering rule is relatively simple, and can be represented as follows:

Figure 2: Structure of Formalistic Expression



The relationship between formalistic altering rules and generic senses of "formalism" is not difficult to see. Legal formalities work by circumventing interpretation altogether. To determine the legal state of affairs, an adjudicator need look only to the use of the formality, not at its ordinary meaning, the user's intent, or how it should be understood in the circumstances.[84] The application of a formalistic altering rule therefore requires little evidence beyond what was said or done, and the outcome is largely context insensitive. This is not to say extrinsic evidence cannot enter. Except in the most extremely formalistic altering rules, use of a contract formality does not preclude the introduction of context evidence to show duress, misrepresentation, mistake of fact, or another invalidating cause. Use of a formality does not, generally speaking,

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82 Ayres, *supra* note 29, at 2080–83; Charles J. Goetz & Robert E. Scott, *The Limits of Expanded Choice: An Analysis of the Interactions Between Express and Implied Contract Terms*, 73 CALIF. L. REV. 261, 282 (1985); Llewellyn, *supra* note 2, at 711.

83 Fuller, *supra* note 8, at 801 (quoting RUDOLF VON JHERING, II GEIST DES RÖMISCHEN RECHTS 494 (8th ed. 1921)); *see also* Neil MacCormick & Joseph Raz, *Voluntary Obligations and Normative Powers*, 46 PROC. ARISTOTELIAN SOC'Y 59, 81 (1972) (describing the function of legal formalities).

84 One might say that a formality has a *legal* meaning, which is the legal effect attached to it. Identifying that meaning does not, however, require interpretation. Consider, for example, the sentence: "cheating on your taxes *means* you risk a penalty should you be audited." Sometimes "meaning" is used in a non-interpretive sense.

preclude raising a formation defense. And as will be discussed below, defeasible formalistic altering rules create only a presumption of legal change, which might be overcome by interpretive evidence of the parties' contrary intent.[85] In all these cases, however, the evidence is relevant to show only that the formality has malfunctioned, has been redesigned, or is rebutted. In the first instance, formalities support, and even demand, a high degree of formalism.

Although in their application formalities relieve courts from interpreting the parties' intent, the purpose of a legal formality is to provide a cheap and effective tool for parties to realize their intent. As Lon Fuller observes, "[F]orm offers a legal framework into which the party may fit his actions, or, to change the figure, it offers channels for the legally effective expression of intention."[86] Interpretation of parties' words and actions can be prone to error and its results difficult to predict. By obviating the need for interpretation, a formalistic altering rule aims to provide parties an instrument for realizing their legal intentions, a tool for getting the legal result they want.[87] So long as all parties are familiar with the tool, mechanical application of the formalistic rule is likely to produce intended outcomes.

The successful use of a formality is a juristic act. It is the expression of an intent to effect the legal change associated with the formality through the very expression of that intent in the formality. Knowingly affixing a seal to a writing, including "F.O.B." in written contract for the sale of goods, or stating that goods are sold "as is" are each the expression of intent to effect the associated legal change by way of that expression. Formalistic altering rules are therefore perforce also juristic altering rules. Interpretive altering rules, in distinction, can be juristic or nonjuristic, depending on whether they require expression of an intent to effect the associated legal change.

The formalistic altering rules found in contract law can be further distinguished along two dimensions: the character of the altering act and the character of its legal effect.

2. Pure Formalities and Ordinary Language Formalities

Consider the primordial common law contract formality: the seal. The form of the seal has changed over time. Originally it was an impression in wax affixed to the writing; later a paper wafer glued to the

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[85] *See infra* Section III.A.3.

[86] Fuller, *supra* note 8, at 801.

[87] This is not to say this is the only function a formality can have. *See supra* Section II.A (mentioning impeding and separating formalities). *See generally infra* Section IV.A.4.

writing sufficed; still later, the words "seal" or the letters "L.S." (*locus sigilli*) opposite a signature were enough.[88] Although the forms differed, none was drawn from everyday English or had an obvious nonlegal meaning.

An altering act that has no nonlegal meaning a *pure formality*. Contract law contains a number of pure formalities. Although the Uniform Commercial Code renders the seal inoperative for the sale of goods,[89] it provides for several pure formalities. For example, Article Two attaches to "F.O.B.," "F.A.S.," "C.I.F.," and "C.&F." precisely defined effects on the seller's legal obligations to ship.[90] Although the terms originated in ordinary language ("free on board," "free alongside," etc.), the initialisms today operate as pure formalities. They do not wear their meanings on their sleeves. The fact that they do not have ordinary language meanings puts the user on notice that each is a technical term, to which specific legal consequences are likely to attach. This is the advantage of a pure formality: a person is unlikely to use it unless they intend to perform a legal act, and a person encountering it is likely to recognize it as a legal term of art. At the same time, a pure formality does not inform the user of its legal effects. A buyer who encounters "F.O.B." in a seller's offer must already know its legal effect or consult a lawyer, law book, or the internet to discover it.

Other formalities are built out of ordinary language. A formality that has a nonlegal meaning is an *ordinary-language formality*. The Code contains ordinary-language formalities as well. Examples include "as is" and "with all faults," each of which operates to exclude all implied warranties,[91] and "net landed weights," "payment on arrival," and "no arrival, no sale," which govern payment and shipping terms.[92] The advantages and disadvantages of an ordinary-language formality are the inverse of those of a pure formality. Because an ordinary-language formality is constructed out of words with nonlegal meanings, it might not put a user on notice that they are performing an act with a specified legal effect. A nonsophisticated buyer might not know that there exist implied warranties of title, merchantability, and fitness, much less that

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88 Frederick E. Crane, *The Magic of the Private Seal*, 15 COLUM. L. REV. 24, 24–25 (1915).

89 U.C.C. § 2-203 (AM. L. INST. & UNIF. L. COMM'N 2022).

90 *Id.* § 2-319 to -320.

91 *Id.* § 2-316(3)(a). Although the rule is written as if the phrases are mere examples, in practice it establishes these ordinary-language terms as sufficient to achieve the relevant legal effect. *See, e.g.*, Meyer v. Alex Lyon & Son Sales Managers & Auctioneers, Inc., 889 N.Y.S.2d 166 (App. Div. 2009) (holding that an "as is" clause disclaimed all implied warranties without further inquiry); Welwood v. Cypress Creek Ests., Inc., 205 S.W.3d 722 (Tex. App. 2006) (same); Prudential Ins. Co. of Am. v. Jefferson Assocs., Ltd., 896 S.W.2d 156 (Tex. 1995) (same); Warner v. Design & Build Homes, Inc., 114 P.3d 664, 668–69 (Wash. Ct. App. 2005) (same).

92 U.C.C. §§ 2-321, -324 (AM. L. INST. & UNIF. L. COMM'N 2022).

the appearance of "as is" in the contract functions to extinguish all three. But an ordinary-language formality can use words that describe the relevant legal consequences. "As is" and "with all faults" at least communicate to the unsophisticated user something about their legal effects.

The above ordinary-language formalities, though originating in customary usage, are today established by statute. Scholars have suggested that the judicial construction of boilerplate contract language—strings of words that appear unchanged across many contractual writings—can be usefully employed to create new formalities. In an influential 1985 article, Charles Goetz and Robert Scott suggest that "[s]killful use of the [plain meaning] presumption by courts will, over time, increase the supply of officially recognized invocations [i.e., formalities] and other express conventions."[93] Marcel Kahan and Michael Klausner have argued that "[i]nterpretation of standard terms should be treated like the interpretation of laws: Judges, not juries, should interpret them, and their interpretation should have precedential value."[94] More radically, Ian Ayres suggests that "[i]n deciding interpretation disputes, and in fact in deciding any contractual issue concerning defaults, judges should presumptively provide in their decisions contractual language that would allow future contractors to achieve the results desired by the losing party."[95] Ayres's idea is that such dicta would generate new formalities parties could employ to get the legal outcomes they desire.

An ordinary language formality generated by the judicial construction of standard language is a *boilerplate formality*. Section IV.A.2 discusses the advantages and disadvantages of boilerplate formalities. For the moment it suffices to note that except in a few specialized areas, the boilerplate formality is a *rara avis*. One court's interpretation of contract language typically does not bind other courts

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[93] Goetz & Scott, *supra* note 82, at 316; *see also id.* at 282 (defining "invocations" to mean "terms that, once deliberately called upon, have a legally circumscribed meaning that will be heavily—perhaps even irrebuttably—presumed"); *id.* at 288 ("A . . . critically important benefit of standardized formulations is the reliability that results from the process of 'recognition.' A term is recognized when it is identified through adjudication or statutory interpretation and blessed with an official meaning. . . . Contract interpretation therefore serves to determine and announce relatively reliable definitions of contractual formulations that are protected by official acceptance.").

[94] Marcel Kahan & Michael Klausner, *Standardization and Innovation in Corporate Contracting (Or "The Economics of Boilerplate")*, 83 VA. L. REV. 713, 765 (1997); *see also* Michael Klausner, *Corporations, Corporate Law, and Networks of Contracts*, 81 VA. L. REV. 757, 776 (1995) (arguing that network benefits accrue from the fact that "[a] judicial opinion that interprets one corporation's contract term in effect embeds that interpretation in the contracts of all firms that use the same term").

[95] Ayres, *supra* note 29, at 2055.

considering different transactions using the same language.[96] The reasons are substantive, procedural, and factual. The substantive reason is that the primary goal of contract exposition is to determine the parties' intent. Because parties to different transactions can attach different meanings to the same words, the interpretation of even standard language is generally unsuitable for the application of stare decisis. Several aspects of U.S. procedural law also render judicial decisions ill-suited to the creation of widely applicable formalities. The United States does not have a generally applicable federal law of contract, and a court's decision of law in one U.S. jurisdiction does not bind courts in another. Even within a single jurisdiction, one trial court's decision of law is not binding on another trial court. Add to the above the familiar fact of verbal drift—lawyers' relentless tinkering with standard language[97]—and the idea of widespread boilerplate formalities begins to look somewhat far-fetched.

That said, judicially created formalities do occasionally appear.[98] When a statute or regulation requires that certain language be included in a contractual writing, courts have suggested that it should be interpreted uniformly and in accord with the purpose of the law requiring that language.[99] Where all or nearly all transactions in a market employ standard language drafted by an industry association and there are significant gains from uniform terms, courts tend to rely on one another's interpretations of that standard language.[100] And courts certifying consumer contract class actions have recently found common issues of law to predominate by applying Section 211(2) of the Second Restatement,[101] which provides that a standardized agreement "is interpreted wherever reasonable as treating alike all those similarly

96 As the Fifth Circuit observed: "[T]he determination of ambiguity, like other fact questions, will sometimes be a question to be answered by the judge and not the jury. . . . The determination, however, does not become imbued with *stare decisis* effect just because a judge made it." S. Hampton Co. v. Stinnes Corp., 733 F.2d 1108, 1115 n.5 (5th Cir. 1984).

97 *See* John F. Coyle & W. Mark C. Weidemaier, *Interpreting Contracts Without Context*, 67 AM. U. L. REV. 1673, 1675 (2018).

98 For a more detailed mapping of judicially created formalities, see Gregory Klass, *Boilerplate and Party Intent*, 82 LAW & CONTEMP. PROBS. 105, 112–15 (2019).

99 *See, e.g.*, Kolbe v. BAC Home Loans Servicing, LP, 738 F.3d 432, 442 (1st Cir. 2013) (en banc) (Lynch, C.J.) ("When dealing with uniform contract language imposed by the United States, it is the meaning of the United States that controls.").

