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NEOFORMALISM IN A REAL WORLD OF FORMS

WILLIAM J. WOODWARD, JR.*

INTRODUCTION

“Reality-based” television is the latest fad to have worked its way into our national consciousness. It began with the “Real World,” a successful show on MTV, and has been followed by newer versions such as “Big Brother,” “Survivor,” “Survivor 2,” and (inevitably) “Temptation Island.” These shows purport to show “real” human beings solving the kinds of real problems that confront all of us. But “Real World” is an ironic title: while these shows are marketed to be more “real” than a sitcom or movie, they are anything but “real.” They involve strangers carefully selected and brought together by a producer to live with one another in an unnatural (or unusual) environment surrounded by TV cameras. Can we learn anything truly reflective of the human condition from these little dramas? Given the artificial and unnatural setting into which the individuals have been dropped, one must be extremely skeptical.

We encounter a similar problem when we attempt to project normative recommendations about the shape of the law using man-made models of citizen behavior. Such efforts usually involve an author’s construct of the contracting environment and projection from that model the rules she contends would improve the “real world” of contract law. Inevitably the models will be “off” to one degree or another and the contended-for rules will thus be “off” as well. Since modeling is probably an essential tool for making useful comments about law, the question is not *whether* the model is “off”—it always is; rather the question is how far off is the model from the phenomena it is supposed to model.

In contracts, the focus of this Symposium, the theorist’s job is harder today than it used to be because the modern, real world of contracting is understood to be far more complex than it was in earlier years. Beginning in the late 1950s, empirical studies have hinted at this complexity and confirmed a serious mismatch between our relatively simple rules of contract law and the complex environment within which it must operate. There has been a scholarly agenda for many years whose object has been to study and better understand the complex environment so that the rules might be better fitted to work within it.

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One of our oldest and most successful commercial statutes, article 2 of the Uniform Commercial Code (U.C.C.), is a statute that does not come close to mirroring the complexity of real world contracting. Indeed, its textual simplicity seems to stand in stark contrast with what we know about business contracting. Still, the Code seems to have accommodated business complexity very well. Its drafting began in the 1940s and it has remained largely unchanged since first widely adopted in the early 1960s. Its stability over time may well be due to its open structure which tends to use “standards” instead of “rules”¹ and, perhaps for that reason, tends to hide the very complex demands it makes of those who use it.² To the extent article 2 of the U.C.C. has influenced the development of business practice at all,³ the Code does not seem to have restricted its growth and development.

Recently, there has been a burst of scholarly activity that begins with now-familiar observations of real world complexity, moves in the direction of comparably simple rules, but tentatively advocates far sharper rules for contract law generally and article 2 of the Code in particular. These “Neoformalists”⁴ claim that predictability, certainty, and economic efficiency require a simple and more formal approach, not one that masks its complexity through the use of “standards” instead of “rules.” Much of the most interesting work focuses on the article 2 rules governing interpretation of contracts.

The normative theories coming from this recent work are complex; some are based on valuable new empirical observations suggesting that

1. With the rise of literature dealing with formalism has come a broad literature addressing the many ways that “rules” and “standards” differ from one another and why those differences matter. See generally Louis Kaplow, *Rules Versus Standards: An Economic Analysis*, 42 DUKE L.J. 557 (1992); Pierre J. Schlag, *Rules and Standards*, 33 UCLA L. REV. 379 (1985); Kathleen M. Sullivan, *Foreword: The Justices of Rules and Standards*, 106 HARV. L. REV. 22 (1992).

2. The Code can be characterized as tending to have flexible “standards” such as “reasonable” and “material” rather than “rules” and tends to be permissive in admitting complex evidence of the commercial context of any given Code contract. Formalism is not generally perceived to be its approach. See Robert E. Scott, *The Case for Formalism in Relational Contract* 94 NW. U. L. REV. 847, 866 (2000).

3. Many observations of the real world of business contracting suggest that contract rules do not have a great deal to do with observable business practices. See, e.g., Karl N. Llewellyn, *What Price Contract?—An Essay in Perspective*, 40 YALE L.J. 704 (1931); Stewart Macaulay, *The Use and Non-Use of Contracts in the Manufacturing Industry*, 9 PRAC. LAW. 13 (1963); Russell J. Weintraub, *A Survey of Contract Practice and Policy*, 1992 WIS. L. REV. 1.

4. There have been references to “neoformalists” in the contemporary literature. E.g., James G. Wilson, *The Morality of Formalism*, 33 UCLA L. REV. 431, 461 (1985). Professor Charny refers to the contemporaries as “anti-antiformalists” in David Charny, *The New Formalism in Contract*, 66 U. CHI. L. REV. 842 (1999) and explains how they differ from the “formalists” of the early 20th Century who were condemned by the Legal Realists. Professor Grey also distinguishes the new phenomenon from its ancestor in Thomas C. Grey, *The New Formalism*, Stanford Working Paper No. 4, at http://papers.ssrn.com/paper.taf?abstract_id=200732 (Sept. 6, 1999).

whole industries prefer a formal interpretive approach to one that is more nuanced. Yet the normative recommendations have a "Back to the Future" quality to them. For example, some have advocated much-reduced roles for trade usage⁵ and course of performance evidence in commercial contracts governed by the U.C.C.,⁶ and new life for the "plain meaning rule."⁷ Most of the approaches have been driven by economic models and an economic-type of analysis asserting that, ultimately, it is better—because it is more efficient—for courts to interpret contracts using a more formal approach and it would be better if our governing law would prompt or compel them to do so.

It seemed useful to review some of this recent literature and its critiques and then consider the implications of bringing these ideas into the "real world" of sales, which tends to be dominated by form contracts, rather than contracts that are actually negotiated, and which is governed by a U.C.C. sales law that functions across an extraordinarily wide range of contract settings. In short, I want to consider how "Neoformalism" might operate in the complex, real world populated by busy lawyers and real business people, and governed by article 2 of the U.C.C.

The discussion will proceed in two Parts. The first will abstractly consider formalism in contract interpretation in an attempt to see why a legislature might wish to increase interpretive formalism through a statute such as the U.C.C. It concludes that, ultimately, legislative decisions should depend on empirical evidence and that the empirical evidence for a move toward more formalism in contract interpretation is lacking. The second Part will consider the implications of bringing a more formal interpretive approach into the U.C.C. regardless of the quality of the reasons for doing so. It will conclude that, however theoretically justified it might be, such a change in the context of the actual operation of the U.C.C. will produce undesirable consequences that outweigh whatever benefits the change might bring.

I.

A. Formalism as Power Allocation

Surely one of the best conceptual introductions to formalism is a 1988 article by Professor Frederick Schauer.⁸ His arguments are difficult to do justice to in a short amount of space, but a key insight is that

5. See generally Lisa Bernstein, *Formalism in Commercial Law: The Questionable Empirical Basis of Article 2's Incorporation Strategy: A Preliminary Study*, 66 U. CHI. L. REV. 710 (1999).

6. *Id.*; Omri Ben-Shahar, *The Tentative Case Against Flexibility in Commercial Law*, 66 U. CHI. L. REV. 781 (1999).

7. Scott, *supra* note 2, at 848.

8. Frederick Schauer, *Formalism*, 97 YALE L.J. 509 (1988).

formalism is largely about power.⁹ As he developed it, formalism is denying a decision-maker the power to use her discretion in a given setting, even when that person's best judgment is that the discretionary outcome would be "better" than that dictated by a strict construction of the given rule. Formalism is denying the army private the discretion to decide not to march when given the order "march."¹⁰ In the more relevant context of legislation, a formal approach would limit a decision maker's broad interpretive powers and require deference to legislative language even if the result were absurd.¹¹ By contrast, a less formal approach might have the court taking an active lawmaking role to reach the "right result" in the interests of justice, even if the language to be interpreted didn't quite produce the result unaided. If formalism in interpretation is ultimately about power, this question of power begs an earlier question: who or what dictates the allocation to or away from courts?

When deciding the approach to interpreting statutes, many would agree that the likely power source on questions of statutory interpretation ought to be "the legislature." One might imagine a legislature demanding that judges interpret a given statute literalistically,¹² or the other way around.¹³ Judges themselves might also limit their own power by deciding that, for one reason or another, the power to make a purposive interpretation of a statute was outside their "jurisdiction" (to use Schauer's term).¹⁴ Inasmuch as our common law (and even constitutional law) traditions have courts functioning as lawmakers as well as law-interpreters, and inasmuch as many courts will see their roles as generalists to include reaching sensible results in individual cases unless told to do otherwise, one might expect judicial self-discipline without

9. *Id.* at 543.

10. *See id.* at 531.

11. *Id.* at 543.

12. Such would be the inference one might draw from many of the provisions of new U.C.C. Article 9. Compare U.C.C. § 9-102 (2000 revision), which has some eighty definitions, with the current statute which, in U.C.C. §§ 9-105 to 9-107 (1994) and other scattered provisions, has less than half as many definitions.

13. The Sherman Act is an example of a statute where Congress left the courts a great deal of discretion. *See* 15 U.S.C. §§ 1-15 (1994); *see* Grey, *supra* note 4.

14. Schauer, *supra* note 8, at 540. Examples of this phenomenon might be found in some recent Supreme Court rulings in the bankruptcy area. *See generally* Lawrence Ponoroff, *The Dubious Role of Precedent in the Quest for First Principles in the Reform of the Bankruptcy Code: Some Lessons from the Civil Law and Realist Traditions*, 74 AM. BANKR. L. J. 173 (2000); Daniel J. Bussel, *Textualism's Failures: A Study of Overruled Bankruptcy Decisions*, 53 VAND. L. REV. 887 (2000). Courts can rationalize a stricter, more formal approach to statutory interpretation as giving legislatures "incentives" to legislate more carefully. That this sort of formalistic interpretation was not intended by Congress in the bankruptcy area (or, alternatively, that Congress was, indeed, in need of Supreme Court "discipline") is suggested by the fact that Congress has legislatively overruled several of these "textual" decisions. *Id.* at 887.

some form of legislative mandate to be the exceptional rather than the common occurrence.¹⁵

In the context of legislation, whether a given approach to interpretation should be characterized as “formal” depends to a large extent on whether the court has an opportunity to “make things better” or to search for the “right result” even when the language of the rule seems to dictate something different.¹⁶ Schauer’s focus was on the extent to which the judge had been denied any discretionary role in making a decision. If she was, then a formal approach to the reading of the statute was called for; the judge was merely required to determine whether the problem was “within” or “outside of” the statute.¹⁷

Moving from statutes to commercial law and contracts more generally, we encounter another dimension when considering the role of formalism in interpretation. Formalism-as-power here is complicated by the presence of the contracting parties and the strong norm in commercial law to give the parties what they want, a norm sloganized as “freedom of contract.”¹⁸ If we look for power sources for a formalistic approach to interpreting language in commercial contracts, there are not two sets of relevant actors, there are three: the courts, the legislatures, and the parties themselves.

Nearly everyone would agree that when setting out the terms of an agreement, the parties have, in a fairly real sense, become the primary¹⁹ “lawmakers.”²⁰ Schauer’s analysis would suggest that, as to matters of interpretation of agreements (as opposed to statutes), an added question might be whether *the parties* have withdrawn from the court the power or opportunity to give a purposive interpretation of their agreement, even when such an interpretation seems to deviate from the mandates they have placed into their writing. In other words, in the contract setting,

15. Cf. Sullivan, *supra* note 1, at 123 (“In [the Justices of Rules’] view, only rules can discipline the courts and thus maintain judicial legitimacy as a non-political branch.”).

16. See Schauer, *supra* note 8, at 510.

17. *Id.* at 539-40.

