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Enforcing Promises: An Examination of the Basis of Contract*

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The obligation to keep promises is a commonly acknowledged moral duty.[1] Yet not all promises—however solemnly vowed—are enforceable at law.[2] Why are some promises legally binding and others not? Orthodox doctrinal categories provide only modest assistance in answering this persistent question. Conventional analysis, for example, has distinguished promises made in exchange for a return promise or performance from nonreciprocal promises.[3] Indeed, common law "bar-

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1. Pound, *Promise or Bargain?* 33 TUL. L. REV. 455, 455 (1959) ("From antiquity the moral obligation to keep a promise [has] been a cardinal tenet of ethical philosophers, publicists, and philosophical jurists.") [hereinafter cited as *Promise or Bargain?*]; *see id.* at 457-63. *See generally* Pound, *Individual Interests of Substance—Promised Advantages*, 59 HARV. L. REV. 1, 3-11 (1945). In terms of moral obligation, promises have been clearly distinguished from other representations or predictions. "A promise is not, therefore, merely an assurance one gives to help another, just as it is not merely an expression of a resolution to perform an action. It is, in addition, to *underwrite* any endeavor the other party to the transaction may choose to launch. . . ." A. MELDEN, RIGHTS AND PERSONS 46, 47-54 (1977). The peculiar status of promissory representations forms the basis of the law of contract.

2. The hint of this restraint is revealed in the common definition of contract as a promise that is legally enforceable. *See, e.g.*, 1 RESTATEMENT OF CONTRACTS § 1 (1932) [hereinafter cited without cross-reference as RESTATEMENT 1ST]. This definition of contract is retained in the *Second Restatement.* RESTATEMENT (SECOND) OF CONTRACTS § 1 (Tent. Draft Nos. 1-7, 1973) [hereinafter cited without cross-reference as RESTATEMENT 2D].

3. *See* RESTATEMENT 2D § 75. The traditional distinction between bargained-for and gratuitous promises suggests that only two categories can be identified. Actually the institutional environment is more accurately described as having three distinct contexts. Explicitly bargained-for promises are only a part of a larger exchange context in which the opportunity for interactive communication remains. We define nonreciprocal promises as being limited to those contexts in which the promisee has no realistic ability to obtain adjustments in promise-making through bargaining. *See* p. 1301 & note 38 *infra.*

gain theory" is classically simple: bargained-for promises are presumptively enforceable; nonreciprocal promises are presumptively unenforceable. But this disarmingly simple theory has never mirrored reality.[4] Contract law has ventured far beyond such narrow limitations, embracing reliance and unjust enrichment as additional principles of promissory obligation.[5]

Thus, a promise may be enforceable to the extent that the promisee has incurred substantial costs, or conferred benefits, in reasonable reliance on the promise.[6] Promissory estoppel under Section 90 of the *Restatement of Contracts* is the primary enforcement mechanism when action in reliance follows the promise.[7] If the change of position by the promisee precedes the promise, its nexus with the promise is more subtle. For example, a promise is enforceable when it follows a nondonative material benefit conferred by the promisee. Unjust enrichment principles are typically invoked to enforce such "past consideration" promises.[8] Despite this expansion of liability, "gratuitous" promises of gifts or unilateral pledges to confer benefits remain legally unenforceable.[9]

4. Professor Grant Gilmore has argued provocatively that a clearly defined "bargain theory" of contract never really existed in the first place. The "theory," he argues, was simply the creature of nineteenth-century formalism. *See* G. GILMORE, THE DEATH OF CONTRACT (1974).

5. The first breach in the armor of classical bargain theory is credited to Professor Corbin. *See id.* at 62-66. *See generally* 1 A. CORBIN, CONTRACTS §§ 109, 110 (1963). Subsequently, the pioneering scholarship of Lon Fuller and Stanley Henderson has demonstrated that the environment of promissory liability differs markedly from conventional assumptions. *See, e.g.*, Fuller & Perdue, *The Reliance Interest in Contract Damages* (pt. 1), 46 YALE L.J. 52 (1936); Henderson, *Promises Grounded in the Past: The Idea of Unjust Enrichment and the Law of Contracts*, 57 VA. L. REV. 1115 (1971) [hereinafter cited as *Unjust Enrichment*]; Henderson, *Promissory Estoppel and Traditional Contract Doctrine*, 78 YALE L.J. 343 (1969) [hereinafter cited as *Promissory Estoppel*].

In addition to Professor Gilmore's essay, the development of contract theory is thoughtfully explored by Lawrence Friedman, *see* L. FRIEDMAN, CONTRACT LAW IN AMERICA (1965), and by Patrick Atiyah, *see* P. ATIYAH, THE RISE AND FALL OF FREEDOM OF CONTRACT (1979).

6. *See* pp. 1345-54 *infra*. Under classical common law doctrine, a mere promise could be elevated to a legally binding contract only by the formality of a seal or a bargained-for exchange of consideration for the promise. L. FULLER & M. EISENBERG, BASIC CONTRACT LAW 124 (1972).

7. *See* note 106 *infra*. The inclusion of section 90 in the *Restatement 1st* is generally identified as the initial doctrinal recognition of the inadequacy of the simple bargain model in explaining the enforcement of promises. Professor Gilmore suggests that Corbin's "revolutionary" attack on bargain theory predates the *Restatement* by several decades. G. GILMORE, *supra* note 4, at 58. Following the adoption of the *Restatement*, scholarly attention turned to describing the emerging principle. *See* Boyer, *Promissory Estoppel: Principle From Precedents* (pts. 1 & 2), 50 MICH. L..REV. 639, 873 (1952); *Promissory Estoppel, supra* note 5; Shattuck, *Gratuitous Promises—A New Writ?* 35 MICH. L. REV. 908 (1937).

8. *See* pp. 1349-54 *infra*.

9. *See* pp. 1339-45 *infra*.

These often overlapping, yet seemingly unconnected, principles of bargain, detrimental reliance, and unjust enrichment characterize all legally enforceable promises. They, in turn, are linked with corresponding sanctions that determine the level of enforcement for a given set of promises.[10] Contract damage rules embrace a variety of remedial choices. But the principles determining this choice of remedies are largely unarticulated. In most cases *A* can seek the value of what he expected from *B*'s promise. Such standard "compensatory" recovery puts *A* in the economic position he would have occupied had *B* fulfilled his obligation.[11] There are alternatives to the compensation rule, however. Thus, *A* may seek restitution of any benefit conferred on *B* as a result of *B*'s promise.[12] Alternatively, *A* may seek to recover identifiable costs incurred in reliance on *B*'s promise.[13] Recovering conferred benefits and reliance expenditures has the stated objective of returning the parties to the same economic position they occupied before the promise was made.

How can these interlocking doctrinal patterns be explained? Damage and liability rules have both redistributive and behavior-adaptive functions. In an earlier paper we commented on the apparently random—and arguably regressive—distributive effects of the basic contract remedial options.[14] The adaptive effects of contract rules seem to offer greater explanatory possibilities.[15] A liability or damage rule induces

10. *See* Farnsworth, *Legal Remedies for Breach of Contract*, 70 COLUM. L. REV. 1145 (1970); Fuller & Perdue, *supra* note 5; Goetz & Scott, *Liquidated Damages, Penalties and the Just Compensation Principle: Some Notes on an Enforcement Model and a Theory of Efficient Breach*, 77 COLUM. L. REV. 554, 558-62, 568-77 (1977); Shattuck, *supra* note 7.

11. *See* Goetz & Scott, *supra* note 10, at 558-59. Notwithstanding the universality with which the goal is articulated, scholars have long doubted the rigor of the law's commitment to compensation. We have previously suggested that "a strong argument can be made that the theory of damages is designed to err toward undercompensation." *Id.* at 558 n.19.

12. *See* p. 1337 *infra;* Childres & Garamella, *The Law of Restitution and the Reliance Interest in Contract*, 64 NW. U.L. REV. 433 (1969); Dawson, *Restitution or Damages?* 20 OHIO ST. L.J. 175 (1959).

13. *See* p. 1337 *infra*. The definitive work in this area remains Fuller & Perdue, *supra* note 5.

14. Goetz & Scott, *supra* note 10, at 566-68.

15. A wealth of theories has been advanced to explain the enforcement of promises. The "intuitionist" theory of the inherent moral force of promises formed the basis of obligation for the social contract theorists of the 17th and 18th centuries. Although the intuitionist perspective is appealing, it fails to explain the simple fact that no legal system attempts to enforce all promises. The 19th-century response to the morality of promising was the "will" theory of contract. The law of contract was conceived of as merely executing and protecting the will of the parties. The 19th-century formalists, typified by Langdell and Pollock, used the notion that the essence of contract is the agreement of wills—or the meeting of minds—to craft the classical bargain theory of consideration.

The obvious limitations of the will theory have produced a reaction among 20th-

contracting parties to adapt their behavior in ways that will affect social welfare. The rules of promissory liability can, therefore, be examined usefully in terms of these welfare effects. It is important to emphasize that the proper focus here is on prospective effects, that future promising is the behavior to be influenced by the rules summarized above. If only promises already made were considered, ease of measurement is a primary factor that might commend the compensation rule over any more complex damage measure.[16] With respect to past promises, choosing among reliance, compensatory, or punitive remedies involves primarily a distributional issue; the damage rule allocates the gains or losses from any particular broken promise between the promisor and promisee. But, considered prospectively, rules of promissory liability have efficiency consequences as well: they frequently alter the actual magnitude of the gains or losses to be divided between the parties. Whether a particular type of promise will be enforceable, and to what extent, are choices that may powerfully modify the nature and amount of future promising. We will evaluate these choices by separating the enforcement question into two parts:

First, which system of promissory enforcement yields the maximum net social benefits from promise making?

Second, does such an optimal enforcement scheme explain current doctrinal patterns?

Part I of this Article considers the first of these questions by developing an analytical model that examines both the function of promises and the impact of liability on the making of promises. Clarifying the function of promising is a necessary first step in deriving an optimal enforcement model. It is critically important to realize that a promise is conceptually distinct from the actual transfer that it announces. As advance information signaling a future transfer, a typical promise prospectively carries *both* benefit if kept and harm if broken. This entanglement of benefits and harms substantially complicates the en-

century contract scholars that leads toward an instrumentalist view of promissory liability: promises are enforceable because enforcement secures socially desirable ends. *See, e.g.*, Atiyah, *Contracts, Promises and the Law of Obligations*, 94 LAW Q. REV. 193, 197-98 (1978); Patterson, *An Apology for Consideration*, 58 COLUM. L. REV. 929, 941 (1958); *Promise or Bargain?*, *supra* note 1, at 463. Although evaluation of promises in terms of their welfare effects dominates current contract jurisprudence, alternative evaluations based on shared ethical norms or common moral intuitions continue to be asserted. *See* J. RAWLS, A THEORY OF JUSTICE 342-50 (1971); Havighurst, *Consideration, Ethics and Administration*, 42 COLUM. L. REV. 1, 9 (1942). Such claims have not proved very helpful, however, in explaining the observable limits that the law sets on enforcing the sanctity of promises. And if moral force is attached to promises merely because people rely upon them, the argument is subject to the claim that such reliance is dependent upon legal enforceability.

16. *See* Goetz & Scott, *supra* note 10, at 566-68.

forcement question. Thus, the enforcement of promises may have harmful consequences by deterring socially useful future promising. Alternatively, nonenforcement encourages more promises but also reduces the reliability of the announcement; the promisor's intent to perform is not tested against a potential penalty for its nonperformance. The value of social welfare is maximized by a system of legal rules that provides the optimal balance between the beneficial and the harmful effects of promising.

In Part II, we discuss the practical compromises necessary to implement efficient regulation of promises in a world of costly legal process and imperfect information. We examine common law rules of liability as proxies for theoretically optimal rules rendered impractical by the inherent difficulties of measuring the true social effects of promising. We conclude that a substantial congruence exists between traditional contract rules and optimal promissory enforcement. Indeed, this congruence offers a persuasive explanation for the peculiar patterns of promissory liability observed in actual practice.[17]

I. Optimal Enforcement of Promises

Attempts have been made to explain the overlapping patterns of promissory liability in terms of the economic implications of promise-making. Bargained-for promises support value-enhancing exchanges. Such promises are thus seen as fully enforceable under the compensation rule in order to protect and encourage value-maximizing resource allocation.[18] Measuring damages in terms of expectation rather than reliance is said to encourage more efficient breach decisions once the contract is made.[19] A nonreciprocal promise, on the other hand, is

17. A recent scholarly debate has centered on the hypothesis that the common law can be explained in terms of principles of economic efficiency. *See, e.g.*, R. POSNER, ECONOMIC ANALYSIS OF LAW 404-05, 439-41 (2d ed. 1977); Rubin, *Why is the Common Law Efficient?* 6 J. LEGAL STUD. 51 (1977); Priest, *The Common Law Process and the Selection of Efficient Rules*, 6 J. LEGAL STUD. 65 (1977); Michelman, *A Comment on* Some Uses and Abuses of Economics in Law, 46 U. CHI. L. REV. 307 (1979). We take no position on the extent to which economic efficiency is a dominant or merely subsidiary element in explaining the development of common law doctrine in general. Our intent is the more modest one of measuring a relatively narrow segment of legal doctrine against some underlying economic optimality considerations.

18. *See* RESTATEMENT 2D § 76, Comment b ("Bargains are widely believed to be beneficial to the community in the provision of opportunities for freedom of individual action and exercise of judgment and as a means by which productive energy and product are apportioned in the economy.") The assumption that enforcement of bargains promotes allocative efficiency is widespread. *See* Hays, *Formal Contracts and Consideration: A Legislative Program*, 41 COLUM. L. REV. 849, 852-53 (1941); Llewellyn, *What Price Contract?—An Essay in Perspective*, 40 YALE L.J. 704, 716-18 (1931); Patterson, *supra* note 15, at 945-48.

19. R. POSNER, *supra* note 17, at 88-93.

frequently labeled as a "sterile transaction," which does not facilitate the movement of resources to more valued uses.[20] On this basis, enforcement is justified only as a deterrent to the harm caused by any detrimental reliance on the promise.[21] In sum, these lines of analysis suggest that full enforcement of bargains consolidates benefits while protection of reliance-based promissory interests minimizes harms.

But existing explanations of the legal enforcement of promises are incomplete and perhaps misleading. A principal limitation has been the failure to consider the effects of various levels of legal enforcement on the making of promises. Inquiry has generally focused instead on the effects of legal sanctions on decisions to breach or perform, assuming that the promise has already been made.[22] Yet, a decision to enforce promises, and the subsequent choice of remedy, does not merely mold the performance behavior of contracting parties; it also shapes both the nature and amount of promise-making activity.

Appropriately calibrated enforcement rules can be used to achieve the optimal number and type of promises based on the degree and form of adaptation by promisor and promisee. Thus, the effects of legal enforcement on promise-making are critical factors in evaluating the seemingly disparate liability and damage rules of contract. In Part I we examine these effects by first describing the reactions of both the promisee and promisor to the risks inherent in promising. We then specify an enforcement model that encourages the socially optimal interaction between the promising parties.

A. *The Function of Promises: Adaptation by the Promisee*

In analyzing the promisee's reactions to a promise, it is critically important to bear in mind the conceptual distinction between the promise itself and the future benefit that it foretells. By communicating a

20. *See* C. BUFNOIR, PROPRIÉTÉ ET CONTRAT 487 (2d ed. 1924); Fuller, *Consideration and Form*, 41 COLUM. L. REV. 799, 815 (1941); *cf.* R. POSNER, *supra* note 17, at 69 (gratuitous, nonreciprocal promises not part of "process by which resources are moved").

21. *See* R. POSNER, *supra* note 17, at 69-70; Fuller, *supra* note 20, at 811.

22. *See generally* Shavell, *Damage measures for breach of contract*, BELL J. ECON. (forthcoming 1980); W. Rogerson, Economic Efficiency and Damage Measures in Contract Law (unpublished paper on file with *Yale Law Journal*).

In order to increase its accessibility to a legal readership, this Article uses relatively nontechnical terms to present an underlying economic model that typically would be articulated by economists in highly formal mathematical terms. The formal model developed in the economic literature by Shavell and extended by Rogerson differs conceptually from ours in some important areas. For instance, we focus upon the influence of potential remedies on the quality and quantity of promises, rather than upon the optimal enforcement of a promise, the character of which is already determined. In addition, our definition of reliance damages differs because we incorporate the notion of "reasonableness." Hence, the implicit model underlying this Article is somewhat more complex conceptually than are those cited above.

promise, the promisor informs the promisee about the proposed future receipt of a benefit. The promise itself is merely the production of a piece of information about the future. Normally, advance knowledge of a future transfer will increase the benefit to the promisee because he can more perfectly adapt his consumption decisions to the impending change in wealth. For instance, a person informed of a $25,000 bequest to be made one year hence may revise some of the plans that he otherwise would have followed in the interim twelve months. Because of the revisions in plans, the individual can achieve a higher intertemporal level of satisfaction than if the wealth were transferred without any advance notice. Such adaptive gain from the information embodied in a promise may appropriately be termed "beneficial reliance." The problem occurs, however, when the transfer foretold by the promise is not actually performed. In this case, the information conveyed by the promise turns out to have been misleading and the promisee's induced adaptation in behavior makes him worse off than he would have been without the expectation of a future benefit. Losses incurred by ill-premised adaptive behavior are commonly termed "detrimental reliance." Because the role of promises as units of information is so fundamental to the entire analysis developed below, we will use an economic indifference curve model to give more rigorous content to such key legal concepts as reliance and the reasonableness of the promisee's adaptation process.

1. *Reliance Reactions of a Promisee*

Figure 1 will be used to develop a very simple intertemporal allocation model, one in which a person must allocate his income between two periods, present and future. *A*, the potential promisee, begins with $100, which he can divide between consumption now and consumption in the future. In Figure 1, his possible choices are represented by the straight line budget constraint indicating all combinations of present and future consumption that sum to $100. His preferences about alternative combinations of present and future consumption are summarized by the indifference curves, which define a kind of topographic map of the desirability of different present-future consumption patterns.[23] On these assumptions, the highest preference level consistent with the scarce resources is point e_1, where indifference curve I_1 is

23. Indifference curves may be thought of as a topographical map of a "preference mountain," on which higher "elevations" represent the greater preferences of outcomes. The points in any single indifference curve constitute equally preferred outcomes. An individual thus will be indifferent between any two points on an indifference curve. In the model represented by Figure 1, the higher an indifference curve lies to the northeast, the more utility the individual derives from the outcomes represented by the curves.