100 *See, e.g.*, *In re* Lehman Bros. Holdings Inc., No. 8-13555, 2015 WL 7194609, at *11 (S.D.N.Y. Sept. 16, 2015) ("To the extent they have adopted the ISDA standard forms, it is reasonable to infer that the parties have no quarrel with ISDA's intention that 'transactions that use ISDA standard form documents and definitions . . . are enforced so as to promote legal certainty and hence, market stability.'" (quoting Brief for Cadwalader, Wickersham & Taft LLP as Amicus Curiae Supporting Defendant-Appellant at 6, AON Fin. Prods. v. Societe Generale, 476 F.3d 90 (2d Cir. 2007) (No. 6-1080-cv), 2006 WL 4877188)).

101 *See infra* note 176 (citing exemplar cases).

situated, without regard to their knowledge or understanding of the standard terms of the writing."[102] Boilerplate formalities, though uncommon, are not unknown.

To summarize: There are two broad categories of formalities. Pure formalities, such as the seal or "F.O.B.," are signs, signals, or acts that have no obvious nonlegal meaning. Ordinary-language formalities, such as "as is" or "with all faults," attach legal effects to words that also have nonlegal meanings. Within the category of ordinary-language formalities one can further distinguish between those created by legislation or custom and those created by the application of stare decisis to the judicial interpretation of boilerplate.

3. Defeasible and Nondefeasible Formalities

One can also categorize formalities according to their legal effects, which might be either dispositive or merely presumptive, in other words, nondefeasible or defeasible.

The history of the private seal provides a helpful example. Williston reports that at one time no evidence of a party's contrary intent would alter a seal's legal effect: "If the forms are observed, the obligation is binding. . . . [A]t common law mutual assent or any intention on the part of either obligor or obligee was entirely unnecessary."[103] Even fraud and duress were no defense: "[O]ne whose seal was attached to an obligation was bound, even though the seal had been stolen and attached to the instrument without his consent."[104] Such a rule is *nondefeasible*: the legal effects of the formality are mandatory. Evidence of the legal actor's contrary intent will not alter the formality's legal effect.

Over time, the effects of the seal became increasingly *defeasible*. By the late twentieth century, the Second Restatement stated that "[t]he adoption of a seal may be shown or negated by any relevant evidence as to the intention manifested by the promisor."[105] At this point, the formality operated to establish only a new default legal state of affairs: its

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102 RESTATEMENT (SECOND) OF CONTS. § 211(2) (AM. L. INST. 1981).

103 WILLISTON, *supra* note 1, § 205, at 412; *see also* JAMES BARR AMES, LECTURES ON LEGAL HISTORY AND MISCELLANEOUS LEGAL ESSAYS 98 (1913) (describing the early history of the seal).

104 WILLISTON, *supra* note 1, § 205, at 412.

105 RESTATEMENT (SECOND) OF CONTS. § 98 cmt. a (AM. L. INST. 1981); *see also id.* § 96 cmt. b ("[A] document which bears a seal does not establish its own authenticity. Evidence of extrinsic circumstances may be necessary to show that a promisor affixed or adopted a seal and that the document was delivered."); 1 RICHARD A. LORD, WILLISTON ON CONTRACTS § 2:2 n.11 (4th ed. 1990); Eric Mills Holmes, *Stature and Status of a Promise Under Seal as a Legal Formality*, 29 WILLAMETTE L. REV. 617, 636–37 (1993) (discussing the modern requirement of a party's intent to deliver the sealed instrument).

use effected the legal change only absent evidence of the user's contrary intent. Altering rules of this type are defeasible. The altering act's effect is a new default legal state of affairs, which might be modified by additional altering acts or other evidence of the parties' contrary intent.

Keeping with its broader strategy of preferring default to mandatory rules,[106] Article Two's formalistic altering rules are all expressly defeasible. "As is" and "with all faults" operate to exclude all implied warranties "unless the circumstances indicate otherwise."[107] And each of the provisions providing legal meanings of various shipment terms—"F.O.B.," "F.A.S.," etc.—is qualified with "[u]nless otherwise agreed."[108] These altering rules are both formalistic and defeasible. The use of words of the right form suffices to effect a change in the legal state of affairs, while each leaves the door open for further interpretive inquiry into the parties' actual intent.

The distinction between defeasible and nondefeasible altering rules is independent of that between pure and ordinary language formalities. A pure or ordinary language formality might be defeasible or nondefeasible.

B. *Interpretive Formalism*

Contract law has its share of formalities, but they hardly dominate. The list of contract formalities is relatively short. And there are no formalities associated with important acts such as making an offer, accepting an offer, expressly warranting the quality of goods, liquidating damages, integrating a writing, waiving a condition, or repudiating a contract.[109] These legal changes can be made only when one or both parties say or do something with the right meaning. In addition, where formalistic altering rules exist, they are today almost always accompanied by interpretive altering rules.[110] Words or actions with the right meaning often also suffice to effect the legal change. And when a formality is defeasible, its legal effect might be altered by words or actions with the

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106 U.C.C. § 1-302(a) (AM. L. INST. & UNIF. L. COMM'N 2022) ("Except as otherwise provided . . . the effect of provisions of [the Uniform Commercial Code] may be varied by agreement.").

107 *Id.* § 2-316(3)(a).

108 *Id.* §§ 2-319 to -325.

109 *See* RESTATEMENT (SECOND) OF CONTS. § 24 (AM. L. INST. 1981) (offers); *id.* § 50 (acceptances); *id.* § 84 (waivers); *id.* §§ 209–10 (integrations); *id.* § 250 (repudiations); *id.* § 256 (liquidations of damages); U.C.C. § 2-313 (AM. L. INST. & UNIF. L. COMM'N 2022) (express warranties).

110 *See, e.g.*, U.C.C. § 2-319 to -325 (AM. L. INST. & UNIF. L. COMM'N 2022) (defining various formalities without requiring that any be used to effect the associated legal change).

right meaning. For these reasons, interpretive altering rules are everywhere in contract law.

Whereas formalistic altering rules are always formal, an interpretive altering rule can be more formal or less formal. John Henry Wigmore identifies two questions any law of interpretation must answer: "The first question must always be, What is the *standard* of interpretation? The second question is, In what *sources* is the tenor of that standard to be ascertained?"[111] By "standard of interpretation" Wigmore means the *type* of meaning the rule seeks to identify; by "sources" he means the *evidence* that the rule permits an interpreter to consider. The answers to each can produce interpretive altering rules that are more formal or less formal.

1. Semantic Formalism

An interpretive altering rule requires that one or both parties say or do something with the right meaning. As noted in Section I.A, the word "meaning" itself has multiple meanings. People interpret the meanings of historical events, social institutions, novels, metaphors, dreams, a moment of silence, a slip of the tongue, a glance across the room, a constitution, a statute, a judicial opinion, and of course the words and actions of persons who might or might not have entered a contract. A single altering act can have different types of meaning: a literal meaning in general usage, a conventional meaning within a local community, the meaning intended by the speaker, the communicative intent a reasonable person might attribute to the speaker, and so forth.

Especially salient to legal exposition is the distinction philosophers and linguists draw between semantic meaning and pragmatic meaning.[112] The *semantic meaning* of a word or string of words is, roughly speaking, its conventional meaning, what is sometimes referred to as its "literal" or "dictionary" meaning. The *pragmatic meaning* of a text or utterance is the meaning the speaker or writer appears to intend the words to convey.[113]

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[111] WIGMORE, *supra* note 64, § 2458, at 367.

[112] These are not the only types of meaning that contract interpretation might address. Contract interpretation might seek out the parties' beliefs and intentions, rather than the communicative content of their acts. It might look to local usages of trade or to broader conventional meanings; and, of course, it can look to either the objectively reasonable meanings or subjectively understood ones.

[113] The above definitions of "semantic meaning" and "pragmatic meaning" are the ones most useful for legal analysis. Theorists have suggested others. Robyn Carston identifies five separate ways scholars have tried to draw the distinction between semantic meaning and pragmatic meaning. Robyn Carston, *Linguistic Communication and the Semantics/Pragmatics Distinction*,

Often semantic and pragmatic meaning coincide. People often say what they mean. The two types of meaning come apart when a speaker intends or appears to intend that their words to convey something other than their conventional meaning. In *Embry v. Hargadine, McKittrick Dry Goods Co.*, for example, a company president allegedly said to an employee threatening to quit if not given a new contract: "Go ahead, you're all right. Get your men out, and don't let that worry you."[114] The words' semantic meaning was that the employee should get back to work and should not worry about the contract. The court found, however, that in context "no reasonable man would construe that answer to Embry's demand that he be employed for another year, otherwise than as an assent to the demand."[115] Although the court did not put it this way, the pragmatic meaning of the manager's words departed from their semantic meaning, and it was the pragmatic meaning that controlled.

An interpretive altering rule that conditions legal outcomes on the semantic meaning of an altering act, as distinguished from its pragmatic meaning, is an example of what this Article calls *semantic formalism*. Such an altering rule is a form of formalism because, as compared to pragmatic meaning, semantic meaning is relatively context independent and requires less evidence to identify.

Although a few contract theorists have advocated semantic formalism,[116] it is not a feature of contemporary contract law. The interpretation of even integrated contractual writings looks to their pragmatic, not semantic, meanings. As will be discussed below, even in highly formalist jurisdictions, if a writing's literal meaning does not correspond to the parties' apparent purpose, a court will look to its intended meaning.[117] Williston, in the first edition of his treatise, formulated the rule:

> [I]n giving effect to the general meaning of a writing particular words are sometimes wholly disregarded, or supplied. Thus "or" may be given the meaning of "and," or vice versa, if the remainder of the agreement shows that a reasonable person in the position of the parties would so understand it.[118]

165 SYNTHESE 321, 322 (2008). For other discussions of ways of drawing the distinction, see KRISTIN BÖRJESSON, THE SEMANTICS-PRAGMATICS CONTROVERSY 293–98 (Anita Steube ed., 2014), and Kent Bach, *The Semantics-Pragmatics Distinction: What It Is and Why It Matters*, *in* LINGUISTISCHE BERICHTE 33–34 (Eckard Rolf ed., 1997).

114 105 S.W. 777, 777 (Mo. Ct. App. 1907).

115 *Id.* at 779.

116 *E.g.*, Schwartz & Scott, *supra* note 53, at 547.

117 *See infra* Section III.B.2.b.

118 WILLISTON, *supra* note 1, § 619, at 1199 (footnotes omitted).

When the whole of a writing evinces a purpose contrary to the semantic meaning of one of its clauses, the parties' apparent intentions—the writing's pragmatic meaning—control.

Contract law's emphasis on pragmatic meaning is unsurprising. As discussed in Part II, the most basic (if not only) goal of contract altering rules is to accurately identify the parties' intent. As the Second Restatement puts the point, "[T]he primary search is for a common meaning of the parties, not a meaning imposed on them by the law."[119] When admissible evidence shows that parties intended something other than the conventional meaning of their words, courts look to the words' pragmatic rather than semantic meaning. Semantic formalism is not a feature of contract law.