18. Contract law also has a regulatory aspect that is often hidden from view. See, e.g., Jean Braucher, *Contract Versus Contractarianism: The Regulatory Role of Contract Law*, 47 WASH. & LEE L. REV. 697 (1990). While these regulatory aspects might enter a judicial decision through the back door of contract interpretation, how the courts interpret the parties’ deal is, arguably, the area in which the parties’ views should be dominant.

19. One subscribing to a strong version of “freedom of contract” ideology, for example, Richard A. Epstein, *Confusion about Custom: Disentangling Informal Customs from Standard Contractual Provisions*, 66 U. CHI. L. REV. 821, 828 (1999), might urge that the parties are the *only* lawmakers as to matters of interpretation. Even here, however, matters may not be entirely in the parties’ hands. While the analysis might be couched in terms of “party intent,” many decisions are easily understood as expressions of community or social values masquerading under the guise of “party intent.” See K.N. Llewellyn, *Book Review*, 52 HARV. L. REV. 700, 702-03 (1939). This is as it should be in a legal enforcement system that is based, at least in part, on “doing justice.”

20. W. David Slawson, *Standard Form Contracts and Democratic Control of Lawmaking Power*, 84 HARV. L. REV. 529, 530 (1971).

Schauer's analysis might translate into the extent to which the parties (as primary—but not exclusive—"lawgivers")²¹ have created a "rule" in their document which they intend courts to apply mechanically despite the possibility of a "better," "fairer," or "more just" decision when looking at the whole situation.

B. Contract Law Applications

The parol evidence rule is a prime battleground for a debate about formalism in interpreting contracts. As is well known, the rule aims to limit the evidence a court can consider in deciding what the ambit and meaning of the parties' agreement is. Ignoring its myriad exceptions and subtleties,²² the dominant parol evidence rule and related "plain meaning rule"²³ question is whether the writing is to be deferred to by the court (and therefore, read to mean what it seems to say "on its face") or whether the court may go beyond the writing to discover whether the interpretation contended for actually advances the parties' "real" intentions.

If the question were whether to construe a statute in a formal way, one would ask whether the legislature (or the judge in a showing of modesty²⁴ or self-control) had decided that a purposive interpretation was off-limits. If the discretion of the army private were the focus, one would ask if her superiors had withdrawn the authority to determine whether marching at that particular moment was the "best alternative under all the circumstances" when she heard the order "March."

In the contract setting, the formality with which a court approaches the interpretative question depends on whether purposive interpretation had or had not been withdrawn from the court. And if Schauer's analysis is correct, that formalism is all about power, it is useful then to ask this question: if the power had been withdrawn from the court, who withdrew it?

21. *Id.*

22. Thayer referred to this character of the Rule early with his near-famous comment that "few things are darker than this or fuller of subtle difficulties." Thayer, *The "Parol Evidence" Rule*, 6 HARV. L. REV. 325 (1893).

23. I have merged the two rules for simplicity of discussion. It is "hornbook law" that the parol evidence rule does not bar evidence of what the words of the writing mean. E. ALLAN FARNSWORTH, *CONTRACTS* § 7.3, at 461 (1982). Of course, the alert advocate will find such evidence of meaning in the pre-writing negotiations of the parties, the same negotiation evidence which the parol evidence rule aims to exclude. This large loophole in the parol evidence rule is traditionally plugged by the "plain meaning" rule which requires a court to interpret the contract from the "plain meaning" of the writing rather than from extrinsic evidence supplied by the parties. It does not do for a theorist advocating more formality in contract interpretation to advocate a tighter parol evidence rule without also advocating a return to a plain meaning approach to interpreting writings. See, e.g., Scott, *supra* note 2.

24. Cf. Schauer, *supra* note 8, at 543.

As suggested above, in the contract setting, one would think the parties should be preeminent in deciding how others will interpret an agreement they have made. The free market system is grounded on the primacy of the parties and the effectuation of their “true” contractual intent.²⁵ If the parties wished a formalistic approach on the one hand or a purposive one on the other, and if we regard their intent on how others should interpret their agreement to be of prime importance,²⁶ then a court, one would think, would be guided—whether constrained or liberated—by their decision.

If formalism really is about power, then Schauer’s analysis sheds light on a key historical debate about the parol evidence rule: how a court should go about determining whether the agreement is “complete” so that the rule bars the admission of evidence of terms not in the writing. The central historical debate has been whether to judge that question from the face of the document, or to take evidence from the parties on their intent to integrate the document.²⁷ If the parties are the primary “lawgivers” in matters of contract interpretation, it would follow as a matter of first approximation, that Professor Corbin and Justice Traynor had the right approach to the parol evidence rule when they advocated the consideration of extrinsic evidence. Whether, and to what extent, a court is to consider the document integrated ought to depend in the first instance on how the *parties* intended the court to go about its interpretive job.²⁸

More generally, if the parties are the primary lawgivers on interpretive matters in commercial law, this might also suggest that the U.C.C. has the right approach to incorporation of trade usage and the like in the absence of party intent to the contrary. After all, the parties did negotiate in *some* context and one might consider it unlikely that they would wish an interpretive approach that jettisoned the context within which they contracted. If the parties want a less obvious approach to

25. The battle cry of “freedom of contract” is often heard in connection with neoformalist attacks on the status quo. See, e.g., Epstein, *supra* note 19, at 822, 830.

26. As suggested above, see *supra* note 19, one’s view of the exclusive role of party intent in matters of interpretation depends on how strongly one subscribes to the ideology of “freedom of contract.” As suggested in the last note, neoformalists tend to embrace the norm more strongly than commentators of other persuasions. The discussion here asks how neoformalism would operate in the real world and, for purposes of advancing that argument, I will give party intent more primacy than I might in a different context.

27. One of the best discussions of this debate is John D. Calamari & Joseph M. Perillo, *A Plea for a Uniform Parol Evidence Rule and Principles of Contract Interpretation*, 42 IND. L.J. 333 (1967).

28. Compare the interpretive approach of Justice Traynor in *Masterson v. Sine*, 436 P.2d 561 (Cal. 1968), with the relatively more formal approach of the court in *Mitchell v. Lath*, 160 N.E. 646 (N.Y. 1928). While one might imagine the text of a large negotiated contract providing strong evidence of an intent to integrate, see, e.g., *Betaeo, Inc. v. Cessna Aircraft Co.*, 103 F.3d 1281 (7th Cir.1996), the contrary will clearly be true in very large numbers of the kinds of commercial contracts on which we will focus here.

interpretation, they can signal that to a court, and if the parties' intent is "the law," a court ought to follow it.

It is probably agreed by all that when the parties have created their rule—say that the seller will deliver 100 widgets—the court should defer to their intent. A critical component in reading their intent is whether to approach the interpretive problem formalistically or purposively. Schauer's analysis helps us see that to approach the interpretive question formally, we must conclude that, as a matter of power, the court has no business dealing in—and has nothing useful to add to—what the parties apparently brought to this problem in their document. But, as just suggested, that question—what approach the court should take in deciphering the parties' agreement—has to depend on an earlier question: is it someone's intent that the court be so modest, or formal, in considering the parties' text and, if so, whose intent is it that the court take that approach?

Those who would advocate the creation of more formal interpretive methods in the U.C.C. make the State (through the U.C.C.) a more direct partner in the process of interpreting private agreements. The State, not the parties, will dictate (at least in the first instance) whether or not evidence outside the writing ought to be looked at by the court. On what basis might the State dictate the interpretive approach in this situation?

One obviously well-worn approach is to consider that the State's involvement in the matter is simply the State's creating the background or default rule.²⁹ If a particular interpretive approach and its translation into a U.C.C. rule of interpretation emanated from what the parties in the large run of cases otherwise intended, then a default rule to this effect would save the parties the effort of specifying the power allocation as between the parties and a court within their contract. If most parties "want" a formalistic (or, alternatively, a purposive) approach, it is cheaper to set that approach as a default rule than effectively to require the parties to specify the approach in each contract. The position one takes in setting this default rule ultimately depends on empirical evidence that contracting parties "usually" want one approach to a given matter or another. Such evidence, as we have seen, is often inconclusive.

Industry tolerance for the U.C.C.'s flexible parol evidence rule in article 2 and the Code's embrace of the incorporation of trade usage and the like even where there are express agreements,³⁰ might contribute

29. Where transactions costs are too high for parties to fashion their own rule, it seems normatively correct to provide them with the rule that they probably would have chosen for themselves at the time of contracting had they been able to bargain. Atypical parties, after all, are not disadvantaged by the specification of a "majoritarian" default rule, as they remain free to opt out of the default and design their own tailor-made alternative. See Scott, *supra* note 2, at 850.

30. The new Uniform Computer Information and Transactions Act (UCITA) has partly followed the approach of U.C.C. article 2 for many interpretive matters. *E.g.*, UCITA § 101(4) (definition of "agreement" includes trade usage and the like); § 301

quasi-empirical support to the proposition that contracting parties in the majority of cases desire a default rule that does not remove judicial power to make sense of a situation that might come before a court.³¹ If, as has been alleged, business lawyers dominate the U.C.C. revision process,³² one might interpret the reaffirmation of the Code's approach as a "vote" against a more formal approach by those whose clients are affected by the law.³³

(parol evidence similar to U.C.C. § 2-202); § 302 (hierarchy of express terms, course of performance, course of dealing, and trade usage similar to U.C.C. §§ 1-205 and 2-208). It has been widely believed that the UCITA drafting effort was dominated by persons from the software industry who were able to obtain many provisions to their liking. The fact that they did not insist on (or, apparently advocate) a more formal approach to interpretive matters might suggest, as an empirical matter, that they didn't *want* a formal approach to interpretation of the contracts controlled by those provisions of the statute.

31. The fact that the Code's approach to interpretation has not only been re-incorporated but also subsequently incorporated into a new statute such as UCITA suggests, at least, no widespread dissatisfaction of business lawyers with the current rules. The lawyers involved in U.C.C. revision are typically involved with the American Bar Association's Section of Business Law. This entity is, in turn, dominated by transactional lawyers who worry most about the certainty and predictability the contracts that they draft will have in the courts. Many include in their practices the drafting of form contracts, to be used "as is" by the masses with whom their clients do business.

On the other hand, the complexity of the process that generates the U.C.C. cautions against drawing any strong empirical conclusions from the existence of any particular Code rules. The rules of interpretation could, for example, be explained as simple inertia. The realities of the U.C.C. (and Uniform Laws) enactment process caution statute drafters not to diverge too far from the status quo lest enactment be imperiled. *See generally* William J. Woodward, Jr., *The Realist and Secured Credit: Grant Gilmore, Common Law Courts, and the Article 9 Reform Process*, 82 CORN. L. REV. 1511 (1997). On the other hand, some rules of the U.C.C. are changed in the revision process if they are perceived to be a source of difficulty. A telling example is proposed U.C.C. § 2-207. *See discussion infra* Part II.A.2.

32. *See, e.g.*, Robert E. Scott, *The Politics of Article 9*, 80 VA. L. REV. 1783 (1994); William J. Woodward, Jr., *Private Legislation in the United States—How the Uniform Commercial Code Becomes Law*, 72 TEM. L. REV. 451 (1999). The alleged dominance of industry lawyers in the article 9 revision process may be manifest in the appearance of the new statute. What will replace old article 9 is a far more technical, far more formal statute than its predecessor. Indeed, this phenomenon resembles what Professor Bernstein observed in the trades that she studied. Bernstein, *supra* note 5.

What is different from the trade codes Professor Bernstein observed is that new article 9 will cover those outside the "trade," that is, borrowers. It is a very different matter to write a trade code to govern members of a trade than it is to govern both trade members and those outsiders who do business with the trade members.

