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WHY THERE IS NO LAW OF RELATIONAL CONTRACTS

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The identification of relational contracts as a critical construct and an important field of study has led to important insights concerning the economics and sociology of contracting. It has not, however, led to a body of relational contract law: that is, we do not have a body of meaningful and justified contract law rules, either in place or proposed, that apply to, and only to, relational contracts. In this Article, I will show why this is so.

I. CLASSICAL CONTRACT LAW

Like most modern contract theories, relational contract theory can only be understood against the backdrop of the school of classical contract law, to which it stands in opposition. I will therefore begin with a brief tour of that school.

A. The Characteristics of Classical Contract Law

Classical contract law was marked by several characteristics. It was axiomatic and deductive. It was objective and standardized. It was static. It was implicitly based on a paradigm of bargains made between strangers transacting on a perfect market. It was based on a rational-actor model of psychology.

1. The Axiomatic and Deductive Nature of Classical Contract Law. Classical contract law was axiomatic in nature. Axiomatic theories of law take as a premise that fundamental doctrinal propositions can be established on the ground that they are self-evident. At least in their strictest versions, such theories allow no room for justifying doctrinal propositions on the basis of social propositions—that is, propositions of morality, policy, and experience. So, for example, Langdell, speaking to the question of whether an acceptance by mail was effective on dispatch, said:

> The acceptance . . . must be communicated to the original offerer, and until such communication the contract is not made. It has been claimed that the purposes of substantial justice, and the interests of contracting parties as understood by themselves, will be best served by holding that the contract is

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> complete the moment the letter of acceptance is mailed; and cases have been put to show that the contrary view would produce not only unjust but absurd results. The true answer to this argument is that it is irrelevant. . . .[1]

As Holmes observed, axiomatic theories may easily be coupled with deductive theories, which take as a premise that at least some doctrinal propositions can be established solely by deduction from other, more fundamental doctrinal propositions. "I sometimes tell students," Holmes said, "that the law schools pursue an inspirational combined with a logical method, that is, the postulates are taken for granted upon authority without inquiry into their worth, and then logic is used as the only tool to develop the results."[2] Classical contract law was based on just such a coupling. It conceived of contract law as a set of fundamental legal principles that were justified on the ground that they were self-evident, and a second set of rules that were justified on the ground that they could be deduced from the fundamental principles.

For example, it was an axiom of classical contract law that in principle only a bargain promise had consideration—that is, was enforceable—although exceptions were recognized for certain kinds of promises that were enforceable on purely historical grounds. The issue then arose whether a firm offer—an unbargained-for promise to hold an offer open—was legally enforceable. The conclusion of classical contract law was, no.[3] This conclusion was justified by deduction alone. The major premise was that only bargains had consideration. The minor premise was that a promise to hold a firm offer open is not bargained for. The conclusion was that a firm offer was not enforceable.

Another axiom of classical contract law was that bargains were formed only by offer and acceptance. The issue then arose whether an offer for a unilateral contract—an offer to be accepted by the performance of an act—was revocable before performance had been completed, even if the offeree had begun to perform. The conclusion of classical contract law was, yes.[4] This conclusion too was justified by deduction alone. The major premise was that an offeror could revoke an offer at any time prior to acceptance unless he had made a bargained-for promise to hold the offer open. The minor premise was that an offer for a unilateral contract was not bargained for and was not accepted until performance of the act had occurred. The conclusion was that an offer for a unilateral contract was revocable before performance had been completed, even after the offeree had begun to perform.

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[1] C.C. LANGDELL, A SUMMARY OF THE LAW OF CONTRACTS 15, 20-21 (2d ed. 1880).

[2] Oliver Wendell Holmes, *Law in Science and Science in Law*, *in* COLLECTED LEGAL PAPERS 210, 238 (1920).

[3] *See, e.g.*, Dickinson v. Dodds, 2 Ch. D. 463 (1876).

[4] *See, e.g.*, Petterson v. Pattberg, 161 N.E. 428 (N.Y. 1928).

Langdell's view that an acceptance can be effective only on receipt was also based on deductive reasoning. By axiom, a bargain can be formed only by offer and acceptance. By axiom, an expression cannot be an acceptance unless it is communicated to the addressee. By deduction, an acceptance can be effective only on receipt.

2. The Objective and Standardized Nature of Classical Contract Law. The principles of contract law can be ranged along various spectra according to the kinds of variables on which the application of any given principle depends. One such spectrum runs from objectivity to subjectivity. A principle of contract law lies at the objective end of this spectrum if its application depends on a directly observable state of the world, and at the subjective end of the spectrum if its application depends on a mental state. For example, application of the plain-meaning rule of interpretation depends on a determination of observable meanings attached to words by established communities. In contrast, application of the rule that if both parties attach the same meaning to an expression, that meaning prevails, depends on a determination of the parties' mental states.