This arguably distinguishes contract interpretation from the interpretation of public laws.[120] The most common arguments for construing a constitution, statute, regulation, executive order, or judicial opinion according to its semantic meaning do not apply to contract-altering acts. Whereas the text of a public law is addressed to the population at large and to persons far in the future, for whom semantic meaning can be a more effective method of communication,[121] many contractual agreements are communications between two parties and take place against a shared background understanding, where the pragmatic meaning is clear. Whereas a focus on semantic meaning in statutory interpretation arguably serves as a means of limiting judicial discretion, on the theory that the conventional meaning of words is more certain than the purpose they are used for,[122] contract interpretation raises no such separation-of-powers issues. And there are interests at stake in contract law with no public law analogs. These include the parties' autonomy interest in controlling their legal relationship and, in some transactions, society's interest in congruence between parties' legal and moral obligations. A contracting party whose words are interpreted by a court in a way they could not reasonably anticipate—that is contrary

119 RESTATEMENT (SECOND) OF CONTS. § 201 cmt. c (AM. L. INST. 1981).

120 This paragraph touches on a topic that would take much more analysis to fully unpack. It does not, for example, discuss differences within contract law—such as differences between the interpretation of oral agreements, negotiated contractual writings, form contracts, adhesive consumer contracts, and so forth.

121 *See* William N. Eskridge, Jr., *The New Textualism*, 37 UCLA L. REV. 621, 667 (1990) ("By focusing on the plain meaning a statute would have for the ordinary, reasonable reader, the new textualism has the intuitive appeal of looking at the most concrete evidence of legislative expectations and at the material most accessible to the citizenry. The statutory text is what one thinks of when someone asks what the 'law' requires.").

122 *Id.* at 648. The premise that semantic meaning is more certain than pragmatic meaning is of course debatable. *See, e.g.*, Anita S. Krishnakumar, *Textualism in Practice*, 74 DUKE L.J. (forthcoming 2024), https://ssrn.com/abstract=4441426 [https://perma.cc/4KVG-7URR].

to that party's objectively reasonable understanding of their meaning—suffers a type of legal wrong a legislator cannot. In these respects, contract exposition fundamentally differs from the exposition of public laws.

2. Evidentiary Formalism

If semantic formalism is rare in contract law, another variety of interpretive formalism is quite common. Interpretive altering rules can also be more formalist or less formalist depending on the types of evidence the interpreter may consider, on what Wigmore labels the "sources" of interpretation.[123] This Article terms limitations on the evidence that can go into interpretation *evidentiary formalism*.

a. Interpretation Thick and Thin

A rule of interpretation might be pictured as a function, mapping a domain of interpretive inputs onto a range of interpretive outputs.[124] The inputs always include the direct objects of interpretation: the text, spoken words, gestures, or other acts or omissions whose meaning is at issue. They also always include the interpreter's background understanding of the language and the world. Other possible but not necessary inputs include dictionary definitions and rules of grammar; evidence of local linguistic practices; information about who the parties are and the commercial setting of the transaction; other communications among or by the parties, before, during, or after formation; the parties' earlier or subsequent dealings with one another; and other surrounding circumstances relevant to the production and the parties' understanding of the interpretive object.[125] The interpretive output is a meaning

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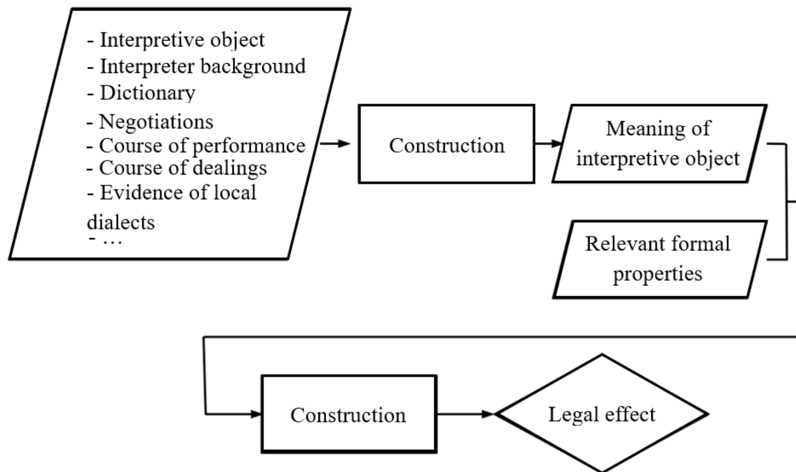
123 WIGMORE, *supra* note 64, § 2458, at 367.

124 The indeterminacy of interpretation renders this helpful analogy also imperfect. *See* DONALD DAVIDSON, *Belief and the Basis of Meaning*, *in* INQUIRIES INTO TRUTH AND INTERPRETATION 141, 144 (2d ed. 2001); DAVIDSON, *Radical Interpretation*, *in* INQUIRIES INTO TRUTH AND INTERPRETATION, *supra* note 124, at 125, 125–26.

125 For other lists of available interpretive inputs, see Schwartz & Scott, *supra* note 53, at 572 (listing "the parties' contract, a narrative concerning whether the parties performed the obligations that the contract appears to require, a standard English language dictionary, and the interpreter's experience and understanding of the world," plus "(1) the parties' practice under prior agreements; (2) the parties' practice under the current agreement; (3) testimony as to what was said during the negotiations; (4) written precontractual documents (memoranda, prior drafts, letters); and (5) industry custom relevant to determining what the agreement's words meant to the contracting parties"); 11 LORD, *supra* note 105, § 32:7 (arguing that even when a writing is integrated the interpreter should consider surrounding circumstances such as "the commercial or other setting in which the contract was negotiated and other objectively determinable factors that give a context to the transaction between the parties," including "whether one or both parties was new to the trade,

associated with the interpretive object. In legal interpretation, that meaning, together with relevant formal features of the interpretive object (in the case of mixed interpretive altering rules), serve as inputs for construction, which is the determination of legal effects. The process of applying an interpretive altering rule can therefore be represented as follows:

Figure 3: Structure of Interpretive Exposition



What inputs should go into contract interpretation? With respect to contractual writings, scholars have mounted general defenses of both textualist and contextualist approaches.[126] But the choice of interpretive inputs is not binary. Any given rule of interpretation can permit more or less evidence depending on the types of evidence it authorizes (a rule of contract interpretation might permit, for example, usage of trade but not course of performance), on when that evidence is allowed in (always, only when the semantic meaning is ambiguous, only in informal or nonintegrated communications, etc.), on who may consider the evidence (only the judge, also the jury), and so forth. The question is not simply whether to limit the interpretive domain to the text and a dictionary, but how much evidence of what type to allow under what circumstances, where the possible answers include "none ever," "all always," and many points between.[127]

whether either or both had counsel, and the nature and length of their relationship, as well as their age, experience, education, and sophistication").

126 *See, e.g.*, Schwartz & Scott, *supra* note 53 (textualism); Eisenberg, *supra* note 5 (contextualism).

127 *See* Smith, *supra* note 8, at 1157–66 (identifying ways that rules can be designed to achieve a "differential formalism"); Katz, *supra* note 8, at 515–19 (observing several ways in which courts can permit more or less evidence in interpretation).

This Article uses the terms *thick* and *thin* to describe the relative quantity of inputs a legal rule of interpretation permits. Rules of interpretation that allow more interpretive inputs are *thicker*, those that permit fewer interpretive inputs are *thinner*. Textualist rules of interpretation are at the far thin end of the spectrum. Schwartz and Scott suggest, for example, that the minimum interpretive inputs are "the parties' contract, a narrative concerning whether the parties performed the obligations that the contract appears to require, a standard English language dictionary, and the interpreter's experience and understanding of the world."[128] Fully contextualist approaches lie at the thick end of the spectrum and permit all the above-listed forms of additional interpretive evidence and more.

b. Thin Interpretation: Plain Meaning Rules

Although the debate over how formalist contract interpretation should be is an important one, no one advocates thin interpretation for every type of contract altering act. This Article uses *contractual writing* to denote a writing or other record parties use to reach or memorialize a contractual agreement. Those who argue for formalist approaches to contract interpretation focus almost exclusively on contractual writings. Courts typically apply evidentiary formalism to an even narrower category: integrated contractual writings. An integrated contractual writing is one the parties intend as a final expression of some or all of their agreement. New York's plain meaning rule provides a useful example.

In *W.W.W. Associates, Inc. v. Giancontieri*, the New York Court of Appeals formulated the New York rule as follows:

> [W]hen parties set down their agreement in a clear, complete document, their writing should as a rule be enforced according to its terms. Evidence outside the four corners of the document as to what was really intended but unstated or misstated is generally inadmissible to add to or vary the writing.[129]

Note that the rule applies only to "complete document[s]," which is to say those that are integrated.[130] The New York rule is that extrinsic evidence may be introduced to interpret an integrated writing only when

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128 Schwartz & Scott, *supra* note 53, at 572. The weight that should be given to dictionary definitions when an adjudicator is fluent in the language parties used should be approached with skepticism.

129 566 N.E.2d 639, 642 (N.Y. 1990); *see also* R/S Assocs. v. N.Y. Job Dev. Auth., 771 N.E.2d 240, 242 (N.Y. 2002) (affirming New York's plain meaning rule).

130 *Giancontieri*, 566 N.E.2d at 642.

the writing is ambiguous.[131] In New York's relatively formalist version of the rule, ambiguity is also to be determined from the text alone: "[E]xtrinsic and parol evidence is not admissible to create an ambiguity in a written agreement which is complete and clear and unambiguous upon its face."[132] The interpreter of an integrated contractual writing may consider extrinsic evidence only if the court first determines that writing is ambiguous on its face.[133]

This thin interpretive base gives a contractual writing's semantic meaning greater role in its interpretation. But New York courts do not adhere to semantic formalism. *Giancontieri* also provides that a writing is to be "read as a whole to determine its purpose and intent."[134] Or as the Court of Appeals explained in another decision: "The meaning of a writing may be distorted where undue force is given to single words or phrases. We read the writing as a whole. We seek to give to each clause its intended purpose in the promotion of the primary and dominant purpose of the contract."[135] This emphasis on interpreting the contractual writing as a whole in light of its apparent purpose takes interpretation beyond semantic meaning to considerations of probable intent and the text's pragmatic meaning.

In sum, New York's plain meaning rule exhibits a high degree of evidentiary formalism. Absent ambiguity on the face of an integrated contractual writing, interpretive inputs should include only the contractual writing, the nature of the transaction, any extrinsic evidence

131 *See id.*

132 *Id.* at 642 (quoting Intercontinental Plan., Ltd. v. Daystrom, Inc., 248 N.E.2d 576, 580 (N.Y. 1969)).

133 *See id.*

134 *Id.*

135 Empire Props. Corp. v. Mfrs. Tr. Co., 43 N.E.2d 25, 28 (N.Y. 1942); *see also* William C. Atwater & Co. v. Pan. R.R. Co., 159 N.E. 418, 419 (N.Y. 1927) ("Reason, equity, fairness—all such lights on the probable intention of the parties—show what the real agreement was."); Fleischman v. Furgueson, 119 N.E. 400, 401 (N.Y. 1918) ("In construing a contract the whole instrument must be considered, and from such consideration a conclusion reached as to what the parties intended to do or sought to accomplish."); Wolkind v. Berman, 248 N.Y.S. 513, 517 (App. Div. 1931) ("A contract must be considered in its entirety, and the intention of the parties must be determined from the entire instrument, and not from some detached portion."). Even more radical are early statements by the Illinois Supreme Court:

> The rule is that the intention of the parties must govern, but that intention is not to be sought merely in the apparent meaning of the language used, but that the meaning of the language may be enlarged or limited according to the true intent of the parties, as made manifest by the various provisions of the contract considered as a whole.