33. Purposive interpretation is, of course, more costly than is formalistic interpretation because it considers more evidence. Thus, the U.C.C.'s position on the question could be interpreted as an expression of lawyer self-interest and not the preferences of the clients. On the other hand, it is widely recognized that a more formal adjudicatory regime will force more care—and therefore lawyer costs—into the drafting of contracts; indeed, giving others incentives to be careful in their contract drafting is one of the instrumental arguments made in support of more formalism in contract interpretation. Which approach is more in lawyers' self-interest is unknown. Suffice it to say that far more contracts are negotiated than are litigated. If lawyer self-interest were

Professor Lisa Bernstein has supplied evidence that might suggest the opposite. She studied both the development of trade codes³⁴ and the dispute resolution preferences³⁵ of several discrete trades. The trades she studied seemed to prefer dispute resolution that tended to be formal,³⁶ and trades had great difficulty agreeing on what their "usages" were when attempting to codify them.³⁷ Assuming it points in a more formal direction, research into discrete industries, while valuable, is very inconclusive on the desires of business people more generally. Business people in situations where transactions are highly homogenous may have completely different needs and desires than those parties to the broad, heterogeneous range of transactions the Code covers.

Similarly, if as Professor Bernstein suggests,³⁸ "trade usages" as envisioned by Llewellyn do not, in fact, exist, then the idea that contracting parties would, by default, allocate power to courts to interpret their agreements by reference to such (non-existent) usages is absurd. Instead of having the U.C.C.'s broad embrace of trade usage and related evidence (and therefore, the allocation of power to courts to engage in somewhat more purposive interpretation of cases before them), one could construct the opposite default rule, that trade usage is not to be considered by a court (because it is non-existent or rare) unless the parties explicitly give power to the court to consider it through their contract.³⁹

This position, too, ultimately rests on "real world" empirical facts, and here, once again, one can read Lisa Bernstein's valuable empirical investigations of several trades as suggesting that commercial parties would, in fact, prefer the default rule on trade usage opposite to that found

dominant, a more formalist interpretive regime might well yield more lawyer business than a less formal approach.

34. Bernstein, *supra* note 5.

35. Lisa Bernstein, *Merchant Law in a Merchant Court: Rethinking the Code's Search for Immanent Business Norms*, 144 U. PA. L. REV. 1765 (1996).

36. *Id.* at 1769-70.

37. Bernstein, *supra* note 5, at 719.

38. *Id.* at 716. Again, Professor Bernstein has made a valuable contribution in showing the difficulty of accommodating the kinds of trade usage she discovered with the vision of Karl Llewellyn.

39. Professor Bernstein does not go nearly that far. Rather, she argues that the Code be amended to include a "safe harbor" provision that would give merchant-transactors a simple and reliable way either to opt out of the Code's adjudicative approach or selectively opt out of its usage of trade, course of performance, or course of dealing provisions. Such a safe harbor would enable merchant-transactors to select their preferred degree of conceptualized adjudication and would transform the Code's quasi-mandatory interpretive approach into a default approach that merchant-transactors could avoid when they found it advantageous to do so. Bernstein, *supra* note 35, at 1821. She argues only for a safe harbor because "the Code also governs other types of contracting relationships, such as merchant-to-consumer transactions, where the arguments in favor of contextualized adjudication may be stronger than they are in merchant-to-merchant transaction." *Id.* at 1820-21.

in the U.C.C.⁴⁰ But the world of specific trades may not correctly model the world in which the U.C.C. must operate. Trade usage issues may well be less likely to surface, for example, in contract cases where both parties (and perhaps the arbitrator) are members of the same industry. Such questions may well be more common in disputes between parties in different industries and the usages (if we can call them that, “contexts” if we cannot) may well be vaguer than those Professor Bernstein uncovered, tantamount to “in my world we understand things this way.”⁴¹ If those are the empirical facts, then the operation of trade usage in specific, narrow trades is less significant in understanding the operation of the Code’s rules and their ability to bring positive results to interpretive questions. This would obviously be true whether or not Karl Llewellyn had the right idea of their existence and operation.

While likely to be couched in efficiency terms, these kinds of default rules reduce transaction costs precisely because they do by rule what the parties otherwise would have to do by contract provision.⁴² If contracting parties generally wished for a more formal approach to some aspect of interpretation and the Code embraced this desire by rule,⁴³ an enacting legislature would have, in effect, acted as an agent for the bulk of contracting parties and saved them the trouble of providing for such an approach in their individual contracts. Such a rule would remove from courts the power (and indeed the temptation) to engage in purposive interpretation of agreements using the now-forbidden evidence; the legislature’s basis for doing so would rest (as would the construction of the opposite baseline rule), ultimately, on party intent, expressed here through aggregated practice.

Thus far, as between the parties to contracts, the courts, and the legislatures, the construction of default rules such as these do not implicate a sharp clash between party will (considered in the aggregate) and the legislature. Rather, the legislature would have simply determined that most parties either do, or wish to, contract in a particular way and constructed a general rule to save them the trouble of doing it in every contract. There are, however, at least two justifications for legislative power-setting that do not proceed so directly from contracting parties and implementing their empirically-determined intent.

The first is the idea of creating rules not because it is what people generally desire, but because it will make them behave one way or the other, either in the initial contracting process or during performance.

40. Cf. David Charny, *Formalism in Commercial Law: The New Formalism in Contract*, 66 U. CHI. L. REV. 842, 847 (1999).

41. See, e.g., *Frigalimont Importing Co. Ltd. v. B.N.S. Int’l Sales Corp.*, 190 F. Supp. 116, 119 (S.D.N.Y. 1960).

42. See ROBERT SCOTT & DOUGLAS LESLIE, *CONTRACT LAW AND THEORY* 94-95 (2d ed. 1993).

43. For an example of such a formal rule that was considered and then dropped by the Code drafters, see discussion *infra* Part II.B.

When it works, this approach, first used to analyze *Hadley v. Baxendale's* consequential damages rule,⁴⁴ can induce the exchange of information or encourage settlement which, presumably, would not have occurred as much absent the rule. Using such "penalty default" rules is an unabashedly instrumental approach: the State creates the rule not because, in some sense, it is the rule most parties want; rather it creates the rule to motivate action—to force information exchange, to motivate parties toward settlement, etc.⁴⁵ The "plain meaning rule" can be seen as an illustration of this approach: if parties know that their contract will be interpreted in a standardized way, they will take care to draft it using standardized terms.⁴⁶

A fresh version of this approach is the idea that if the U.C.C. were to scale back on permissive use of trade usage, contracting parties would learn that such evidence would be unavailable to them at trial and, as a result, spend more time at the outset setting out terms and thereby make contracting more predictable and certain. Another contemporary example would reduce the Code's permissive use of evidence of the parties' course of performance.⁴⁷ The rationale here is that the current permissive approach can make the parties distrustful of, and inflexible with, one another while performing their contract because they will fear that whatever breaks they extend to the other side will change the deal they struck at the outset. With the opposite rule, it is contended they will be more flexible in performing their contract because they won't have to worry about the effects of past practice on adjudication. Put more simply, allowing course of performance evidence at adjudication "causes" inflexibility in performance; removing the use of this evidence at the adjudication stage will unlock flexibility at the performance stage.⁴⁸

Whether instrumental "motivators" such as these will work depends on whether the targets of the rules will learn of them and whether those targeted will in fact behave as predicted once they learn. These are empirical questions but, starting with Stewart Macaulay's work in the 1960s, there has developed a strong empirical basis for believing that business people make and perform agreements in ways one would not predict from a study of legal rules and the incentives those rules are said

44. Ian Ayers & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 *YALE L.J.* 87 (1989).

45. Compare Bernstein, *supra* note 5, at 778 n. 243.

46. We can also view it as a "majoritarian" default rule, that is, one that most parties *would* select, given the chance. One, presumably, chooses between the two rationales for the rule on the basis of empirical evidence.

47. See Ben-Shahar, *supra* note 6, at 789-93; Bernstein *supra* note 35.

48. Obviously, this contention can be justified as an "ordinary" default rule based on the idea that most contracting parties "want" the disallowance of course of performance evidence at trial. Professor Bernstein's empirical insights into "relationship preserving norms" and "end game norms" can be seen as specific examples of the experience and desires of most commercial contracting parties.

provide to those subject to them.⁴⁹ Classical formalism—the approach that gave us the “plain meaning rule” and the “duty to read”—was a dominant approach to interpretation in the early twentieth century.⁵⁰ It was thought to produce more care with written agreements but was later condemned as actually generating uncertainty in case outcomes. Importantly, however, no empirical evidence has ever surfaced to show that the approach actually “caused” enough care in drafting on the one hand or in reading contracts on the other to offset the undesirable effects of the approach.

If State-imposed instrumental rules such as these lack the capacity to motivate the behavior of a reasonably large number of contracting parties, such rules will be very counterproductive, even if measured strictly in efficiency terms. The parties who do not learn of the rule or appropriately respond to it will be stuck with a result that, by hypothesis, they may not want—an inefficient outcome. Persuasive evidence of the instrumental effectiveness of interpretive rules is wholly lacking.

A second reason for the State (as distinguished from the parties or the legislature as their agent) removing power from judges by requiring them to proceed more formally has recently been advanced. This shares a perspective developed for generations of contracts students by the stories in Richard Danzig’s book, *The Capability Problem in Contract Law*.⁵¹ An essential insight that Danzig’s series of vignettes brings to the student is the chaotic nature of the adversary process and the number of irrelevant factors that can limit attempts to advance the underlying goals (whatever they may be) of the legal system.⁵² Those factors include the preparedness of the lawyers,⁵³ the availability of witnesses,⁵⁴ and to some extent, the capabilities of various actors in the legal system.⁵⁵

These ideas find their contemporary manifestation in the far more simple proposition that judges may be “incompetent” to the task of full-bodied interpretation.⁵⁶ From this premise follows the solution, which is

49. See sources cited *supra* note 3. Empirical work in the bankruptcy area has surfaced a similar disparity between the law on the books and the law in action. See, e.g., Jean Braucher, *Lawyers and Consumer Bankruptcy: One Code, Many Cultures*, 67 AM. BANKR. L.J. 501 (1993).

50. Professor Grey gives a history of classical formalism in Grey, *supra* note 4, at 5-15.

51. RICHARD DANZIG, *THE CAPABILITY PROBLEM IN CONTRACT LAW: FURTHER READINGS ON WELL-KNOWN CASES* (1978). The “Wisconsin Contracts Materials,” now STEWART MACAULAY ET AL., *CONTRACTS: LAW IN ACTION* (1995), have been developing these insights since the early 1970s; its authors were directly involved in creating at least two of the seven chapters that make up the Danzig book.