A second spectrum of principles runs from standardization to individualization. A principle of contract law lies at the standardized end of this spectrum if its application depends on an abstract variable that is unrelated to the intentions of the parties or the particular circumstances of the transaction, and it lies at the individualized end of the spectrum if its application depends on situation-specific variables that relate to intentions and other individual circumstances. For example, application of the doctrine that adequacy of consideration will not be reviewed depends on a single variable—the presence of a bargain—that is deliberately designed to screen out all information concerning individual circumstances. In contrast, application of the doctrine of unconscionability depends on a number of situation-specific variables that are wholly concerned with individual circumstances.

The rules of classical contract law lay almost wholly at the objective and standardized end of these spectra. So, for example, classical contract law adopted such standardized rules as the bargain principle, the parol evidence rule, and the objective theory of interpretation, and it rejected such individualized rules as unconscionability, the duty to negotiate in good faith, and subjective principles of interpretation.

3. The Static Nature of Classical Contract Law. Another characteristic of classical contract law is that it was static rather than dynamic. Classical contract law focused almost exclusively on a single instant in time—the instant of contract formation—rather than on dynamic processes such as the course of negotiation and the evolution of a contractual relationship.

4. The Implicit Paradigm of Classical Contract Law. Next, classical contract law was implicitly based on a paradigm of bargains made between strangers transacting in a perfect market. So, for example, classical contract law rejected principles of unfairness, which typically have their fullest application in transactions that occur either off-market or on very imperfect markets and have little application to contracts made between strangers on perfect markets.

5. The Rational-Actor Model of Psychology. Finally, classical contract law was based on a rational-actor model of psychology, under which actors who make decisions in the face of uncertainty rationally maximize their subjective expected utility, with all future benefits and costs discounted to present value. In particular, the rules of classical contract law were implicitly based on the assumptions that actors are fully knowledgeable, know the law, and act rationally to further their economic self-interest. This model accounts in part for such rules as the duty to read, whose operational significance was that actors were conclusively assumed to have read and understood everything that they signed. It also accounts in part for the rule that bargains would not be reviewed for fairness: if actors always act rationally in their own self-interest, then, in the absence of fraud, duress, or the like, all bargains must be fair.

B. A Brief Critique of Classical Contract Law

Mary McCarthy once said of Lillian Hellman that every word Hellman wrote was dishonest, including "and" and "the."[5] Something similar could be said of classical contract law. Every aspect of that school of law was incorrect.

1. Law Must be Justified by Social Propositions. To begin with, axiomatic theories of law cannot be sustained. No significant doctrinal proposition can be justified on the ground that it is self-evident. Doctrinal propositions can ultimately be justified only by propositions of morality, policy, and experience. A distinction must be drawn here between the justification of a doctrine and the justification for following a doctrine. Once a doctrine has been adopted it may justifiably be *followed,* either in the interest of stability, reliance, and the like, or because of social reasons for following rules that have been adopted in a certain way. However, those elements only justify following the doctrine; they do not justify the doctrine itself.

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[5] *See* Hellman v. McCarthy, 10 MEDIA. L. REP. 1789, 1790 (1984). Hellman sued for libel, but died while the suit was pending. *See* Daniel Kornstein, *The Case Against Lillian Hellman: A Literary/Legal Defense,* 57 FORD. L. REV. 683 (1989).

Deductive theories are no more sustainable than axiomatic theories. A doctrine, even if normatively justified, cannot alone serve as the premise of deductive reasoning, because all doctrines are always subject to as-yet-unarticulated exceptions based on social propositions. Such an exception may be made because the social propositions that support the doctrine do not extend to a new fact pattern that is within the doctrine's scope. Alternatively, such an exception may be made because a new fact pattern that is within the doctrine's stated scope brings into play other social propositions that require the formulation of a special rule for that fact pattern.

For example, suppose there is a justified doctrinal rule that donative promises are unenforceable. A case then arises in which a donative promise was reasonably relied upon to the promisee's cost. If the extension of a legal rule to a new fact pattern that is within the stated scope of the rule could be justified by deductive logic alone, the promisor would not be liable. The major premise would be that donative promises are unenforceable, the minor premise would be that the promise was donative, and the conclusion would be that the promise is unenforceable. But this conclusion should not be drawn, because a social proposition other than those that support the donative-promise principle applies to the case: When one person, *A*, uses words or actions that he knows or should know would induce another, *B*, to reasonably believe that *A* will take a certain course of action, and *A* knows or should know that *B* will incur costs if *A* does not take the action, *A* should take steps to ensure that if he does not take the action, *B* will not suffer a loss.[6] This proposition is weightier, in the donative-promise context, than the propositions that support the donative-promise rule in the absence of reliance. Therefore, an exception should be made to the donative-promise rule when the promisee has reasonably relied.

Accordingly, the applicability of a doctrine to a fact pattern that falls within the doctrine's stated scope is always dependent on a conclusion that social propositions, on balance, do not justify creating an exception for the fact pattern. Correspondingly, even an application of a doctrine that seems perfectly straightforward and easy is such not as a matter of deductive logic alone, but because social propositions do not justify the creation of an exception to cover the case at hand. The concept, implicit and often explicit in classical contract law, that contract law can be developed axiomatically and deductively, cannot be sustained.