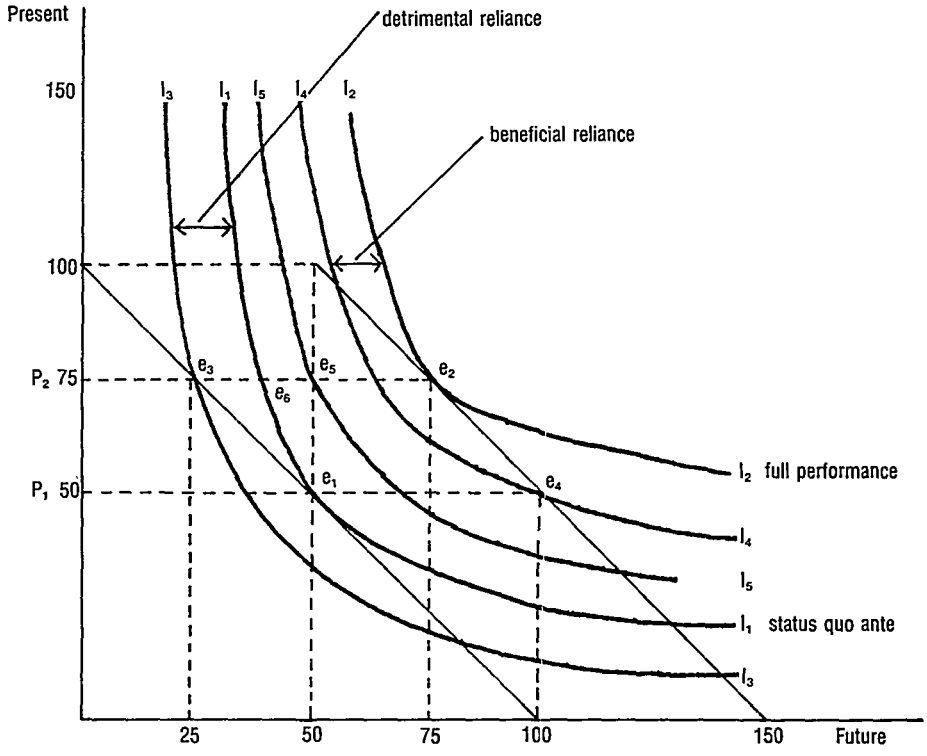

Figure 1

tangent to the budget constraint. This involves spending $50 now and a planned expenditure of $50 in the future.

Suppose now that *B* promises *A* a transfer of $50 to be made in the future period and that *A* believes the promise. Even neglecting the possibility of borrowing against his future wealth, *A*'s budget constraint will shift out to the dotted line in Figure 1.[24] The new constraint indicates that, although no more than $100 can be spent in the present, the two-period consumption levels may now total $150 rather than $100. Based on the new information, *A*'s best two-period plan would be point e_2. *A* is thus led to revise his current consumption upward to $75 and to project $75 worth of future consumption.[25] But what happens if

24. For simplicity, we assume that the interest rate on money is zero in order to produce a one-to-one tradeoff between present and future consumption. The introduction of interest is irrelevant to this analysis because it merely alters the rate of tradeoff, reflected in the slopes of the budget lines.

25. The promisee's consumption of all goods with nonzero income elasticities will be modified. His intertemporal consumption stream will be adjusted to the higher wealth level created by the gift.

the promise is broken when the second period actually arrives? *A* has already expended $75 and has only $25, rather than the prospective $75, left to spend. In terms of Figure 1, breach of the promise pushes *A* leftward from his anticipated outcome of e_2 back to his original budget constraint at e_3. As indifference curve I_3 indicates, *A* is worse off at the post-breach result e_3 than he was at e_1, the pre-promise point on indifference curve I_1. In sum, *A* has been misled by the promise into making what is now recognizable as a mistake; the consequences of that detrimental reliance are captured in the difference between indifference curves I_1 and I_3.

Because detrimental reliance is widely regarded as a basis for damage computation, an advantage of the Figure 1 model is that it clearly illustrates why it is a mistake to use *A*'s observable action in reliance on a promise as the measure of his damages. Under the facts assumed, *A*'s observable reliance is the $25 extra he spends in period 1. If, however, he were awarded this $25 as damages for breach, his ultimate position would be at e_5 on indifference curve I_5. He would have spent $75 in the first period and, including the $25 damages, would have available $50 for the final period. But since return to the status quo ante requires only that indifference curve I_1 be achieved, the true reliance damages are equal only to the lesser amount indicated by the horizontal distance between e_3 and e_6 in Figure 1. The common-sense explanation for this, of course, is that detrimental adaptation in behavior is usually only a partial rather than a total loss. In this case, *A* did get some benefit from the excessive $25 consumption, even though not as much as he would have if the consumption had been postponed to the optimal time. Reliance is, simply, the opportunity cost of the broken promise. Thus, true damages are measured by the difference between the value of the stream of consumption choices not taken—indifference curve I_1—and those choices induced by the promise—indifference curve I_3. Because it is important to distinguish compensation based on observable reliance from true reliance damages, we shall refer to the former as "reimbursement damages" in the discussion below.

Even where the precise meaning is imperfectly captured, the notion of detrimental reliance tends to be better understood than that of beneficial reliance. This is unfortunate because the production of beneficial reliance is perhaps the principal social rationale of promising; the risk of detrimental reliance is merely the unavoidable concomitant cost. Figure 1 aptly illustrates the beneficial consequences of promising when the promise is performed. Assume, for instance, that the $50 in our hypothetical is merely transferred to *A* in period two

without any advance warning. Not knowing about the wealth increase, *A* will have committed himself to plan e_1. When period two arrives, *A* will unexpectedly find himself with $100 to spend. At this point, the best available choice is at e_4, which is on a lower indifference curve than e_2, the point that would have been achievable had *A* obtained advance knowledge of the transfer. In common-sense terms, the difference between I_2 and I_4 illustrates the benefits to *A* of being able to adjust, because of the promise, to revised expectations about the future.

2. *The "Self-Protection" Reaction to Uncertain Promises*

Conceptualizing beneficial and detrimental reliance in the context of a simple model such as Figure 1 does have one major limitation. We have assumed implicitly that the promisee places total credence in the promise. Against the background of the Figure 1 model, however, it is possible to consider at least heuristically the imperfect credibility situation. When the promisee does not completely believe a promise, the results illustrated in Figure 1 can be understood as extreme or limiting cases of reliance.

What happens if the promisee knows that the probability of the promisor's performance is less than certain? In this case, the beneficial results of any adaptive behavior when the promise is performed must be weighed against the detrimental results of the same adaptive behavior if the promise is breached. A prospective gain from an adaptive action is balanced against the risk of loss.[26] Whatever the reasons for the riskiness attached to the performance prospects of any promise, the promisee can protect himself against prospective losses from detrimental reliance by limiting his behavior adjustments. In practice, the attempt to do this is frequently manifested in intermediate courses of action taken by promisees who do not completely ignore the implications of a promise in their planning but do not react as fully as if performance were certain. The price for this self-protection against the risk of detrimental reliance is, therefore, the value of the prospective beneficial reliance that would accrue from full adaptation to the advance knowledge of a promissory performance.[27]

26. In formal statements of this balancing process, the promisee is usually regarded as weighting the alternative consequences by the probabilities of performance and nonperformance. It should be noted that the promisee's central concern is whether the preannounced transfer will take place, not whether the performance is a purely voluntary one as opposed to one motivated by legal or other sanctions. Thus, because legal sanctions presumably affect the expected performance probability of many promises, the extent of the reliance experienced can be modified by the legal treatment of promises.

27. An important observation with regard to the promisee's adjustments to uncertain

The possibility of self-protection adjustments by promisees undermines the common assumption that detrimental reliance is the only behavior modified by the enforcement choice. This assumption often leads to characterizing certain "gratuitous" promises as incapable of inducing any reasonable reliance. Once the legal rule is announced, detrimental reliance on such announcements would, it is argued, not be reasonable. But the problem is quite simply that policies that reduce the reliability of promises are likely to reduce both beneficial and detrimental reliance. Thus, legal rules that encourage self-protective adaptation by the promisee achieve desired reductions in detrimental reliance only at the cost of concomitant reductions in beneficial reliance.

B. *Making Promises: Actions of the Promisor*

Understanding the behavior of the promisor is the next important step in our analytic model. How do promisors act and how do prospective sanctions modify their behavior? The initial phase of our analysis employs some strong simplifying assumptions. First, we assume that although future events may be uncertain, retrospective information is perfectly accurate. Second, we also posit that legal process costs are negligible, so that the theoretical gains from an otherwise beneficial regulatory rule are never counterbalanced by implementation costs. These assumptions are relaxed below when we discuss the practical compromises that may be dictated in a more realistic setting.

Potential promisees view promises as beneficial actions and as desirable economic goods. One can thus consider a promisor's willingness to make promises in much the same manner as his willingness to pursue any other economic goal. To predict the level of promise-making activity, the costs of promising must be examined.

1. *The Costs of Promising: The Regret Contingency*

Derivation of the promisor's cost of promising requires consideration of a number of potentially confusing factors. Therefore, we shall begin with the simplest possible environment. First we shall assume

prospects is that even very uncertain promises may produce substantial detrimental reliance if their prospective beneficial reliance is high. The mere improbability of performance does not destroy the informational significance of the promise. Recognition of this fact suggests that the legal concept of "reasonable" reliance is more complex than is sometimes realized. For example, it is perfectly reasonable and rational to rely detrimentally, to some extent, on many promises even though there is a substantial probability of nonperformance.

that the cost of communicating the promise is negligible.[28] Second, we assume that no legal mechanism exists to enforce promises. Absent a legal compulsion, the promisor remains free to refuse performance. If he does, the making of the promise will have generated costs in the amount of the detrimental reliance imposed on the promisee.

The option of nonperformance also imposes costs on the promisor in two situations. The first case is when the promisor exhibits some welfare interdependence with the promisee; that is, he is to some extent altruistic and cares about costs incurred by the promisee.[29] Then, the detrimental reliance costs imposed by nonperformance become, to some degree, costs to the promisor himself. Intrafamilial promises and promises between close friends are most likely to exemplify this phenomenon. In addition, and closely related, guilt may accompany the promisor's imposition of harmful results on others. In any event, this class of breach-related costs, which arise out of an altruistic or ethical sense, may be termed "self-sanctions."

The second extra-legal sanction arises when nonperformance would produce some post-breach reaction, either from the promisee or others, that is costly to the promisor. The resulting costs may range from hostile, retributive behavior to a mere loss of others' esteem to foreclosure of future beneficial dealings.

What are the effects of these extra-legal sanctions for breaking promises? To the extent that such sanctions are effective, their prospect acts as a "cost" of promising and deters promises that are worth less to the promisor than the prospective cost. Thus, extra-legal sanctions are a supplement to, or substitute for, legal sanctions.[30] Given the

28. On these facts, the cost of promising may be zero. One key question to ask, of course, is whether the act of promising has foreclosed any future opportunities to the promisor or made such opportunities more expensive.

29. The economic terminology for such relationship is "interdependent utility functions." The intrafamilial promise offers an obvious illustration of how such interdependency can increase the utility of any given transfer. *See* Posner, *Gratuitous Promises in Economics and Law*, 6 J. LEGAL STUD. 411, 412, 418-19 (1977).

30. Although the existence of extra-legal sanctions may properly affect the choice of legal measures, extra-legal sanctions have several disadvantages as mechanisms for inducing optimal promise-making. First, extra-legal penalties are highly circumstantial, are difficult to calibrate, and vary widely in their efficacy from individual to individual. Second, a sanction must constitute a cost to the person on whom it is imposed; it is not necessary, however, that no one benefit from the sanction. When damages or performance are extracted from a promisor, the resources are transferred to someone else who benefits thereby. Consequently, there may be no net social cost associated with the sanction; at least, the net loss is less than the gross loss imposed on the promisor. By contrast, many forms of extra-legal sanction represent a cost to one party without counterbalancing benefit to another. Prospects of retributive reaction or guilt, for example, tend to be inefficient sanctions in the sense that they could be replaced by resource transfers from promisor to promisee so that the promisee is made better off while the promisor is made no worse off than under the extra-legal sanction.

existence of extra-legal sanctions, under what circumstances might a promisor fail to perform his promise? When a promise is made in good faith, the promisor presumably believes that he is likely to perform. Still, many good-faith promisors would acknowledge the possibility that events may arise that cause them to regret having made the promise. Thereafter, if it were costless to do so, they would indeed breach the promise. Such contingencies may involve a wide range of factors, from changes in personal conditions to disappointment about external considerations that orginally made the promise seem desirable. The term "regret contingency" will be used to denote the future occurrence of a condition that would motivate breach if breach were a costless option for the promisor. Assuming any reliance, the occurrence of a regret contingency necessarily implies that either the promisor or promisee must bear a cost.

When a regret contingency arises, the promisor's options are either to bear the loss attributable to performance, which now costs more than it is worth, or to breach and accept the cost of any corresponding sanction. Presumably the promisor would adopt the cheaper of these regret costs. In any event, someone will suffer a net loss whenever a regret contingency arises, whether in the form of regret costs to the promisor, uncompensated detrimental reliance to the promisee, or both.[31]

2. *Adaptation by the Promisor: Precautions and Reassurance*

By what means does the promisor adapt to the prospective costs of promising?[32] The promisor can substantially influence the probability of a regret contingency, and thus its prospective costs, by adjusting his behavior ex ante. One means of mitigating potential costs is by altering the form of the promise. For instance, the promisor may condition performance on the proviso that certain circumstances—potential regret contingencies—not arise. Alterations in the form of the promise will generally entail a cost to the promisor either in terms of direct resource

31. The regret contingency is a key concept because much of the discussion below will involve either how society can adjust to an optimal volume of exposure to regret contingencies or how to achieve the objective that any given volume of such risk exposure be borne in a least-cost manner.

32. The prospective cost of promising is based on a two-step estimation process by the promisor. First, what is the probability that a regret contingency will arise? Second, if one does arise, what is the magnitude of the accompanying regret costs? The promisor uses the probability of the regrettable outcome to discount the costs of that outcome. Because the future consequences of promises are frequently uncertain, it should be emphasized that the adjective "prospective" is used in a particular sense. Specifically, it indicates that a set of alternative future consequences have been weighted by their probabilities, adjusted for any risk preference, and reduced to a single-valued equivalent.

cost—time and trouble—or in the possibility that the benefit of the promise-making to the promisor will be diminished. The second means of avoiding regret costs is simply to make fewer promises. The costs of this option are forgone benefits from unmade promises.

The costs that result from restrictions in the scope or number of one's promises can be termed "precautionary costs." It is useful to distinguish these further as either quality precautions or quantity precautions. Quality precautions involve adjustments restricting the scope of promises and impose a cost of decreased reliability. Quantity precautions, which consist of reductions in the number of promises made, result in a loss of benefits from promising. A rational promisor will pursue precautionary adjustments up to the point at which marginal precautionary costs are exactly balanced by marginal reductions in regret costs.

Precautionary adjustments by the promisor decrease the value of the promise. Conversely, when the promise is worth more to the promisor than its prospective cost, the promisor may engage in "reassurance." Reassurance includes such actions as the offer of guarantees, verbal persuasions, and the development of a reliable reputation, designed to convince the promisee that the promise is valuable. Reassurances increase the value of the promise to the promisee. Indeed, promisees may regard voluntary reassurance measures as substitutes for sanctions. Reassurance usually entails some cost to the promisor and, hence, will be pursued up to the point at which marginal reassurance costs are exactly balanced by increases in resulting benefits to the promisor.

Precautionary and reassurance reactions by promisors are triggered by variations in the cost of promising. It should be apparent, therefore, that an additional legal sanction will raise prospective costs, thereby precipitating adjustments of the scope and volume of promises. The net effects of these changes can be evaluated by combining the descriptive models of promisee and promisor reaction developed above.

C. *Optimizing Promisor-Promisee Interaction*

To what extent do legal sanctions optimize the interactions between promisor and promisee? In the present context, optimization is defined as maximizing the net social benefits of promissory activity—that is, the benefits of promises minus their costs.[33] This approach is equivalent

33. The adjective "prospective" should be applied to such costs and benefits, and this sense is intended below even when the term is not explicitly used. Strictly speaking, the maximization of prospective benefits need not produce results that, viewed retrospectively, will have truly maximized the net benefits ultimately realized. This is not a serious

to the balancing of prospective costs and benefits under the widely accepted Learned Hand test for the required duty of care in potential tort-producing activities.[34] Indeed, there are strong theoretical parallels between the production of dangerous, but useful, products and the making of promises.[35]

The role of damages or sanctions in generating socially optimal behavior can be focused more sharply by observing the distinction between internal and external effects.[36] Because self-interested maximiz-

objection, however, because the prospective benefits criterion amounts to one under which people are induced to maximize benefits to the extent possible within the limits of the information at their disposal at the time the relevant decisions are made. There is no reason to believe that, as a practical matter, any other criterion can function as well.

34. Under the Hand definition, an actor is guilty of negligence if the loss caused by the accident multiplied by the probability of its occurrence exceeds the burden of taking adequate precautions. United States v. Carroll Towing Co., 159 F.2d 169, 173 (2d Cir. 1947).

35. The optimization process can be analyzed most clearly in terms of marginal effects—that is, the incremental variations in costs and benefits associated with a proposed change in legal treatment. If the marginal benefits attributable to a rule adjustment exceed the marginal costs, then the adjustment is beneficial, and vice versa. The system is optimized when no changes exist for which the marginal net benefits are positive. It is not necessary, therefore, to know the absolute levels of costs and benefits associated with alternative legal rules as long as the increases or decreases in the levels of costs and benefits can be estimated.

Social optimization implicitly presumes that the welfare of promisors and promisees is given equal weight ex ante. In the extreme, this assumption implies that even a promise with a high prospect of net cost to the promisee is optimal if the promisee's costs are outweighed by sufficient benefits to the promisor. In particular classes of cases, such results may be quite discomforting; their possibility constitutes one of the caveats applicable to any efficiency analysis of legal policy. In situations in which such cases arise, supplemental norms may be applied. One such case may be that of the bad-faith promisor who does not intend to perform, but who seeks nevertheless to benefit by making the promise. Here, standard intentional fraud analysis, providing for damages at least equalling the amount of detrimental reliance necessary to make the victimized promisee whole, would be appropriate. Indeed, it might be socially desirable to increase the sanction and extract any unjust gains from the bad-faith promisor.

The most commonly adopted measure of damages for fraud is the "benefit of the bargain" rule. Similar to the compensation principle, the rule puts the plaintiff in the same financial position as if the fraudulent representation had in fact been true. *See* Auffenberg v. Hafley, 457 S.W.2d 929, 938-39 (Mo. App. 1970); Lawson v. Citizens & S. Nat'l Bank, 255 S.C. 517, 180 S.E.2d 206 (1971).

Punitive damages are available when the defrauder has been guilty of morally reprehensible conduct. This generally requires more aggravated conduct than a mere intentional misrepresentation of fact or intentional lie; rather, the fraud must be gross, oppressive, or violative of a position of trust and confidence. *See, e.g.*, J. Truett Payne Co. v. Jackson, 281 Ala. 426, 203 So. 2d 443 (1967); Fowler v. Benton, 245 Md. 540, 552-53, 226 A.2d 556, 564, *cert. denied*, 389 U.S. 851 (1967).

When the plaintiff has transferred property or conferred benefits upon the defendant, he is entitled to a disgorgement of the property or its value. *See* Brooks v. Conston, 364 Pa. 256, 72 A.2d 75 (1950); RESTATEMENT OF RESTITUTION § 202 (1937).

36. Internal effects are those costs and benefits felt by the individual actor. External effects are those consequences of an act that are felt only by individuals other than the actor. Only if a party makes decisions as if he were experiencing all of the consequences of his behavior, external as well as internal, will his behavior be socially optimal.

ing behavior entails consideration of only internal costs and benefits, unfettered individual behavior is incompatible with social optimization in circumstances in which significant external costs or benefits are present. Individuals will oversupply activities with external costs and undersupply those with external benefits. By imposing costs and creating incentives, the law can cause individuals to consider external effects in their decisionmaking and thus "internalize" them.