52. See DANZIG, *supra* note 51, at 1-3.

53. See *id.* at 15-18.

54. See *id.* at 141.

55. See *id.* at 223-53.

56. Eric A. Posner, *A Theory of Contract Law Under Conditions of Radical Judicial Error*, 94 NW. U. L. REV. 749 (2000); Scott, *supra* note 2, at 859-62.

to remove from judges (or have them decline to exercise) the power to engage in such interpretation and, instead, to limit their approach to interpretation to that which is more formal. Once again, if, using Schauer's lens, the move to formalism is seen as a shift in power, here the shift is from the parties (who may or may not desire a formal approach to interpretation) or the court (who may or may not feel "incompetent" to the given task) to the legislature which (if the solution works) has deprived both the courts and the parties from engaging in a more free-ranging approach to interpretation. There is no hard empirical evidence that courts are, in fact, incompetent to perform the difficult interpretive job modern commercial law hands to them⁵⁷ or that results in litigation would be more predictable, understandable, or fair with a more formal approach.⁵⁸

As many have suggested, whether we ought to move to a more formalistic, simpler contract law ultimately rests on empirical evidence which, thus far, is very inconclusive. Do the bulk of contracting parties "want" more formal adjudication? Or are they content with the status quo? At what rate do businesses respond to incentives in the law of contracts, particularly to those designed to induce action that may be different from what they would normally do? Professor Bernstein has made a wonderful and laudable contribution to the mountain of empirical work that needs doing, but generalizing from observations in discrete, relatively homogeneous business areas to the broad spectrum of contracts covered by the Uniform Commercial Code is unjustified at this point.⁵⁹

57. Cf. Elizabeth Mertz, *An Afterword: Tapping the Promise of Relational Contract Theory—'Real' Legal Language and a New Legal Realism*, 94 NW. U. L. REV. 909, 918 (2000).

58. *Id.* Case law can provide very little empirical evidence on this point of judicial competency. Among other things, a more formal approach to adjudication is less labor-intensive than is a more open approach and one cannot exclude the possibility that those courts that use a formal approach do so as a labor-saving device rather than out of modesty. Similarly, an essential teaching of Legal Realism is to watch what courts *do*, not what they say. "Plain meaning" interpretations cannot necessarily stand for either judicial modesty or confession of incompetence. They could, on the contrary, stand for judicial competency and creativity in rule-choice in order to reach a satisfactory result in the particular setting of an individual case. Moreover, one cannot discount the possibility that the set of reported cases is not in any sense, a "random sample" either of disputes requiring some form of intervention or of disputes that reach the courts. For the suggestion that the actual construction of precedent can depend on lawyer strategy, see Marc Galanter, *Why the "Haves" Come Out Ahead: Speculations on the Limits of Legal Change*, 9 L. & SOC'Y. REV. 95 (1974). A modern treatment that is based, in part, on Professor Galanter's analysis is Lynn M. LoPucki & Walter O. Weyrauch, *A Theory of Legal Strategy* 49 DUKE L.J. 1405 (2000).

59. Dean Robert Scott has suggested that the empirical evidence is sufficiently strong at this point as to shift the burden to others to justify the U.C.C.'s retention of its current approach. See Scott, *supra* note 2, at 848. While, obviously, I disagree about the strength of the new evidence, Dean Scott himself was one of the first to observe the strong influence of business lawyers in the "private legislature" that produces the U.C.C. Robert E. Scott, *The Politics of Article 9*, 80 VA. L. REV. 1783 (1994). Even though their voices

II.

Part I contended that the empirical support for more interpretive formalism in the U.C.C. was lacking. This Part will consider the consequences that would likely follow if more interpretive formalism were brought into the U.C.C., regardless of the underlying justification. Here the discussion will be limited to business contracts but will further be limited to business contracts of one particular kind: those business contracts in which one or the other party specifies the standard terms in a form for a mass market and permits little or no adjustment of those standard terms in the making of its contracts.⁶⁰ The exact edges of this working definition are unimportant for my purposes,⁶¹ however it is interpreted, the category includes most contracts within the chains of distribution.⁶²

To compound matters, the Code has made my job a little more difficult by drawing a sharp (formal) distinction between contracts where only one business uses a form, and those where both businesses use forms, the latter being treated by the Code's famous "battle of the forms" section.⁶³ So, within the broad category of business form contracts, I will have to consider the impact of more Code formalism on the two kinds of form contracts separately.

are far more diverse in the article 2 context than they are within Article 9, *see* Scott, *supra* at 1825, if there were a business consensus toward more formal interpretation, one might expect to see it develop in the statute, at least with respect to non-consumers. As will be seen below, such initiatives have been rejected by those who drafted the U.C.C.

60. Within this category are contracts which begin on one party's or the other's form but are then negotiated to some extent. A far stronger case might be made for a formalistic approach to interpretation in such contracts than in those of a more "adhesive" nature; but unless one kind of such contracts can be distinguished from the other, treating them all using one approach will be counterproductive.

61. Professor Rakoff more precisely defines "adhesion contracts." Todd D. Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96 HARV. L. REV. 1173 (1983).

62. Professor Slawson put the figure at ninety-nine percent in 1971, but did not include many informal contracts in his universe of "all" contracts. Slawson, *supra* note 20, at 529. Professor Rakoff was comfortable that adhesion contracts represented a majority of *all* contracts, including in his wider universe theater tickets, babysitter contracts, cash sales, and the like. *See* Rakoff, *supra* note 61, at 1189 n. 57. Once we shrink Professor Rakoff's universe to "business contracts" within our system of distribution of goods, the percentage of form contracts will be larger, perhaps far larger. Indeed, it is hard to think of any but an amateur business that will not use some kind of form contract for most of its recurring purchases and non-consumer sales.

The category obviously does not include those longer-term supply and other relationships which the parties actually negotiate in advance and then perform through discrete purchase orders or other mechanisms. These kinds of contracts occupy an important niche in the distributional system, but how large a niche is unknown.

63. U.C.C. § 2-207 (2000).

A. Formalism in the Context of Business Form Contracts

1. ONE FORM BUSINESS CONTRACTS

Most of the literature promoting an increase in interpretive formalism in Code methodology builds the analysis on a free, informed contracting model and on the assumption that both parties understand and desire either the whole contract with the terms within it, or the discrete term at issue,⁶⁴ and the neoformalists have, by and large, been working with this simple model. Obviously, if many of the U.C.C. contracts in question do not resemble the contracts used in the model, the analysis has encountered a problem.

A superficially easy way for the analyst to reduce the criticisms one might level at analysis built on a "free contracting" model is to limit the normative target to some subset of all contracts. Those who press for more Code formalism have, for the most part, excluded consumer transactions from their analysis.⁶⁵ But this leaves all other Code contracts. These commercial contracts can be large or small, negotiated or non-negotiated. "Commercial contracts" includes the huge subset of form contracts that is my focus.

The lawyer buying a \$100 software program who, through the clickwrap, "chooses" the (very different) law of Maryland, is making a "commercial contract" just as is a business acquiring multi-million dollar equipment.⁶⁶ While the U.C.C. has effectively lumped both of these

64. Professor Richard Epstein appears to assume that nearly all business contracts are full and complete agreements which may be found almost entirely in the writing. He rejects Kessler and Gilmore's statement that "[o]nly an infinitesimal fraction of [parties' assumptions about the future] ever comes to the conscious attention of the parties; as with the iceberg, the great bulk of the contractual construct lies beneath the surface." Instead, he claims:

Sorry. If anything, the ratio is reversed in standard merchant transactions. Only an infinitesimal fraction of contingencies (by probability of occurrence) are not covered; most of this iceberg floats above the surface. No one who has ever looked at a well-drafted trust instrument (a contract, as it were, for one person) could bemoan the paltry capacities of language; when time pressures and tactical issues are suppressed, the precision and completeness of language prove remarkable.

Epstein, *supra* note 19, at 827-28. One can give the point to Professor Epstein when only one person is making "a contract." If Professor Epstein is talking about the business adhesion contract, he is correct, but it begs the question of the quality of the "agreement" of the non-drafter to the form. His observation both begs the question of "agreement" and makes little sense in a battle of the forms setting. Other contemporary theorists contend that most contracts are "incomplete." See, e.g., Alan Schwartz, *Relational Contracts in the Courts: An Analysis of Incomplete Agreements and Judicial Strategies*, 21 J. LEGAL STUD. 271, 278-79 (1992).

65. For example, Professor Bernstein limits her analysis to "disputes between merchants." Bernstein, *supra* note 5, at 712 n.4.

66. The purchasing agent for a large corporation may learn the terms of its vendors' contracts if it does repeat business with them but, in those circumstances, it may

contracts (and everything in between) together by differentiating only “consumer contracts” for special treatment, that fact does little to suggest that, as a normative matter, we can use one or the other kind of “commercial contract” as a model to generate optimal rules for all contracts between these different extremes. In particular, these two paradigm “commercial contracts” are different in just about every way imaginable except as to the general statements of law said to govern them. The U.C.C. has partly recognized this by treating a sizeable subset of these contracts—those involving two forms—with its “battle of the forms” rule. But apart from those, there has been little distinction made between “adhesive” form contracts and negotiated contracts within our black letter commercial statutes.⁶⁷ They are all treated as the Code contracts that remain once we have removed “consumer contracts” for special treatment.

In the context of interpreting whether a given party has assented to a term or, for that matter, to the whole contract, moving to a more formalistic approach generally involves strengthening the parol evidence rule or giving more conclusive meaning to various acts that signal whether a purported written agreement is to have literal binding effect or not. Schauer’s observations that link formalism to power help us to understand more clearly that, if these moves are embedded in the U.C.C., the legislature has (at least temporarily) removed from the judge the power to come to what she regards as a sensible decision in some individual cases that will come before her.⁶⁸ If the rule is a default rule, the parties could restore the judge’s power by a suitable provision in their contract but, unless they do, the rule has been set by the legislature. A

be more likely to find a negotiated contract at the beginning of the relationship followed by a series of purchase orders or other documents that, without the large contract up-front, do not resemble “contracts” at all. Cf. MACAULAY ET AL., *supra* note 51, at 138-46.

67. There was an attempt by the article 2 Drafting Committee to treat “Standard Form Contracts” with special rules in its section 2-206, July 1996 Draft. It dropped out of subsequent drafts.

68. In this context, the legislature would merely be circumscribing the game rules within which contracts and contract adjudication were conducted. As suggested earlier, the legislature might want to do this for a variety of reasons: (1) it may think that formal interpretation is, in fact, the desire of most parties and, therefore, it is “efficient” to create such an approach so that the bulk of parties have no need to be specific about it in their contract; (2) the legislature might think that formal interpretation is the desire of most parties in the “end game” and formalizing interpretation would induce them to be more flexible within their contract because they would then have no fear that their “loose” practice would modify their contract terms through course of performance; (3) it might think that formal interpretation is *not* what most parties would want and, in order to avoid a bad result in adjudication, they would negotiate more explicitly about contract terms at the negotiation stage; or finally, (4) the legislature might think that judges were not up to the task of contextual or purposive interpretation (and, implicitly) that the quality of decision making would go up by giving judges an easier task to perform in contract interpretation.

default rule calling for formalistic approach to interpretation is not likely to be reversed in a form contract.⁶⁹

To consider the implications of these normative approaches to Code matters of interpreting assent in business form contracts, I want to suggest a fact that everyone understands to be true: there is no “assent,” in the way we commonly understand it, in many mass-produced form contracts, whether they involve one form or two.⁷⁰ We have, by and large, come to agreement on this question in consumer contracts and the U.C.C. seems, increasingly, willing to carve off “consumer contracts” for differential treatment.⁷¹

69. It would be far-fetched indeed to think that, if the Code’s default rule called for a formalistic interpretive method, the drafter of a form contract would reverse it through a provision in the form. The widespread use of merger clauses in form contracts suggests that drafters of forms want a formal approach to interpretation.

As noted above, Professor Bernstein recommended that the Code contain a provision providing businesses a “reliable way to either opt out of the Code’s adjudicative approach or selectively opt out of its usage of trade, course of performance, or course of dealing provisions.” See Bernstein, *supra* note 35, at 1821. An analogous form of such an opt-out provision is routine in form contracts: the merger clause. In the context of many form contracts, a conclusive validation of merger clauses would do injustice to those who either did not read the clause or did not understand it. Alternatively, it could encourage what amounts to irrational behavior on the part of businesses (i.e., spending valuable time reading or committing resources to an informed understanding of others’ forms) in small form contract settings. See *supra* text accompanying note 90.