Street v. Chi. Wharfing & Storage Co., 41 N.E. 1108, 1111 (Ill. 1895); *see also* McCoy v. Fahrney, 55 N.E. 61, 63 (Ill. 1899) ("Particular expressions will not control where the whole tenor or purpose of the instrument forbids a literal interpretation of the specific words." (quoting Updike v. Tompkins, 100 Ill. 406, 410 (1881))).

of local conventional meanings, the interpreter's background understanding of the English language and the world, and perhaps a dictionary. That said, the goal of interpretation under the rule is to identify the writing's pragmatic meaning, to the extent it can be gleaned from the thin evidentiary base and the text as a whole. Although a contractual writing's plain meaning often is its semantic meaning, sometimes the writing and common sense indicate a purpose at odds with that meaning, in which case the parties' probable intentions and the text's pragmatic meaning control. The output of this interpretive process is the text's *plain meaning*. Only when the plain meaning is ambiguous or otherwise fails to determine the legal state of affairs may the interpreter look to other interpretive evidence of the words' pragmatic meaning or the parties' relevant beliefs and intentions.

There is more to say about plain meaning rules. This Article has not, for example, discussed the respective roles of the judge and jury.[136] Nor are New York courts perfectly consistent in the rule's application or articulation. And this Article has not canvassed other states' approaches to plain meaning. But the above stylized version will serve as a useful example for thinking in Part IV about how and when lawmakers should adopt evidentiary formalism.

c. Thick Interpretive Rules: Contextualism

Not all jurisdictions employ plain meaning rules. In *Pacific Gas & Electric Company v. G.W. Thomas Drayage & Rigging Company, Inc.*, Judge Traynor famously rejected the very idea of plain meaning, concluding that "rational interpretation requires at least a preliminary consideration of all credible evidence offered to prove the intention of the parties."[137] Under the *Pacific Gas* rule,

> The test of admissibility of extrinsic evidence to explain the meaning of a written instrument is not whether it appears to the court to be plain and unambiguous on its face, but whether the offered evidence is relevant to prove a meaning to which the language of the instrument is reasonably susceptible.[138]

This is a relatively thick interpretive rule, even for integrated writings. A court should consider all relevant evidence when deciding whether a writing is susceptible to one or another interpretation.

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[136] *See, e.g.*, Nucci v. Warshaw Const. Corp., 186 N.E.2d 401, 403 (N.Y. 1962) ("The interpretation of written contracts ordinarily presents a question of law for the court.").

[137] 442 P.2d 641, 645 (Cal. 1968).

[138] *Id.* at 644.

Scholars have paid considerable attention to this divide between California and New York law.[139] But it should not be forgotten that the divide, properly understood, applies to a relatively narrow range of contract-altering acts: integrated contractual writings. Many contracting parties do not employ an integrated writing. A contract might be formed by oral agreement, by nonverbal acts of performance, by non-integrated writings, and in some circumstances by a party's silence or inaction. In none of these instances do courts limit themselves to the plain meaning of the parties' words.

Consider, for example, the casebook classic *Lucy v. Zehmer*, which concerned the legal effect of an agreement to sell a farm for $50,000 written on the back of a restaurant check.[140] At issue was whether a seller's agreement to the transaction was in jest. In concluding that the transaction appeared to be serious, the court addressed inter alia: the alleged buyer's past offers to purchase the farm; that the parties signed the instrument after thirty to forty minutes of negotiations and some redrafting; the fact that the parties were drinking; testimony that the alleged seller negotiating the transaction told his wife that it was a joke; the buyer's offer, immediately after signing, of five dollars "to seal the deal" (a customary, nonlegal formality); the negotiating seller's rejection of the five dollars; and the buyer's subsequent actions in reliance on the transaction.[141] Although the court's conclusion might be described as "formalist" in the sense that it held that the writing was binding, the opinion nowhere suggests excluding evidence beyond the writing. Because the writing was not integrated, the interpretative approach is nonformalist.

C. *Summary*

One finds two forms of formalism in the law of contract: formalities and evidentiary formalism. The basic divisions might be represented graphically as follows:

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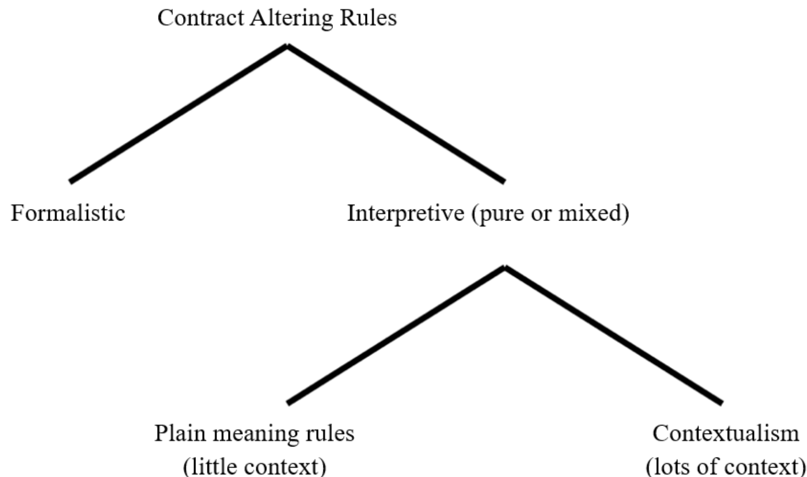
139 *See, e.g.*, Kraus & Scott, *supra* note 10, *passim*.

140 Lucy v. Zehmer, 84 S.E.2d 516, 518 (Va. 1954).

141 *Id.* The offer of $5 to seal the deal was an attempt to invoke a nonlegal formality. Because of the buyer's refusal to accept the $5, that particular formality was not completed. *Id.* The absence of the formality did not, however, prevent the court from finding that the parties had entered into a contract. *Id.* at 522.

Figure 4: Two Forms of Formalism in Contract



The rules on the left side of each divide constitute the two forms of formalism one finds in contract law.

Formalistic altering rules achieve formalism by avoiding interpretation altogether. Formalities come in various forms. A formality that has no nonlegal meaning is a pure formality; one whose words have a nonlegal meaning is an ordinary-language formality. Ordinary-language formalities can arise from custom, from statute, or in rare cases from the judicial construction of boilerplate. A contract formality is nondefeasible if its legal effects cannot be altered by evidence of the parties' contrary intent; a formality is defeasible if its legal effects can be altered by such evidence.

There are two ways interpretive altering rules might be formalist. First, an interpretive rule is semantically formalist when it identifies a relatively fixed form of meaning as legally relevant. Though some argue for semantic formalism in the interpretation of public laws, it is not a feature of contract law. More common in contract is a second type: interpretive formalism, which limits the evidence of meaning an interpreter may consider. Plain meaning rules are the most common form of evidentiary formalism. They are properly applied, however, only to integrated contractual writings. Because many contract-altering acts—before, during, and after formation—do not involve integrated writings, contextualist interpretation is also common even in jurisdictions that adopt plain meaning rules.

IV. MAKING FORMALISM WORK

Having distinguished two forms of formalism in contract law, this Article now turns to assessing the value of each. Section II.A identified six factors to consider in the design of altering rules: accuracy, adjudication costs, compliance costs, relational costs, knowability, and the promotion of social goals independent of party intent. In theory, one might assign a variable to each factor and combine them into a single expression whose value lawmakers should seek to maximize. But that generic formula would be of little practical value. One would not know for any given altering rule how to begin assigning values to the variables. Nor are all the costs and benefits at stake commensurable or uncontested.

Rather than looking for a grand synthesis, this Part applies these factors to examine four aspects of contract formalism: the design of formalities, how parties opt in to evidentiary formalism, relational costs of formalism, and the case for developing new formalities for certain terms.

A. *Designing Formalities*

Formalities have three obvious advantages. First, a formality can be designed to be cheap for knowledgeable parties to use. It takes less effort to add the letters "F.O.B" and a place name to a written sales contract than it does to explain that the seller will bear both the expense and risk of shipping the goods to that place and must do so in the manner provided by the roughly 380 words in UCC Section 2-503.[142] Second, formalities are relatively cheap to adjudicate. Use of "F.O.B." obviates the need to consider additional evidence of the parties' intent. That does not mean such evidence never gets in. If the formality is defeasible, a party might introduce interpretive evidence that the parties were using it in a nonstandard way. The UCC rule for "F.O.B." applies "[u]nless otherwise agreed."[143] But interpretive evidence is relegated to a secondary role. Use of the formality shifts the burden of producing such evidence. Third, formalities provide highly knowable outcomes. Contracts casebooks are filled with opinions in which the best interpretation of the parties' words and actions is uncertain.[144] By avoiding interpretation, formalities achieve

142 *Compare* U.C.C. § 2-319(1)(b) (AM. L. INST. & UNIF. L. COMM'N 2022), *with id.* § 2-503.

143 *Id.* § 2-319(1).

144 The *locus classicus* in the United States is Judge Friendly's opinion in *Frigaliment Importing Co. v. B.N.S. Int'l Sales Corp.*, 190 F. Supp. 116 (S.D.N.Y. 1960).

high knowability. If one knows the code (or in the case of "F.O.B.," the Code), one knows the formality's legal effect.

If there is a worry about formalities, it concerns their accuracy. With respect to formalities, adjudicators are unlikely to err identifying the associated legal effect. The more significant worry is party error. As Ayres observes, altering rules can produce both Type I and Type II errors, in other words, false positives and false negatives.[145] A Type I error is one or more party's use of the formality absent an intent to effect the associated legal change. A Type II error occurs when one or more parties wish to achieve a legal result but fail to use the requisite formality. This Article considers each in turn, with special attention to the risk that Type I errors boilerplate formalities pose.

1. Type I Errors

The accuracy of any formality depends on parties' awareness of the relevant legal rules. Parties are *responsive* to a legal rule when they are aware of and craft their words or otherwise act in response to it. Formalities work best when parties are responsive to the legal rule. Responsive parties can use legal formalities to their benefit; unresponsive parties are less likely to notice formalities, understand their legal effects, or know to use them.[146]

Responsive parties are sometimes described as "sophisticated."[147] But that word suggests that responsiveness is a personality trait—that a party is always responsive or nonresponsive. In fact, a person might exhibit different degrees of responsiveness in different circumstances. A party might, for example, be more responsive to legal rules in some stages of a transaction (e.g., formation, when lawyers are involved) and less responsive during others (e.g., performance). And as every corporate counsel knows, even experienced businesspeople, whom one might think of as sophisticated, sometimes do not take the legal effects of their words and actions into account.[148]

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145 Ayres, *supra* note 29, at 2066.

146 Although the extent to which parties are responsive to formalities is a factual question, there has been relatively little empirical study of party responsiveness to formalities. *See generally* David A. Hoffman & Zev J. Eigen, *Contract Consideration and Behavior*, 85 GEO. WASH. L. REV. 351 (2017) (experimentally studying the effects of recitals of consideration on subjects' willingness to defect from an agreement and noting the dearth of other empirical work on the subject).

147 *See, e.g.*, Kraus & Scott, *supra* note 10, *passim*.