Inducing optimal promise-making therefore requires that the promisor's costs of promising be adjusted to reflect any external effects on the promisee.[37] But this adjustment process is complex. Changes in the costs and benefits of promising are highly interactive in two senses. First, an individual's adjustments may substitute one category of his costs for another. Second, the actions of one party may produce reactions by the other and, in turn, feedback responses to the first party. The role of legal damages in optimizing this interaction depends upon whether a promise is reciprocal or nonreciprocal. Nonreciprocal or gratuitous promises, which are not conditioned upon performance of a return promise, do not typically enjoy the presumption of enforceability attached to reciprocal or bargained-for promises. As the analysis below reveals, the critical variable that distinguishes these categories of promises is whether the parties can interactively influence the nature and amount of promise-making through bargaining. It is the existence of effective impediments to interaction in the case of nonreciprocal promises that seems to explain why the law treats these two types of promises in such different fashions.[38]

1. *Nonreciprocal Promises*

Consider the case of a gratuitous promisor who has adjusted his promise-making to an arbitrarily assumed level of extra-legal sanction so that he cannot further improve his situation. In addition, assume that social considerations effectively prevent the promisee from influencing the promisor's calculations through bargaining. Under these conditions, when does the intervention of the law lead to optimal

37. As long as the effects of the announcement of the promise itself are carefully distinguished from those of any actual resource transfer, the value of the performance per se to the promisee can be ignored.

38. Barriers to effective interaction between parties to promises may arise from many different sources. Ordinary transaction-costs impediments may exist as a result of the time and trouble involved in negotiating. Alternatively, there may be something inherent in the very relationship of the parties that renders interaction impractical, such as a social taboo, a status relationship, or an institutional environment that obstructs meaningful communication. *See* Leff, *Injury, Ignorance and Spite—The Dynamics of Coercive Collection*, 80 YALE L.J. 1, 41 (1970).

results? We shall first discuss the conditions under which nonenforcement of such a nonreciprocal promise will produce suboptimal reassurance and precautionary adjustments. We then derive an optimal damage formula for those cases in which some level of enforcement is suggested.

a. *Legal Enforcement and Reassurance*

Legal enforcement of a particular class of nonreciprocal promises increases the reliability of the promises. This added reassurance increases social benefits in three situations. First, legal enforcement increases the net benefits of promissory reassurance if a legal sanction such as money damages displaces existing extra-legal penalties such as guilt or social pressure. If the total level of the sanction stays the same, the promisor's costs, benefits, and behavior all remain unchanged, while the promisee's benefits are increased by the receipt of the damages. The promisee's self-protection costs also fall. Because the consequences of a regret contingency are reduced by a prospect of legal compensation, the promisee can spend less on mitigating the risk of uncompensated detrimental reliance. In the event of breach, damage payments reduce the cost of nonperformance to the promisee. Thus, his beneficial reliance on the promise will increase. In essence, the substitution of one type of sanction for the other provides the promisee with the benefits of more reassurance against the regret contingency at no additional cost to the promisor. Hence, the imposition of legal sanctions may increase net reassurance benefits, if extra-legal sanctions are replaced by legal enforcement.[39]

Second, legal enforcement may increase net reassurance benefits regardless of the degree of substitutability of sanctions. Such an opportunity arises when a gratuitous promisor assesses the risk of a regret contingency at zero, because he is certain he will perform. In this case, if the law intervenes by raising the sanction for breach, the promisor's prospective regret and precautionary costs remain at zero. The prospect of sanctions is largely irrelevant to such a promisor. If the promisee knew that the risk of a regret contingency were in fact zero, he too would be unaffected by a stronger sanction. He would be perfectly assured already and, consequently, would incur no self-protection costs. Generally, however, a promisee's subjectively perceived risk of a regret contingency will be greater than the actual zero risk known to the

39. In the case of nonreciprocal promises, no basis appears for predicting when legal enforcement will successfully replace extra-legal sanctions. To the extent that sanctions are cumulative rather than substitutable, the net reassurance benefits of legal sanctions will be reduced.

promisor. Therefore, the increased sanction provides greater reassurance and permits a promisee who was originally engaging in excessive self-protection to decrease his self-protection costs.[40]

Third, even the gratuitous promisor who is not totally certain of future performance may prefer more enforcement. This will occur, for instance, when the promisor cares about the welfare or the reaction of the promisee. Then, the net benefit of promising to the promisor may be enhanced by the provision of additional reliability to the promisee through legal enforcement. Although enforcement puts such promisors at additional risk, the greater reassurance to the promisee may generate increased benefits to the promisor that outweigh any increased costs.[41]

Under what circumstances, then, will legally induced increases in the reliability of nonreciprocal promises be socially optimal? When the mutual interests of both parties are furthered by more assured promises, the promisor will voluntarily seek legal mechanisms for providing additional reassurance. However, often it will not be in the self-interest of the promisor to undertake voluntarily a more reliable promise. Even when some benefits to the promisor are produced by additional reassurance, the external benefits from performance may be inadequately communicated to the promisor by self-sanctions. As a general empirical premise, therefore, enforcement will be more likely to optimize promissory reassurance when extra-legal sanctions are relatively ineffective. The social desirability of enforcement, however, ultimately depends upon whether those gains are offset by corresponding costs. Before proposing a sanction for particular nonreciprocal cases, therefore, we must consider the societal effect of the promisors' precautionary adjustments triggered by legal liability.

b. *Legal Enforcement and Precautionary Action*

Although legal enforcement of nonreciprocal promises will initially increase the reliability of such promises, it may induce both qualitative and quantitative precautionary action by promisors. The net societal

40. As has been noted in different terms, the value of the transfer to the promisee is enhanced because the information content of the promise is improved and the beneficial reliance is increased. *See* Posner, *supra* note 29 (discussing the enforceability of gratuitous promises). The Posner analysis, though persuasive, is limited by its pristine premises.

41. Based on essentially this line of reasoning, Posner is critical of the abandonment of the formal promise under seal as a means of permitting a promisor to opt for legal enforcement of his gratuitous promise. *Id.* at 419-20. Reintroducing measurement costs may conceivably explain the abandonment of the seal. However, as a theoretical principle, an opportunity for the promisor voluntarily to adopt an enforceable form of promise does hold out the opportunity for gains to both parties.

effect of legal enforcement of a class of promises depends on the relative social value of these interacting adjustments.

Qualitative precautionary adjustments by promisors to increased sanctions may be thought of as merely the converse of reassurance. These precautionary moves entail a lessening of the scope of the promise and a shifting of the risk of potential regret contingencies to the promisee, while reassurance enhances the value of the promise and constitutes an assumption of risk by the promisor. These qualitative dimensions of a promise encompass two conceptually distinct effects: first, risk minimization by providing the promisee with better information on which to determine his degree of reliance; and, second, risk allocation by dividing the costs of regret contingencies between promisor and promisee. Analysis of these two factors suggests that legal sanctions can be used to induce risk-minimizing precautionary adjustments by both parties, but are much less successful in directing risk-bearing choices.

By providing the promisee with information concerning regret contingencies, precautionary adjustments by the gratuitous promisor improve the accuracy of the promisee's degree of reliance. Without a legal sanction, the benefits generated by the information effect of precautionary adjustments may not be maximized. The promisor is motivated to make precautionary adjustments only to the extent that his increased precautionary costs are outweighed by decreases in his regret costs. For instance, when only minimal extra-legal sanctions are imposed on breach, the savings in regret costs are relatively trivial, and precautionary moves by the promisor are not likely to be cost-effective. Under these circumstances, the promisee will be insufficiently forewarned about the risks of breach and will consequently overrely, failing to protect himself adequately against the prospect of breach.

Thus, where the external costs of a nonreciprocal promise are unlikely to be conveyed to the promisor, legal enforcement can induce the promisor to make optimal precautionary adjustments. Alternatively, the promisee must optimize self-protection and reliance in the light of the information he now possesses about the reliability of the promise. Paradoxically, if promises are unenforceable, the promisee has the correct incentives to protect himself to the optimal level against risks. Because the promisee bears all risks of breach, in this environment, he will rely on a promise only to the extent that the prospective cost of reliance is outweighed by prospective benefits. In contrast, if a promise is legally enforceable, and the regret costs shift to the promisor, the promisee may engage in a greater than optimal level of reliance. Be-

cause the reduction of regret costs becomes an external benefit of the promisee's actions, the promisee may ignore these costs in determining the extent of his reliance. In order to discourage the promisee from overrelying, the promisor must not be held liable for damages when the promisee knew or should have known that the marginal cost of self-protection was lower than the corresponding marginal reduction in prospective regret costs. This rule gives meaning to the concept of "reasonable reliance" and avoids not only an underinvestment in self-protection by the promisee, but also an overinvestment in precautionary adjustments by the promisor. It fills essentially the same function as does the rule of contributory negligence in tort.[42]

In addition to these risk minimization effects, legally induced qualitative precautionary moves reallocate the risk of regret to the promisee. What can be said of the risk allocation implications of these qualitative adjustments? The allocation of risk to a least-cost risk bearer by the manipulation of legal liability may have efficiency consequences that justify the costs of such adjustments. However, in the case of most nonreciprocal promises, the risk of a regret contingency ultimately will be borne by the promisee in spite of the promisor's risk-bearing advantages. Initially, the imposition of a legal sanction allocates some or all of the risk of a regret contingency to the promisor. But so long as the promisor is free to make qualitative adjustments, by conditioning his promise, he can shift that risk back to the promisee. In some cases, of course, the promisee may be the least-cost risk bearer. However, because it is the enforcement of the promise that removed the risk from the promisee initially, legally induced precautionary moves to shift it back again cannot be regarded as efficiency gains attributable to the liability rule. Thus, in terms of risk allocation, qualitative adjustments have only distributional consequences; their implementation costs may be regarded as net social losses.[43]

This analysis suggests that qualitative precautionary adjustments by

42. Imposition of a legal sanction equal to full detrimental reliance would, in the absence of a mitigation limitation, encourage overinvestment in reliance by promisees. Indeed, it has been suggested that enforcement of promises under a reliance scheme would create a moral hazard in terms of the promisee's adjustments. In other words, a promisee might be tempted to extend his reliance beyond any objectively reasonable point; if the promise is kept, he reaps the benefits, while if it is broken, the promisor bears the full costs under the liability rule. *See* Shavell, *supra* note 22. Optimal legal sanctions can respond to the problem of over-investment in reliance by structuring a compound liability rule under which the behavioral adaptations of both parties are scrutinized. Of course, the implementation costs of such a rule may be substantial. *See* pp. 1289-90 *infra*.

43. If promises are unenforceable, however, promisors may also engage in qualitative reassurance adjustments. This also entails social costs of implementation. These costs will be reduced under an enforcement rule.

the gratuitous promisor have mixed effects. Increasing these adjustments by legally enforcing nonreciprocal promises is optimal, therefore, only when gains in promisee reliance from improved information exceed the net implementation costs of reallocating the risk of regret to the promisee. This implies, as an empirical generalization, that enforcing nonreciprocal promises will improve outcomes when there exists a substantial prospect of beneficial information exchanges through qualitative adjustments. Conversely, in contexts in which self-sanctions are already effective and the prospects of improved information are poor, the social gains from enforcement are negligible and may be exceeded by implementation costs. Nonenforcement of such nonreciprocal promises is thus the optimal choice.

c. *An Optimal Damage Formula*

The effect of a decision to enforce legally any particular class of nonreciprocal promises depends upon the nature of the sanction imposed for breach. Promisors will respond to higher levels of sanction by increasing their qualitative and quantitative precautions, reducing both the reliability of a given volume of promises and the number of promises actually made.

A necessary starting point in determining an optimal damage rule is to specify the external effects of a nonreciprocal promise as the supply of such promises is increased by one marginal unit. The external effects are the prospective detrimental reliance incurred if the promise is broken and the prospective beneficial reliance enjoyed if the promise is performed. Proper reflection of external effects therefore requires not only that the promisor be charged for the harm expected from broken promises, but also that he be rewarded for the prospective benefits of performance. It is helpful to state this condition symbolically. Let p be the promisor's reasonable, subjective assessment of the probability that he will perform a promise under an existing legal rule calling for damages of D in the event of breach. For the damage rule to deter all promises with net social costs and encourage those with net benefits, the amount of damages awarded must satisfy the following equation:

$$(1 - p)\mathrm{D} = (1 - p)\mathrm{R} - p\mathrm{B}$$

where R and B are the values of detrimental and beneficial reliances, respectively. Assuming that all broken promises are litigated, the left-hand side of the equation represents the expected value of the prospective legal sanction. Because only broken promises are affected by the

law, the probability $(1 - p)$ of the promise being broken is used to "discount" the damages D. The values for R and B on the right-hand side of the equation should be understood as those resulting from optimal self-protection by the promisee. Thus, promisees will appropriately minimize the value of the right-hand term, which is the net social cost of the promise. In calculating this prospective net reliance, the magnitudes of the potential detrimental and beneficial reliances are each discounted by their probabilities. When the equation is satisfied through the imposition of optimal damages D, the promisor's internal cost-benefit calculus will reflect the external effects of his promise-making. If the external effects are thus accounted for, the promisor's maximization of his internal net benefits is consistent with supply of the socially optimal quantity and quality of promises. We call this damage rule the "prospective net reliance" formulation.

In some cases, the prospective beneficial reliance from a promise will exceed its prospective detrimental reliance. Because the net external effect of such a promise is beneficial, it would be optimal to reward the making of such promises. However, in the nonreciprocal setting no practical legal mechanism exists for rewarding promises. This limitation renders true optimization impossible; the situation is necessarily second-best. At minimum, promises with prospects of net beneficial reliance should not be the subject of damages if breached. Only promises with prospective net detrimental external effects should be enforceable.

The prospective net reliance formulation developed above can be used to analyze the optimal level of enforcement. By dividing both sides of the original equation by the probability of breach $(1 - p)$, the following damage rule emerges:

$$D = R - \left[\frac{p}{(1-p)}\right] B.$$

The optimal damage rule thus subtracts from the promisee's reliance cost a fraction of his potential beneficial reliance. This fraction is the ratio of the ex ante subjective probability of performance to that of nonperformance. It determines the extent to which the prospect of beneficial reliance when the promise was made is credited against the promisee's prospective detrimental reliance. Because this ratio may be thought of as an index of the promisor's good faith, we call it the "good-faith ratio." A damage offset based on the good-faith ratio and on the amount of potential beneficial reliance will encourage the optimal quantity and quality of promises by reflecting in the promisor's decision calculus both the harmful and beneficial effects of his promise-

making. This optimal legal sanction is likely to be unattainable in an environment of costly legal process and imperfect information.[44] But specifying an optimal sanction permits more rigorous evaluation of the error produced by any practical adjustment attributable to process costs. In addition, the good-faith ratio and the damage offset suggest a possible explanation for the language of the *Restatement of Contracts*, which conditions both the enforceability and the magnitude of reliance-based sanctions upon the "requirements of justice."[45] This language may reflect the view that the prospective beneficial effects of a promise should be considered in effecting a remedy for nonperformance.

The rule suggested by the formula above will admittedly result in a large quantity of uncompensated damages from broken nonreciprocal promises. Although greater damages would deter many injurious transactions, a stricter standard also would deter beneficial transactions in even greater magnitudes. Viewing an already-broken promise, the affected promisee would always prefer the highest possible damage award. But from the ex ante standpoint, a promisee would not wish to discourage a promise that creates a prospect of gain outweighing the risk of uncompensated loss. Such promises are "good bets" for the promisee over the long run, even though some of the promises will result in uncompensated harm. The penalty formulation developed above awards damages both to protect promisees from "bad bet" promises and to avoid deterrence of promises that are "good bets."

Under this prospective net reliance damage formula, the gratuitous promisor also has an incentive to undertake cost-effective qualitative precautions to modify prospective reliance induced by any promise actually made. A properly calibrated legal sanction will induce the promisor to convey to the promisee socially beneficial information about the risk of regret contingencies. In essence, such a promisor is encouraged to make cost-effective adjustments in both the quality and the quantity of his promises because the legal rule converts social benefits into savings for him. If, in addition, the law recognizes only the amount of damages that constitutes a "reasonable"—*i.e.*, cost-effective—reliance by the promisee, then the promisee will also have an incentive to minimize net social costs. Thus, the rule penalizes each party for failing to take cost-effective steps to minimize the social costs of promising. Damages exceeding those described above will tend to induce the promisor to invest too much in precautionary adjustments. This phenomenon is analogous to the excessive level of prudence anticipated if tort victims were awarded a multiple of their true damages.

44. *See* pp. 1289-90 *infra*.
45. RESTATEMENT 1ST § 90; RESTATEMENT 2D §§ 89B(2), 89D, 90(1), 217A(1).

2. *Reciprocal Promises*

Promising is reciprocal when the parties can adjust interactively to the nature and amount of promise-making. The prospective net reliance formulation is equally applicable to reciprocal as well as to nonreciprocal promises. But the net reliance damage rule seems in sharp conflict with accepted legal doctrine in the reciprocal promise context, in which damages for breach are typically based on the promisee's full-performance expectation rather than on his detrimental reliance. Upon analysis, the apparent conflict can be dissipated; moreover, reciprocal promises are easier than nonreciprocal promises for the law to address.

This conclusion is buttressed by two independent lines of argument. First, in the case of reciprocal promises, a plausible empirical generalization is that a promisee's acceptance of one promise frequently requires his foregoing a potential substitute promise. The forgone value of the best substitute promise available—the opportunity cost—is key in determining the promisee's detrimental reliance when an accepted promise is subsequently broken. In a well-organized market, alternative promises will be close, if not perfect, substitutes. In that case, detrimental reliance is equal to the full performance value of the breached promise.[46] Similarly, beneficial reliance will be small, because the promisor's pledge, even if performed, will not constitute a very substantial improvement over the potential beneficial reliance from substitute promises. This empirical generalization implies that, in the damage formula developed above, full performance expectation E can be substituted for detrimental reliance R because $E \approx R$. Furthermore, because $B \approx 0$, the term of $\left[\frac{1-p}{P}\right] B$ drops out. We are left with $D \approx E$; thus, expectation damages are a good proxy for the prospective net reliance damage formulation developed above.[47]

Second, a fundamental theoretical difference exists between reciprocal and nonreciprocal promises. In the case of a reciprocal promise,

46. The correlation between detrimental reliance and full performance expectation whenever there is a competitive market for the broken promise was first observed by Fuller and Perdue. *See* Fuller & Perdue, *supra* note 5, at 62-63.

47. Nothing in the logic of this argument limits its applicability to reciprocal promises. Although the argument's empirical premise tends to have greater validity with respect to bargained-for promises, classes of nonreciprocal promises may exist for which forgone substitute promises also yield a close convergence between reliance and expectation. The implications of using expectation as a proxy for reliance on reciprocal promises will become apparent when we introduce practical problems of measurement below. *See* pp. 1288-1321 *infra*.

the principal objective of a promisor is to obtain consideration in the form of a return promise. The value of the return promise elicited is the main element of the promisor's benefit. Therefore, changes in the qualitative aspects of the promise are reflected in commensurate shifts of benefits to the promisor; a higher quality promise motivates a more valuable return promise, and vice versa. In contrast to the case of nonreciprocal promises, qualitative adjustments are internalized in the promisor's cost-benefit calculus by generating a more or less valuable consideration for his promise. Hence, the bargaining process accomplishes an important part of the behavioral regulation that, for nonreciprocal promises, must be performed by the legal system.

Furthermore, the bargaining process, not available by definition in the nonreciprocal context, can facilitate the optimal allocation of risk for reciprocal promises. Precautionary action is subject to a test of the ability of the promisee to bribe the promisor to make an unconditioned promise. Within any scheme of enforcement, then, the parties can reallocate the risks of regretted promises by buying or selling protection through the terms of their agreement. The least-cost bearer of any risk will presumably agree to absorb that risk in exchange for an enhanced return promise.