Giving conclusive effect to a merger clause would also effectively give the drafter’s sales force a license to make unenforceable pre-signing commitments because the evidence for those commitments would be barred by the now-conclusive merger clause working through the parol evidence rule.

The article 2 redrafting effort embraced a provision that would have given conclusive effect to a merger clause in its May, 1997 Draft. See *supra* text accompanying note 84. The proposal was short-lived and dropped out of later Drafts.

70. Rakoff, *supra* note 61, at 1179 n.21. Edward L. Rubin, *Types of Contracts, Interventions of Law*, 45 WAYNE L. REV. 1903 (2000). When the form recipient is a “repeat player” as well, assent may be more likely. See *supra* note 66.

71. The U.C.C. has a relatively narrow definition of “consumer contract.” For example, proposed article 2 defines “consumer” as follows: “Consumer” means an individual who buys or contracts to buy goods that, at the time of contracting, are intended by the individual to be used primarily for personal, family, or household purposes.” U.C.C. § 2-102(11) (November 2000 Draft). Comparable definitions are found throughout the U.C.C. Texas, by contrast, defines “consumer” far more broadly in its Deceptive Trade Practices-Consumer Protection Act:

“Consumer” means an individual, partnership, corporation, this state, or a subdivision or agency of this state who seeks or acquires by purchase or lease, any goods or services, except that the term does not include a business consumer that has assets of \$25 million or more, or that is owned or controlled by a corporation or entity with assets of \$25 million or more.

TEX. BUS. & COM. CODE ANN. § 17.45(4) (2000). With consumer contracts, the dominant underlying rationale seems to be a lack of sophistication with legal terms by the class of “consumers” as a whole. But often we make the mistake of leaping to the opposite conclusion. We think: “since we agree that consumers cannot be expected to assent in form contract settings, we can expect the opposite from business people who, after all, are more sophisticated.”

Real assent to any given term in a form contract, including a merger clause, depends on how "rational" it is for the non-drafter (consumer and non-consumer alike) to attempt to understand what is in the form. This, in turn, is primarily a function of two observable facts: (1) the complexity and obscurity of the term in question and (2) the size of the underlying transaction.⁷² The vendee's perception of the effort to be expended in securing alternatives to the terms in the form is also important in a recipient's decisions (1) whether to read the form in the first instance and (2) whether to seek alternatives either through negotiation with the vendor or through a search for alternative vendors. The commonly-held idea that a business vendee that accepts the goods has assented to the entire form because she could have foregone the purchase (and, by making the purchase, took the risk of whatever happened to be in the form) does not hold up analytically.⁷³ A single transaction⁷⁴ can carry only a given investment in understanding it, however sophisticated, wealthy, or powerful the non-drafter. The more complex or obscure the term, the greater the effort (in the form of reading, puzzling, or legal research) required to understand it; the smaller the transaction, the less such effort the contract can support.

To demonstrate, suppose we have a sale of a \$100 software program to a business person into which are inserted two clauses. Clause 1 says the vendor cannot be responsible for uses to which the Program is put and disclaims liability for defects in the Program and their consequences. Clause 2 says that the law of Ireland governs the contract.⁷⁵

While sophistication with legal terms (or more ready access to lawyers) is, no doubt, important in understanding assent issues in form contracts, other, potentially more important factors critically affect the likelihood of real assent. As a matter of transactional dynamics, the generally small value involved in most transactions represented by consumer contracts effectively makes the terms of those contracts inaccessible to even the most sophisticated consumer.

72. The bulk of this analysis is developed at greater length in William J. Woodward, Jr., *"Sale" of Law and Forum and the Widening Gulf Between "Consumer" and "Nonconsumer" Contracts in the U.C.C.*, 75 WASH. U. L.Q. 243 (1997).

73. See *id.* at 270-75.

74. If the vendee is embarking on a series of like transactions, the costs can be spread across the series and, at some point, it will make economic sense to scrutinize the form.

75. The form contract through which many purchased WordPerfect 8 from the Corel Corporation (a Canadian corporation) provides that the law of Ireland governs the contract. Curiously, according to the contract, if the purchase is made in Canada, Canadian law (and not the law of Ireland) controls. See Corel WordPerfect license, para. I (on file with the author). Obviously, there is a vast difference in the complexity of these two clauses. In the context of a \$100 contract (and depending on the physical appearance of the form within which the clauses appeared), we expect a customer to see, understand, and assent to the first term far more readily than to the second. In the somewhat unlikely event that the customer actually read the contract, there is a reasonable chance that she would understand the significance of the first term and thereby be able to "price" the term when deciding whether or not to go forward with the transaction. The chances that she

If we raise the size of the contract to \$1000, the dynamics change somewhat. Now, depending on the significance of a \$1000 outlay to the customer,⁷⁶ there is a greater chance that the customer will consider the first clause and, at least, read the second. There is still a very small chance that the customer will "assent" in any other than a formal sense to the choice of Irish law. If we raise the size of the contract to \$100,000, there is a chance that the customer will undertake some investigation into the meaning and significance of Irish law. Perhaps it subjects those who agree to Irish law to the jurisdiction of Irish courts or provides more copyright protection for the vendor than does United States law. Or, perhaps, the law of Ireland does not recognize consequential damages or restricts them more severely than does domestic law. Such investigation will probably require professional advice. Pricing a term of that complexity will be very difficult even in a \$100,000 contract.

To generalize from these examples, the smaller the contract and more obscure or complex the term, the greater the chance that the non-drafter's true understanding of the deal—an understanding adequate to evaluate and "price" the exchange—will deviate from what is in the writing. The "distance" between the non-drafter's real "assent" and the writing will depend on the size of the contract and on the complexity and obscurity of the term in question.⁷⁷ This dynamic will be true whether the contract is formed on one form or two.⁷⁸

would be able to "price" the choice of law term are virtually nil, and it would be irrational for her to try.

76. Except for the fact that this is a software contract, Bill Gates might be far less likely to read the form contract than you or I would.

77. One might object that if *some* customers learn of bad terms in vendors' form contracts, the word will spread and will thereby impose market constraints on the form drafters. See Alan Schwartz & Louis L. Wilde, *Intervening in Markets on the Basis of Imperfect Information: A Legal and Economic Analysis*, 127 U. PA. L. REV. 630 (1979). Some authors seem to take the matter as settled with a simple citation to this argument. Yet there is little empirical evidence of the dynamic Schwartz and Wilde imagine. Moreover, we now have at least one bit of empirical evidence to the contrary.

The computer market is known for its intense competition and most would regard computer buyers both to have a reasonably high level of sophistication and the capacity to share information better than other segments of the population. Yet Gateway 2000, one of those fierce competitors, has demonstrated that its own forms are unlikely to be "customer sensitive." In the now-famous *Brower v. Gateway 2000, Inc.*, 676 N.Y.S. 2d 569 (N.Y. App. Div. 1998), the court printed in its opinion Gateway's extremely onerous arbitration provision and held it was *substantively* unconscionable. See *id.* at 574-75. Although the court did not simply invalidate the arbitration clause altogether, this was a victory of sorts for consumers. But what is important for purposes here is that Gateway did not settle the case. Rather, it permitted a Federal court to publish its onerous arbitration term and to denominate it "unconscionable." Either Gateway was poorly advised with respect to the effect of the term on its business or, more likely, it concluded that even a reported judicial decision parsing its form contract would have virtually no impact on its business.

It should be noted that Gateway's website shows that it has changed its arbitration clause since *Brower*. This may be of little solace for consumers, however. For under Judge Easterbrook's opinion in *Hills v. Gateway 2000, Inc.*, 105 F.3d 1147 (1997), it is

Current law provides, as default rules, for the incorporation of trade usage, course of dealing, and course of performance when they can somehow be reconciled with the text of the agreement.⁷⁹ The U.C.C.'s parol evidence rule currently gives courts the power to be flexible in considering evidence that may clash with the apparent meaning of the text. What would be the implications for business form contracts of a legislative move to more formality in the U.C.C., that is, withdrawal of the courts' power to consider these matters as permissively as they do today?

In general, in a one-form contract, a more formal approach increases the likelihood that what is in the writing will be interpreted as the lawyers for the vendor intended it, even when that meaning deviates from what the customer understood (and therefore "priced") in the context of the deal. As suggested above, the likelihood of real non-drafter assent will primarily be a function of the size of the contract and the complexity of the term. A non-formalist approach to interpretation will permit customers to assert their "true" agreement in those contexts in which it was irrational to carefully consider what was in the form. By contrast, form drafters will want their forms to count and would desire a more formal interpretive regime for a variety of reasons.⁸⁰ Perhaps the worst reason to seek more formality in interpretation is to obtain legal sanction for what amounts to a form of deception. If a seller can hide in its form a term that adversely affects the value of what it is selling, it can obtain an "unearned" advantage from its buyer and a competitive advantage over its competitors who do not so hide the reduced value of their products. While this kind of vendor might hide behind "caveat emptor" or the "duty to read," a deliberate attempt to hide a warranty disclaimer (difficult today because of U.C.C. § 2-316), prohibitively expensive binding arbitration, or similar value-shifting terms within small or light print or

what the consumer finds in the box, not what is on the web site that counts. Customers may still have to buy a Gateway to learn what Gateway's current arbitration clause says.

78. In the context of a business large enough to have purchasing and sales departments, responsibility for reviewing others' forms and making decisions may change depending on the size of the given transaction. As the contract gets larger, responsibility for making decisions about it is likely to move to higher-level managers within the company.

79. U.C.C. §§ 1-205; 2-208 (2000); Professor Dennis Patterson disagrees that there is any hierarchy among terms found in the writing versus those found in trade usage and comparable evidence. See Dennis M. Patterson, *Good Faith, Lender Liability, and Discretionary Acceleration: Of Llewellyn, Wittgenstein, and the Uniform Commercial Code*, 68 TEX. L. REV. 169, 192 (1989).

80. Apparent reliability of the form is, perhaps, the most justifiable of the reasons. In the mass market context, the price at which the vendor will sell goods will depend, in part, on its after-sale risks of warranty and consequential damages liability. The quality of business decisions on how to price what is being sold rests critically on the dependability of the risk-shifting that takes place in the form. Form drafters thus have powerful reasons to wish for a literalistic approach to interpretation because, if their form is well-drafted, such an approach will seem to give the form more reliability. See *infra* Conclusion.

incomprehensible legal jargon has little to distinguish it from actual fraud. For a brief time, form drafters seemed to have the upper-hand in the article 2 redrafting process: formalist proposals that would have more readily given drafters what they wanted in non-consumer contracts surfaced in earlier drafts of the new article 2.

For example, an earlier redraft of article 2 attempted to deal with business form contracts as follows:

SECTION 2-206. STANDARD FORM RECORDS.

(a) If all of the terms of a contract are contained in a record which is a standard form or contains standard terms and the party who did not prepare the record manifests assent to it by a signature or other conduct, that party adopts all terms contained in the record as part of the contract except those terms that are unconscionable.

....

(c) A term adopted under subsection (a) becomes part of the contract without regard to the knowledge or understanding of individual terms by the party assenting to the standard form record, whether or not the party read the form.⁸¹

The effect of the provision is that, had that Draft become law, it would have brought the "reasonable expectations" test of the Restatement into the Code for consumer contracts but, at the same time (perhaps as a tradeoff), would have created a far more formal approach to business contract interpretation than is currently the law. Similarly, an earlier draft of article 2's parol evidence rule attempted to treat merger clauses in business form contracts formally:

81. Proposed U.C.C. § 2-206 (1996 Draft). Interestingly, this provision mimicked Restatement (Second) of Contracts, § 211 (1979), but did not include subsection 3 of the Restatement provision which has often generated controversy. It reads:

Where the other party has reason to believe that the party manifesting such assent would not do so if he knew that the writing contained a particular term, the term is not part of the agreement.