2. Many Rules of Contract Law Should be Individualized, Subjective, or Both. The basic principle that should determine the content of contract law is that the law should effectuate the objectives of parties to a promissory transaction if appropriate conditions are satisfied and subject to appropriate constraints. Because the objective of contract law should be to further the interests of the contracting parties, the rules of contract law must

[6] *See* Thomas Scanlon, *Promises and Practices*, 19 PHIL. & PUB. AFF. 199 (1990).

often be formulated so that their application will turn on the particular circumstances of the parties' transactions and, in certain cases, on the parties' subjective intentions. Whether a given rule of contract law should be objective or subjective, and whether it should be standardized or individualized, are matters that must be decided on a rule-by-rule basis. The overriding preference of classical contract law for objective, standardized rules was incorrect.

3. Contract Law Should Take Account of the Dynamic Aspects of the Contracting Process. Promissory transactions seldom occur in an instant of time. They have a past, a present, and a future, and often it is not easy to say where the past ends and the present begins (because, for example, the process of concluding a deal is often a rolling process) or where the present ends and the future begins (because, for example, the contract is partly what it was at the time of contract formation and partly what it becomes thereafter). Because promissory transactions seldom occur in an instant of time, contract law, if it is to effectuate the objectives of parties to promissory transactions, must reflect the reality of contracting by adopting dynamic rules that parallel that reality, rather than static rules that deny that reality.

4. The Paradigmatic Case of Classical Contract Law is an Abnormal Case. The implicit empirical predicate of classical contract law, that the paradigm contract is one made by strangers transacting on a perfect market, was also flawed. Contracts are seldom made on perfect markets, and seldom made between strangers. This point will be discussed further in Part II.[7]

5. Rational-Actor Psychology Does Not Adequately Explain the Behavior of Contracting Parties. A great body of theoretical and empirical work in cognitive psychology within the last thirty or forty years has shown that rational-actor psychology, under which actors who make decisions in the face of uncertainty rationally maximize their subjective expected utility, with all future benefits and costs discounted to present value, often lacks explanatory power.[8] Although rational-actor psychology is the foundation of the standard economic *model* of choice, the empirical evidence shows that this model often diverges from the *actual psychology* of choice, because it fails to take into account the limits of cognition. As Tversky and Kahneman point out, expected-utility (rational-actor) theory "emerged from a logical analysis of games of chance rather than from a psychological analy-

[7] *See infra* notes 29-34 and accompanying text.

[8] *See* Thomas S. Ulen, *Cognitive Imperfections and the Economic Analysis of Law*, 12 HAMLINE L. REV. 385 (1989).

sis of risk and value. The theory was conceived as a normative model of an idealized decision maker, not as a description of the behavior of real people."[9]

In contrast to rational-actor psychology, cognitive psychology recognizes the limits of cognition. For purposes of contract law, three kinds of limits of cognition are especially salient: bounded rationality, irrational disposition, and defective capability.

a. Bounded Rationality.—To begin with, the substantive action that would maximize an actor's utility may not even be considered by the actor, because actors set process limits on their search for and their deliberation on alternatives.[10]

b. Irrational Disposition.—In addition, actors are, as a systematic matter, unrealistically optimistic.[11] (Lawyers don't realize this, because they are trained to be systematically pessimistic.) The dispositional characteristic of undue optimism is strikingly illustrated in a study by Baker and Emery, appropriately titled *When Every Relationship Is Above Average.*[12] Baker and Emery asked people who were about to get married to report on their own divorce-related prospects, as compared to the divorce-related prospects of the general population. The disparities between perceptions as to the general population and expectations as to self were enormous and almost invariably in the direction of optimism. For example, the respondents correctly estimated that fifty percent of American couples will eventually divorce. In contrast, the respondents estimated that their own chance of divorce was zero.[13] Similarly, the respondents' median estimate of how often spouses pay court-ordered alimony was that forty percent paid. In contrast, one hundred percent of the respondents predicted that in the event of a divorce, their own spouse would pay all court-ordered alimony.[14]

c. Defective Capability.—Finally, cognitive psychology has established that actors use certain decisionmaking rules (heuristics) that yield systematic errors. As Tversky and Kahneman put it, "[T]he deviations of actual behavior from the normative model are too widespread to be ignored, too systematic to be dismissed as random error, and too fundamental to be

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[9] Amos Tversky & Daniel Kahneman, *Rational Choice and the Framing of Decisions*, 59 J. BUS. S251, at S251 (Supp. 1986).

[10] *See* Herbert A. Simon, *Rational Decision Making in Business Organizations*, 69 AM. ECON. REV. 493 (1979).

[11] *See* Neil D. Weinstein, *Unrealistic Optimism About Future Life Events*, 39 J. PERSONALITY & SOC. PSYCHOL. 806 (1980).