148 Consider recent experience with judicial interpretations of *pari passu* clauses in sovereign debt contracts. In the immediate aftermath of judicial rulings on the legal meaning of the standard clause that went against the understanding of most lawyers in the field, those lawyers did not redraft

In the case of formalities, Type I errors are especially likely when unresponsive parties agree to writings drafted by responsive parties—when only one side knows the code. Just this risk appears to have been the impetus for the early twentieth-century wave of state legislation limiting the legal effects of the seal or abolishing it entirely.[149]

It is difficult to unearth the history of the decline of the private seal in the United States. But in a 1915 essay in *Columbia Law Review*, New York Supreme Court Judge Fredrick Crane suggests two interconnected arguments for its abolition.[150] First, the formality had become less and less noticeable. Crane quotes an early nineteenth-century opinion by Chancellor Kent:

> A scrawl with a pen is not a seal, and deserves no notice. . . . The calling a paper a deed will not make it one, if it want the requisite formalities. . . . The policy of the rule consists in giving ceremony and solemnity to the execution of important instruments, by means of which the attention of the parties is more certainly and effectually fixed, and frauds less likely to be practi[s]ed upon the unwary.[151]

As the wax seal was replaced by a wafer and then by mere notation, it became less likely that users would notice that they were performing an act with a specific legal effect. Second, the seal's legal effects became increasingly baroque.[152] As a result, Crane argued, "While the necessity for the private seal has virtually gone, its use still remains, with many serious and ensnaring effects. A study of the cases will convince one that people make use of the printed or written 'L.S.' without fully appreciating its effect."[153]

Crane's diagnosis is of a piece with the idea that a formality is a tool the law gives parties to achieve intended legal effects. For the tool to work, the user must know that they are performing a legally effective act and what its effects are. As the seal lost its ceremonial quality, the first was less likely to pertain. Users were less likely to realize that they were performing a legally significant act. And as the seal's legal effects became increasingly complex, there was a decline in the second type of knowledge. Users who knew they were performing a legal act became less

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their standard contracts to clarify the clauses' meaning. *See* MITU GULATI & ROBERT E. SCOTT, THE THREE AND A HALF MINUTE TRANSACTION: BOILERPLATE AND THE LIMITS OF CONTRACT DESIGN 45–72 (2013).

149 The private seal is still operative in many U.S. jurisdictions, although its legal effect has changed over time. *See* Holmes, *supra* note 105, *passim*; RESTATEMENT (SECOND) of CONTS., Stat. Note (AM. L. INST. 1981) (summarizing relevant statutes).

150 *See* Crane, *supra* note 88, at 24.

151 *Id.* (quoting Warren v. Lynch, 5 Johns. 239, 245–46 (N.Y. Sup. Ct. 1810)).

152 *Id.* at 25–36.

153 *Id.* at 25.

likely to fully understand its consequences. Both increased the risk of Type I errors.

This double requirement, that users know that they are performing a legally effective act and what the effects are, indicates the relative advantages and disadvantages of pure and ordinary language formalities. Neil MacCormick and Joseph Raz describe the advantages of a pure formality:

> [The choice-promoting function of legal powers] explains why they are exercised either by special formal and ceremonial acts as in making a deed or getting married . . . . It also explains why most legal powers are exercised by acts with only negligible non-normative consequences, like signing, so that there are few reasons for or against doing them apart from their legal or other normative consequences.[154]

Because it has no nonlegal meaning, a pure formality puts the user on notice that they are performing a legally significant act. And as Crane suggests, the more ceremonial a pure formality, the more likely it is to have this effect.[155] A pure formality does not, however, inform users what those legal effects are. This was the problem with the seal. Although it put users on notice that they were performing a legal act, it did not tell them what its effects were. And as the legal effects became more baroque, users were less likely to understand them.

A well-designed ordinary language formality might address both problems. Depending on the words comprising it, an ordinary language formality can convey information to its users, turning unresponsive parties into responsive ones.[156] Although not a formality in the strict sense,[157] the Consumer Finance Protection Bureau's model mortgage disclosure form provides an example.[158] Through empirical study, regulators identified a form of expression more likely to effectively communicate to consumers the terms of the transaction.[159] If pure

154 MacCormick & Raz, *supra* note 83, at 81.

155 *See* Crane, *supra* note 88, at 24.

156 For more on the design error-reducing altering rules generally, see Ayres, *supra* note 29, at 2068–84.

157 The mortgage form is not a formality in my sense of the term because failure to use it does not render the loan invalid but subjects the lender to possible legal liability. 12 U.S.C. §§ 2605(f), 2615.

158 *Closing Disclosure Explainer*, CONSUMER FIN. PROT. BUREAU, http://www.consumerfinance.gov/owning-a-home/closing-disclosure [https://perma.cc/7WPY-AKRH].

159 *Id.* For background on the form's design, see JAMES M. LACKO & JANIS K. PAPPALARDO, FED. TRADE COMM'N, IMPROVING CONSUMER MORTGAGE DISCLOSURES: AN EMPIRICAL ASSESSMENT OF CURRENT AND PROTOTYPE DISCLOSURE FORMS: A BUREAU OF ECONOMICS STAFF REPORT (2007), https://www.ftc.gov/reports/improving-consumer-mortgage-disclosures-empirical-assessment-current-prototype-disclosure [https://perma.cc/698Y-98QC].

formalities are problematic because some users do not know their legal effect, the solution would seem to be to require words that say, in ordinary language, just what those legal effects are.

That said, the more information lawmakers attempt to pack into a formality, the more expensive it is to use. This is an example of a common dynamic Ayres identifies in the design of altering rules: a trade-off between transaction costs and error reduction.[160] Even more concerning is empirical evidence that many parties do not respond to information.[161] If consumers or other nonresponsive parties do not read the agreements they sign, it does not matter what words the law requires for their effectiveness. Whether, when, and how formalities might be designed to avoid Type I errors is an empirical question likely to receive different answers in different contexts, depending on factors such as the identity of the parties and the nature of the transaction between them.

A second and common strategy for avoiding Type I errors is defeasibility. A formality is *defeasible* if parties can introduce interpretive evidence that they did not in fact intend the associated legal effect. Defeasibility gives parties the opportunity to show that the formality was used by mistake and adjudicators the opportunity to fix such mistakes. Assuming evidence of error is reliable, defeasibility should reduce Type I errors. This explains why few if any contemporary contract formalities are nondefeasible.

Defeasibility's gains in accuracy come at the expense of more costly adjudication and reduced knowability. When a formality is nondefeasible, its use ends the inquiry. That advantage is lost if parties are permitted to introduce interpretive evidence that the formality was used by mistake.

2. Boilerplate Formalities

The risk of Type I errors is especially salient in boilerplate formalities, which merit special consideration.

For several centuries, the standardized language in a Lloyd's marine insurance policy used the following words to describe covered risks:

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160 Ayres, *supra* note 29, at 2061–63.

161 *See, e.g.*, Yannis Bakos, Florencia Marotta-Wurgler & David R. Trossen, *Does Anyone Read the Fine Print? Consumer Attention to Standard Form Contracts*, 43 J. LEGAL STUD. 1 (2014) (finding that virtually no consumers read online end user license agreements); OMRI BEN-SHAHAR & CARL E. SCHNEIDER, MORE THAN YOU WANTED TO KNOW: THE FAILURE OF MANDATED DISCLOSURE (2014) (discussing the limited effectiveness of disclosure rules). *But see* Richard Craswell, *Static Versus Dynamic Disclosures, and How Not to Judge Their Success or Failure*, 88 WASH L. REV. 333 (2013) (arguing that Ben-Shahar and Schneider's all-or-nothing approach fails to recognize the incremental gains disclosure can secure).

> Touching the Adventures and Perils which we the Assurers are contented to bear and do take upon us in this Voyage, they are, of the Seas, Men-of-War, Fire, Enemies, Pirates, Rovers, Thieves, Jettisons, Letters of Mart and Counter-mart, Surprisals, Takings at Sea, Arrests, Restraints and Detainments of all Kings, Princes, and People, of what Nation, Condition or Quality soever, Barratry of the Master and Mariners, and of all other Perils, Losses and Misfortunes that have or shall come to the Hurt, Detriment, or Damage of the said Goods and Merchandises and Ship, &c., or any Part thereof.[162]

In his 1914 treatise, Sir Douglas Owen observed of the Adventures and Perils clause:

> It is an ancient and incoherent document, occasionally the subject of judicial remarks in the highest degree uncomplimentary. But nobody minds this or dreams of altering the ancient form, nor, one may imagine, is it ever likely to be altered. Insurance experts know—or very often know—exactly what it means, and with generations of legal interpretations hanging almost to every word, and almost certainly to every sentence, in it, it would be highly dangerous to tamper with it.[163]

Translated into the language in this Article, Owen is saying that the Adventures and Perils clause is a boilerplate formality. To understand its purpose and legal effects, one does not need to interpret the words in it. In fact, attention to the words' meaning will lead one astray. The clause's purpose and legal effect lies entirely in the judicial opinions construing it.

There is a way in which a boilerplate formality like the Lloyd's Adventures and Perils clause is the worst of both worlds. Because the clause is cast in ordinary language, it does not put nonresponsive users on notice that it is a formality—that the law attaches specific legal effects to it. And due to the gap between the clause's ordinary meaning and its legal effects, it also fails to inform those users of what they are doing by agreeing to the clause.

This was perhaps not much of a problem in the eighteenth and nineteenth century British marine insurance market. The Lloyd's policy was used by a small group of highly responsive repeat players.[164] But

162 I am grateful to Jim Oldham for bringing this example to my attention. James Oldham, *Insurance Litigation Involving the* Zong *and Other British Slave Ships, 1780–1807*, 28 J. LEGAL HIST. 299, 301 (2007).

163 DOUGLAS OWEN, OCEAN TRADE AND SHIPPING 155 (1914).

164 For a description of the British marine insurance market in the late eighteenth century as it related to the development of the Lloyd's standard policy, see CHARLES WRIGHT & C. ERNEST FAYLE, A HISTORY OF LLOYD'S: FROM THE FOUNDING OF LLOYD'S COFFEE HOUSE TO THE PRESENT DAY 126–52 (1928). During that period, only twelve judges comprised the entirety of the central courts of London—the Court of Kings Bench, the Court of Common Pleas, and the Court of Exchequer—and only some twenty or thirty barristers practiced at the Court of Kings Bench. *See* JAMES OLDHAM, ENGLISH COMMON LAW IN THE AGE OF MANSFIELD 12–14 (2004).

boilerplate also appears in contracts with nonresponsive parties. Michele Boardman argues that years of judicial construction given the effect of stare decisis have rendered standard clauses in contemporary consumer insurance contracts "a private conversation between drafters and courts," one that consumers who rely on the written contract's literal meaning are likely to misunderstand.[165] Boilerplate formalities create a special risk of Type I errors.

It is also worth considering the capacity of courts of general jurisdiction to establish useful boilerplate formalities. Responding to Lisa Bernstein's studies of trade associations, David Charny expresses doubts:

> As Bernstein reports, [trade association] tribunals frequently include in their opinions drafts of contract terms that should be incorporated into contracts to avoid future disputes. Note how this procedure lays the foundation for formalism in the next round: the trade association adjudicator can now insist that the dispute be resolved decisively by the presence or absence of a particular term, which, for the tribunal, has a built-in imprimatur and a preannounced meaning. In contrast, common law courts lack the institutional machinery for this prospective rulemaking: they are inexpert, they do not face contract cases from any specific industry often enough to mold practice, and they lack the means to communicate their decisions in a way that would reach the full range of transactors.[166]

Again the Lloyd's covered-risk clause is instructive. Not only was it used by a close-knit community of highly sophisticated repeat players, but courts interpreting it regularly empaneled special expert juries to advise them on commercial practices.[167] The conditions for the creation of successful boilerplate formalities might not be present in a country the size of the United States that uses courts of general jurisdiction.

This is not to say that boilerplate formalities are never appropriate. This Article has identified three instances where they can be: when the inclusion of a boilerplate clause is mandated by statute or regulation,

165 Michelle E. Boardman, Contra Proferentem*: The Allure of Ambiguous Boilerplate*, 104 MICH. L. REV. 1105, 1105 (2006).