RESTATEMENT (SECOND) OF CONTRACTS, § 211 (c) (1979). Subsection 2 of the 1996 Draft of the section did include a provision comparable to RESTATEMENT (SECOND) OF CONTRACTS § 211(c), but only for consumer contracts. It read:

(b) A term in a record which is a standard form or which contains standard terms to which a consumer has manifested assent by a signature or other conduct is not part of the contract if the consumer could not reasonably have expected it unless the consumer expressly agrees to the term. In determining whether a term is part of the contract, the court shall consider the content, language, and presentation of the standard form or standard term.

a contractual term indicating that the record is a complete and exclusive statement of the agreement of the parties is conclusive evidence of the intention of the parties.⁸²

Both proposals have dropped out of the current draft perhaps in recognition that many form contracts do not—and cannot—invite the non-drafter's free assent even if she signs (or clicks) the form. Had the proposals remained, enacting State legislatures would have removed from their courts the flexibility to operate across the range of business form contracts subject to article 2. If courts were to obey such legislative injunctions, form-drafter intent would bind businesses even in cases where it would be irrational for the non-drafter to assent in any real sense.⁸³

In contracts formed on one party's form only, the distributional effects of a move toward a more formal method of interpretation will produce similar distributional effects regardless of the reason or theory for moving toward more formalism in interpretation. Strengthening the Code's parol evidence rule, or recognizing⁸⁴ a hierarchy that gives the writing more primacy vis-à-vis other sources of party intent, will move resources from non-drafters to drafters in smaller contracts or in contracts with particularly obscure or complex terms without the return to non-drafters of corresponding value.⁸⁵

82. Revised U.C.C. §2-202(b) (May 1997 Draft).

83. In the parol evidence setting, this would have freed form drafters to engage in all sorts of sales pitches and other pre-form commitments without their having a binding effect. The formal approach would have the effect, however, only if there were no other outlets within the facts and other legal doctrine that would permit a court to arrive at a result seemingly foreclosed by the interpretive restriction. Since the rise of the Legal Realists, it has been an open secret that contract law contains enough complexity and rule choice that such legislative constraints might be no constraints at all. It is this complexity, and courts' ability to use it to achieve preferred results, that gave rise to Karl Llewellyn's famous observation that "covert tools are never reliable tools." Llewellyn, *supra* note 19, at 703.

84. Professor Edwin Patterson claims that the hierarchical approach to matters of interpretation suggested by U.C.C. § 1-205 was contrary to Llewellyn's concept of agreement. Patterson, *supra* note 79, at 192.

85. This will be the case in transactions under the Uniform Computer Information Transactions Act (UCITA) which has a series of formal rules which find "assent" to vendor forms in circumstances where it would be irrational for the vendee to, in fact, read the form and consider the risk-shifting that occurs within it. See Memorandum from Jean Braucher, The Uniform Computer Information Transactions Act (UCITA): Objections From The Consumer Perspective, (August 15, 2000) (on file with the author). In business cases, a "click" will signify vendee agreement to, among other things, application of the law of any country in the world to the contract. See William J. Woodward, Jr., *Contractual Choice of Law: Legislative Choice in an Era of Party Autonomy*, ___ SMU L. REV. ___ (forthcoming Spring 2001). The failure of UCITA to address assent issues from a vendee perspective may be responsible in part for the withdrawal of American Law Institute's support for the proposed statute and its being expelled from its position as article 2B of the Uniform Commercial Code. See A.L.I. Proc. 459-72 (1998); 1999 A.L.I.

In all cases involving one-form business form contracts, the consequences of moving toward formalism will be that the enforceable contract will adhere more tightly to the decision-maker's interpretation of the text of the form and therefore, again, depending on the size of the contract and complexity of the term, to the drafter's intent alone (assuming it is "plain" enough to coincide with the decision-maker's). From a distributional perspective, a move to a more formal approach to interpretation in non-consumer contracts will clearly favor those who draft contracts for mass consumption because, in a more formal regime, it will be somewhat⁸⁶ more likely that those drafters will "get what they want" through their carefully-crafted writing. Form-recipients in such transactions who can carry the costs of inquiry will be able to price some of the contract's terms or engage in negotiations about them but, where the term is complex or the transaction small, that term will be irrelevant to the customer's decision whether or not to enter the contract.⁸⁷ Thus, to take the simplest and most obvious example, if a vendor can disclaim liability without the customer knowing it, the vendor has charged more than the customer, if fully informed, should have been willing to pay in a competitive market.⁸⁸ Put differently, the customer's money has bought less of a product than she thought, the vendor received more value than the product was "worth," and the vendor has achieved advantage over similar competitors operating without the term or presenting it in a more accessible form.

Given these distributional implications of a move toward more U.C.C. formality in single-form business contracts, it may be worth reconsidering the instrumental argument, that non-drafters will eventually learn to read their contracts or suffer the consequences of not having done so, and we will all benefit from non-drafters more carefully reading their contracts. The idea implies a strong form of "market intervention" and, in

Proc. 405. In non-form settings, UCITA takes the open approach of article 2. *See supra* note 30.

86. That is, unless the court embarks on a "covert" analysis that favors the non-drafter. *See Llewellyn, supra* note 19.

87. One could argue that the non-drafter simply runs the risk that the transaction will turn out to be worth zero and that the loss on the value of the deal is exceeded by the transaction cost of investigating the writing. This analysis covers some, but certainly not all, of the available terms in the contract. At minimum, any clause that might shift liability or other losses on the non-drafter in excess of the value of the transaction would not be subject to such an analysis. Thus, contract terms that restrict consequential damages, liquidate damages, or shift attorneys' fees would not be subject to this analysis. Perhaps the *possibility* of losing more than one spent *ought* to force transactors to investigate others' forms and we should penalize those who don't do so. The evidence we have suggests that commercial law is not particularly effective in inducing behavioral changes on the part of businesses. *See generally* Woodward, *supra* note 32.

88. *Cf.* Arthur Allen Leff, *Unconscionability and the Code—the Emperor's New Clause*, 115 U. PA. L. REV. 485, 543-46 (1967).

the form contract context, there is little evidence to support it or to believe it would work.

At the individual contract level, the economics of the small adhesion contract discussed above means it would be “inefficient” (or “irrational”) for the non-drafter to expend the resources sufficient to gain an understanding of the drafter’s carefully crafted terms.⁸⁹ It is likely that few form recipients read the forms given to them because they consider it a waste of time or an interruption of what they perceive to be more productive activity.⁹⁰ Theorists who bring a market approach to their scholarship would likely argue that the form recipients are the best judges of how to use their time efficiently and that there should be strong evidence to the contrary before market intervention is justified.⁹¹ Moreover, truly effective market intervention here would be counterproductive when seen from a broader perspective. It is unlikely that we want all those who receive form contracts to stop what they are doing to decipher the form. Transaction costs would come here in the form of a much-slowed process of making contracts the net effect of which might be that business would “slow to a screeching halt.”⁹²

2. TWO-FORM BUSINESS CONTRACTS

The current draft of the proposed article 2 has addressed some of the dynamics of form contracts and, ironically, has done so in a relatively formal way. It does so by sharply distinguishing the two-form business form contract from the one-form contract and treating the two situations

89. Cf. Edward L. Rubin, *Types of Contracts, Interventions of Law*, 45 WAYNE L. REV. 1903, 1910 (2000). As many have recognized, forcing the parties to be more attentive to drafting may be counterproductive even in ideally negotiated contract situations. Increased judicial effort due to unclear terms occurs only in litigated cases; the instrumental approach induces more front-end effort in all cases, litigated or not.

90. In *McCutcheon v. David MacBrayne, Ltd.*, [1964] 1 W.L.R. 125, quoted in MACAULAY ET AL., *supra* note 51, at 526-34, the contract at issue was a “risk note” which would have disclaimed liability for the carrier’s negligence, had the plaintiff signed it or received it prior to shipping his car by ferry. Lord Devlin paraphrased some of the evidence:

People shipping calves, Mr. McCutcheon said (he was dealing with an occasion when he had shipped 36 calves), had not much time to give to the reading. Asked to deal with another occasion when he was unhampered by livestock, he said that people generally just tried to be in time for the boat’s sailing; it would, he thought, take half a day to read and understand the conditions and then he would miss the boat. In another part of his evidence he went so far as to say that if everybody took time to read the document, “MacBrayne’s office would be packed out the door.” [He] evidently thought the whole matter rather academic because, as he pointed out, there was no other way to send a car.

MACAULAY ET AL., *supra* note 51, at 672.

91. *But cf.* Seott, *supra* note 2, at 866.

92. Ian R. Macneil, *Bureaucracy and Contracts of Adhesion*, 22 OSGOODE HALL L. J. 5, 5-6 (1984).

very differently.⁹³ Proposed U.C.C. section 2-207⁹⁴, November 2000 Draft will apply in all contracts in which each side has a form and the forms are exchanged.⁹⁵ The proposed section simplifies the battle of the forms by providing, essentially, that only terms in the two forms that match become part of the contract. In one sense, the provision is more formal than what preceded it since it deletes the flexibility inherent in the current Code section's approach.⁹⁶ Under the new provision, unless there is actual agreement on the term in question,⁹⁷ the conflicting terms drop out ("materiality" is no longer a factor) and the matching terms are supplemented by Code provisions. If one of the thrusts of neoformalism in contracts is that contracting parties either do or should pay more attention to the language they use in their contracts, this provision makes a powerful contrary statement.

The presence of this proposed section in the statute is somewhat surprising because it could make far less meaningful the work that lawyers now put into carefully crafting forms for their clients. If only matching terms "count," it likely means that nearly all lawyer-crafted boilerplate will not. As an empirical matter, tolerance for the proposal in a U.C.C. drafting process so dominated by business lawyers might suggest that neither business people nor their lawyers place much legal stock in the provisions in their own forms in the first place, at least in

93. Draft Official Comment 2 contemplates that a one-form contract will be controlled entirely by the one form. It provides, in part,

The rule would be different where no agreement precedes the performance and only one party sends a record. If, for example, a buyer sends a purchase order, there is no oral or other agreement and the seller delivers in response to the purchase order but does not send its own acknowledgment or acceptance, the seller should normally be treated as having agreed to the terms of the purchase order.

94. The proposed provision states:

SECTION 2-207. TERMS OF CONTRACT; EFFECT OF CONFIRMATION.

If (i) conduct by both parties recognizes the existence of a contract although their records do not otherwise establish a contract, (ii) a contract is formed by an offer and acceptance, or (iii) a contract formed in any manner is confirmed by a record that contains terms additional to or different from those in the contract being confirmed, the terms of the contract, subject to Section 2-202, are:

- (1) terms that appear in the records of both parties;
- (2) terms, whether in a record or not, to which both parties agree; and
- (3) terms supplied or incorporated under any provision of [the Uniform Commercial Code].

U.C.C. § 2-207 (2000).

95. This is likely to be limited to business settings because, unless consumers begin sending forms to their sellers, the new statute will not likely apply to them.

96. The current provision makes the inclusion of a given new term depend on whether it "materially" alters the contract, U.C.C. § 2-207(2), a standard virtually impossible to implement without a complex inquiry.