[12] Lynn A. Baker & Robert E. Emery, *When Every Relationship Is Above Average: Perceptions and Expectations of Divorce at the Time of Marriage*, 17 LAW & HUM. BEHAV. 439 (1993).

[13] *See id.* at 443.

[14] *See id.*

accommodated by relaxing the normative system."[15] For example, actors systematically make decisions on the basis of data that is readily available to their memory, rather than on the basis of all the relevant data. Furthermore, actors systematically give undue weight to instantiated evidence as compared to general statements, to vivid evidence as compared to pallid evidence, and to concrete evidence as compared to abstract evidence.[16] Similarly, actors are systematically insensitive to sample size and erroneously take small samples as representative samples.

Another defect of capability concerns the ability of actors to make rational comparisons between present and future states. For example, the sample consisting of present events is often wrongly taken to be representative and therefore predictive of future events.[17] Actors also systematically give too little weight to future benefits and costs as compared to present benefits and costs.[18] Thus, Feldstein concludes that "some or all individuals have, in Pigou's . . . words, a 'faulty telescopic faculty' that causes them to give too little weight to the utility of future consumption."[19]

A defect of capability related to faulty telescopic faculties is the systematic underestimation of risks.[20] Based on the work of cognitive psychologists, Arrow observes that "it is a plausible hypothesis that individuals are unable to recognize that there will be many surprises in the future; in short, as much other evidence tends to confirm, there is a tendency to underestimate uncertainties."[21] In fact, empirical evidence shows that actors often not only underestimate but also ignore low-probability risks.

In sum, cognitive psychology has established that cognition is limited in ways that are not accounted for by rational-actor psychology. Classical contract doctrines, which assumed that parties to contracts are rational actors, often did not reflect the actual circumstances of contract formation.

II. RELATIONAL CONTRACT THEORY

Relational contract theory, fathered by Ian Macneil, stands as a mirror image of classical contract law. Classical contract law was axiomatic and deductive; relational contract theory is open and inductive. Classical contract law was standardized; relational contract theory is individualized. Classical contract law was based on the paradigm of strangers transacting on a perfect market; relational contract theory is based on the paradigm of transactions by actors who are in an ongoing relationship, and often in a

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[15] Tversky & Kahneman, *supra* note 8, at S252.

[16] *See* ROBYN M. DAWES, RATIONAL CHOICE IN AN UNCERTAIN WORLD 92-94 (Jerome Kagan ed., 1988).

[17] *See* Kenneth J. Arrow, *Risk Perception in Psychology and Economics*, 20 ECON. INQUIRY 1, 5 (1982).

[18] *See* Martin Feldstein, *The Optimal Level of Social Security Benefits*, 100 Q. J. ECON. 303, 307 (1985).

[19] *Id.* at 307.

[20] *See* THOMAS H. JACKSON, THE LOGIC AND LIMITS OF BANKRUPTCY LAW 237-40 (1986).

[21] Arrow, *supra* note 17, at 5.

bilateral monopoly. Classical contract law was static; relational contract theory is dynamic. Classical contract law was based on rational-actor psychology; relational contract law is not. (Thus, Macneil eloquently points out that "[m]an is both an entirely selfish and an entirely social creature, in that man puts the interests of his fellows ahead of his own interests *at the same time* that he puts his own interests first.")[22]

This rejection of the basic approaches and assumptions of classical contract law is all to the good. However, constructing a body of relational contract law requires more than rejecting the approaches and assumptions of classical contract law. It also requires the formulation of a new body of legal rules based on approaches and assumptions that are justified by morality, policy, and experience. This is a place to which relational contract theory has not gone and cannot go. To begin with, it is impossible to locate, in the relational contracts literature, a definition that adequately distinguishes relational and nonrelational contracts in a legally operational way—that is, in a way that carves out a set of special and well-specified relational contracts for treatment under a body of special and well-specified rules.

One approach to the problem of definition has been to define relational contracts as those contracts that are not "discrete." This approach, of course, requires a definition of discrete contracts. Vic Goldberg has defined a discrete contract as a contract "in which no duties exist between the parties prior to the contract formation . . . ."[23] However, even in the case of a relational contract no duties can exist *under the contract* prior to its formation. (Of course, the parties may be under other duties to each other prior to formation, but that is true whether the contract is relational or discrete.) Similarly, although a duty may arise, prior to the formation of a contract, to negotiate the terms of a contract in good faith, that duty arises as a result of a preliminary commitment, or on the basis of preliminary actions taken by one or both parties, not under the terms of the contract.

Macneil sometimes treats discreteness as an end of a spectrum rather than as a definition of a body of contracts. Under this approach, a contract is characterized as lying at the discrete end of the spectrum if it has less of certain characteristics—for example, less duration, less personal interaction, less future cooperative burdens, less in the way of units of exchange that are difficult to measure—and as lying at the relational end of the spectrum if it has more of the relevant characteristics.[24]

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[22] Ian R. Macneil, *Values in Contract: Internal and External*, 78 NW. U. L. REV. 340, 348 (1983).