For much the same reasons, the consequences of excessive damages for breaching reciprocal promises are also mitigated, as long as the rule providing for excessive damages is understood in advance. The parties can always bargain out from the rule, for instance by a limited damages agreement. Thus, when transactions costs are zero, the particular damage rule selected for reciprocal promises is irrelevant. Although the existence of transactions costs renders bargaining over damage rules costly in practice, the feedback adjustment of the return promise markedly reduces the potentially inefficient effects of legal rules. While in the nonreciprocal case, excessive damages overdeter the promisor from promissory activity, in the reciprocal relationship, the promisee will regard the excessive damages as a quality improvement and will offer an enhanced return promise. The enhanced return promise will tend to offset the deterrence effect of the damages. However, some inefficiencies remain. Legally mandated "overinsurance" induces a moral hazard because the promisee will not exercise optimal self-protection. Furthermore, there is a cheaper allocation of risk than the legally mandated level of reassurance provided to—and paid for by—the promisee.[48]

48. There is a close conceptual analogy between excessive contractual damages and specific guarantees or minimum quality requirements imposed by law on consumer

The result may be even more costly, however, when the law provides a suboptimal level of enforcement. The extreme case of a complete refusal to enforce reciprocal promises provides an instructive illustration.[49] The initial impact of the rule, which is to underdeter promisors, will be counterbalanced by reductions in the value of return promises. Promisors may then substitute extra-legal forms of reassurance for legal sanctions. Creating adequate extra-legal enforcement mechanisms is likely to be less efficient than legally sanctioned reassurance. If so, the inefficiency consequences of underenforcement may be more serious than those of overenforcement.

In sum, the theoretical damages principles developed in connection with nonreciprocal promises apply to reciprocal promises as well. The difference in their legal treatment may be due to a close empirical identity of reliance and expectation in reciprocal promises. However, modification of the return promise is a powerful additional adjustment mechanism, which exists, by definition, only for reciprocal promises. By internalizing many of the promissory interactions among contracting parties, the return promise reduces the stress placed on legal rules for optimally influencing the behavior of promisors and promisees.

D. *Summary and Implications*

The preceding analysis suggests that the function of promises can be observed more precisely by conceptually distinguishing the effects of the advance information from the actual transfer. Information from promises induces reliance whenever the promisee attaches a positive probability to performance. Reliance responses are beneficial when a promise is kept and detrimental when it is broken. The principal normative justification for permitting promises to be made freely is the belief that, on balance, promissory benefits exceed harms. Legally enforcing promises can sometimes increase this net social gain by encouraging cost-reducing behavior by both promisors and promisees.

The treatment of promises when performance or nonperformance is certain is simple: such promises can be fully enforced so as to maximize benefits or minimize costs respectively. In the sure performance case,

products. Because the product is required to be "better," it can command a higher price, which overcomes at least in part the reluctance of producers to supply a more expensive output. Nevertheless, a suboptimal result exists because consumers and producers could, if permitted, work out a mutually advantageous trade of less quality for less money.

49. In contrast to bargained-for limitations of standard damage measures, attempts to contract for supranormal remedies may run afoul of the rule against penalties. *See* Goetz & Scott, *supra* note 10, at 558-62.

enforcement, without deterring the promisor, increases the reliability of the promise to the promisee. In the certain nonperformance case, maximum deterrence of promises serves to prevent a bad-faith promisor from enriching himself at certain cost to the promisee.

The more important case of promises for which performance is potentially uncertain is more complex, because each promise carries both potential benefits and harms that must be balanced. Future contingencies may materialize rendering performance of such promises unattractive to the promisor. The risk of this regret contingency can be allocated several ways. On the one hand, nonenforcement of promises induces self-protective reductions in reliance by the promisee. These, in turn, may trigger reassurance reactions from the promisor. On the other hand, enforcement of promises increases promisee reliance, but also induces precautionary adjustments by the promisor. The social cost of the regret contingency is minimized when the optimal interactive adaptations are encouraged.

An examination of the function of legal rules in optimizing the interactions between the promisor and promisee explains the traditional distinction between nonreciprocal and reciprocal promises. In the case of reciprocal promises, the bargain mechanism provides a feedback of costs and benefits to the promisor and promisee. Thus, the liability rules for reciprocal promises do not directly influence promise-making; instead, they affect the costs of contracting between bargainers. For nonreciprocal promises, however, enforcement substantially shapes the adaptive responses of both parties.[50] For example, enforcement of nonreciprocal promises will optimize social benefits when extra-legal sanctions are minimal and the promisor can be encouraged to adapt the form of the promise to the risk of regret. Calibration of the optimal damages for such enforceable promises requires a consideration of both the beneficial and the detrimental reliance prospectively induced by the promise. Such a prospective net reliance formulation encourages promisors accurately to internalize social effects and thereby induces appropriate qualitative and quantitative adjustments.

But the practical implications of this ideal enforcement scheme must be considered. When nonenforcement is optimal, no measurement difficulties impede its implementation. When enforcement is indicated, implementation of the optimal rule is more difficult. A standard expectation-interest sanction may impose supra-optimal damages and deter socially valuable promise-making by inducing excessive precautionary behavior in promisors. The traditional reliance damage formulation—

50. *See* pp. 1307-08 *infra.*

return of the promisee to the status quo ante—most clearly approximates the optimal level of enforcement.[51] However, despite the language usually invoked, the status quo ante goal is rarely achieved by courts awarding so-called reliance damages. This systematic disparity between principle and practice isolates a central dilemma of promissory liability. True reliance damages, which include the value of opportunities forgone as well as the costs of actions taken, are extraordinarily difficult to measure accurately. Courts have generally responded to this largely unarticulated measurement conundrum by simply reimbursing the promisee for the gross value of any actions taken or actual expenditures incurred in reliance on the promise.[52] The recovery of such expenditures, which we have termed "reimbursement damages," should be distinguished from the theoretical objective of reliance damages.

We have developed the preceding model under an assumption of perfect measurement in order to evaluate the effects of legal rules on promissory behavior. Existing patterns of promissory liability often appear to produce substantial error costs in failing to regulate this conduct efficiently. Can this systematic error be explained? The complexity of the preceding analysis suggests that measurement of the true social cost of promising is likely to be itself a very costly activity. Enforcement costs increase the risk that the promisee's true reliance losses will not be fully recouped.[53] Moreover, process costs necessary to ascertain and implement the optimal level of enforcement may be so high that they exceed the error costs attributable to simpler rules of thumb such as no enforcement, full enforcement, or reimbursement. In Part II we relax the assumptions of perfect measurement and zero process costs to evaluate the efficiency of the rules of promissory obligation from a more practical standpoint.

II. Efficient Rules of Promissory Obligation

The second aspect of the promissory enforcement question asks whether the optimal enforcement model when adjusted for enforcement costs explains current patterns of promissory liability. We address this question first by describing the legal costs necessary to enforce promises and examining the relationship of these costs to different substantive rules. We then evaluate the rules of promissory liability by examining three basic categories of promises: fully bargained-for reciprocal prom-

51. *See* p. 1298 *infra.*

52. *See* pp. 1292-93 *infra.*

53. *See* Goetz & Scott, *supra* note 10, at 558 n.19; Schwartz, *The Case for Specific Performance,* 89 YALE L.J. 271, 274-78 (1979).

ises within the common law "consideration" model; nonreciprocal promises distinguishable by the parties' inability to adjust interactively the nature and amount of promising; and, finally, the intermediate category of unilateral promises in a reciprocal context, which, under the narrow common law standard, may be unenforceable despite the possibility of bargaining.

A. *Problems of Proof, Process, and Error Costs*

In Part I we developed damage rules that encourage the socially optimal production of beneficial reliance on future promises. Except when a nonenforcement rule is appropriate, imposition of such an optimal sanction necessitates that the detrimental reliance losses from the broken promise be ascertained. Unfortunately, promissory reliance is peculiarly impervious to accurate measurement and proof when it diverges from full performance expectation.[54] Because true reliance cost is equal to the opportunity cost of the promise, measurement of the loss requires a comparison of the promisee's behavior in response to the promise with his prospective conduct in the absence of the promise: the promisee's detrimental reliance cost is the difference in satisfaction between these two positions. This calculation entails identifying the value of alternative opportunities forgone because of the promise and the benefits retained from the actions taken in reliance. Generally, these values can be determined solely by evaluating the subjective claims of the promisee. Only when a competitive market generates prices indicating the value of foregone opportunities will there be reliable evidence of the position the promisee would have occupied had no promise been made.[55]

Furthermore, an optimal legal sanction may also include a discount for the effects of extra-legal factors—such as reputational losses or social restraints on breach—that independently reward the performing promisor for taking into account some of the social effects of promising.

54. The process costs of measuring reliance include both direct costs of litigation and the effects of "error," which are social costs that arise when the procedural mechanism fails to apply accurately the substantive rule. *See* Posner, *An Economic Approach to Legal Procedure and Judicial Administration*, 2 J. LEGAL STUD. 399, 400-02 (1973); Scott, *Constitutional Regulation of Provisional Creditor Remedies: The Cost of Procedural Due Process*, 61 VA. L. REV. 807, 810, 844-46 (1975).

Reliance expenditures are extraordinarily difficult to measure even in business contexts. Such expenditures often consist of overhead expenditures and joint costs not readily allocable to particular contracts. *See, e.g.*, Reiss & Weinsier, Inc. v. United States, 116 F. Supp. 562 (Ct. Cl. 1953); Houston Ready-Cut House Co. v. United States, 96 F. Supp. 629 (Ct. Cl. 1951).

55. Presumably, in a competitive market the prevailing market price reveals the opportunities forgone in reliance on the broken promise.

Thus, any theoretically precise reliance-based damage calculation may require an additional computation of the prospective beneficial effects that performance of the promise would have conveyed.[56] In addition to computing the magnitude of both detrimental and beneficial reliance, this "good-faith" calculation requires ascertaining the promisor's subjective probability of performance at the time the promise was made.

Adjustment of the damage formula may be necessary if measurement costs prohibit even the approximation of true reliance losses. The award of reliance-based reimbursement damages does not—despite its stated purposes of restoring the status quo ante—accurately measure true reliance.[57] In fact, there is no a priori reason to believe that a reimbursement award is preferable in any particular case to nonenforcement or full performance compensation.[58] In sum, the administrative and error costs of attempting to apply a theoretically optimal net reliance standard suggest that it may be worthwhile to adopt a surrogate measure that is cheaper to apply.

The ease of administration of rules regulating promising are in part a function of the clarity of the substantive rule. Clarity is enhanced by use of a substantive rule that reduces the number and complexity of facts to be determined. A clear rule, such as nonenforcement or full performance compensation, yields benefits of reduced litigation costs and increased procedural accuracy. The primary cost of a clear rule is that it regulates promissory conduct imprecisely.[59] Full performance compensation, for example, may deter some promises with positive expected benefits that an optimal rule would encourage. But a rule that better reflects true promissory reliance requires resolution of more

56. *See* p. 1283 *supra*.

57. In order to approximate the status quo ante position of the promisee, the damage rule must measure two additional variables: the cost of forgone opportunities and the gain to the promisee from the induced action. Mere recovery of the out-of-pocket costs of the induced action will overvalue the harm induced by actions taken and undervalue the hidden losses incurred from forbearance. Yet, only when there is a competitive market for such promises can either of these variables be measured confidently. *See* pp. 1296-97 *infra*.

58. When forbearance is significantly greater than out-of-pocket expenditures, a reimbursement award will be substantially lower than the value of true reliance. Alternatively, when the induced actions involve substantial expenditures that produce difficult-to-measure benefits to the promisee, a reimbursement award may substantially exceed the value of detrimental reliance.

59. A clearer enforcement/nonenforcement rule may be both overinclusive and underinclusive. For example, full performance enforcement may restrain some socially beneficial promises by imposing an excessive sanction. Alternatively, nonenforcement may fail to charge promisors for the social costs of nonperformance. *Cf.* Ehrlich & Posner, *An Economic Analysis of Legal Rulemaking*, 3 J. LEGAL STUD. 257, 267-71 (1974) (explaining how precision of legal rules generates costs of overinclusion and underinclusion).

factual issues and thereby reduces the rule's clarity. Thus, a particular rule is efficient when both substantive and procedural components are constructed so as to provide the cost-minimizing balance between accuracy and clarity.[60]

A theory of promissory liability that minimizes these costs remains elusive. The foundations for such a theory were established by Professor Lon Fuller over fifty years ago.[61] Fuller's claim for the preeminence of reliance, however, seems inconsistent with established bargain theory. For example, a gratuitous promise, unsupported by consideration, is commonly presumptively unenforceable. Yet that same promise, if a product of a bargained-for exchange, is fully enforceable without any evidence of reliance. Fuller explained this apparent anomaly by suggesting that gratuitous promises are unenforceable because reliance is lacking, while the bargained-for promise is fully enforceable in order to facilitate likely reliance.[62] Our analysis of the information function of promises confirms the inadequacy of these explanations. Gratuitous promises can induce reliance, whose costs are ignored under nonenforcement.[63] Furthermore, facilitation of likely reliance by awarding full compensation for executory bargains may deter the future production of socially useful promises.[64]

However, the rules of promissory liability can be reconciled with the reliance principle. The existing tension between bargain and reliance is a product of the failure to discriminate adequately between ideal and pragmatic objectives. For example, common law bargain theory and the doctrine of consideration, as well as the modern concept of promissory estoppel, can be examined best as cost-minimizing surrogates for true reliance. Introducing the complexities of measurement and proof indicates that the traditional choice between reliance damages and the alternatives of nonenforcement and full performance compensation should be recast as an attempt to select from potential contract rules the best achievable approximation of the optimal enforcement standard.

60. *See id.* at 262-71.

61. *See* Fuller & Perdue, *supra* note 5; Fuller, *supra* note 20. Three critical insights can be extracted from Fuller's exploration of the remedial and formal structures of contract: first, reliance is the organizing principle that supports all contractual obligation; second, typical contractual remedies—such as compensatory damages—serve as cost-reducing administrative surrogates for reliance; and third, a direct relationship can be identified—through the formal structure of promissory liability rules—between process considerations and the substantive rules of contract.

62. *See* Fuller, *supra* note 20, at 815-18.

63. *See* pp. 1267-70 *supra.*

64. *See* pp. 1285-86 *supra.*

B. *Reciprocal-Bargain Promises: The Consideration Model*

First, we examine reciprocal promises reached by bargaining, for which the common law developed the consideration doctrine.

1. *The Functions of Bargain*

Evaluating contract rules as cost-reducing surrogates for the theoretically optimal enforcement rule reemphasizes the importance of the distinction between reciprocal and nonreciprocal promises. Promises that satisfy the reciprocal exchange requirement of consideration are presumptively enforceable. Breach entitles the promisee to full performance compensation. The enforceability of reciprocal promises is supported by a rich normative literature emphasizing the social utility of bargains.[65] But more importantly, as suggested above, the bargain mechanism can reduce discrepancies between optimal and actual enforcement rules.

We have pointed out the identity between detrimental reliance and full-performance expectation whenever markets for promises are competitive.[66] Furthermore, bargaining tends to produce the optimal amount of promissory reliance even when the legal rule deviates from the optimal reliance principle. By modifying contractual terms, the parties can vary the standard liability rule in order to maximize net reliance benefits.[67]

What effects can be predicted from full enforcement of reciprocal bargain promises? As the model developed in Part I suggests, application of sanctions for breach imposes the risk of the regret contingency

65. *See, e.g.*, 1 A. SMITH, THE WEALTH OF NATIONS 12-15 (Everyman's Library ed. 1937); Patterson, *supra* note 15, at 945; *Promise or Bargain?*, *supra* note 1, at 463-65.

66. The competitive market offers one polar case in which the promisees' detrimental reliance is precisely equal to full performance expectation. *See* Goetz & Scott, *Measuring Sellers' Damages: The Lost Profits Puzzle*, 31 STAN. L. REV. 323, 333-35 (1979) (measuring damages in competitive markets). The other pole is represented by the classic bilateral exchange in which the promise made to one or both parties is singular or unique. An example drawn loosely from the facts of Hamer v. Sidway, 124 N.Y. 538, 27 N.E. 256 (1891), may illustrate this point. Suppose William II promises his Uncle William to refrain from smoking and drinking, while the uncle promises in return to pay his nephew $5000 for each year in which the youth remains an abstainer. Subsequently, Uncle William reneges on his promise. Because no alternative market existed in which William II could have obtained a promise of money in exchange for his own promise, he has not forgone any alternative promise and his "immediate reliance" is zero. Nonetheless, receipt of even a singular bargain promise does induce a "consequential reliance" of alterations in consumption, whose magnitude is unpredictable.

67. The bargaining context invites a promisee to obtain any promise with a positive expected value. Legal liability, like any other risk in an executory exchange, can be optimally allocated between the parties.

on the promisor. As the promisor's potential liability is increased, he is encouraged to take precautionary action to minimize the expected liability, by conditioning promises more carefully in negotiations. The promisee, in turn, may bargain for a less restricted promise by paying explicitly for the additional reassurance provided by a compensation award.

Alternatively, a rule denying enforcement of a bargained-for promise reduces precautionary costs incurred by promisors seeking to minimize the risks of regret, because it shifts that risk to the promisee. The promisee may adapt to this increased uncertainty by discounting the price he is willing to pay for the promise. If the promise is actually worth more than the promisee estimates, the promisor will incur costs up to the expected value of the promise in order to assure the promisee of the true worth of the promise. These additional reassurance costs induced by the promisee's adaptive behavior could include the voluntary assumption of legal liability through collateral guarantees or performance bonds.

Thus, because bargainers will attempt to allocate the risk of regret optimally themselves, the effects of enforcement rules depend on the transaction costs of risk allocation. Evaluation of these costs requires an analysis of how bargainers adapt to the risks of regret contingencies. If in certain transactions precautionary efforts by promisors would be more expensive than reassurance, nonenforcement enables the parties to shift the risk of regret more cheaply. Alternatively, when reassurance is more costly, fully enforcing promises induces cheaper precautionary conduct. If each type of transaction can be identified ex ante, specifying the cost-effective rule in advance produces the outcome that the parties would reach if they bargained over legal liability for breach.

2. *The Design of the Bargain Paradigm*

The classical bargain model can be examined on the basis of these assumed variations in precautionary and reassurance costs. Not all promises made in a bargaining context are presumptively enforceable. Indeed, the reciprocal bargain or consideration model is considerably more limited than the larger exchange context that it occupies. For example, promises made during preliminary negotiations[68] and prom-

68. In the words of the *Restatement 2d*: "A manifestation of willingness to enter into a bargain is not an offer if the person to whom it is addressed knows or has reason to know that the person making it does not intend to conclude a bargain until he has made a further manifestation of assent." RESTATEMENT 2D § 25; *see* 1 A. CORBIN, *supra* note 5, §§ 26-27, at 95-100.

ises to discharge contractual obligations[69] are traditionally unenforceable even though they are made in the context of a bargain. This failure to impose liability in certain exchange contexts can be contrasted with the wholly executory completed bargain, which is fully enforceable when supported by consideration. In each case, the liability rule can be explained by its impact on transactional efficiency.