97. Proposed U.C.C. § 2-207(2), November 2000 Draft.

two-form transactions small enough to be accomplished through a battle of the forms.⁹⁸

A better possibility, perhaps,⁹⁹ is that the old, paper purchase-order and acknowledgment way of doing business is rapidly going the way of the horse and buggy and will be replaced by something different in an E-Business environment. Currently one finds “terms and conditions” on (or, perhaps, “in”) business web sites and it may be that, if competition permits, businesses will prevent those with whom they contract from adding anything to their orders but the “dickered terms.” If this comes to pass, E-commerce transactions will be “one-form” transactions¹⁰⁰ subject to the more flexible Code methodology. Moving to a more formal approach to interpreting the terms of those “one-form” e-commerce transactions will have the distributional effects suggested earlier.¹⁰¹

The proposed statute is designed to apply only to two-form contracts.¹⁰² Thus, if the proposed statute stays in its current form, all old-fashioned businesses will want to ensure that they use forms so as to “neutralize” their partner’s form in cases where the other party uses its own form. And one can bet that lawyers for E-businesses will be busy developing ways to have their own terms and conditions control,¹⁰³ or,

98. A slightly more negative inference is that the real action in form contracts is in the consumer and very small business areas where there is inevitably only one form—the vendor’s. Once the vendee is sophisticated enough to generate its own form, the risk of *that* form controlling (rather than the vendor’s) is sufficiently large or uncertain that new § 2-207 becomes a plausible compromise. Central to this hypothesis is that the new provision not apply to one-form contracts. The comment, quoted at *supra* note 95, may be designed to reassure one-form parties that their forms will remain intact.

The fact that a term in a form may not be enforceable in court does not necessarily mean it will have no effect or that it is pointless to include it in the form. Many form recipients (at least in the one-form setting) will assume that the form is binding and, as a result, will never visit a lawyer in the first place.

99. Thanks to Jean Braucher for suggesting this possibility.

100. Draft Official Comment 2, quoted at *supra* note 95, makes no reference to e-Commerce other than its use of the term “record.” One would expect businesses to pay just as little (or perhaps less) attention to the contents of the form-preparer’s form in the E-Commerce context as they do in paper transactions. The economics of spending valuable resources deciphering another party’s form do not change when that party’s terms are found somewhere within the preparer’s web site in electronic form.

101. Indeed, the distributional effects may be more extreme in an unregulated e-Business environment because businesses will have so many devices other than ordinary “fine print” with which to make it difficult to find and understand the terms they set. Put differently, in an E-Business economy, vendors may have many more tools with which to raise the transaction costs their individual contracting partners will have to expend in order to correctly evaluate exactly what they are getting. If few customers pay attention to forms until a problem arises, market control of this phenomenon will be unlikely.

102. See *supra* note 95.

103. See Frederick D. Lipman, *On Winning the Battle of the Forms: An Analysis of Section 2-207 of the Uniform Commercial Code*, 24 BUS. LAW. 789, 802 (1969). This would be a modern variant of the “first shot” problem where the business that generated the first form would benefit by having its form control. See generally FARNSWORTH, *supra* note 23, at 157-66. Rather than going to other businesses’ web sites to acquire

when they fail in that, developing ways to argue that their E-commerce transactions are “really” based on two sets of terms, not just one.

Revised section 2-207 is clearly an improvement on its predecessor in “battle of the forms” settings. But it is, at best, a very weak solution to the more general problem of determining assent to standard form contracts in the business setting. Moreover, it is surely questionable that a commercial statute that attempts to deal with the standard form problem should place such a premium on the number of forms the parties use in accomplishing their objectives.

For those contracts that actually become subject to proposed section 2-207, the effects on the parties’ drafting efforts will be different than in the one-form situation. Unlike the single form contract where the drafter was more likely to get what it wanted and the non-drafter less likely, here neither party is likely to get what its form drafter intended. The greater formalism the provision brings to the term selection process will not likely have the kinds of distributional effects that flow to “the drafter” in the single form contract.

Once the terms of the contract are mechanically selected through the new provision, however, there might also be room for a still more formal approach to interpreting the contract’s terms by, for example, restricting the use of trade usage and similar evidence to augment the amalgamated “writing.” It is very difficult, however, to understand how such an approach might work in this context. Proposed section 2-207 tells us that the terms in the forms that match become part of the contract, the remaining terms on the forms drop out, and the contract is supplemented by the U.C.C.’s default terms. While judicial precedent will constrain the court’s analysis of the U.C.C. default terms that will become part of the contract under this provision, the open-textured nature of many U.C.C. provisions¹⁰⁴ will make it very hard for a court to interpret even those provisions without the benefit of trade usage and the like.

A more formal approach to interpretation will be at least as difficult with the “dickered terms.” Suppose, for example, the Code contained a new provision that forbade the court to consider trade usage and the like if the parties specified such a command through a general “no extrinsic evidence” clause within their contract.¹⁰⁵ Suppose further that the buyer

goods, one could imagine businesses inviting vendors to sell to them and posting their own terms and conditions somewhere within their own web sites.

104. This will be true of the many provisions of the proposed Statute (and its predecessor) which use the term “reasonable.” *E.g.*, proposed Section 2-305 (open price term); U.C.C. § 2-309 (2000) (absence of specific time provisions and notice of termination). *Compare* Scott, *supra* note 2, at 868.

105. This would be the effect of the “safe harbor” provision suggested by Professor Bernstein. Bernstein, *supra* note 35. As she recognizes, the Code makes it very difficult for parties to negate trade usage or the like unless they are very specific about it. *Columbia Nitrogen Corp. v Royster Co.*, is a case in which the court looked to trade usage to find that express price and quality terms in a contract were merely projections and

has ordered “red” widgets, the seller has agreed to sell them, and the parties have (pursuant to the hypothetical Code provision) forbidden the court to go beyond their documents in determining the meaning of their agreement. In the seller’s industry, “red” embraces a wider range of colors than it does in the buyer’s industry, but neither side knows that. Seller supplies “red” widgets at the outer fringes of its understanding of the term and that color is not considered “red” in the buyer’s understanding. Buyer claims breach and seller denies it.¹⁰⁶ Without the benefit of extrinsic evidence, a “plain meaning” or literalistic approach¹⁰⁷ would simply bring the decision-maker’s own views of the range of “red” to resolving such a controversy.¹⁰⁸ The result would be either an interpretation one way or the other (based on the decision-maker’s own understanding of “red”), or a finding of no agreement despite the parties’ use of the same words in their agreement.¹⁰⁹ Could the parties’ use of the general “no extrinsic evidence” clause have been intended to order such an interpretive approach to this particular ambiguity, one that, by hypothesis, the parties did not recognize when they made their contract?

There are little hard data suggesting that ordinary parties engaged in the battle of the forms would prefer such a haphazard approach to the

admitted such evidence despite its apparent contradiction with the fixed price appearance of the contract. See 451 F.2d 3, 9-10 (4th Cir. 1971). The case can be read as one in which the court was persuaded that the parties could not have intended to foreclose such a trade approach merely by the use of a fixed price in their contract. Being in the trade, one might argue that the parties would have anticipated this problem, one way or the other, and made provision for it in the contract. Given the contracting environment they were apparently in, the fact they made no specific provision to cover this problem suggests more strongly that they did not think of the problem, rather than that they actually addressed it by making a fixed price form of contract.

106. This example, of course, is a simplified version of the famous “chicken” case, *Frigaliament Importing Co. v. B.N.S. Int’l Sales Corp.*, 190 F. Supp. 116 (S.D.N.Y. 1960).

107. Cf. Scott, *supra* note 2, at 848.

108. Dean Scott refers to non-literalist interpretation as “activist.” See, e.g., Scott, *supra* note 2, at 848 (“While the case for formalism is a tentative one, the evidence is sufficient to shift the intellectual burden of proof to those who would defend the activist strategies unleashed by the U.C.C.”). Approaching the interpretive task in the way described in the text may involve less judicial work, to be sure, but it is no less “activist” in the sense of injecting the court’s own views into the meaning of the contract than is an approach that took evidence on the parties’ meaning. Indeed, as this example may make clear, a purposive approach is less “activist” in my sense since the court’s own views will be tempered and constricted by the labor-intensive evidentiary process that a purposive interpretation involves. Dean Kathleen Sullivan has argued that an “activist” court tends toward rules rather than standards, whatever the judge’s political leanings. See Sullivan, *supra* note 1, at 100-03.

109. The case may sound like *Raffles v. Wichelhaus*, 159 Eng. Rep. 375 (Ct. of Exchequer 1864), but it describes a far more common phenomenon than presented by the famous “Peerless Case.” Cf. FARNSWORTH, *supra* note 23, at 480. Ambiguity can be found in unanticipated places and the potential for one side or the other to escape their obligations in ambiguity settings through mutual mistake would insert substantial risks and opportunities for strategic behavior into many contracts.

unanticipated ambiguities in their dickered terms to the current Code approach permitting recourse to trade usage unless "carefully negated."¹¹⁰ Until there is strong evidence supporting contracting parties' desire for such an approach to resolving unanticipated ambiguities, we should be reluctant to construct a formal Code rule that enabled the parties to insist on it through a general provision in their contract.

Should such a "plain meaning" approach be imposed, alternatively, on the parties for instrumental reasons? Will it induce them to create contracts with less ambiguity under pains of idiosyncratic adjudication? Again, there is little evidence to suggest that an instrumental approach induces changes in business practice; such an instrumental approach has been effectively rejected by many of the Code's formation rules.¹¹¹

Original section 2-207 adjusted the law to the business practice of not reading forms and, implicitly, rejected the idea that, by retaining the mirror image rule or other more formal approaches to the problem, business practice could be molded to the law. Then, as now, the U.C.C. process included a healthy complement of business lawyers whose views about business practice, and its responsiveness or unresponsiveness to legal rules, surely helped to shape the contours of section 2-207. It has apparently not been cost effective for parties in battle of the forms settings either to scrutinize forms or negotiate with one another; lawyers seem to concentrate instead on "winning" the battle of the forms.¹¹² Under those circumstances, Code rules designed to induce the opposite business behavior would likely be ineffective in practice and produce inefficient (and unjust) outcomes in adjudication.

110. Professor Bernstein's empirical research into the existence or non-existence of trade usage and the like in various trades does not shed light on this cross-trade type of problem which appears very common in decided cases. *See, e.g.*, *Frigalim Importing Co. v. B.N.S. Intern. Sales Corp.*, 190 F. Supp. 116 (S.D.N.Y. 1960); *see generally* FARNSWORTH, *supra* note 23, at § 7.13.

111. Some of the pre-Code formation rules, e.g., that one must accept a written offer for a prompt shipment of goods by a writing, not by shipping the goods, could be justified as inducing parties to accept offers in the "correct" ways or later suffer the "penalty" that they will have no contract. *See, e.g.*, FARNSWORTH, *supra* note 23, at 133-35. Such rigid rules have been rejected in several places in the Code and will remain rejected in the revision process.

The strong presence of business lawyers in the U.C.C. drafting over the years has ensured an actual (and probably strong) connection between business practice and Code rules. While not "empirical evidence" in any scientific sense, *see supra* note 31, the original Code and its revisions could not become law without the support and involvement of business interests and, in that sense, reflect the judgment of business interests about the law that structures business relationships. Real empirical work into actual business practice remains extremely valuable and provocative; the practices reflected in the Code may be the result of anecdotal evidence, speculation, or the particular make-up of given drafting committees. But, given the nature of the U.C.C. process, very strong evidence is necessary to overcome the business judgments reflected in the Code provisions themselves, as well as by the evolution of U.C.C. § 2-207 over the years.

112. *See, e.g.*, Lipman, *supra* note 103, at 802-04.