[23] Victor Goldberg, *Towards an Expanded Economic Theory of Contract*, 10 J. ECON. ISSUES 45, 49 (1976). I interpret this definition to mean that no *contractual* duties exist prior to contract formation. As Macneil has pointed out, in discussing this definition, if no duties of *any kind* exist between the parties prior to a contractual exchange, "then theft by the stronger party is more likely to occur than is exchange." Ian R. Macneil, *Economic Analysis of Contractual Relations: Its Shortfalls and the Need for a "Rich Classificatory Apparatus,"* 75 NW. U. L. REV. 1018, 1020 (1981).

[24] *See* IAN R. MACNEIL, CONTRACTS: EXCHANGE TRANSACTIONS AND RELATIONS 12-13 (2d ed. 1978) [hereinafter EXCHANGE TRANSACTIONS AND RELATIONS].

A spectrum approach is certainly acceptable if we view relational contracts only from a sociological and economic perspective. However, the enterprise of contract law entails the formulation of rules, and a spectrum approach is inadequate to that enterprise, because it cannot be operationalized. Under such an approach, many or most contracts will have both relational and discrete elements. Accordingly, except for the relatively few cases that lie at one end of the spectrum, or that satisfy or fail to satisfy every item on the checklist, there would be no way to know whether the general rules of contract law or special rules of relational contract law should be applied in any given case. Rules whose applicability depended on where a contract is located in a spectrum—that is, on how many relational indicia the contract has and of what kind—would be rules in name only.

Therefore, if there is to be a body of contract-law rules to govern relational contracts, it is imperative to establish a definition of relational contracts that centers on one or more characteristics that meaningfully distinguish relational and discrete contracts, and the definition must do so in a way that justifies the application of a special body of contract rules to relational contracts as so defined. One characteristic on which such a definition might turn is duration. Indeed, as Goetz and Scott have pointed out, "Although a certain ambiguity has always existed, there has been a tendency to equate the term 'relational contract' with long-term contractual involvements."[25] Thus, the phrase "long-term contracts" has become virtually a synonym for relational contracts. But as Goetz and Scott have also pointed out, this variable won't do the job—"temporal extension per se is not the defining characteristic" of relational contracts. For example, a long-term fixed-rent lease in which the tenant is responsible for maintenance, insurance, and taxes may involve little relationship between landlord and tenant. Similarly, a long-term lease of capital equipment, like aircraft, may require almost no contact between the parties so long as periodic payments are made. In contrast, a two-week contract to remodel a room may be highly relational, as may be a one-day contract between a photographer and a portrait sitter.

Although long duration is not a defining characteristic of relational contracts, it might be treated as an independent variable in contract law, so that there would be special rules for all long-term contracts, regardless of whether they are relational. For example, John Stuart Mill, who argued that "laissez faire . . . should be the general practice" and "that every departure from it, unless required by some great good, is a certain evil,"[26] nevertheless concluded:

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[25] Charles J. Goetz & Robert E. Scott, *Principles of Relational Contracts*, 67 VA. L. REV. 1089, 1091 (1981).

[26] JOHN STUART MILL, PRINCIPLES OF POLITICAL ECONOMY 950 (W. Ashley ed., 1965).

> [An] exception to the doctrine that individuals are the best judges of their own interest, is when an individual attempts to decide irrevocably now what will be best for his interest at some future and distant time. The presumption in favour of individual judgment is only legitimate, where the judgment is grounded on actual, and especially on present, personal experience; not where it is formed antecedently to experience, and not suffered to be reversed even after experience has condemned it. When persons have bound themselves by a contract, not simply to do some one thing, but to continue doing something . . . for a prolonged period, without any power of revoking the engagement . . . [any] presumption which can be grounded on their having voluntarily entered into the contract . . . is commonly next to null.[27]

Although Mill did not elaborate the reason for this view, a reason is not hard to find. As shown above, modern cognitive psychology instructs us that actors have telescopic faculties that degrade their cognitive ability to make comparisons between present and future costs and benefits. The further out in time a given cost or benefit is located, the less capacity an actor has to determine his own best interests. Similarly, actors systematically underestimate most risks, and often wrongly take the sample consisting of present events to be representative and therefore predictive of future events. Both of these limits on cognition become increasingly salient as the time span of a contract becomes increasingly long. But whether or not there should be special rules for contracts of long duration, long duration does not of itself make a contract relational, and short duration does not of itself make a contract discrete.