Under traditional bargain theory, promises made during preliminary bargaining are not enforceable until the bargain is sealed by an agreed exchange. Complex rules of offer and acceptance have been developed in order to distinguish enforceable bargained-for promises from unenforceable preliminary negotiations. Suppose *A* promises to sell, and *B* to buy, 1000 widgets "at cost plus a nice profit." Subsequently, in a disagreement over the price, *A* refuses to deliver the widgets to *B*. Because the price term was not determined, the bargain remains incomplete. Hence *A*'s promise will probably be characterized as an unenforceable preliminary promise.[70] If, instead, a ten percent profit were negotiated, both promises would be fully enforceable. But assume that after the widgets have been delivered *A* promises *B*, "Your obligation will be cancelled. I will release my right to the $1000 that you owe me." As with the preliminary negotiation, this discharge promise is unenforceable. The rights that were created by the bargain cannot be extinguished by agreement without consideration.[71]

Freedom from liability upon entry and exit from bargaining, coupled with full enforcement of wholly executory promises once agreement has been achieved, is the basic design of the bargain model of traditional contract law.[72] This pattern typically has been explained in terms of differences in the magnitude of either actual or likely reliance. Neither explanation is persuasive. Disregarding the effect of the rule itself,

69. On promises to discharge contractual obligations, the *Restatement 2d* states the following: "A promise to discharge [a] duty must, like any other promise, be supported by consideration in order to be enforceable." RESTATEMENT 2D, Introductory Note, §§ 343-347, at 5 (Tent. Draft No. 13, 1978); *see* 5 A. CORBIN, *supra* note 5, § 1236; RESTATEMENT 1ST § 406.

70. *See* C.H. Leavell & Co. v. Grafe & Assocs., 90 Idaho 502, 414 P.2d 873 (1966); RESTATEMENT 2D § 32, Comment 7, Illustration e.

71. RESTATEMENT 2D § 343, Illustration 1 (Tent. Draft No. 13, 1978).

72. There are some imperfections in the symmetry of the common law design. The traditional preexisting-duty rule held that when a promisee agreed in exchange for a promised benefit to do what he was already legally obligated to do, the exchange lacked consideration and the return promise was unenforceable. *See* 1 A. CORBIN, *supra* note 5, §§ 171-192; Patterson, *supra* note 15, at 936-38. Because this rule was both overinclusive and underinclusive with respect to the coercive conduct it purported to attack, the modern view finds promises that modify a prior agreement presumptively enforceable absent unfair pressure or bad faith. *See* U.C.C. § 2-209(1), Comment 2; RESTATEMENT 2D §§ 76A, 89D, Comment b.

there is no a priori reason to believe that reliance on either a preliminary or a termination promise will be less prevalent than reliance on the main promise itself. The enforcement choice, however, will affect the expected costs of bargaining between *A* and *B*. Enforcement of preliminary or termination promises will increase the cost of promising to promisors. Potential promisors will be willing to incur greater precautionary costs to avoid the risks of liability. Alternatively, a nonenforcement rule increases the cost of promises to promisees. Consequently, the amount of bargaining devoted to assurances of performance will be increased. The enforcement pattern could be explained if, during entry into, and exit from, bargaining, reassurance were cheaper than precaution. Then, the risk of a regret contingency could be allocated more cheaply by adjusting reliance once the promise is made rather than restricting the promise itself.

The design of the consideration model can be explained if the categories of bargaining risks are conceptually distinguished. Each bargainer, being both a promisor and promisee, faces two sets of parallel risks. As a promisor, the bargainer confronts the risk of liability should he fail to keep his promise. He also faces the risk of detrimental reliance should the promise made to him in return be broken. Based on the common empirical assumption that bargainers are generally risk-averse, the consideration model is justifiable in economic terms. Because the outcomes of negotiations are uncertain and gains and losses are indefinite, risk-averse parties will choose to forgo uncertain gains rather than incur equally uncertain losses of the same magnitude. In other words, risk-averse bargainers will prefer to bear uncertain risks as promisees rather than as promisors. Moreover, because a promisee can control reliance costs more easily than can a promisor, the risk of detrimental reliance is lower if borne by the promisee rather than the promisor. An enforcement rule would encourage excessive precautionary adjustments by risk-averse bargainers, because the uncertain consequences of nonperformance could not be controlled. Therefore, negotiations by such bargainers to reallocate risks through precautionary action would be more costly than the reallocation of identical risks through reassurance.[73]

73. The basic economic justification for such a scheme is that it saves most parties the costs of negotiating the preferred allocation of risks. Considerable flexibility to rearrange the risks of liability are retained by individual bargainers. Generally, the parties can elect to incur liability during preliminary exchanges by signaling their intention to be bound. *See* U.C.C. § 2-204(3) (requiring reasonably certain basis for granting remedy); RESTATEMENT 2D §§ 25, 32, Comment b (same). Alternatively, bargainers can choose a nonenforcement regime by indicating an intention not to be bound. *See* RESTATEMENT 2D § 21B, Comment b.

But bargainers prefer the risk of uncompensated reliance only on the periphery of bargaining. The crucial distinction between the periphery and the core of bargaining is the shift toward greater certainty of outcome. The impetus to bargain is the assumption that expected gains will exceed expected losses. Thus, when the transaction is finally negotiated, the expected value of gain outweighs the risk of liability upon breach.[74] Thus, after agreement, bargainers prefer to bear remaining risks as promisors rather than as promisees, thereby mutually enhancing the expected benefits to each. Consequently, expenditures required for reassurance under nonenforcement would exceed the investment in precaution required by full enforcement.[75]

The reluctance to enforce peripheral promises, on entry or exit, can also be explained on process grounds, even if the parties intend to be legally bound. The more incomplete and uncertain the details of an exchange, the greater the adjudicatory and error costs in resolving subsequent disputes. A greater allocation of resources to negotiation of the details of an agreement saves the parties expected litigation costs in case of subsequent dispute. If both litigation and negotiation costs were fully borne by bargainers, it would be efficient to permit them to negotiate to the point at which marginal expenditures in negotiations equalled marginal reductions in expected litigation costs. However, because litigation costs are partially subsidized by taxpayers, parties will engage in a suboptimal amount of negotiation and thereby generate an overinvestment in litigation. The refusal of the common law rules to enforce indefinite bargains can be seen as an attempt to compensate for this process distortion.[76]

In sum, the design of the consideration model can be explained persuasively by an analysis of efficient risk allocation. Manipulation of the liability rule shifts the risk of a regret contingency between prom-

74. Changed conditions producing regret will not necessarily induce the promisor to breach. Breach occurs only when the cost of performance exceeds liability for nonperformance. Breach is motivated, at least in part, by a belief that the promisee is better able to salvage or minimize the effects of the changed conditions than is the promisor. For example, a seller-promisee can generally resell unwanted goods more cheaply than a buyer-promisor who no longer wants to retain them. *See* Goetz & Scott, *supra* note 66, at 344 (optimal liability rule would make choice between performance and breach a matter of indifference).

75. Discharge negotiations seem characterized by less ambiguity and uncertainty than are preliminary negotiations. This intuition is confirmed by the fact that the nonenforcement rule has been applied much more hesitantly in the discharge context.

76. *See* 1 A. CORBIN, *supra* note 5, §§ 95-97; RESTATEMENT 1ST § 32; 1 S. WILLISTON, CONTRACTS §§ 37-48 (3d ed. 1957). Although the Uniform Commercial Code shifts the presumption in favor of party autonomy, it retains the injunction against enforcing indefinite bargains unless "there is a reasonably certain basis for giving an appropriate remedy." U.C.C. § 2-204(3).

isees and promisors. These varying liability patterns can induce interactive adaptations by the parties to allocate the social costs of promising efficiently. This cheapest-risk-allocation design is buttressed by process considerations that justify imposing promissory liability only if agreement upon the basic transaction has been reached.

3. *Remedies for Nonperformance of Bargained-for Promises*

The impact of any enforcement rule ultimately depends on the character of the remedy for nonperformance. Full enforcement compensation is the standard recovery for breach of reciprocal-bargain promises, whenever such an award can be determined accurately. The stated objective of this compensation rule is to place the promisee in the same economic position he would have occupied had the promise been performed.[77] As we have argued above, this rule, by imposing a sanction in excess of the social costs of breach, overdeters socially useful promising, except in competitive markets in which expectation is equivalent to reliance. The bargain context, however, enables the parties to vary, with low transactions costs, the legal rule by agreement and thereby mitigate the effects of any remedial distortion. Moreover, the disparity between compensatory recovery and optimal reliance damages is usually more than offset by gains in the clarity of the rule. Suppose *A* promises *B* $5,000 in exchange for *B*'s agreement to paint *A*'s portrait. After the painting is completed, *A* reneges. Because the market for similar promises is likely to be thin, the immediate reliance or opportunity cost of *A*'s promise may vary unpredictably from the $5,000 contract price. Furthermore, *A*'s promise and breach will have produced a detrimental adjustment in *B*'s pattern of consumption. The amount of such consequential reliance is even more difficult to measure. Full performance compensation in this example is precisely and objectively measured by the $5,000 face value of *A*'s promise. The administrative advantages of this clear rule outweigh the potential costs of distortion.

When the promisee's expectation includes the consequences of performance, the damage rule becomes more complicated. Suppose *A* promises to sell *B* the raw materials for manufacturing 1,000 widgets at the current market price of $5,000. *A*'s breach causes *B* to lose two weeks of production of widgets. The $5,000 contract price no longer approximates *B*'s expectations from performance. In this situation, *B* will not be entitled to recover his lost profits from *A* unless they were

77. 5 A. CORBIN, *supra* note 5, § 992.

foreseeable when the contract was made and can be proved with reasonable certainty.[78] If *B*'s expectation is unforeseeable or difficult to establish, reimbursement damages may be awarded rather than full performance compensation.

It is tempting to conclude that reimbursement recoveries are always preferable to full-performance damages as a more accurate approximation of the optimal reliance-based sanction. However, as suggested above, reimbursement recoveries are limited on practical grounds to the amount of the expenditures induced by the promise.[79] Courts have not even attempted to ascertain the value of forgone opportunities; expenditures have been reduced to their net value only when a salvage market exists. Thus, a reimbursement remedy is not necessarily a more accurate proxy for the optimal reliance-based sanction than full-performance compensation.

Following a total breach by the promisee, the value of a partial performance by the promisor can also be recouped through a reimbursement recovery.[80] The intricate patterns of recovery in partial performance cases can be explained by variations in magnitude of the costs of proof and valuation.[81] Courts usually award whichever recovery of reimbursement and compensation is readily measurable in monetary terms. In the more common cases in which neither compensation nor reimbursement is easily measured, the promisee may elect either compensation or reimbursement damages for partial performance so long as he is not made better off than his original expectation.[82]

Although objectively measurable recovery has the advantage of re-

78. *See* Farnsworth, *supra* note 10, at 1158-59 (also requiring effort to mitigate damages); Note, *Lost Profits as Contract Damages: Problems of Proof and Limitations on Recovery*, 65 YALE L.J. 992, 997-98 (1956) (relating causation to foreseeability and certainty).

79. *See* Royce Chem. Co. v. Sharples Corp., 285 F.2d 183 (2d Cir. 1960); L. Albert & Son v. Armstrong Rubber Co., 178 F.2d 182 (2d Cir. 1949); Gruber v. S-M News Co., 126 F. Supp. 442 (S.D.N.Y. 1954).

80. 5 A. CORBIN, *supra* note 5, § 1104; RESTATEMENT 1ST § 347.

81. The relation between process costs and the choice of remedies can be illustrated by returning to the example that was described above. Suppose *A* promises to sell *B* the raw materials for manufacturing 1,000 widgets at the current market price of $5,000. *A* reneges. If *B* has paid the agreed price, he is entitled to a $5,000 restitutionary reimbursement even though performance by *A* would have yielded a loss to *B*. *See* Bush v. Canfield, 2 Conn. 485, 488 (1818). Conversely, if *A* were to deliver the raw materials and *B* were to breach his promise to pay $5,000, reimbursement of expenditures would be denied to *A*; rather, *A* would be limited to his $5,000 expectancy even when the value of the raw materials delivered was significantly greater. *See* Oliver v. Campbell, 43 Cal. 2d 298, 306, 273 P.2d 15, 20 (1954).

82. A court will not "knowingly put the plaintiff in a better position than he would have occupied had the contract been fully performed." Fuller & Perdue, *supra* note 5, at 79; *see* Farnsworth, *supra* note 10, at 1178-79.

ducing process costs, ease of measurement does not fully explain the selection of damage rules. In addition to the uncertainty of the loss, findings of remoteness and unforeseeability are used to limit consequential recoveries.[83] Courts appear unwilling to inflict socially harmful overdeterrence when the gains from awarding compensation are attenuated. Furthermore, the damage limitations of uncertainty and unforeseeability are not uniformly applied. The doctrines have been rigorously applied in cases in which liability appeared disproportionate to the gains the promisor anticipated from the contract, but have been rarely invoked when recoveries were of more limited magnitude.[84]

These limitations on consequential losses are consistent with the assumption of risk aversion discussed above. If a risk-averse promisor faces potential consequences of breach that are disproportionately large as well as unpredictable, he will increase his precautionary efforts. Limitation of the legal sanction divides the risk of regret between promisors and promisees. Promisors continue to bear the risk of the known and ascertainable consequences of concluded bargains, while promisees bear the risk of uncertain and unforeseeable consequences. A partial reallocation of the risk will reduce promisors' precautionary costs and increase their investment in reassurance. However, the expenditures on reassurance should be less than the investment in precaution under a fully compensatory scheme. First, risk-averse bargainers will choose to forgo gains rather than risk losses of equal magnitude. The cost to the promisee of forgoing profitable but unforeseeable actions in reliance on a promise will be lower than the cost to the promisor of bearing the risks that the promisee will engage in such action and that a regret contingency will arise. Thus, bargainers will prefer to bear the risk of uncertain and potentially severe consequences as promisees rather than as promisors. Second, because the consequences of breach are better known to the promisee, he is better able to select the optimal mix of promisor reassurance and self-protection through

83. *See* Fuller & Perdue, *supra* note 5, at 373-77 (analyzing other factors that limit recovery); *cf.* Note, *supra* note 78, at 997-1000 (criticizing rules limiting recoveries).

84. *See* Fuller & Perdue, *supra* note 5, at 375-76. *Compare* Dieffenbach v. McIntyre, 208 Okla. 163, 254 P.2d 346 (1952) (denying recovery for anticipated profits to plaintiff who received some damages) *with* Smith v. Onyx Oil & Chem. Co., 120 F. Supp. 674 (D. Del. 1954), *modified*, 218 F.2d 104 (3d Cir. 1955) (allowing recovery for anticipated profits to plaintiff who otherwise would recover nothing).

In addition to the disproportionate verdict problem, the bad faith or willfulness of the promisor's breach has been a relevant variable influencing the application of the uncertainty and foreseeability limitations. *See* Bauer, *The Degree of Moral Fault as Affecting Defendant's Liability*, 81 U. PA. L. REV. 586, 592 (1933); Fuller & Perdue, *supra* note 5, at 374-75. Imposition of full enforcement sanctions on the bad-faith promisor is consistent with the optimal enforcement model developed above. *See* note 35 *supra*.

limited reliance. In addition, the limitation on the award of damages for unascertainable consequences of breach induces the promisee to disclose to the promisor information that the promisor may not have concerning the consequences of breach. This information would not be disclosed to the promisor under a full-performance compensation rule and benefits from promise-making would not be maximized. Thus, the limitation on damages for unforeseeable consequences of breach increases the efficiency of promissory activity by stimulating the provision of information between bargainers.[85]

4. *The Implications of the Consideration Model*

Dissatisfaction with the mechanical rules of the common law has induced courts and commentators to offer more flexible alternatives.[86] For example, detrimental reliance has been urged as a basis for imposing discretionary liability for broken promises made in a bargaining context.[87] The current liability design of the consideration model appears to rest on crucial assumptions about bargainers' risk preferences and relative abilities to minimize risks. The indeterminacy of these empirical assumptions may explain the rigidity of the common law pattern. Liability based on future actions such as those in reliance increases bargaining uncertainty, the cost of which reduces the social value of the exchange. Whenever the outcome of private bargaining is unpredictable, liability rules that clearly specify the consequences of alternative actions will minimize uncertainty. By sharply distinguishing fully enforceable bargains from unenforceable promises, the formal rules of consideration permit bargainers to choose the outcome that minimizes expected bargaining costs.

The preceding analysis explains only the basic design of the consideration model. It does not help identify where to draw the line between enforcement and nonenforcement. At common law the category of enforceable bargained-for promises was rigidly narrow. The reluctance of common law courts to impose liability for a broader category of bargain promises perhaps can be explained by the frequent

85. Hadley v. Baxendale, 9 Exch. 341, 156 Eng. Rep. 145 (1854); *see* U.C.C. § 2-715(2)(a). Denial of lost profits as too uncertain or remote is generally accompanied by the recovery of reimbursement damages for expenditures incurred in pursuing the venture, on the presumption that the promisee would at least have covered his losses. *See, e.g.*, C.C. Hauff Hardware, Inc. v. Long Mfg. Co., 260 Iowa 30, 35, 148 N.W.2d 425, 428 (1967). In any event, the burden of reducing recovery below plaintiff's expenditures must lie on the defendant. *See, e.g.*, L. Albert & Son v. Armstrong Rubber Co., 178 F.2d 182, 189 (2d Cir. 1949).

86. *See, e.g.*, Knapp, *Enforcing the Contract to Bargain*, 44 N.Y.U. L. REV. 673 (1969).

87. *See, e.g.*, RESTATEMENT 2D §§ 89B(2), 89C(c), 89D(c), 90.

distortion between the standard compensation rule and the optimal reliance sanction. Because nonenforcement eliminates distortions in measurement, it may be the preferable treatment for bargain promises when full enforcement provides no compensating advantages. We suggest below, however, that the recent expansion of promissory liability is consistent with the judgment that, for certain types of bargain promises, a larger core of liability can be defined without causing a significant increase in enforcement costs. Our analysis of this development can be clarified by first examining promise-making outside the exchange model.

C. *Nonreciprocal Promises*

Promises that are not conditioned upon a return promise are, unlike bargained-for promises, generally unenforceable.[88] Although unbargained-for promises are frequently made in exchange contexts, we consider here only the case of promises made outside a bargain setting. Such nonreciprocal promises typically include promises of gifts, charitable subscriptions, and other unilateral pledges to confer benefits.

The substance rather than the form of bargain triggers the distinction between reciprocal and nonreciprocal promises.[89] For example, social engagements, domestic bargains, and sham exchanges may use the bargain form for an essentially gratuitous promise. Courts typically explain the nonenforceability of social promises with the tautology that no legal obligation was intended.[90] In the case of intraspousal bargains, this rationale is reinforced by an expressed deference to the marital relation. For sham exchanges, courts generally find "nominal consideration" insufficient to support the gift promise, whose enforceability depends on the reality, not the form, of bargain.[91] Enforcement of such purely formal bargains could entail high process costs, inasmuch as such frequently trivial promises would be relatively expensive to adjudicate. However, it is no less expensive to litigate most small contracts. Non-

88. "[A] mere promise, without more, lacks a consideration and is unenforceable," Stonestreet v. Southern Oil Co., 226 N.C. 261, 263, 37 S.E.2d 676, 677 (1946), though it "cannot be broken without a violation of moral duty," Mills v. Wyman, 20 Mass. (3 Pick.) 207, 210 (1825).

89. Obviously, any distinction between bargaining and nonreciprocating contexts is an arbitrary one. The test that we propose is whether the promisee has a realistic opportunity to affect the nature and supply of promising by altering the "price" of the promise. *See* note 38 *supra.*

90. 1 A. CORBIN, *supra* note 5, § 34; RESTATEMENT 2D § 21B, Comment c & Illustration 5.

91. Lawhead v. Booth, 115 W. Va. 490, 177 S.E. 283 (1934); RESTATEMENT 2D § 76, Comment b & Illustration 5, Comment c.

enforcement of these promises can be more plausibly related to the same empirical assumptions that support the general unenforceability of nonreciprocal promises.