Finally, one must consider the idea that judges are simply not up to the job of complex interpretation—that a simplified approach to interpretation will be no more prone to error in approximating “party intent” than will a complex one, and of course, that a simple approach will also be less labor-intensive and therefore cheaper at the litigation stage. There is no way to demonstrate the merits of this proposition empirically. Clearly, Judge Friendly would have saved a great deal of effort in deciding the “chicken case” had he simply decided “chicken means chicken” and therefore the plaintiff has (or has not) sustained its burden of proof.¹¹³ It may be worth relating a story that will expose the reasons for the discomfort that many may feel with this alternative to the approach that Judge Friendly actually took.

As a law student, I worked for a judge who, when asked “what to do” about this issue or that in a given case, would simply say “do the right thing.” This may seem a meaningless—or even lawless—statement, but this judge’s clerks took it to mean decide *this* case in a way that is understandable to the litigants, that is appropriately true to the precedents, that pays intense attention to the facts of the case, and that will satisfy the judge that he had made the “best” decision for the parties that one could have made. I have always taken the idea to reflect the highest ideals of common law judging which progresses incrementally through courts making their best judgments for the specific, real people in diverse, individual cases.¹¹⁴ Judges have to live with and sleep with their decisions which, after all, affect in a very direct way the people who come before them. They are accountable, at least to themselves and to the parties that appear before them, for what they do with their power to decide cases;¹¹⁵ real parties have come before the judge to solve a

113. *Frigalment Importing Co.*, 190 F. Supp. at 117, the famous “chicken case,” involved an international sale of “chicken.” The seller claimed the agreement called for a broad range of chicken that included stewing chicken; the buyer contended that the agreement called for the narrower and more valuable “broiler fryer” chicken. *See id.* Judge Friendly took evidence from both parties on trade usage and, in an elaborate trial court opinion, ultimately concluded that the buyer-plaintiff had not sustained its burden of proving that the narrower broiler/fryer chicken was what the parties had agreed to. *See id.* at 121.

114. This view animates much of Karl Llewellyn’s tribute to common law judging. *See* KARL N. LLEWELLYN, *THE COMMON LAW TRADITION: DECIDING APPEALS* (1960).

115. Dean Scott has contributed a useful analysis of different approaches to judging which he characterizes as “ex ante,” “ex post” and “formalist” in Scott, *supra*, note 2, at 859-60, 865-66. Ex ante judging involves filling gaps in party intent by constructing and applying a default rule to the case before the court. Using primarily commercial impracticability cases, he describes ex post judging as filling gaps in light of the actual circumstances of the parties now before the court. Formalism involves the court’s refusal to fill gaps in the parties’ intent at all. The first and third involve forms of instrumentalism; the second less so, if at all.

The judicial attitude described in the text does not seem to fit any of these categories because many courts use a mixture of the three. To the extent that judging requires a court

problem *they* have not been able to resolve for themselves. Insofar as there is satisfaction in judicial work, it may come primarily from doing *that* job well and only secondarily from crafting good rules that others may use in the future. The parties to an adjudication should emerge from the experience believing that the court has heard all sides and has attempted to arrive at a thoughtful, fair, and just decision for their dispute.¹¹⁶ A legislative limit on the power of a judge to purposively interpret the parties' contract may make it unnecessary to explain in detail why one party's version of "red" was less convincing than was the other's. But this savings in energy could come at a substantial cost to the system¹¹⁷ and, in any event, may merely change the reasoning of the decision, not its outcome.¹¹⁸

to *fully* understand the parties and their problem, the legal system imposes severe barriers to this understanding.

It is nonetheless very difficult to reconcile the judicial attitude described in the text with a decisional approach that emphasizes instrumentalism, that is, one that calls on courts to decide cases based primarily on the effects those decisions will have on other parties either in their contracting behavior or in the performance of their contracts. While there is surely a justifiable element of instrumentalism in the reasoning of many judicial decisions, using given controversies to create rules for others to follow is not at the center of judicial power. Rather, the judicial function consists of the power to decide specific "cases and controversies" and that power is limited, at least at the Federal level, by "standing," "ripeness," and similar doctrines that ensure that courts do not decide questions that are not properly characterized as "cases or controversies." Arguably, the incremental development of the common law consists of the approach described in the text applied to specific, individualized cases by judges trying to "do the right thing" on a daily basis. At a psychological level, I have doubts whether conscientious courts can really avoid intensely context-sensitive judging, however they may articulate their decisions. *Cf. Grey, supra* note 4; *Lake River Corp. v. Carborundum Co.*, 769 F.2d 1284 (7th Cir. 1985).

116. A recent experience in a local judicial selection process underscored this point. Of substantial interest to the selection committee was "judicial demeanor," defined loosely in the Committee to mean projecting a feeling of fairness and thoughtfulness that will make parties who come before the judge believe that they are actually being treated sympathetically, fairly, and with respect.

117. See Stewart Macaulay, *Relational Contracts Floating on a Sea of Custom? Thoughts about the Ideas of Ian Macneil and Lisa Bernstein* 94 *Nw. U. L. REV.* 775, 776 (2000). There, commenting on Ian Macneil's work, Professor Macaulay refers to the function of contract law, identified by Professor Macneil, in helping the culture achieve "organic solidarity." *Id.* at 777. Quoting Macneil's argument that "the more an exchange system is perceived as wrongly uneven the more its beneficiaries must depend on external force to maintain it," IAN MACNEIL, *THE NEW SOCIAL CONTRACT* 45 (1980). Macaulay makes the point that a measure of confidence in the fairness of the economic system is necessary to ensure voluntary compliance with most commitments. Clear, persuasive judicial decisions contribute to "organic solidarity."

118. See generally Grey, *supra* note 4.

B. Formalism Versus Flexibility

With formalism comes a measure of inflexibility;¹¹⁹ less formal approaches prove more flexible. The drafters of the Uniform Commercial Code have rejected efforts toward more formalist interpretation in the development of the new U.C.C. and have sharply distinguished one-form from two-form business contracts. The approach of the current drafters thereby retains the flexibility courts have had to make sense of assent issues across the entire range of business contracts governed by the U.C.C.¹²⁰ Under current and proposed article 2, courts have the flexibility to approach assent issues more formally in larger or less complex form contracts while, at the same time, and to look behind the form where the contract is smaller or the terms more complex. A somewhat more formal approach to interpretation may indeed be justifiable for larger business form contracts where we can expect the non-drafter to more carefully scrutinize the proposal's terms and consider the risk allocation those terms present.¹²¹ But such an approach is not justifiable across the board and, if strictly applied through the range of business contracts covered by the U.C.C., would produce results that are at odds with the likely intent and reasonable understanding of non-drafters.¹²²

Article 2 drafters have been unable to sharply discriminate among the many different kinds of contracts the Code covers. They have, of course, separated "consumer contracts" from the rest and, where business forms are concerned, have separated two-form contracts for special treatment. But, importantly, there is no Code distinction between the presumably-large, fully-negotiated commercial contract—the contract that serves as a model for the neoformalists—and the commercial contracts that (at least numerically) have come to dominate modern business—those non-negotiated contracts formed on one party's form or the other's. Because the Code failed or is unable to better discriminate among

119. Cf. Schauer, *supra* note 8, at 542.

120. Draft article 2 reiterates its intent to be flexible in many places. See, e.g., U.C.C. § 2-206, cmt. 1; § 2-207, cmt. 2.

121. For example, see, *Betaco, Inc. v. Cessna Aircraft Co.*, 103 F.3d 1281 (7th Cir.1996).

122. In a recent work using law and economics to analyze complexity in contracting, Karen Eggleston, Eric Posner, and Richard Zeckhauser appear to be advocating a flexible approach to contract interpretation, one that depends on the reasons a court might discern for the contract's complexity, or lack thereof. Among the factors they consider relevant in a court's more liberal efforts at interpretation are contracts across industries where information is highly asymmetric or contracts with high negotiation costs. See Karen Eggleston, Eric A. Posner & Richard Zeckhauser, *The Design and Interpretation of Contracts: Why Complexity Matters*, 95 *Nw. U. L. REV.* 91 (2000). While their analysis does not contain any extended discussion of the business form contract involving asymmetrical information, their analysis clearly supports the current approach in the Code which permits courts a range of interpretive approaches depending on the circumstances that come before them.

business contracts, a formal rule based on a fully-negotiated model will, of necessity, apply across the full, undifferentiated range of business contracts including the bulk that do not begin to fit the model.

Any effort formally to classify the enormous range of commercial contracts subject to article 2 will be labor intensive, incomplete, temporary, and very contentious. Perhaps in recognition of these problems, the Code makes very little effort to classify commercial contracts at all. This makes it imperative that this important commercial statute continue to permit judges flexibly to address the assent issues in individual cases. Until we develop finer distinctions than "business" and "non-business" contracts, we will not be able to construct models on which to base general Code rules addressing assent. In the meantime, policy makers, courts, and the drafters of the U.C.C. will be wise to reject proposals for general Code rules mandating a more formal approach to contract interpretation.

CONCLUSION

The flurry of neoformalism in contracts scholarship stands in stark contrast to a real world whose complexity and diversity seems to be increasing exponentially. It is impossible to fully model such a contracting world, and if the incomplete models used for policy recommendations are inaccurate or unrepresentative, we run the risk of counterproductive rules and incentives, and unjust outcomes in individual cases. Business people are busier, more diverse, more specialized, and more competitive now than ever before. In this environment, a formalist interpretive approach that lays more stress on *ex ante* planning and a predictable and understandable use of language may be based on an ideal of contracting behavior that may have existed only in a small portion of contracts and whose current likelihood may be smaller than ever.

The argument for a more formal approach to contract interpretation rests on a contracting model that may be valid in some cases but is clearly invalid in most common contracts used in business today. A more formal approach to non-negotiated business form contracts is likely to redistribute resources from non-drafters to drafters of form contracts or, in two-form cases, likely to produce results that parties don't "want" either in individual cases or in the aggregate. And resting such an approach on "judicial incompetency" grounds may, if effective, reduce judicial responsibility for outcomes and leave the parties and the public generally with lowered confidence in the power of our judicial system—and law—to effect justice.¹²³

The real world of business contracting is extremely diverse and the contracts covered by article 2 of the U.C.C. share much of this diversity.

123. See Macaulay, *supra* note 117.

Before adding formality to its interpretive approach, we need more than the negotiated model of contracting from which to project normative recommendations. We also need a Code that discriminates sufficiently among commercial contracts so that the rules produced from our models can be limited to contracts that resemble the models. The case for more formalism in contract interpretation through changes in the U.C.C. has yet to be made. And given the vast scope of article 2, the different levels of assent that we can expect over its diverse contract settings, and the political process leading to the development of the Code's provisions,¹²⁴ it may be a long time in coming.

124. See authorities cited *supra* in note 32. See also Fred H. Miller, *Realism Not Idealism in Uniform Laws—Observations from the Revision of the U.C.C.*, 39 S. TEX. L. REV. 707 (1998) and Fred H. Miller, *The Future of Uniform State Legislation in the Private Law Area*, 79 MINN. L. REV. 861 (1995); Kathleen Patchel, *Interest Group Politics, Federalism, and the Uniform Laws Process: Some Lessons from the Uniform Commercial Code*, 78 MINN. L. REV. 83 (1993); Edward L. Rubin, *Thinking Like a Lawyer, Acting Like a Lobbyist: Some Notes on the Process of Revising U.C.C. Articles 3 and 4*, 26 LOY. L.A. L. REV. 743 (1993); Edward L. Rubin, *Uniformity, Regulation, and the Federalization of State Law: Some Lessons from the Payment System*, 49 OHIO ST. L. REV. 1251 (1989).

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