Goetz and Scott, having properly rejected duration as a test for whether a contract is relational, propose yet another definition: "A contract is relational to the extent that the parties are incapable of reducing important terms of the arrangement to well-defined obligations."[28] However, the fact is that parties to a contract are *never* capable of reducing all of the important terms of their arrangement to well-defined obligations. This point was pungently made more than 100 years ago by Lieber:

> Suppose a housekeeper says to a domestic: "fetch some soupmeat," accompanying the act with giving some money to the latter; he will be unable to execute the order without interpretation, however easy and, consequently, rapid the performance of the process may be. Common sense and good faith tell the domestic, that the housekeeper's meaning was this: 1. He should go immediately, or as soon as his other occupations are finished; or, if he be directed to do so in the evening, that he should go the next day at the usual hour; 2. that the money handed him by the housekeeper is intended to pay for the meat thus ordered, and not as a present to him; 3. that he should buy such meat and of such parts of the animal, as, to his knowledge, has commonly been used

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[27] *Id.* at 959-60.

[28] Goetz & Scott, *supra* note 25, at 1091.

> in the house he stays at, for making soups; 4. that he buy the best meat he can obtain, for a fair price; 5. that he go to that butcher who usually provides the family, with whom the domestic resides, with meat, or to some convenient stall, and not to any unnecessarily distant place; 6. that he return the rest of the money; 7. that he bring home the meat in good faith, neither adding any thing disagreeable nor injurious; 8. that he fetch the meat for the use of the family and not for himself. Suppose, on the other hand, the housekeeper, afraid of being misunderstood, had mentioned these eight specifications, she would not have obtained her object, if it were to exclude all possibility of misunderstanding. For, the various specifications would have required new ones. Where would be the end? We are constrained then, always, to leave a considerable part of our meaning to be found out by interpretation, which, in many cases must necessarily cause greater or less obscurity with regard to the exact meaning, which our words were intended to convey.[29]

What is especially striking about the numerous efforts to define relational contracts, and the failure of all these efforts, is that a straightforward definition of relational contracts is readily at hand. The obvious definition of a relational contract is a contract that involves not merely an exchange, but also a relationship, between the contracting parties. Correspondingly, the obvious definition of a discrete contract is a contract that involves only an exchange, and not a relationship. Macneil himself has sometimes favored such a definition. For example, in *The New Social Contract*, Macneil defines a discrete contract as "one in which no relation exists between the parties apart from the simple exchange of goods."[30] Such a definition not only can be operationalized, but also reflects the everyday, common sense meaning of the term "relational." It also highlights a major shortcoming of competing definitions: any definition of a relational contract that fails to turn on whether the contract involves a relationship is bound to be incongruent with the ordinary meaning of the term it purports to define.

Once such a definition has been adopted, however, we can see that discrete contracts are almost nonexistent, because virtually all contracts either create or reflect relationships. Discrete contracts—contracts that are *not* relational—are almost as imaginary as unicorns. A contract to build something as simple as a fence creates a relationship. A contract to sell almost any commercial product is likely to either create or reflect a relationship. Consumer contracts commonly involve ongoing relationships even when they are made with huge bureaucratic organizations: most shoppers at Macy's have shopped there before and expect to shop there again. Neither Macy's nor the shoppers perceive each individual exchange as an isolated nonrelational transaction. Even contracts on perfect spot markets are likely to involve traders or brokers who have continuing relationships of some sort.

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[29] FRITZ LIEBER, LEGAL AND POLITICAL HERMENEUTICS 18-19 (3d ed. 1880).

[30] IAN R. MACNEIL, THE NEW SOCIAL CONTRACT 10 (1980).

Trying, at least for the sake of argument, to imagine a discrete contract, Macneil is quite naturally driven to extremes:

> [A]t noon two strangers come into town from opposite directions, one walking and one riding a horse. The walker offers to buy the horse, and after brief dickering a deal is struck in which delivery of the horse is to be made at sundown upon the handing over of $10. The two strangers expect to have nothing to do with each other between now and sundown; they expect never to see each other thereafter; and each has as much feeling for the other as has a Viking trading with a Saxon.[31]

Similarly, Oliver Williamson gives as an example of a discrete contract: a purchase of a bottle of local spirits from a shopkeeper in a remote area of a foreign country who one never expects to visit again nor to recommend to one's friends.[32] In the end, Macneil admits that a discrete contract is "an impossibility,"[33] and characterizes discrete contracts as "*entirely* fictional."[34]

One reason for the overthrow of classical contract law is that it was tacitly based on the empirically incorrect premise that most contracts were discrete. Ironically, however, relational contract theory has made an empirical mistake comparable to that made by classical contract law: insofar as relational contract theory supports the idea that there should be a body of special rules to govern relational contracts, it is tacitly based on the incorrect premise that relational contracts are only a special subcategory of contracts as a class. Once relational contracts are properly defined, however, and it is recognized that all or almost all contracts are relational, it is easy to see that relational contracts are not a special subcategory of contracts, and therefore should not and cannot be governed by a body of special contract-law rules. There can be no special law of relational contracts, because relational contracts and contracts are virtually one and the same.