1. *The General Policy of Nonenforcement*

The hypothetical case of *Mortensen v. Central National Bank*[92] provides a convenient vehicle for evaluating the practical legal questions implicit in the treatment of nonreciprocal promises. Assume that on September 15, 1978, 72-year-old Mary Guillette wrote a letter to her nephew, James Mortensen, promising him a $10,000 Persian rug that he had long admired. The letter indicated that the rug would be shipped to Mortensen "sometime after I return from Florida in the spring, but no later than June 1." Guillette died in Florida on January 1, 1979, shortly after assuring Mortensen, "I'm looking forward to sending you the rug as soon as possible; you can count on it." Subsequently, Central National Bank, as the executor of Guillette's estate, refused to deliver the rug to Mortensen.

In practice, Mortensen's right to enforce his aunt's promise would depend crucially on whether the promise, which lacks the requisite bargained-for consideration, induced Mortensen to act visibly in detrimental reliance.[93] In fact, as shown above, detrimental reliance is likely to occur even if no visible evidence of it exists.[94] Between the date of the promise and that of the repudiation, Mortensen will have modified his consumption habits in adjustment to his suddenly increased expected wealth. If this expectation is disappointed, Mortensen's excessive consumption will have produced a permanent net loss in welfare; this loss is his reliance injury. Courts rarely acknowledge the existence of such uncompensated reliance when they refuse to enforce gratuitous promises.[95] The absence of bargained-for consideration triggers instead a presumption of nonenforcement.

The optimal enforcement model identified a series of interactive adaptations induced by legal enforcement of nonreciprocal promises. A legal sanction initially increases the reliability of a promise above the level the promisor voluntarily provided. But enforcement also triggers

92. The facts are drawn loosely from a case on which one of the authors consulted; it was ultimately resolved by settlement.

93. *But see* pp. 1305-07 *infra* (requirements for enforcement under § 90).

94. *See* pp. 1267-70 *supra.*

95. *See, e.g.*, Stonestreet v. Southern Oil Co., 226 N.C. 261, 263, 37 S.E.2d 676, 677 (1946) ("It is said that when one receives a naked promise and such promise is not kept, he is no worse off than he was before the promise was made. He gave nothing for it, loses nothing by it, and upon its breach he suffers no recoverable damage.")

precautionary adjustments by promisors. Whether these interactions are optimal depends upon the promisor's certainty regarding performance, the effectiveness of extra-legal sanctions, and the capacity of qualitative adjustments to minimize the social costs of the regret contingency.

In this hypothetical case, Guillette intended to perform up until the time of her death. When the promisor is subjectively certain of performance, full enforcement offers the social benefits of increased beneficial reliance without countervailing precautionary costs. Even slightly uncertain promisors may obtain benefits through enforcement that exceed any increased precautionary or regret costs.[96] Thus, the certainty of performance seems critical in distinguishing the enforcement of sham bargains from the legal treatment of other nonreciprocal promises. At common law, the formal contract under seal provided a means for promisors to assure enforcement of gratuitous promises.[97] A sham bargain performs a similar function in encouraging deliberation, preserving evidence, and identifying the promisor's intention.[98] Although devices such as seals and sham bargains entail significant administrative costs, the voluntary use of these formal mechanisms suggests that the benefits to both parties of the additional reassurance from legal enforcement outweighs the transactions costs.[99]

The aggravated process costs of regulating social, rather than commercial, conduct seems to underlie nonenforcement even when the promisor is certain of performance. These additional costs may outweigh the gains in reliability under an enforcement rule. Enforcement of nonreciprocal promises in which formality suggests certainty requires

96. *See* pp. 1271-74 *supra.*

97. Dean Pound suggested that the seal fell victim to the "informality of pioneer America." *Promise or Bargain?, supra* note 1, at 468. The status of the seal is tenuous in many jurisdictions. *See* RESTATEMENT 2D, Introductory Note §§ 95-110. It is easy, however, to overlook alternative legal mechanisms that accomplish similar results. In particular, the decline of the seal has been paralleled by a corresponding increase in the use of *inter vivos* trusts and a relaxation in the delivery requirements for the validity of *inter vivos* gifts of personal property. Symbolic transfers, including informal writings, have been sustained when intent was clear and physical transfer was not easily accomplished. *E.g.*, Hawkins v. Union Trust Co., 187 A.D. 472, 473, 175 N.Y.S. 694, 695 (1919).

98. For the classic discussion of the rationale of legal formalities, see Fuller, *supra* note 20; *cf.* RESTATEMENT 2D § 76, Comment c. The sham bargain offers formal advantages that justify a distinction from the treatment accorded a simple donative promise. Although the evidentiary basis may not be any stronger, the fact that the promisor went to the trouble of constructing the sham exchange is substantial evidence of deliberation and intention.

99. One of the functions of legal formality, defined by Fuller as the cautionary function, is to deter inconsiderate action. Fuller, *supra* note 20, at 800. Professor Melvin Eisenberg argues that the information and process costs of ensuring a form adequate to guard against both improvidence and false claims are significant. *See* Eisenberg, *Donative Promises*, 47 U. CHI. L. REV. 1, 8-18 (1979).

additional procedural safeguards to protect against careless promise-making and false claims.[100] The problem of false claims is exacerbated by the context of many nonreciprocal promises. Many donative promises are oral[101] and the claims are often lodged against the promisor's estate.[102] The concern over resulting fraudulent claims is reflected by the more rigorous evidentiary rules governing the actual transfer of these property rights. Testamentary dispositions and *causa mortis* gifts require objective evidence of the transfer not required for *inter vivos* dispositions.[103]

If the gratuitous promisor is at all uncertain about future performance, nonenforcement can be explained by two empirical assumptions unrelated to process costs:

First, extra-legal sanctions against breach are effective in most nonreciprocal settings.

Second, even when extra-legal sanctions are not fully effective, the prospect of increasing the exchange of information through qualitative adjustments is small in most donative contexts.

Donative promises generally are more likely to be performed than are other promises and thus offer prospective benefits that outweigh prospective harms. Extra-legal sanctions are likely to be effective in the donative context because promisors generally care about the welfare of promisees. In contemplating a promise, the promisor may regard costs suffered by the promisee as equivalent to costs suffered by himself. Then, the promisor will have already taken into account the prospective detrimental reliance of the promisee. Thus, the need for a legal sanction to reflect the promisee's interests is obviated.

Furthermore, the supply of donative promises is likely to be very sensitive to the attachment of legal liability. Social considerations frequently will deter the qualitative precautionary option of attaching

100. *See, e.g.*, Haase v. Cardoza, 165 Cal. App. 2d 35, 38, 331 P.2d 419, 421 (1958) (informal promise not enforceable if utterly alone, without past consideration or reliance); Overlock v. Central Vt. Pub. Serv. Corp., 126 Vt. 549, 553, 237 A.2d 356, 358 (1967) (rigorous exactions required for enforceability because reliance unbargained-for and promise gratuitous).

101. *E.g.*, Haase v. Cardoza, 165 Cal. App. 2d 35, 331 P.2d 419 (1958); Dewein v. Estate of Dewein, 30 Ill. App. 2d 446, 174 N.E.2d 875 (1961).

102. *E.g.*, Dewein v. Estate of Dewein, 30 Ill. App. 2d 446, 174 N.E.2d 875 (1961).

103. Although *causa mortis* gifts do not require the same formality as testamentary dispositions, such transfers are policed more carefully than are *inter vivos* gifts. *See, e.g.*, Foster v. Reiss, 18 N.J. 41, 112 A.2d 553 (1955). On the other hand, when a gratuitous promise is in writing, courts have often manipulated the delivery requirements of the law of gifts in order to enforce the transfer. *See, e.g.*, Faith Lutheran Retirement Home v. Veis, 156 Mont. 38, 473 P.2d 503 (1970) (written promise is symbolic delivery executing gift); Hawkins v. Union Trust Co., 187 A.D. 472, 175 N.Y.S. 694 (1919) (delivery of letter evidencing gift sufficient to complete gift).

explicit conditions to the promise. It seems implausible, for example, for Guillette to promise to "deliver the rug unless I decide to take a final Caribbean cruise." The only alternative to announcing a narrow promise may be forgoing any announcement at all. If donative promises are not enforced, promisees will adapt to the risk of a regret contingency by self-protective limitations on their beneficial reliance. These adjustments generally will be more precise and less costly in reduced reliance than the solely-quantitative precautionary adjustments available to promisors reluctant to impair the social relationship. Thus, the legal enforcement of donative promises may produce an excessively costly precautionary reduction in the quantity of future promising.

Although theoretically plausible, these two assumptions require empirical verification. The uncertainty surrounding the determination of the optimal legal sanction for nonreciprocal promises is reinforced by the parties' inability to bargain over legal liability. Without the bargain mechanism to reveal the value of a promise to the promisee, judicial efforts to approximate optimal enforcement are necessarily crude. In the next two sections, we evaluate whether these key empirical assumptions explain those circumstances in which courts have deviated from the general policy of nonenforcement for nonreciprocal promises.

2. *Change of Position in Reliance: Enforcement Under Section 90*

Although promissory estoppel is used most frequently in the context of bargained-for promises, the doctrine was first applied to nonreciprocal promises.[104] Conventional analysis has long assumed that promissory estoppel is a readily available means of enforcing relied-upon nonreciprocal promises.[105] Nevertheless, in the above hypothetical, Mortensen's prospects of obtaining enforcement are unlikely to improve under the provisions of section 90 of the *Restatement of Contracts*.[106] Thus, even if Mortensen could indicate specific actions in-

104. *See Promissory Estoppel, supra* note 5, at 346-54.

105. *See, e.g.*, Devecmon v. Shaw, 69 Md. 199, 14 A. 464 (1888); Ricketts v. Scothorn, 57 Neb. 51, 77 N.W. 365 (1898).

106. Section 90 is quoted below in a form that indicates the language of both the 1932 original *Restatement 1st* and its 1965 revision, the *Restatement 2d*. Bracketed words appear in the *Restatement 1st* but have been deleted in the current version. Italicized words are those added by the *Restatement 2d*.

> A promise which the promisor should reasonably expect to induce action or forbearance [of a definite and substantial character] on the part of the promisee *or a third person* and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise. *The remedy granted for breach may be limited as justice requires.*

Most of the decided cases have used the language of the *Restatement 1st* in evaluating

duced in reliance on the promise, such as execution of a contract to sell the rug, the reliance would likely be found insufficiently "foreseeable" and "reasonable" to justify enforcement.

The existence, foreseeability, and reasonableness of claimed actions in reliance are difficult factual issues that the plaintiff must establish for the promise to be enforced under section 90.[107] Furthermore, under section 90 the plaintiff must demonstrate that "justice" requires the enforcement of the promise. Although in bargaining contexts courts have responded to this invitation to the exercise of judicial discretion with complex analysis, in nonreciprocal situations courts have followed clearer rules. Litigation to enforce nonreciprocal promises under section 90 has centered on charitable subscriptions, employee retirement benefits, and donative intrafamilial promises. An examination of recent decisions reveals distinct patterns of enforcement among each type of promise.

Courts generally refuse to enforce intrafamilial promises under section 90, even when the promisee claims he has incurred costs from tangible actions in reliance.[108] Indeed, in the only recent case in which

section 90 claims. But several courts have explicitly adopted the more flexible standard of the *Restatement 2d*. *See* Chapman v. Bomann, 381 A.2d 1123, 1127 (Me. 1978); Warder & Lee Elevator, Inc. v. Britten, 274 N.W.2d 339, 342-43 (Iowa 1979).

107. Under the terms of the *Restatement 1st*, the promisee would be obliged to establish the "definite and substantial character" of his reliance. Although this condition has been deleted in the *Restatement 2d*, a showing that the promise did actually induce reliance is still required. Courts have not been persuaded by the argument that changes in the promisee's consumption behavior create a presumptive case for the existence of detrimental reliance. For example, in Baggs v. Anderson, 528 P.2d 141 (Utah 1974), the court held that the requirement of substantial change in position because of reliance "is not satisfied by the mere fact that [the promisee] indulged in the pleasant and euphoric assumption that he would not have to meet his obligations and that he bought a more expensive car and moved to a more expensive apartment." *Id.* at 144.

In practice, a promisee will probably be required to indicate specific and identifiable instances of foreseeable reliance. *See, e.g.*, Corbit v. J.I. Case Co., 70 Wash. 2d 522, 539, 424 P.2d 290, 301 (1967). Thus, a plaintiff will tend to be disadvantaged if his behavioral adaptations in reliance on the promise were many, small, and diffuse rather than few, large, and identifiable. RESTATEMENT 2D § 90, Comment b. The specific-foreseeability requirement can be justified as a control on the "reliance shopping" behavior that might otherwise be anticipated. *Id.*

Finally, assume that facts reveal that the promisee knew that the gratuitous promise was not legally enforceable. Thus, it could be argued that reliance was unreasonable because the promisee knew that no legal rights were conveyed by the promise. From the perspective of true reliance this argument seems irrelevant. If a promise carries a substantial nominal value, considerable reliance would be expected even if the promisee were aware of the restrictive legal rules governing nonreciprocal promises. Hence, even assuming nonenforceability upon the death of the promisor, the value of the promise would merely be discounted by the probability of nonperformance. Nonetheless, such reliance is likely to be characterized as unreasonable and, therefore, unworthy of section 90 enforcement. *See, e.g.*, Union Tank Car Co. v. Wheat Bros., 15 Utah 2d 101, 387 P.2d 1000 (1964).

108. *E.g.*, Bush v. Bush, 278 Ala. 244, 246, 177 So. 2d 568, 570 (1964); Dewein v. Estate of Dewein, 30 Ill. App. 2d 446, 449-50, 174 N.E.2d 875, 877 (1961).

enforcement has been granted, specifically foreseeable action in reliance was used merely to buttress a promise grounded on formal evidence of an exchange after fifteen years of services rendered by the promisee.[109] In contrast, as provided by the second *Restatement*, courts tend to enforce fully charitable subscriptions regardless of reliance.[110] The frequent argument that the societal interest in eleemosynary activities explains the distinctive legal treatment of charitable promises is not convincing.[111] The social benefit from promise-making would be similarly impaired if enforcement led to restraints on future charitable promises.

Variations in legal process costs, including the risk of false claims, may explain the divergent enforcement patterns in these cases. Furthermore, the differing contexts of nonreciprocal promises suggest important differences in the ability of the parties to adjust the scope and volume of promises. Although charitable promises are formally nonreciprocal, they often are exchanged implicitly for recognition and esteem.[112] Hence, charitable promises are to some extent susceptible

109. *In re* Estate of Bucci, 488 P.2d 216 (Colo. App. 1971). In *Bucci*, after fifteen years of living with and being cared for by the plaintiff, the plaintiff's grandfather promised to give the plaintiff $17,000 to allow plaintiff to purchase a house, when the grandfather sold a certain tract of land or within three years, whichever came first. In reliance upon the promise, the plaintiff withdrew $2,000 of her savings and secured an option on the house. The grandfather died within three years without selling his land. The court held the promise enforceable on two grounds. First, "natural love and affection" constituted sufficient consideration to support the promise based on the 15 years of care and prior services performed. *Id.* at 218-19; *see* pp. 1310-12 *infra*. Second, the administratix of the estate was estopped from denying liability because of the promisee's detrimental reliance on the promise. The court concluded that the plaintiff would not have entered into the option contract without the assurance of completion provided by the promise. 488 P.2d at 219.

110. RESTATEMENT 2D § 90(2) ("A charitable subscription or a marriage settlement is binding under Subsection (1) without proof that the promise induced action or forbearance.")

Salsbury v. Northwestern Bell Tel. Co., 221 N.W.2d 609 (Iowa 1974), is illustrative of the cases that have supported a conclusive presumption of reliance. In *Salsbury*, the defendant telephone company promised to donate $15,000 to a newly formed college. The college failed and the defendant did not pay its pledge. The court held the promise enforceable without proof of detrimental reliance, on the basis of public policy. Requiring evidence of reliance, the court reasoned, may result in the enforcement of fewer charitable promises. *Id.* at 612-13; *cf.* Hirsch v. Hirsch, 32 Ohio App. 2d 200, 289 N.E.2d 386 (1972) (consideration for pledge to eleemosynary institution is accomplishment of purposes for which institution is organized).

Not all courts, however, have adopted the conclusive presumption of reliance. *See, e.g.*, Mount Sinai Hosp., Inc. v. Jordan, 290 So. 2d 484 (Fla. 1974). In *Mount Sinai*, the court refused to enforce the decedent's charitable pledge because the hospital did not "affirmatively show actual reliance of a substantial character." *Id.* at 487.

111. *See, e.g.*, Danby v. Osteopathic Hosp. Ass'n, 34 Del. Ch. 427, 434-35, 104 A.2d 903, 907 (1954); RESTATEMENT 2D § 90, Comment f.

112. The exchange model of charitable donations is not wholly explanatory. When the donation is purely altruistic, as in a gratuitous promise to make a charitable gift, the context may seem directly analogous to the intrafamilial donation. Enforcing such prom-

to bargaining.[113] Intrafamilial donations, on the other hand, are peculiarly resistant to interactive adjustment and epitomize the nonreciprocity of donative promises. When the nature and amount of promising can be adjusted, the choice of liability rule has less impact. As the importance of specifying the optimal enforcement choice is reduced, the value of a certain, clear rule increases.

The choice between the equally clear rules of full enforcement and nonenforcement, however, must rest upon other factors. First, self-sanctions are probably less effective in the charitable than in the intrafamilial setting, because extra-legal sanctions are often limited to the goodwill value of the promisor's word.[114] Second, in the extrafamilial context, promisors are not as disabled by social considerations from making qualitative precautionary adjustments. Thus, in general, enforcement may induce cost-effective precautionary adjustments that increase the net beneficial reliance on charitable promises. Excessively costly self-protection by promisees may be reduced both because qualitative precautions improve the information concerning future regret contingencies and because legally imposed reassurance improves the promise's overall reliability.

Other types of nonreciprocal promises are more difficult to categorize. For example, promises relating to employee retirement benefits occur in a wide variety of promissory settings.[115] For purely gratuitous promises, enforcement efforts on grounds of either promissory estoppel or unjust enrichment have been largely unsuccessful.[116] However, when inferences of reciprocity can be drawn, pension promises have been enforced even though they are not strictly bargained-for.[117]

ises is partially explicable in process terms. The costs of identifying a narrow category of unenforceable promises would substantially increase process costs. A clear and certain rule is advantageous when the judgment whether to perform the promise is frequently made by risk-averse executors and administrators. But, more important, the enforcement choice may also be consistent with the judgment that self-sanctions are significantly reduced in these essentially arms-length transactions.

113. There are a number of mechanisms by which a promise can be solicited from a reluctant charitable donor by adjusting the cost of the subscription. For example, the common practice of commemorating the charitable donor by publicizing his name is one of the key strategies of charitable solicitation. *See, e.g.*, Allegheny College v. National Chautauqua County Bank, 246 N.Y. 369, 375, 159 N.E. 173, 175 (1927) (promisor imposed condition that "gift" be known as "Mary Yates Johnston Memorial Fund").

114. Of course, when a recurring pattern of similar promises exists, the loss of goodwill from nonperformance may be as substantial as other disincentives to breach. An interesting question for further empirical inquiry is whether the magnitude of reputational losses provides a reliable basis for distinguishing variations in the enforcement of promises made in commercial environments.

115. *See Unjust Enrichment, supra* note 5, at 1172-74; *Promissory Estoppel, supra* note 5, at 371.

116. *See, e.g.*, Pitts v. McGraw-Edison Co., 329 F.2d 412, 415-16 (6th Cir. 1964).

117. *E.g.*, Hurd v. Hutnik, 419 F. Supp. 630, 644-45 (D.N.J. 1976); Wickstrom v. Vern E. Alden Co., 99 Ill. App. 2d 254, 261-64, 240 N.E.2d 401, 405-07 (1968).