166 Charny, *supra* note 4, at 848; *see also id.* at 843 nn.2–3 (citing Lisa Bernstein, *Merchant Law in a Merchant Court: Rethinking the Code's Search for Immanent Business Norms*, 144 U. PA. L. REV. 1765 (1996) [hereinafter Bernstein, *Merchant Law*]; Lisa Bernstein, *The Questionable Empirical Basis of Article 2's Incorporation Strategy: A Preliminary Study*, 66 U. CHI. L. REV. 710 (1999)).

167 *See* James C. Oldham, *The Origins of the Special Jury*, 50 U. CHI. L. REV. 137, 173–75 (1983). In *Wright v. Shiffner*, for example, in ruling the legal effect of a clause in an insurance policy, Lord Ellenborough emphasized that "Mr. Taylor, a special Juryman, said, that this was the construction universally put upon these policies in the city of London." (1809) 170 Eng. Rep. 1145, 1146 (QB); *see also* Brough v. Whitmore, (1791) 100 Eng. Rep. 976 (KB) (determining the meaning of the word "furniture" in a marine insurance policy based on the special jury's judgment as to merchant usage).

when contractual writings are highly standardized and uniformity is important to the market, and when uniform construction empowers consumers to bring a class action. Section IV.A.4 argues that in each of these examples, the social benefits of treating boilerplate as a formality can outweigh the added risk of Type I errors.

3. Type II Errors

A Type II error is a false negative. Parties commit Type II errors in the application of altering rules when they wish to achieve a certain legal outcome but fail to perform an altering act that secures it. In the case of formalistic altering rules, Type II errors occur when parties who want to achieve a legal outcome fail to say the magic words, whether because they do not know them or because they make a mistake in expression.

Type II errors can be reduced by a rule that provides that correct use of the formality is sufficient but not necessary to effect the legal change—by supplementing formalistic altering rules with interpretive ones. A *requisite formality* is one that is both necessary and sufficient to achieve a legal effect. An *optional formality* is one that is sufficient but not necessary to do so. By providing that parties can achieve the desired legal effect without using the formality—by making the formality optional—lawmakers can make it easier for nonresponsive parties to achieve the legal effects they want.[168]

Consider Section 2-316's rule for the implied warranty of merchantability.[169] Subsection 3(a) of the provision provides the formalistic altering rule: a seller can disclaim all implied warranties by using the formalities "as is" or "with all faults."[170] Subsection 2 provides a second way to alter a default warranty: "[T]o exclude or modify the implied warranty of merchantability or any part of it [under this section] the language must mention merchantability and in case of a writing must

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168 Ayres provides a similar explanation of why altering rules commonly identify acts that are sufficient but not necessary to achieve legal change:

> Giving effect to a multiplicity of methods [to avoid the default] reduces the costs of learning the law—especially the necessity to learn the altering rules themselves. A contract law that includes necessary elements for displacement will tend to increase the cost of becoming (and remaining) informed of the requisite procedures for displacement.

Ayres, *supra* note 29, at 2055 (footnote omitted); *see also id.* at 2081–82 (arguing that the best "password altering rules . . . are nonexclusive means—and are merely sufficient safe harbors—for achieving particular contractual outcomes").

169 *See* U.C.C. § 2-316 (AM. L. INST. & UNIF. L. COMM'N 2022).

170 *Id.* § 2-316(3)(a).

be conspicuous . . . ."[171] The subsection 2 rule is a mixed interpretive one. Though the language must mention "merchantability" and, if in a writing, be conspicuous, the rule does not identify magic words sufficient to disclaim the implied warranty. The seller need only make a statement with the right meaning: that the seller does not warrant merchantability. The formalistic "as is" altering rule in subsection 3(a) is accompanied by a mixed interpretive one in subsection 2. "As is" is an optional formality.

Again there are trade-offs. Requiring use of the formality means greater knowability and lower costs of adjudication. If the parties have not said the magic words, they have not effected the legal change. This is no longer the case if the formality is but one way to achieve the legal change. Moreover, if it is possible to design an ordinary language formality to educate nonresponsive parties, one might want to require its use. In that case, the gains from reducing Type I errors—misunderstanding of the legal effects—might outweigh the costs of any resulting Type II errors—failing to use the right words to achieve those effects.

4. Other Social Goals

There exists another category of reasons for adopting formalities. The analysis so far has focused on accuracy and the costs of achieving it. Accuracy is key to several of contract law's core functions: helping parties realize their individual and shared preferences, resolving disputes between them, and providing remedies for breach. All involve in one way or another giving legal effect to a party's chosen obligations. But contract law is about more than giving legal effect to party choice. There are four ways a contract formality can be used to promote other social goals: by helping to create uniform terms across a market, by construing mandatory contract language to establish a government-favored mandatory term, by requiring parties to perform an otherwise socially beneficial act, and by sorting among parties.

Some markets benefit from uniform terms across all transactions.[172] Over ninety percent of over-the-counter derivative transactions, for example, use the International Swaps and Derivatives Association's (ISDA) Master Agreement.[173] Alan Greenspan has credited large

[171] *Id.* § 2-316(2).

[172] For more on this function of formalities, see Klass, *supra* note 98, at 119–36.

[173] *In re* Lehman Bros. Holdings, Inc., No. 8-13555, 2015 WL 7194609, at *1 n.1 (S.D.N.Y. Sept. 16, 2015).

increases in the liquidity of that market to that standardization.[174] The insurance market is another example. Uniform terms in insurance contracts enable the pooling of actuarial data, simplify the reinsurance market, and allow greater regulatory oversight.[175] In such markets, uniformity can be achieved by giving boilerplate language the same construction across all transactions, no matter the understanding of the parties in any given transaction.

In addition to making some markets more efficient, uniform terms can sometimes reduce the costs of litigation. In the past two decades, courts have begun to adopt uniform constructions of consumer contracts of adhesion to satisfy commonality and related requirements for certifying class actions.[176] Here the relevant social goal is not uniformity in the marketplace (though that might be the drafter's aim), but the effective litigation of claims that might otherwise be too low-value to bring a claim. Again accuracy in individual transactions takes a back seat to the social benefit uniform terms provide.

A second possible social benefit appears when the state requires that certain language appear in contracts of a certain type.[177] The Federal Housing Administration and the Department of Housing and Urban Development, for example, mandate that all residential mortgages include specified language setting forth various covenants.[178] It is difficult to imagine why the government would want to mandate that contracts include those words, yet allow their construction to vary across transactions. More likely is that it seeks to mandate that residential mortgages include certain terms by mandating language stating those terms. If that is right, mandatory language should be construed not in accordance with the parties' intent, but to further the policy reasons for requiring its inclusion. The language should be construed as a formality, effecting a certain legal change no matter what the parties' intent.

Third, requisite formalities can help realize social goals by employing an altering act with positive secondary effects. Recall Lon Fuller's observation that formalities can serve a "cautionary function," inducing the user to consider their actions more carefully than they might

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[174] Alan Greenspan, Chairman, Fed. Rsrv. Sys., Remarks to the Federal Reserve Bank of Chicago's 41st Annual Conference on Bank Structure 7 (May 5, 2005).

[175] *See* KENNETH S. ABRAHAM, INSURANCE LAW AND REGULATION: CASES AND MATERIALS 31–37 (4th ed. 2005); RESTATEMENT OF LIAB. INS. § 2 cmt. d (AM. L. INST. 2019).

[176] *See* Klass, *supra* note 98, at 134 n.148 (citing cases); *see, e.g.*, Gillis v. Respond Power, LLC, 677 F. App'x 752, 756 (3d Cir. 2016); *In re* TD Bank, N.A. Debit Card Overdraft Fee Litig., 325 F.R.D. 136 (D.S.C. 2018); Feller v. Transamerica Life Ins. Co., No. 16-cv-01378, 2017 WL 6496803, at *11, *13 (C.D. Cal. 2017).

[177] For a more detailed discussion, see Klass, *supra* note 98, at 116–19.

[178] *See* Requirements for Single Family Mortgage Instruments, 53 Fed. Reg. 25434 (proposed July 6, 1988).

otherwise. In the case of the seal, "The affixing and impressing of a wax wafer—symbol in the popular mind of legalism and weightiness—was an excellent device for inducing the circumspective frame of mind appropriate in one pledging his future."[179] The goal here is not or not only to inform users of legal effects, but to influence them in other ways. Several requisite noncontractual formalities are designed in this way. The U.S. Presidential Oath of Office, for example, requires that the president-elect recite specific words solemnly swearing or affirming that they will to the best of their ability preserve, protect, and defend the U.S. Constitution.[180] Similarly, the Catholic marriage requires the bride and groom to memorize and recite precisely worded promises and prayers.[181] Both formalities serve not only to inform users that they are effecting a normative change or of the nature of that change, but to force them to perform an act with independent normative significance. Although contemporary contract law does not include requisite formalities of this type, one could imagine them.

Finally, requisite formalities can serve a sorting function. Ayres makes this point: "An altering rule with arbitrary language operates as a password that allows knowledgeable parties to achieve a desired result without running the risk that unknowledgeable parties will mistakenly invoke the sufficient condition."[182] Type II errors by nonresponsive parties can be desirable when society wants to restrict who can exercise a legal power—not to give legal effect to party choice, but to limit it. A formality that is both arcane and requisite can produce such sorting. More generally, requisite formalities can be designed to make it costly to alter the default legal state of affairs. Sometimes there is a social interest in ensuring that a default sticks—that parties do not contract around it.[183] Requisite costly formalities such as recitations, waiting periods, notarization, recording taxes, and the like can ensure that only those who attach a high value to the resulting legal change will take the trouble.[184]

The last three strategies work only when the formality is not only sufficient to effect the relevant legal change, but when it is necessary to do so. If they are not commonly pursued in contemporary contract law, it is perhaps in part because the common law does not have a mechanism for establishing requisite formalities. Be that as it may, they remain design options.

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179 Fuller, *supra* note 8, at 800.

180 U.S. CONST. art. II, § 1, cl. 8.

181 THE ORDER OF CELEBRATING MATRIMONY (2016).

182 Ayres, *supra* note 29, at 2081.

183 *Id.* at 2084–96.

184 Similar advantages can be secured by adding formal requirements to interpretive altering rules.

B. *Evidentiary Formalism and Party Choice*

Whereas formalities serve to avoid interpretation altogether, evidentiary formalism limits the inputs to interpretation. This difference affects the design question in several ways. For example, whereas a formality can (though need not) reduce both compliance and adjudication costs, evidentiary formalism is more likely to entail a trade-off between the two. Limiting admissible interpretive evidence reduces adjudication costs at the cost of increasing responsive parties' costs of compliance. Knowing evidence of context will not be admitted, responsive parties will expend more drafting effort to ensure that the plain meaning of their words captures their shared understanding.[185] Another difference is that whereas in the case of formalities, inaccuracies are likely due to user error, thick and thin interpretive altering come with a risk of adjudicator error—instances in which a third-party adjudicator misreads the intended or apparent meaning of parties' words. Especially salient in the United States are questions concerning whether judges or juries are more reliable interpreters and whether plain meaning is appropriate for judicial resolution.[186] Also crucial in the choice between thin and thick interpretive rules are broader questions about whether and when additional evidence of meaning increases interpretive accuracy. Finally, whereas in the case of formalities, concerns about user error can be addressed by making the formality defeasible or recognizing alternative paths for achieving the same legal outcome—in effect allowing interpretation to come in the back door—those safety valves are not available in the case of evidentiary formalism, which already involves interpretation.