Consider, in this connection, the special rules proposed for relational contracts in some of the relational contract literature. These include the following: (1) Rules that, in the case of relational contracts, would soften or reverse the bite of the rigid offer-and-acceptance format of classical contract law, and the corresponding intolerance of classical contract law for indefiniteness, agreements to agree, and agreements to negotiate in good faith. (2) Rules that would impose upon parties to a relational contract a

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[31] EXCHANGE TRANSACTIONS AND RELATIONS, *supra* note 24, at 13.

[32] *See* Oliver E. Williamson, *Transaction-Cost Economics: The Governance of Contractual Relations*, 22 J.L. & ECON. 233, 247 (1979). This transaction, however, involves little or no promise and little or no futurity. The same is true of another example, given by Macneil: "A purchase of nonbrand name gasoline in a strange town one does not expect to see again." EXCHANGE TRANSACTIONS AND RELATIONS, *supra* note 24, at 13.

[33] Ian. R. Macneil, *Contracts: Adjustment of Long-Term Relations Under Classical, Neoclassical, and Relational Contract Law*, 72 NW. U. L. REV. 854, 857 n.10 (1978).

[34] MACNEIL, *supra* note 30, at 11.

broad obligation to perform in good faith. (3) Rules that would broaden the kinds of changed circumstances (impossibility, impracticability, and frustration) that constitute an excuse for nonperformance of a relational contract. (4) Rules that would give content to particular kinds of contractual provisions that may be found in relational contracts, such as best-efforts clauses or unilateral rights to terminate at will. (5) Rules that would treat relational contracts like partnerships, in the sense that such contracts involve a mutual enterprise and should be construed in that light. (6) Rules that would keep a relational contract together. (7) Rules that would impose upon parties to a relational contract a duty to bargain in good faith to make equitable price adjustments when changed circumstances occur, and would perhaps even impose upon the advantaged party a duty to accept an equitable adjustment proposed in good faith by the disadvantaged party. (8) Rules that would permit the courts to adapt or revise the terms of ongoing relational contracts in such a way that an unexpected loss that would otherwise fall on one party will be shared by reducing the other party's profits.[35] Because there is no significant distinction between contracts as a class and relational contracts, these rules, and others like them, can be separated into two broad classes: those that are good for all contracts and therefore should be general principles of contract law, and those that are not good for any contracts.

For example, the relational contract literature is correct in pointing to the deficiencies of classical contract law concerning the rigid offer-and-acceptance format of classical contract law and, more particularly, the intolerant treatment, in classical contract law, of such issues as indefiniteness, agreements to agree, and agreements to negotiate in good faith. If parties believe they have a deal, indefiniteness should rarely be a good defense. And if parties agree to agree or to negotiate in good faith, that is a deal. All this holds true, however, for all contracts. Correspondingly, there should be an obligation to perform contracts in good faith, but this obligation should also apply to all contracts.

Similarly, the principles that determine when changed circumstances should serve as an excuse should be applicable to all contracts. Indeed, some of the best-known impossibility, impracticability, or frustration cases, like *Taylor v. Caldwell*[36] and *Krell v. Henry*,[37] involved contracts that were of very short duration and entailed little in the way of a relationship. Rules that give content to terms like best-efforts or termination-at-will provisions

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[35] *See, e.g.*, David Campbell & Donald Harris, *Flexibility in Long-Term Contractual Relationships: The Role of Co-Operation*, 20 J.L. & SOC. 166 (1993); Robert A. Hillman, *Contract Excuse and Bankruptcy Discharge*, 43 STAN. L. REV. 99, 132-33 (1990); Robert A. Hillman, *Court Adjustment of Long-Term Contracts: An Analysis Under Modern Contract Law*, 1987 DUKE L.J. 1 (1987); Macneil, *supra* note 33; Richard E. Speidel, *Court-Imposed Price Adjustments Under Long-Term Supply Contracts*, 76 NW. U. L. REV. 369 (1981).

[36] 122 Eng. Rep. 309 (K.B. 1863).

[37] 2 K.B. 740 (Eng. C.A. 1903).

should also apply to all contracts. Finally, the conception that contracts are mutual enterprises, and can be analogized to partnerships, is also applicable to all contracts.[38]

On the other hand, the concepts that parties have an obligation to negotiate in good faith to make equitable price adjustments when circumstances change, and that the courts can revise the terms of ongoing contracts, are highly questionable for any contracts. There are a variety of ways to contract for the possibility of price adjustments—for example, the use of hardship or equitable-adjustment provisions. In the case of long-term contracts, where such adjustments would be most plausible, normally both parties will be sophisticated and well-advised, and will have the capacity to make use of such a provision if they chose to do so. Therefore, the omission of such a provision in a long-term contract should normally be viewed as a deliberate decision. (A corollary of this position, of course, is that the courts should liberally enforce such provisions when they are utilized.)

Similarly, although the rules of contract law should operate to prevent one party from opportunistically using an insubstantial breach or the nonfulfillment of an insignificant condition as a contrived excuse for breaking a *deal*, the concept that legal rules can keep a living *relationship* together is quixotic. Association compelled by law against the wishes of a party is not a living relationship, or at best is a highly impoverished relationship.