The nonenforcement and full-enforcement options can be compared usefully with the intermediate scheme proposed by section 90(1) of the second *Restatement*.[118] This reformulation of section 90 eliminates the threshold requirement that action in reliance be definite and substantial and instead limits the degree of enforcement "as justice requires." The optimal damage formula proposed in Part I may explain the nature and role of this limited sanction. As we showed earlier, if the ex ante probability of a promisor performing a promise were high, the prospective beneficial reliance from the promise could exceed prospective detrimental reliance, in which case the overall ex ante prospects would represent a net social benefit. Section 90(1) can thus be read to authorize award of optimal damages based upon this calculation of the promisee's prospective net reliance. This may necessitate damages in amounts less than both full performance and full detrimental reliance.

The justification for abandoning the clearer alternatives of nonenforcement and full enforcement is the error cost of using remedies that do not accurately shape optimal promise-making. The advantage of an optimal net reliance rule is lost, however, if the rule cannot be applied accurately without substantial process costs. The problem in implementing a section 90(1) enforcement rule for nonreciprocal promises lies in the difficulty in determining true reliance on the basis of observable facts. Indeed, the intermediate sanction of reimbursement is as much an approximation of an optimal reliance rule as are the more extreme alternatives. Although relying upon crude liability options may be unsatisfying, incurring the costs necessary to apply more complex rules of recovery and to resolve more factual issues would not necessarily improve the outcomes.

The inclination of courts to ground legal rules in fact-specific contexts illustrates the risks of stipulating one rule for all actions for reliance-based recovery. Section 90 was drafted to address a variety of recurring circumstances in which promises outside the perimeters of traditional bargain theory have been enforced. Although within these specific factual contexts the effects of the enforcement choice could be more carefully observed, as a rule of general application, section 90 demands a degree of precision beyond current empirical understanding. Furthermore, a broad general rule blurs distinctions between bargaining and nonreciprocal environments that may legitimately influence judicial decisions.[119]

118. *See* note 106 *supra*.

119. Arguably, distributional goals explain the judicial discretion invited by the concern for the requirements of justice found in section 90. These goals are, perhaps, more effectively implemented by general statements of principle than by adherence to specific

3. *Moral Obligation: Promise for Benefit Received*

Conferral of benefits on the promisor by the promisee prior to a nonreciprocal promise may affect the decision whether to enforce the subsequent promise. Under the common law material benefit rule, a promise may be enforced if the benefits were conferred after either an express or an implied request of the promisor.[120] When the services were requested, the subsequent promise functions as a mechanism for valuing the implied preexisting bargain.[121] Alternatively, when unsolicited benefits create no quasi-contractual obligation, subsequent promises are ordinarily not enforced.[122] More recently, the material benefit rule was reformulated to reflect the broader instinct for enforcement suggested by case law development. Thus, section 89A of the second *Restatement* provides that a subsequent promise recognizing a prior benefit is enforceable unless "the promisee conferred the benefit as a gift or for other reasons the promisor has not been unjustly enriched."[123]

Discussion of the enforceability of the subsequent promise implies that the original conferral of benefits was not sufficient to support restitution for unjust enrichment. The subsequent promise may, however, fill the interstices between contract and quasi-contract by minimizing the prospect of reward for forcible imposition of "benefits." By removing these objections to a quasi-contractual liability, the subsequent promise justifies recovery of the conferred benefits.[124] But consider the effect of such an enforcement rule on future promising. When a promisor is uncertain about future performance, enforcement will deter socially beneficial promises, thus undermining the policy of

rules designed to regulate future conduct. But neither has a distributional principle that clarifies the enforcement choice under section 90 been identified nor have courts engaged in the kind of factual inquiry necessary to support principled redistributive outcomes. *See* pp. 1320-21 *infra*.

120. *See* 1 S. WILLISTON, *supra* note 76, §§ 144-147. The material-benefit rule requires a finding that it is reasonable to suppose that the promisee expected to be compensated in some way for the conferred benefits, thereby creating a "moral obligation." Manwill v. Oyler, 11 Utah 2d 433, 436, 361 P.2d 177, 178-79 (1961). As Henderson has suggested, liability imposed under this formulation is haphazard and imprecise. *See Unjust Enrichment, supra* note 5, at 1120-26.

121. 1 S. WILLISTON, *supra* note 76, § 146; *see* Jacobs v. Brock, 66 Wash. 2d 878, 883-86, 406 P.2d 17, 20-22 (1965).

122. *See* Perreault v. Hall, 94 N.H. 191, 193-94, 49 A.2d 812, 813-14 (1946); Pershall v. Elliott, 249 N.Y. 183, 187-88, 163 N.E. 554, 556 (1928).

123. RESTATEMENT 2D § 89A. As the Reporter conceded, this section "fairly bristles with unspecific concepts." Braucher, *Freedom of Contract and the Second Restatement*, 78 YALE L.J. 598, 605 (1969); *see Unjust Enrichment, supra* note 5 (charting case-law development underlying § 89A formulation).

124. *See* RESTATEMENT 2D § 89A, Comment b; *Unjust Enrichment, supra* note 5, at 1165-76.

restoring a benefit unjustly retained.[125] A broader justification for enforcement can be identified. The emphasis on isolated cases involving the provision of emergency[126] or mistaken[127] services has blurred the true significance of the liability principle incorporated in section 89A. The concept of unjust enrichment can be examined most usefully as a symbol for the detrimental reliance resulting from an abortive exchange relationship.[128]

How do past events illuminate the detrimental reliance resulting from the broken promise? The application of section 89A sharpens the distinction between reciprocal and nonreciprocal settings. A subsequent promise is typically enforced when it recognizes a benefit conferred in the context of an exchange.[129] Alternatively, enforcement is denied if the benefits were donated or provided to satisfy existing contractual obligations.[130] Examination of the prior events that induced the promise may rebut the assumption of benevolence and instead suggest that the promise was made in a reciprocal context.

If the promise can be located in a bargaining context, the detrimental reliance on the promise can be approximately measured by the price paid in conferred benefits. Indeed, partial performance of this newly discovered bargain provides the strongest basis for the claim of unjust enrichment if the return promise is found enforceable.[131] Identification of the promise within an exchange also reduces the risk of false claims and process errors resulting from the absence of formality.[132] Furthermore, the assumption of reciprocity implies that the promisor can adjust to legal liability by attaching more explicit conditions to the promise. In general, when such qualitative precautionary adjustments

125. *See* p. 1275 *supra*. In the case of the certain promisor, for whom the probability of performance is either zero or one, use of the subsequent promise as a device for clarifying a prior unjust enrichment will have no deterrent effects on future promising. The bad-faith promise can be enforced fully under any circumstances. The more interesting question concerns the promisor who is certain that future performance will be forthcoming. When nonenforcement of such promises is justified on process grounds, the prior benefits may provide formal support for an otherwise gratuitous undertaking.

126. *E.g.*, Webb v. McGowin, 232 Ala. 374, 168 So. 199 (1936); Boothe v. Fitzpatrick, 36 Vt. 681 (1864); *see* RESTATEMENT 2D § 89A, Comment d.

127. *See* Drake v. Bell, 26 Misc. 237, 55 N.Y.S. 945, *aff'd on other grounds*, 46 A.D. 275, 61 N.Y.S. 657 (1899); RESTATEMENT 2D § 89A, Comment c.

128. *See Unjust Enrichment*, *supra* note 5, at 1158.

129. *See, e.g.*, Holland v. Martinson, 119 Kan. 43, 237 P. 902 (1925); Reece v. Reece, 239 Md. 649, 212 A.2d 468 (1965); Jacobs v. Brock, 66 Wash. 2d 878, 406 P.2d 17 (1965).

130. *See, e.g.*, Collord v. Cooley, 92 Idaho 789, 792, 451 P.2d 535, 538 (1969); Youngberg v. Holstrom, 252 Iowa 815, 819-21, 108 N.W.2d 498, 500-01 (1961); Jensen v. Anderson, 24 Utah 2d 191, 468 P.2d 366 (1970); RESTATEMENT 2D § 89A, Comments e & f.

131. *See* Fuller, *supra* note 20, at 812; Fuller & Perdue, *supra* note 5, at 53-57; *Unjust Enrichment*, *supra* note 5, at 1136-37, 1147-49, 1157-59, 1178-83.

132. *See Unjust Enrichment*, *supra* note 5, at 1159-65.

are feasible, the promisor has more accurate knowledge of future contingencies and, hence, can avoid risk more cheaply than can the promisee.[133]

The prior benefits principle of section 89A reflects an expanding enforcement of promises outside the consideration model even more clearly than does the promissory estoppel concept of section 90. Classic bargain theory delimited the borders of enforcement too narrowly to incorporate the full regulatory benefits of the exchange context. Courts are expanding liability under a variety of guises in order to reach the perimeters of exchange. Only when the effects of enforcement cannot be internalized by individual bargaining is the policy of nonenforcement clearly retained.

D. *Unilateral-Bargain Promises: The Expansion of Bargain Theory*

Reciprocal-bargain promises and nonreciprocal promises represent the polar extremes of promissory settings. The recent expansion in promissory liability has been concentrated in the intermediate contexts, in which bargaining and exchange remain a realistic, if not realized, prospect. Indeed, the main source of tension between traditional bargain theory and the optimal enforcement of promises lies in the incongruence between the narrowly drawn consideration model and

133. For promises judged enforceable under the prior benefits principle, section 89A invites a limitation of remedy when the face value of the promise is disproportionate to the benefit conferred. "A promise is not binding under Subsection (1) [of § 89A] . . . (b) to the extent that its value is disproportionate to the benefit." RESTATEMENT 2D § 89A. Framing the question of remedy in terms of disproportion may seem puzzling. A reimbursement recovery equal to the value of the conferred benefits is not necessarily an accurate approximation of the true reliance induced by the promise. The disproportion principle is more plausibly examined as a means of resolving the peculiar problem of mixed motivations. If limiting recovery to the reasonable value of the promisee's services successfully separates the hybrid elements of gift and bargain, the harmful consequences of overenforcement of nonreciprocal promises are reduced. Limiting enforcement to that portion of the promise that is subject to an exchange can be explained, therefore, as a further illustration of the distinction between nonreciprocal and reciprocal contexts.

Courts' traditional reluctance to assess the adequacy of consideration can be reconciled with the disproportion principle of section 89A by locating the promissory context on a continuum between the poles of benevolence and bargain. As promises approach the pure bargain, the uncertainty costs of judicial review of relative values increase. Even when both parties concede that a transaction is part bargain and part gift, common law consideration rules support full enforcement. *See, e.g.*, RESTATEMENT 2D § 81, Comment c; *id.* § 75, Comment c ("Even where both parties know that a transaction is in part a bargain and in part a gift, the element of bargain may nevertheless furnish consideration for the entire transaction.") The lesson of the expanding liability reflected in section 89A is that the exchange environment extends beyond the classic bargain model. In the prior benefits transaction, the elements of bargain are somewhat attenuated, as are the costs of judicial assessment of disproportion. Limiting recovery to the value of services exchanged is efficient when the resulting increase in uncertainty is outweighed by a reduction in the damaging effects of excessive enforcement on nonreciprocal transactions.

this broader exchange context. Courts have responded to this tension by using alternative theories of liability to enforce a much wider range of bargain promises, such as subsequent promises to renew an antecedent legal obligation barred by bankruptcy or the statute of limitations.[134] In addition, reliance-based theories have often been employed when rules of consideration deny enforcement.[135] We designate representations lacking any legally enforceable consideration as "unilateral-bargain" promises. Much of the uncertainty concerning the enforcement of such promises arises because the doctrinal support for enforcement has emerged from the gratuitous context. However, although the boundaries have been redefined, the distinction between the enforcement of nonreciprocal and reciprocal promises remains largely undisturbed.

Enforcement rules for unilateral-bargain promises may never be as precisely defined as the provisions regulating other promissory categories. Nevertheless, under recurring circumstances, patterns of enforcement emerge from which individual variables can be isolated. The examination of cases in which courts have recently expanded liability is necessary to isolate the key elements in the enforcement decision.

1. *Reduced Transactions Costs*

We have suggested that the classic consideration model can be explained by analysis of the transactions costs of exchange. When outcomes are uncertain, the risk of legal liability may be perceived as a greater threat than the risk of uncompensated reliance from a broken promise, because each actor can exercise greater control over his own detrimental reliance than over the potential losses of his promisee. Thus, all other things equal, forgoing an uncertain gain by reducing

134. *See* A. CORBIN, *supra* note 5, § 222 (observing this practice); G. GILMORE, *supra* note 4, at 55-65 (describing the historical use of alternative theories of obligation); 1 S. WILLISTON, *supra* note 76, § 158 (observing practice). The rhetoric of the cases typically explains enforcement of such promises on the basis of the moral obligation created by the original bargain. *See, e.g.*, Stanek v. White, 172 Minn. 390, 391, 215 N.W. 784, 784 (1927). The same pattern—enforcing subsequent promises arising out of a completed exchange—is found in those decisions renewing contractual obligations voidable by fraud or infancy. *See* 1 A. CORBIN, *supra* note 5, § 228 (fraud); S. WILLISTON, *supra* note 76, § 151 (infancy).

135. In addition to the obvious use of promissory estoppel to enforce promises inducing post-promise reliance, many of the enrichment cases enforcing promises following the conferral of benefits are usefully examined in terms of a presumption that such promises are most likely to induce post-promise reliance. *See Unjust Enrichment, supra* note 5, at 1181. Although the cases examined in this section are largely limited to promissory estoppel claims, many of the prior-benefit cases can be categorized on similar bases. Only a few courts have discussed the relationship of the reliance element. *E.g.*, General Bronze Corp. v. United States, 338 F.2d 117, 122-25 (Ct. Cl. 1964).

reliance will be preferred over suffering an equally uncertain loss of similar magnitude. This assumption helps explain both the offer and acceptance and discharge rules of consideration and the remedial limitations on liability.

Examining the disposition of promissory estoppel claims in bargain settings reveals patterns of enforcement that parallel the design of the consideration model. Promises made in either preliminary or termination negotiations are generally unenforceable under section 90.[136] Alternatively, reliance theories have been used successfully to enforce promises made in the context of an ongoing exchange transaction. Indeed, promises that modify an existing agreement have long been enforced, despite the common law preexisting duty rule, if there is evidence of reasonable reliance.[137] Although the decisions in such "waiver by estoppel" cases often focus doctrinally on equitable estoppel, the impact reliance has on the imposition of liability is clear.[138]

Similarly, courts have enforced a variety of collateral promises reinforcing completed but defective exchanges.[139] For example, in *Wheeler v. White*,[140] after an agreement had been signed, the promisor represented that funds for a projected shopping center would soon be available and convinced the promisee to demolish existing buildings. Although the original agreement was judged indefinite, the subsequent promises of performance were found enforceable under section 90.[141]

By enforcing such promises, the courts have not ventured far beyond the assumptions underlying the consideration model. The requirements for recovery under section 90 have been strictly construed whenever the outcome of bargaining is uncertain, but have been liberally interpreted when the essence of the bargain has been established. When agreements are unclear, risk-averse bargainers prefer to bear the risks

136. *See, e.g.*, Coley v. Lang, 339 So. 2d 70, 74 (Ala. App. 1976) (preliminary negotiations); Malaker Corp. Stockholders Protective Comm. v. First Jersey Nat'l Bank, 163 N.J. Super. 463, 473-74, 395 A.2d 222, 227 (App. Div. 1978) (same); McMath v. Ford Motor Co., 77 Mich. App. 721, 725-27, 259 N.W.2d 140, 142-43 (1977) (termination negotiations).

137. But for the preexisting-duty rule, which requires modifying promises to have a separate consideration, such promises would be fully enforceable at common law without the need to establish reliance. *See* note 72 *supra* (discussing evolution of rules).

138. *See, e.g.*, Albanese v. N.V. Nederl. Amerik Stoomv. Maats., 279 F. Supp. 635 (S.D.N.Y. 1967) (basing defendant's liability on plaintiff's reliance); Shell Oil Co. v. Kelinson, 158 N.W.2d 724, 729 (Iowa 1968) (same); *cf. Unjust Enrichment, supra* note 5, at 1173-74 (reliance theory grounded in notion of promissory estoppel has been "marginally successful").

139. *See, e.g.*, Travelers Indem. Co. v. Holman, 330 F.2d 142, 151 (5th Cir. 1964) (enforcing misleading promise that insurance policy covered specified damages); Alaska Airlines, Inc. v. Stephenson, 217 F.2d 295, 298 (9th Cir. 1954) (enforcing promise that business expenses ancillary to employment contract would be covered).

140. 398 S.W.2d 93 (Tex. 1965).

141. *Id.* at 95-97.

of regret contingencies as promisees, and the nonenforcement rule is optimally retained. When the bargain is clear but fails technically, however, parties may prefer pursuing gains to avoiding losses. Enforcement under section 90 allocates the risk of regret to promisors and thereby shifts resources to more efficient precautionary conduct.

These reflections of the assumptions underlying the consideration model also appear in the remedies provided under the doctrine of promissory estoppel. Generally, full-enforcement compensation has been awarded whenever such damages would have been available under the certainty and foreseeability limitations of bargain theory.[142] Reimbursement has been awarded when the harmful consequences of nonperformance were not reasonably foreseeable and the claim for greater damages was too speculative.[143] Although the rhetoric of some of these decisions suggests that reimbursement damages are the preferred recovery under promissory estoppel, the outcomes imply that courts are animated by the same concerns that have produced the design of the consideration model.

2. *Accuracy: Promises Made in Competitive Markets*

Traditional bargain theory does not distinguish between exchange transactions in established markets and exchanges of unique promises.[144] Because detrimental reliance and full expectancy are equivalent in competitive markets, however, when a promise made in a competitive market induces reasonable reliance, full enforcement is a more accurate approximation of the true detrimental reliance caused by the promise regardless of whether the promise was bargained-for. Enforcement of competitive promises that reasonably induce reliance is efficient, however, only if marginal gains in accuracy exceed marginal increases in the process costs of enforcement. Thus, courts can be expected to expand liability when competitive markets are readily identifiable.

The expanding use of promissory estoppel to impose liability outside traditional boundaries is substantially explained by such net gains in the accuracy of the measurement of damages.[145] For example,

142. *See, e.g.*, Drennan v. Star Paving Co., 51 Cal. 2d 409, 414-17, 333 P.2d 757, 760-61 (1958) (subcontractors' bid); Southwest Water Servs., Inc. v. Cope, 531 S.W.2d 873 (Tex. Civ. App. 1975) (fixed water rates).

143. *See, e.g.*, Associated Tabulating Servs., Inc. v. Olympic Life Ins. Co., 414 F.2d 1306, 1311 (5th Cir. 1969) (new business profits); Goodman v. Dicker, 169 F.2d 684, 685 (D.C. Cir. 1948) (same).

144. *See* note 66 *supra* (discussing unique-bargain promises).

145. Similar inferences can be drawn from an examination of prior-benefits cases. *See, e.g.*, Husted v. Fuller, 361 F.2d 187 (7th Cir. 1966) (subsequent promise to refund forfeited

in a number of cases involving bids by subcontractors, courts have imposed liability for reasonable reliance on a firm offer even though the promise was not supported by bargained-for consideration.[146] The Uniform Commercial Code enforces similarly firm written offers by merchants,[147] and the second *Restatement* generalizes the rule to include all offers reasonably inducing reliance before acceptance, when "necessary to avoid injustice."[148] This discretionary provision can be interpreted as mandating enforcement only when enforcement is an accurate proxy for detrimental reliance. In each of these circumstances, the existence of a competitive market is the variable that best explains the enforceability of firm offers.