These and other hard empirical and normative questions make it difficult to reach general conclusions about where evidentiary formalism is warranted. The cost-benefit question is too complex, the empirical evidence of relevant factors too scarce, and the probable answers too contextually sensitive. As Avery Katz puts the point, "[T]he traditional [cost-benefit] scholarly approach to form and substance founders on a lack of information about the likely consequences of formal and substantive modes of interpretation."[187]

Contract law provides a familiar solution to such informational hurdles. If lawmakers do not know enough to solve the cost-benefit

185 *See* Robert E. Scott & George G. Triantis, *Anticipating Litigation in Contract Design*, 115 YALE L.J. 814, 818–22 (2006) (discussing this trade-off).

186 *See, e.g.*, Charles T. McCormick, *The Parol Evidence Rule as a Procedural Device for Control of the Jury*, 41 YALE L.J. 365 (1932).

187 Katz, *supra* note 8, at 538.

question, sophisticated parties often arguably do. In many instances one can get the right interpretive rule by giving parties the power to choose between thick and thin interpretation of their agreement.

Here, as elsewhere, empowering parties to choose requires a default and an altering rule. Given that contractual altering acts can be very casual—a nod of assent, an indirect statement such as "go ahead," a thumbs-up emoji—the default interpretive approach should permit evidence of context. Especially when parties are not thinking about the legal consequences of their words and actions, accuracy requires considering all the interpretive evidence.

What altering acts should suffice to limit the evidence of meaning? The most obvious would be a plain meaning clause expressly stipulating evidentiary formalism. More common in U.S. contracts, however, is the integration of a contractual writing. This Section considers each in turn.

1. Plain Meaning Clauses

The easiest case is when the parties agree that the plain meaning of a writing shall govern. Jody Kraus and Robert Scott find several contractual writings that include plain meaning clauses like the following:

> The Parties' legal obligations under this . . . Agreement are to be determined from the precise and literal language of this . . . Agreement and not from the imposition of state laws attempting to impose additional duties of good faith, fair dealing or fiduciary obligations that were not the express basis of the bargain at the time this Agreement was made.[188]

The parties' knowing agreement to a plain meaning clause suggests that they have done the cost-benefit analysis for themselves and concluded that evidentiary formalism best serves their interests. In such circumstances, evidentiary formalism can be expected to produce accurate outcomes.[189] One might even say that the parties have agreed to whatever the plain meaning of the contractual writing is, even if it departs

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[188] Kraus & Scott, *supra* note 10, at 1102 n.274 (quoting E.I. du Pont de Nemours & Co. & EarthShell Corp., Alliance Agreement art. 12(h), at 7 (July 25, 2002), http://contracts.onecle.com/earthshell/dupont.collab.2002.07.25.shtml [https://perma.cc/9253-GVR9]).

[189] The above sentence embodies some heroic assumptions, namely, that parties' agreements to such clauses are knowing and that parties are able to competently do the cost-benefit analysis. There is a growing body of empirical evidence that often neither parties nor their lawyers fully comprehend the small print in the contracts they sign. *See* STEPHEN J. CHOI, MITU GULATI & ROBERT E. SCOTT, THE PARADOX OF CONTRACT PRODUCTION (forthcoming) (on file with authors). Yet such assumptions are arguably baked into familiar doctrines such as the duty to read.

from their actual understanding. If this is the case, a plain meaning rule cannot help but be accurate.

2. Integration

Plain meaning clauses are relatively rare in U.S. contractual writings. This is a curious fact, as they would seem to be useful tools for expressing party preferences and ensuring predictable outcomes. That they are not more common is perhaps a historical accident. In any case, the more common way to opt into evidentiary formalism is by adopting a writing as an integration.

The modern view, which dates to Wigmore, holds that absent a seal integration depends on the parties' manifest intentions.[190] A writing is integrated when and only when the parties appear to have agreed that it shall be a final statement of some or all terms of their contract. As Williston explained: "The parol evidence rule does not apply to every contract of which there is written evidence, but 'only applies where the parties to an agreement reduce it to writing, *and agree or intend that that writing shall be their agreement*.'"[191] The clearest evidence of such an intent is the parties' agreement to a merger clause. A merger clause states that the parties intend the writing as the final statement of some or all terms. For example:

> This instrument embodies the whole agreement of the parties. There are no promises, terms, conditions, or obligations other than those contained in this contract, and this contract shall supersede all previous communications, representations, or agreements, either verbal or written, between the parties.[192]

If the writing contains no merger clause, courts ask whether the writing appears to be intended as a final statement of some or all terms. The Second Restatement, for example, provides that "[w]here the parties reduce an agreement to a writing which in view of its completeness and specificity reasonably appears to be a complete agreement, it is taken to be an integrated agreement . . . ."[193] There are no formalities associated with integration. The rule is an interpretive one.

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190 *See, e.g.*, WIGMORE, *supra* note 64, § 2401, at 240. For a more detailed discussion of the rules discussed in this paragraph, see Gregory Klass, *Parol Evidence Rules and the Mechanics of Choice*, 20 THEORETICAL INQUIRIES L. 457, 463–71 (2019).

191 WILLISTON, *supra* note 1, § 633, at 1225 (emphasis added) (quoting Harris v. Rickett (1859) 157 Eng. Rep. 734, 737 (KB)).

192 WILLISTON, *supra* note 1, § 33F:2.

193 RESTATEMENT (SECOND) OF CONTS. § 209(3) (AM. L. INST. 1981).

There is an important difference between plain meaning clauses and merger clauses. Unlike a plain meaning clause, a merger clause does not stipulate how the writing shall be interpreted, only that it is a final statement of terms. Nor in the absence of a merger clause do courts ask whether the parties intended the plain meaning of the writing to control when deciding whether it is integrated. Yet in many jurisdictions the legal effect of integration is not only to exclude evidence of different or additional terms but also to limit the interpretive evidence that will apply to it.

Why should the party's agreement to integrate a writing trigger evidentiary formalism? Williston suggests the following explanation:

> [I]n case of a writing wholly informal in character, but which nevertheless was adopted by the parties as a statement of their bargain, the same principle is applicable. The parties have assented to those words as binding upon them. In an ordinary oral contract or one made by correspondence, the minds of the parties are not primarily addressed to the symbols which they are using; they are considering the things for which the symbols stand. Where, however, they incorporate their agreement into a writing they have attempted more than to assent by means of symbols to certain things, they have assented to the writing as the adequate expression of the things to which they agree.[194]

One can read this explanation in either of two ways.

First, Williston might be making a claim about party responsiveness. In a jurisdiction in which courts interpret integrated writings according to their plain meaning, responsive parties who agree to integrate will choose their words accordingly and will understand that they are also agreeing to be bound by the writing's plain meaning. That plain meaning will correspond to the parties' intentions because they have in fact agreed to be governed by it, if not in so many words. Moreover, at least in theory parties have the power to change the interpretive rule. Their choice not to stipulate that the integrated writing shall be interpreted in light of all the evidence might be read to suggest their preference for plain meaning interpretation.

The explanation has two weaknesses. First, it assumes party responsiveness. As far back as 1885, writing about the Statute of Frauds, Justice James Stephen and Fredrick Pollock argued:

> One cardinal rule, which those who legislate on the common business of life ought always to bear in mind, is that the power of law to control conduct is small, and is constantly exaggerated. Laws ought to be

194 WILLISTON, *supra* note 1, § 606, at 1165; *see also* RESTATEMENT (FIRST) OF CONTS. § 231 cmt. b (AM. L. INST. 1932) (advancing Williston's argument).

> adjusted to the habits of society, and not to aim at remoulding them. The cases in which any law is actually enforced are infinitesimally small in number in comparison with those in which it has no effect whatsoever. Custom, and what is called common sense, regulate the great mass of human transactions.[195]

Responsiveness is another area in which generalizations are difficult. One should expect the incentive effects of interpretive rules to depend in large part on who the parties are, the nature and stage of the transaction, and the type of communication at issue.

Second, the explanation is circular. The responsiveness explanation presupposes the existence of a plain meaning rule that parties are responsive to. It seeks to explain only the accuracy of the rule, not its existence.

A second, noncircular reason to apply evidentiary formalism to integrated writings can be found in the linguistic theory of audience design. Allan Bell has suggested that speakers, and by extension writers, vary their style of speech based on the intended and expected audiences. Bell distinguishes four categories of potential audiences.[196] As Henry Smith helpfully summarizes:

> An addressee is a person to whom the familiar speech acts—assertions, promises, apologies, and so on—are directed. An auditor is like an addressee in that he is known to the speaker and has his participation approved ("ratified"), but he is not directly addressed. An overhearer is known but not ratified or addressed. An eavesdropper is not even known.[197]

Bell observes that speakers adapt their styles primarily to accommodate the comprehension of addressees; that they do so to a lesser extent also for auditors, and to a yet lesser extent for overhears; and that speakers do not shift styles for eavesdroppers, who are unknown to them.[198]

No matter what the legal rule of interpretation, one might expect parties who are not thinking about legal liability to treat one another as addressees without considering possible future third-party adjudicators, whom Bell would then classify as eavesdroppers. Such parties are much more likely to communicate against the background of privately shared understandings. A statement like, "Go ahead, you're all right. Get your

195 James Fitz Stephen & Frederick Pollock, *Section Seventeen of the Statute of Frauds*, 1 L.Q. REV. 1, 6 (1885); *see also* Stewart Macaulay, *Non-Contractual Relations in Business: A Preliminary Study*, 28 AM. SOCIO. REV. 55 (1963) (describing business people's preference for keeping lawyers and formalities out of their transactions).

196 Allan Bell, *Language Style as Audience Design*, 13 LANGUAGE SOC'Y 145, 159 (1984).

197 Smith, *supra* note 8, at 1134.

198 Bell, *supra* note 196, 159–61.

men out, and don't let that worry you,"[199] is enough to signal agreement to renew a contract, though that is not its plain meaning. Because their communications are designed only for one another, plain meaning is unlikely to capture such parties' intentions.

When parties are thinking about legal liability and the possibility of future litigation, they are more likely to treat third-party adjudicators as auditors or even addressees and to speak accordingly, no matter what the legal rule of interpretation and regardless of whether they are responsive to it. According to Bell's theory, such parties are more likely to craft their communications in ways a third-party adjudicator will be able to understand. They are therefore more likely to express themselves in terms that do not rely on context.

Audience design thereby provides a noncircular argument for applying plain meaning rules to integrated contractual writings. A writing is integrated when the parties have agreed that in any future litigation it shall serve as a final statement of some or all terms. Parties who produce integrated writings are already considering the possibility of litigation before a third-party adjudicator. In Bell's way of speaking, they are treating possible third-party adjudicators as at least auditors and perhaps addressees. One should therefore expect parties to an integrated agreement to express themselves in ways a third-party adjudicator can understand—that is, plainly.

This is not to say that the plain meaning of an integrated writing always corresponds to the parties' actual intentions. Drafting costs, agency costs, and relational costs can make it impracticable to expressly record every element of the parties' shared understanding in a contractual writing. Parties can also make mistakes about the plain meaning of their contractual writing. They might not accurately predict how a third-party adjudicator who does not know all they know is likely to understand it. Finally, and most significantly, one or both parties might agree to an integrated writing they have not drafted and have not fully read. In all these cases, the plain meaning of even an integrated writing might not correspond to the parties' actual understanding.

That said, there is a reasonable argument that in many transactions the parties' agreement to an integrated contractual writing is a good reason to read that writing according to its plain meaning.

199 Embry v. Hargadine, McKittrick Dry Goods Co., 105 S.W. 777, 777 (Mo. Ct. App. 1907).

3. Aside: Formalities and Party Choice

Although this Section focuses on the role of party choice in evidentiary formalism, party choice might also figure into the creation of formalities. Stephen Choi and Mitu Gulati suggest, for example, that "contracting parties should have the ability to designate a standard-setting entity to provide a definitive source of interpretive authority for the contract," and that when parties do so courts should be required "to adopt the interpretation of the designated standard setter."[200] If parties and courts followed Choi and Gulati's advice, the result would be boilerplate formalities whose legal effects would be established by a party-chosen nonparty entity. Alternatively, a standard form contract in an industry where uniformity of terms is especially valuable might provide that courts should seek to achieve uniformity in its construction, effectively contracting for a higher level of stare decisis than would otherwise apply. Again the result would be a new set of boilerplate formalities.

I know of no real-world examples of either type of party-generated formality, though either might benefit some transactions.

C. *Relational Costs of Contract Formalism*

This Article has not yet discussed the relational costs of formalism in contract law.

Exchange transactions, even when at arms-length, often depend on and benefit from nonlegal forms of trust. A party who expects to engage in multiple transactions with their counterpart might choose to perform because breach would jeopardize that future income stream. A party who engages in similar transactions with others might worry about the reputational effects of breach. In such instances, the counterparty might trust in the incentives provided by repeat play and reputation as much as or more than in legal protections. And parties in close-knit communities or in longstanding relationships might trust in one another's honor, good will, or moral sensitivity. These extralegal incentives might be as strong or stronger than legal ones, are often of instrumental value in exchange transactions, and can be intrinsically valuable.

As Stewart Macaulay famously observed, "Businessmen often prefer to rely on 'a man's word' in a brief letter, a handshake, or 'common honesty and decency'—even when the transaction involves exposure to

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200 Stephen J. Choi & Mitu Gulati, *Contract as Statute*, 104 MICH. L. REV. 1129, 1162 (2006).

serious risks."[201] This does not mean businesspeople prefer no legal liability for breach. But expressing that preference might signal mistrust and perhaps also untrustworthiness.

Both formalities and evidentiary formalism generate relational costs of this type. Formalities are perforce juristic. To use a formality is to express an intention to effect a legal change. A requisite formality might therefore in some circumstances interfere with and erode extralegal forms of trust by forcing parties to say they want the protection of the law.[202] Plain meaning rules can generate relational costs of a similar type. Richard Posner, invoking his years of experience on the bench, argues that even in arms-length transactions the drafting incentives plain meaning rules create threaten extralegal trust:

> There is frequent conflict between lawyer and client over how detailed a contract should be, the former pushing for the inclusion of endless protective clauses and the latter worrying that pressing for such clauses will not only protract negotiations and increase legal fees but also make him seem a sharpie and kill the deal. Better that the contract should be kept reasonably short, and that if an unforeseen contingency arises it be resolved in a commonsensical fashion. It is reassuring to think that if one's contract should come to grief the court will straighten matters out in a "reasonable" way rather than by recourse to legal technicalities. Businessmen want judges to resolve interpretive issues in the way that a reasonable businessman would.[203]

To the extent plain meaning rules push parties to spell out in advance every aspect of their transaction, they can impede the development of extralegal forms of assurance.

Here theory again hits empirics. The existence and size of relational costs are likely to differ between different types of contractual transactions. A merger agreement between two multinational corporations is not the same as a long-term supply contract between two local businesses, which in turn differs from a promissory exchange between friends or family members. When formalities or evidentiary formalism will impose relational costs and how large those costs will be are empirical questions that theory can identify but not answer.

Moreover, the effects of legal rules on nonlegal forms of trust are complex. Lisa Bernstein suggests that in some contexts plain meaning

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201 Macaulay, *supra* note 195, at 58.

202 Klass, *supra* note 29, at 1474.

203 Richard A. Posner, *The Law and Economics of Contract Interpretation*, 83 TEX. L. REV. 1581, 1607 (2005) (citing BENJAMIN N. CARDOZO, THE NATURE OF THE JUDICIAL PROCESS 142–43 (1921)). Posner attributes what he sees as the excesses of New Formalism "in part to the fact that fewer and fewer legal academics have significant experience in the 'real world' of contract drafting or business litigation." *Id.* at 1592.

rules in fact promote extralegal trust.[204] Whereas Posner focuses on the time of formation, Bernstein looks to the effects of thick interpretive rules during performance. She argues that the Code's permissive rules for course of performance and course of dealings evidence deter parties during the life of a contract from making concessions that would promote extralegal forms of trust. When one party is out of compliance, the other might worry that a concession will later be used as evidence of the parties' agreement, thereby eroding their contractual rights. Thick interpretive rules might in this way discourage the flexible give-and-take that characterizes extralegal forms of trust.[205]

Where contract formalism comes with relational costs, one should expect even more Type II errors. Parties who prefer a legal change might choose not to employ a requisite formality or spell out every nuance of their shared understanding because each is concerned about the signal it will send the other.

The design solutions are the same as above. Plain meaning rules should not be the default interpretive approach but should apply only when parties have expressly chosen them or agreed that a writing shall serve as a final expression of their agreement. And formalist altering rules can be made optional by supplementing them with interpretive altering rules providing alternative paths to the same legal result. Such interpretive rules might be juristic, permitting the parties to use less formal words to express or indicate their legal intent. Or they might be nonjuristic, identifying acts that make legal liability appropriate even though the parties have not expressly asked for it.[206]

D. *The Case for Framework Formalities*

This Article has avoided generic arguments for or against formalism in contract law. But the above analysis suggests that the law of contract would benefit from more formalism of a specific type: legislatively or administratively established formalities for framework terms.

Consider the altering rule courts use to determine whether a writing is integrated. The underlying question is whether the parties have intended or agreed to the writing as a final expression of their agreement.

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204 Bernstein, *Merchant Law*, *supra* note 166, at 1807–15.

205 For more on the question, see Omri Ben-Shahar, *The Tentative Case Against Flexibility in Commercial Law*, 66 U. CHI. L. REV. 781, 781–85 (1999) (providing a formal argument that the use of past practices in interpretation both encourages and deters flexibility, and that in theory these effects cancel each other out).

206 For examples of the latter, see the analysis of spousal agreements in Klass, *supra* note 29, at 1488–97.

Where the parties have included a merger clause in the writing, that usually decides the matter—though in some jurisdictions, extrinsic evidence of the parties' contrary intent remains admissible.[207] Call this the *express prong* of the integration altering rule. Absent a merger clause, the court asks whether the writing appears intended as a final statement "in view of its completeness and specificity."[208] Call this the *implied prong* of the integration altering rule.

This Article questions the wisdom of the implied prong.[209] What this Article emphasizes here, however, is that both prongs are interpretive. They require the court to interpret the parties' intent with respect to integration. Yet integration itself is typically a juristic act: the law treats a writing as integrated because the parties have expressed their intent that it shall be integrated. Moreover, the legal effects of integration are simple and standardized: evidence of contrary or additional terms is excluded, and the writing is interpreted in accordance with its plain meaning.

Given all this, it is more than a little odd that the law does not provide a formality for the integration of contractual writings. Although form books are full of possible merger clauses, there exists in U.S. law no short, effective, standard formula, comparable to "F.O.B." or "as is," that parties can use to integrate a writing. The seal once served that purpose. But it was a blunt instrument, as putting a writing under seal had many other legal effects.[210]

What might such a formality look like? When one or both parties is nonsophisticated, one would want an ordinary language formality designed to inform parties of its effects. A rule that printing the words "Final Statement of All Terms" or "Final Statement of Terms Included" at the top of a writing suffices to integrate it would provide parties a useful tool for realizing their intent to integrate. One might also consider a pure formality that businesses or other sophisticated parties could use, comparable to "F.O.B."—maybe something like "F.S.A.T.," an abbreviation of "Final Statement of All Terms." That there are no integration formalities is a historical accident that might be easily remedied by statute.

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[207] Williston and Corbin fell on different sides of this divide. Williston was of the view that "the contract must appear on its face to be incomplete in order to permit parol evidence of additional terms." WILLISTON, *supra* note 1, § 633, at 1226. Corbin, on the contrary, held: "If the offered evidence is relevant and credible on the issue of . . . integration, it should never be excluded, for the reason that, whatever are the written words, those issues are always debatable." Corbin, *supra* note 2, at 173.

[208] RESTATEMENT (SECOND) OF CONTS. § 209(3) (AM. L. INST. 1981).

[209] *See* Klass, *supra* note 190, at 477–79.

[210] *See supra* Section III.A.2.

The same considerations apply to other contract terms that address not the substance of the parties' agreement but framework rules that govern its legal enforcement. Examples include choice of law clauses, choice of forum clauses, no-consequential-damages clauses, indemnification clauses, no-oral-modification clauses, and conditions precedent. All are perforce juristic acts, for each expresses an intent to alter the legal rules governing the agreement by the very expression of that intent. And their legal effects are relatively standard. As such, they are good candidates for formalistic altering rules. Providing formalities for each would save drafting and adjudication costs, make outcomes more knowable, and if properly designed produce legal outcomes that match the parties' intent. Nor are such formalities likely to entail significant relational costs. Because these acts are juristic ones, legal enforcement is already on the table. The parties are not relying on a mere handshake.

This Article's analysis suggests some basic guidelines for the design of such framework formalities. First, legislatures are more suited to creating them than are judges. Legislation can be both easily accessible and widely applicable; judicial decisions are often neither. And legislatures have familiar procedures for receiving input from market participants and other affected parties that courts do not. Second, when nonsophisticated parties are involved, framework formalities should wear their legal effects on their sleeves. They should be designed to indicate both that they are formalities and their legal effects. One can imagine, for example, a compendium of contract formalities each of the form: "Pursuant to the [State] Code of Formalities Section . . . ," followed by a short canonical ordinary language description of the legal effect, with the "pursuant to" clause putting users on notice that the words are a formality. Third, the legal effects associated with any given formality should be relatively simple. As the example of the seal illustrates, the more complex the legal effect, the more likely it is that users will employ or agree to the formality without understanding that legal effect. Fourth, framework formalities should be both optional and defeasible. Making the rule optional reduces the risk of Type II errors; making it defeasible reduces the risk of Type I errors.

Especially given the importance of industry participation and the existence of a national market, the Uniform Law Commission is especially well-suited to undertake the drafting of such legislation.

CONCLUSION

A large portion of contract law consists of altering rules that determine when a default legal state of affairs does and does not pertain. Salient design questions for such rules include: Should the altering rule employ a legal formality, either as sufficient to effect a legal change or as necessary and sufficient to do so? If lawmakers adopt a formalistic altering rule, what should the formality be? Should its legal effects be defeasible or nondefeasible? If lawmakers opt for an interpretive altering rule, how much evidence of meaning should interpreters be permitted to consider? When and how should interpretive formalism turn on party choice? And how might the law better empower parties to achieve the legal effects they intend?

This Article has not sought to answer all these questions for every type of term or transaction. The answers turn on variables that are unlikely to have the same values across all types of transactions, legal questions, or altering acts. It has instead provided a rubric for understanding and answering them in specific instances.

In the course of the analysis, however, one broad conclusion has emerged. Formalist rules of contract exposition make sense when two conditions are satisfied: the law seeks to give parties the power to purposively alter the legal state of affairs, and parties understand themselves to be exercising that power. Just when the first condition is met is a deeper question than this Article can answer. The many rules of contract law that empower parties to effect a legal change by expressing their intent to do so reflect the fact that contract law is designed to give individuals the power to change their legal situation when they wish. Formalities and evidentiary formalism serve that purpose. At the same time, the many contract rules that give legal effect to nonjuristic acts suggest that contract law often seeks to do more than give individuals that power. When the reason for altering the legal situation between the parties does not turn on their legal intent, neither a formality nor a plain meaning rule is likely to fully serve the law's ends.