It is useful to examine the market for substitute promises in other reliance cases. Courts have generally circumvented the Statute of Frauds only in the presence of clear and substantial evidence of an "unconscionable injury" induced by detrimental reliance on an oral promise.[149]

earnest money enforced). The plaintiff in *Husted* was a businessman, and the promise could reasonably be inferred as having induced a forbearance on his part from alternative financing opportunities.

Because the theory of enforcement for prior-benefits promises focuses attention on prepromise facts, however, the cases rarely explore postpromise circumstances with sufficient detail to permit accurate judgment about the congruence between postpromise reliance and enforcement.

146. *See, e.g.*, Drennan v. Star Paving Co., 51 Cal. 2d 409, 333 P.2d 757 (1958). Since *Drennan*, promissory estoppel has been consistently employed to deny subcontractors the power to withdraw their bids after general contractors have relied on them by incorporating the bids into their prime bid for the construction job. *See, e.g.*, S.M. Wilson & Co. v. Prepakt Concrete Co., 23 Ill. App. 3d 137, 318 N.E.2d 722 (1974); Constructors Supply Co. v. Bostrom Sheet Metal Works, Inc., 291 Minn. 113, 190 N.W.2d 71 (1971). Traditionally, firm offers were not enforced unless they were supported by bargained-for consideration. *See, e.g.*, James Baird Co. v. Gimbel Bros., Inc., 64 F.2d 344 (2d Cir. 1933); Board of Control v. Burgess, 45 Mich. App. 183, 206 N.W.2d 256 (1973).

147. *See* U.C.C. § 2-205 (written offers by merchants, if announced as irrevocable, are binding without consideration for up to three months). The limited scope of § 2-205 increases the likelihood that the firm promises captured by its provisions will have been made in a competitive market.

148. *See* RESTATEMENT 2D § 89B(2) ("offer which the offeror should reasonably expect to induce action or forbearance of a substantial character on the part of the offeree before acceptance and which does induce such action or forbearance is binding as an option contract to the extent necessary to avoid injustice").

149. *See* Monarco v. Lo Greco, 35 Cal. 2d 621, 220 P.2d 737 (1950). *But see* FMC Fin. Corp. v. Reed, 592 F.2d 238, 243 (5th Cir. 1979) (following Mississippi law; holding that Statute of Frauds cannot be circumvented by doctrine of collateral estoppel).

The most familiar factual pattern of these estoppel cases involves oral promises of employment followed by acts of reliance by the promisee. But mere change in job or residence is generally held insufficient unless the forgone alternatives resulted in "unconscionable injury." Such injury has been found in cases in which the promisee relinquished pension benefits and sold a custom home, *see* Lucas v. Whittaker Corp., 470 F.2d 326 (10th Cir. 1972), or resigned from lifetime employment, *see* Ruinello v. Murray, 36 Cal. 2d 687, 227 P.2d 251 (1951). These examples suggest that the notion of unconscionable injury in these cases is usefully examined as a symbol of forgone substitute

In the highly competitive commodities markets, however, oral promises by farmers to deliver their crops to grain elevators have been readily enforced.[150] Courts have also generally been reluctant to allow promissory estoppel to undermine the parol evidence rule.[151] However, in *Ehret Co. v. Eaton, Yale & Towne, Inc.*,[152] the promisee, a sales representative for a manufacturer, obtained enforcement of a promise of "extremely fair treatment" in sharing future commissions despite a fully integrated written agreement to the contrary.[153] The existence of a developed market for the promisee's services helps to explain the court's decision in *Ehret* to enforce the promise.[154]

Competition for the promisee's services explains the enforceability under section 90 of certain preliminary negotiations and indefinite agreements. Thus, detrimental reliance has been found an adequate basis for enforcing promises to lease business facilities,[155] to provide a construction job,[156] and to award a construction contract.[157] These cases are closely linked to decisions enforcing promises of insurance[158]

promises roughly equal in value to the oral one in question. In turn, these cases have provided the support for codifying the reliance principle as a means of enforcing oral promises within the Statute of Frauds. *See* RESTATEMENT 2D § 217A. Section 217A is complementary to section 90 and varies in its form only by identifying five specific "considerations" for determining whether justice can be avoided only by enforcement.

150. In the grain elevator cases, the operators typically use the farmers' oral promises in reselling their produce on the futures market. *See, e.g.*, Jamestown Terminal Elevator, Inc. v. Hieb, 246 N.W.2d 736 (N.D. 1976). *But see* Sacred Heart Farmers Coop. Elevator v. Johnson, 305 Minn. 324, 232 N.W.2d 921 (1975) (holding oral promisor not bound).

151. A number of courts have rejected the proposition that action in reliance might properly permit courts to avoid the application of the parol evidence rule. *See, e.g.*, Mack v. Jorgensen Co., 467 F.2d 1177 (7th Cir. 1972); Clark Oil & Ref. Corp. v. Leistikow, 69 Wis. 2d 226, 230 N.W.2d 736 (1975).

152. 523 F.2d 280 (7th Cir. 1975).

153. *Id.* at 282.

154. The plaintiff, Ehret Company, had an exclusive sales contract with the defendant and had invested up to 10 years of development work to adapt the defendant's products to its customers' needs. *See id.* at 281-83.

155. Mooney v. Craddock, 530 P.2d 1302 (Colo. App. 1974).

156. Hunter v. Hayes, 533 P.2d 952 (Colo. App. 1975).

157. Swinerton & Walberg Co. v. City of Inglewood-Los Angeles County Civic Center Auth., 40 Cal. App. 3d 98, 114 Cal. Rptr. 834 (1974).

158. Promises to procure insurance are the most common circumstances in which the amount of reliance greatly exceeds the face value of the promise. *See, e.g.*, Spiegel v. Metropolitan Life Ins. Co., 6 N.Y.2d 91, 160 N.E.2d 40, 188 N.Y.S.2d 486 (1959) (promise to pay life insurance premium of $39.75 causing reliance equal to $10,650, proceeds of policy). Consequently, some courts have been reluctant to use section 90 to enforce the full amount of the resulting loss. *See, e.g.*, Dillown v. Phalen, 106 Ohio App. 106, 153 N.E.2d 687 (1957). Nonetheless, a number of courts have explicitly used promissory estoppel to enforce a broken promise to insure. *See, e.g.*, Graddon v. Knight, 138 Cal. App. 2d 577, 292 P.2d 632 (1956); East Providence Credit Union v. Geremia, 103 R.I. 597, 239 A.2d 725 (1968). Furthermore, liability is often imposed on the additional basis of negligent failure to perform services gratuitously undertaken. *See, e.g.*, Colonial Sav. Ass'n v. Taylor, 544 S.W.2d 116 (Tex. 1976); RESTATEMENT (2D) OF TORTS § 323 (1965). The *Restatement of*

and gratuitous bailments,[159] for which a similar promise would have been available to the promisee.[160] In this case, the opportunity cost of acceptance of a promisor's representations that designated property would be insured or safeguarded is equal to the entire loss if the risk materializes after the promise is broken.[161]

At the other extreme are cases in which the exchange is negotiated between two unique bargainers. These disputes often materialize as breakdowns in preliminary negotiations,[162] indefinite agreements,[163] or franchise terminations.[164] Notwithstanding several celebrated decisions,[165] promissory estoppel has rarely been applied to enforce incomplete agreements reached by unique bargainers. Under this circumstance, full enforcement is not an accurate proxy for true reliance. Thus, when the exchange is isolated from a competitive market, enforcement is often denied in spite of the existence of credible evidence of detrimental reliance by the promisee.[166] Isolated decisions to enforce

Torts retains the distinction between nonfeasance and misfeasance and expresses no opinion as to whether the nonfeasance of a gratuitous promise is sufficient to establish liability under section 323. *Compare* Siegel v. Spear & Co., 234 N.Y. 479, 138 N.E. 414 (1923) (nonfeasance sufficient to establish liability) *with* Comfort v. McCorkel, 149 Misc. 826, 268 N.Y.S. 192 (Sup. Ct. 1933) (defendant guilty of nonfeasance not liable to plaintiffs).

159. *See, e.g.*, Abresch v. Northwestern Bell Tel. Co., 246 Minn. 408, 75 N.W.2d 206 (1956) (promise); Siegel v. Spear & Co., 234 N.Y. 479, 138 N.E. 414 (1923) (bailment); RESTATEMENT (2D) OF AGENCY § 378 (1958) (codifying enforceability of gratuitous bailments). The formulation of the reliance principle under section 378 is carefully tied to the availability of substitute promises on the market. This approach is consistent with the argument that enforcement is properly related to the existence of a competitive market for the promise in question.

160. *See, e.g.*, Lincolnland Properties, Inc. v. Butterworth Apartments, Inc., 65 Ill. App. 3d 907, 382 N.E.2d 1250 (1978) (promise to release mortgage enforced when competitive financing available); Homestead Supplies, Inc. v. Executive Life Ins. Co., 81 Cal. App. 3d 978, 147 Cal. Rptr. 22 (1978) (promise to offer insurance at quoted rates enforceable when competitive alternatives forgone).

161. *See* Industro Motive Corp. v. Morris Agency, Inc., 76 Mich. App. 390, 256 N.W.2d 607 (1977).

162. *See, e.g.*, Slater v. George B. Clarke & Sons, Inc., 186 F. Supp. 814 (D. Del. 1960); Hoffman v. Red Owl Stores, Inc., 26 Wis. 2d 683, 133 N.W.2d 267 (1965).

163. *See, e.g.*, Dovenmuehle, Inc. v. K-Way Assocs., 388 F.2d 940 (7th Cir. 1968); United Elec. Corp. v. All-Serv. Elec., Inc., 256 N.W.2d 92 (Minn. 1977); Silberman v. Roethe, 64 Wis. 2d 131, 218 N.W.2d 723 (1974).

164. *See, e.g.*, Chrysler Corp. v. Quimby, 144 A.2d 123 (Del. 1958). Other terminations subsequent to promises have been litigated. *See, e.g.*, McMath v. Ford Motor Co., 77 Mich. App. 721, 259 N.W.2d 140 (1977) (employment discharge); Aubrey v. Workman, 384 S.W.2d 389 (Tex. Civ. App. 1964) (release from secondary lien).

165. *See, e.g.*, Goodman v. Dicker, 169 F.2d 684 (1948); Wheeler v. White, 398 S.W.2d 93 (Tex. 1965); Hoffman v. Red Owl Stores, Inc., 26 Wis. 2d 683, 133 N.W.2d 267 (1965).

166. *See, e.g.*, Slater v. George B. Clarke & Sons, Inc., 186 F. Supp. 814 (D. Del. 1960); Baggs v. Anderson, 528 P.2d 141 (Utah 1974); Clark Oil & Ref. Corp. v. Leistikow, 69 Wis. 2d 226, 230 N.W.2d 736 (1975).

The unique promise made in a noncompetitive environment presents the best example of a reciprocal promise for which the original form of an optimal damages formula would be appropriate. Breach of such a promise would ideally entail damages in the

such promises can be explained only by analyzing factors other than accuracy and transactional efficiency.

3. *The Probability of Nonperformance: Bad Faith*

When the behavior of the promisor at the time of promising clearly indicates that the probability of performance is zero, tort doctrines of fraud are adequate to protect the promisee fully.[167] However, in several celebrated cases, promissory enforcement seems to derive from more subtle inferences that the promisor did not intend to perform. In *Chrysler Corporation v. Quimby*,[168] the promisee was asked to buy out other interests in an automobile franchise as a condition for award of the franchise upon the death of the current operator. After the promisee acquired sole control, Chrysler terminated the promisee's franchise and awarded the dealership to another individual, as apparently had been contemplated from the outset.[169] Although the final terms of the agreement had not been resolved, the court awarded full performance damages to the plaintiff for detrimental reliance on Chrysler's promise.[170]

Although the deceit in *Quimby* is clear, the evidence of bad-faith conduct in *Hoffman v. Red Owl Stores, Inc.*[171] is less certain. In *Hoffman*, the promisee was awarded reimbursement damages following the breakdown of extensive negotiations for award of a grocery store franchise. During the negotiating period, the promisee performed several acts in clear preparation for receipt of the franchise, including sale of his bakery business and purchase and resale of a small grocery store. Negotiations were subsequently discontinued when the promisor suddenly increased the capital contribution required of the promisee.

difficult-to-measure middle range, between zero and expectation damages. But measurement costs may dictate a choice between the two extreme remedies.

The decision whether to grant zero or full damages may then be influenced by an empirical asymmetry in the costs to the parties of adjusting enforcement levels. Specifically, it may be cheaper for the parties to bargain out of an excessive enforcement scheme than to create additional enforcement mechanisms when inadequate ones existed. Hence, when some tentative initial allocation of legal rights must necessarily be avoided, erring on the side of excess enforcement has cost-minimization advantages over comparable errors on the side of inadequate enforcement. *See* p. 1286 *supra*.

167. *See* W. PROSSER, HANDBOOK OF THE LAW OF TORTS 728-31 (4th ed. 1971). It has long been established that a promise carries an implied representation of present intention to perform. A promise made without a present intention to perform is a sufficient basis for a tort action of fraud. *See, e.g.*, Kauffman v. Bobo & Wood, 99 Cal. App. 2d 322, 221 P.2d 750 (1950); Sabo v. Delman, 3 N.Y.2d 155, 143 N.E.2d 906, 164 N.Y.S.2d 714 (1957).

168. 144 A.2d 123 (Del.), *modified and aff'd*, 144 A.2d 885 (1958).

169. *Id.* at 128.

170. *Id.* at 132-36.

171. 26 Wis. 2d 683, 133 N.W.2d 267 (1965).

The court expressly declined to enforce the promise on grounds of fraud, finding insufficient evidence to infer that the promisor "made any of the promises . . . in bad faith with [a] present intent that they would not be fulfilled."[172] Nonetheless, the sudden change in contract terms suggests that at some point in the negotiations Red Owl determined not to perform the promise. Although the mere failure promptly to withdraw a rash promise may not constitute fraud, it may help explain the court's use of promissory estoppel to enforce indefinite preliminary negotiations.

The historical nexus between promissory estoppel and equitable estoppel may blur the independent significance of bad-faith conduct, especially when the inferences of bad faith are based on post-promise factual representations concerning future performance. In *Goodman v. Dicker*,[173] for example, the promisor followed a promise to award a franchise with the representation that the promisee's application had been accepted. The court, without distinguishing promise from misrepresentation, held that the defendants were estopped by their statements from refusing to grant the franchise. Because doctrines of fraud and deceit are commonly invoked in equitable estoppel cases, their independent significance may not be clear when promissory reliance is at issue.[174] However, the "requirements of justice" language of section 90 offers courts opportunities to broaden the traditional scope of enforcement for bad-faith representation. When none of the enforcement alternatives carries either a presumption of accuracy or an obvious transactional advantage, the court's assessment of performance probabilities may often prove decisive.

4. *Certainty and Distributional Effects*

When considerations of accuracy, transactional efficiency, and bad faith are eliminated, a significant difference remains between the enforcement theories of bargain and reliance. Bargain rules are more certain; reliance rules invite greater flexibility and discretion. Because reliance-based enforcement requires evidence of future facts unknown at the time of bargaining, the availability of such enforcement doctrines increases bargainers' uncertainty as to the risks of legal liability. Un-

172. *Id.* at 695, 133 N.W.2d at 273.

173. 169 F.2d 684 (D.C. Cir. 1948).

174. The equitable roots of promissory estoppel explain, in part, the continuing confusion between equitable estoppel and promissory reliance that is evident in the case law. *See, e.g.*, Schmidt v. McKay, 555 F.2d 30 (2d Cir. 1977); C. & K. Eng'r Contractors v. Amber Steel Co., 23 Cal. 3d 1, 587 P.2d 1136, 151 Cal. Rptr. 323 (1978).

certainty imposes a social loss that reduces the value of exchange. The inefficiency of a discretionary rule of promissory estoppel may be worth incurring if it results in the achievement of socially desirable distributional goals.[175] However, examination of reliance cases does not yield discernible distributional policies.

Evidence of relative ability to sustain losses or of the reasons for breach is required before the losses, or gains, from the breach can be distributed according to any fairness norms. None of the litigated cases reveals careful exploration of the distributional consequences of alternative decisions. Furthermore, in most cases the redistributional effects of varying rules are difficult to predict. Absent a clear commitment to promissory redistribution, the uncertainty induced by broadly conceived discretionary rules is unjustified. Systematization of the expansion of the bargain model calls for developing clearly articulated liability rules paralleling those that have emerged from the rules of consideration. Such rules can be generally sketched from current patterns of enforcement.

Conclusion

Examination of the economic implications of promising reveals a tension between ideal and practical objectives. Because uncertainty cannot be eliminated, it may be tempting to resist systematization of expanding areas of liability.[176] The suggestion that the results in individual cases can safely be predicted by employing a handful of simple economic tools is misguided. Economic concepts are useful, however, in specifying the effects of legal objectives and in observing and isolating systemic patterns of enforcement. The indeterminacy of empirical parameters necessitates the use of assumptions that only crudely approximate the true theoretical objectives. Often the effects of using estimates are unclear, as undetermined factors affect the behavior under examination.[177] Nonetheless, systematic collection and observation of data increases understanding of the regulation of behavior by legal rules.

We have assumed that the economic objective of regulating promises is to maximize the net beneficial reliance derived from promise-making activity. In general, this objective is best achieved by a scheme of

175. For a discussion of the legitimacy of using contract law to achieve distributional ends, see Kronman, *Contract Law and Distributive Justice*, 89 YALE L.J. 472 (1980).

176. *See* G. GILMORE, *supra* note 4, at 102-03.

177. *See* Leff, *Law and*, 87 YALE L.J. 989, 1005-11 (1978).

promissory enforcement that induces adaptive behavior by the party better able to minimize the risk that future contingencies may materialize and cause the promisor to regret the announcement. Optimal adaptation requires a reduction in the prospective reliance on promising whenever this investment produces a greater decrease in expected harms from nonperformance. Both legal and extra-legal sanctions impose these social costs on the promising parties. Optimal legal sanctions are, therefore, a function of both the magnitude of these extra-legal factors and the parties' relative advantage in risk avoidance. The ideal liability choice ranges from zero enforcement to liability equal to the reasonable detrimental reliance caused by breach. However, because promissory reliance is peculiarly impervious to measurement, alternative rules are often applied as proxies for true reliance.

Promissory liability rules can be examined by classifying promises in three categories along principles of reciprocity and bargain. First, reciprocal promises are distinguishable from nonreciprocal promises on the basis of the ability of bargainers to adjust the volume and form of promising by varying the price of the promise. When such adjustments are not possible, promises are not enforced. Nonenforcement of gratuitous promises is justified because in the nonreciprocal setting, self-sanctions against breach are frequently effective, and promisees are often better able than promisors to adapt to the risks of regret. Second, the narrow consideration model defined by common law delineates a subdivision within the category of reciprocating promises. Enforcement is narrowly limited by assumptions that costs of promise-making are best reduced by precautions at the core of bargaining, and by reassurances on the periphery.

However, courts have used alternate theories of liability to expand enforcement appropriately beyond the confines of the consideration model. Promises have been enforced when increased accuracy, transactional efficiency, or bad faith justified the imposition of liability. These alternative bases of liability have been recently generalized into broad grants of judicial discretion. Although discretion permits the pursuit of distributional goals, it increases the uncertainty facing future bargainers. Absent careful articulation of distributional objectives, the social cost of uncertainty requires the development of clear rules for recoveries grounded on reliance.