Moreover, the concept that parties should be legally forced to stay locked into a *thick* long-term contractual relationship—that is, an intensive long-term contractual relationship that involves personal elements and extends over a significant portion of the parties' lives—ignores the teachings of cognitive psychology. By virtue of the nature of such relationships, it will be almost impossible to predict, at the time the contract is made, what contingencies may affect the relationship's future course. Furthermore, at the time such a contract is made, each party is likely to be unduly optimistic about the likelihood of the relationship's long-term success and about the willingness of the other party to avoid opportunistic behavior during the course of the relationship. Finally, the parties to such a contract are likely to give undue weight to the state of their relationship as of the time the contract is made, which is vivid, concrete, and instantiated; to erroneously take the state of their relationship at that point as representative of the relationship's future state; and to give too little thought to, and place too little weight on, the risk that the relationship will go bad. Rules that would compel the continuation of such relationships only invite opportunistic exploitation. The solution to the problems presented by such contracts is not to hold the relationship together, but to allow either party to readily dissolve the relationship on fair terms, even if the right to dissolve is not written into the contract.

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[38] *See, e.g.*, Jeffrey L. Harrison, *A Case for Loss Sharing*, 56 S. CAL L. REV. 573 (1983).

In contrast to the approach, found in parts of the literature, of developing special rules to apply to relational contracts as a class, Macneil has tried to locate relational contract law in specific statutes, like "ERISA, OSHA, other workplace regulations, wage and hours legislation, . . . the NLRA, LMRA, and a wide range of law governing unions and other aspects of collective bargaining."[39] However, this approach also fails to demonstrate that there either is or should be a law of relational contracts.

To begin with, Macneil's list of statutes reflects in significant part his definition of relational contracts as any form of relations that involve or imply past, present, or future economic or noneconomic exchange.[40] This massive contractualization of human relationships undesirably obscures critical differences between economic and affective relationships, between explicit and tacit reciprocity, between relationships that should be enforceable by both law and social norms and relationships that should be enforceable only by social norms, and between relationships that are triggered by promise and relationships that are not.[41] With only very limited exceptions, contract law consists of the body of rules that apply to relationships that are economic rather than affective, that involve explicit rather than tacit reciprocity, that should be enforceable by both law and social norms, and that are triggered by a promise or at least set in a promissory matrix. This does not mean that contract-law rules have their only *source* in promises. These rules may properly incorporate or reflect social norms, or may properly be sufficiently open-textured to give effect to the norms of the contracting parties. However, without a promise, or at least a promissory matrix, contract law does not get off the ground. Nonpromissory relationships or obligations should be governed not by contract law—relational or otherwise—but by bodies of law that are tailored to the relevant relationship or obligation, like domestic relations law or tort law.

Indeed, even legal rules that govern relationships that *are* triggered by promises are not necessarily contract-law rules. A lawmaker who wants to generally prohibit a certain kind of conduct may include, within the general prohibition, conduct of the relevant kind that finds expression in promise-triggered relationships. A legal rule of this kind does not constitute contract law just because it reaches such relationships. For example, the legal rules that prohibit contracts to buy and sell drugs are not rules of contract law, although they apply to promise-triggered relationships. Similarly, the stat-

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[39] Ian R. Macneil, *Relational Contract Theory: Challenges and Queries*, 94 NW. U. L. REV. 877, 897 (2000).

[40] *See, e.g., id.* at 878; EXCHANGE TRANSACTIONS AND RELATIONS, *supra* note 23, at 13; MACNEIL, *supra* note 30, at 4-5, 13, 20; William C. Whitford, *Ian Macneil's Contribution to Contracts Scholarship*, 1985 WISC. L. REV. 545 (stating that Macneil's theory "becomes in effect a general theory of the social order.").

[41] *See* Melvin A. Eisenberg, *The World of Contract and the World of Gift*, 85 CAL. L. REV. 821 (1997); Douglas K. Newell, *Will Kindness Kill Contract*, 24 HOFSTRA L. REV. 455 (1995); Steven R. Salbu, *The Decline of Contracts as a Relationship Management Form*, 47 RUTGERS L. REV. 1271 (1995).

utes that Macneil identifies are for the most part rules that are designed to regulate conduct and that include within their scope conduct of the relevant kind that is expressed in promise-triggered relationships.

In short, Macneil's list of specific statutes, like the general rules proposed for relational contracts in some of the relational contract literature, fails to demonstrate that there either is or should be a law of relational contracts.

CONCLUSION

Relational contract theory has helped to bring home two of the fundamental weaknesses of classical contract law—its static character, and the flawed nature of its implicit empirical premise that most contracts are discrete. Relational contract theory has also greatly illuminated the economics and sociology of contracting. Finally, relational contract theory has excelled in its treatment of specific types of contracts, like franchise agreements, and specific types of express or implied terms, like best-efforts provisions. As a result of all these contributions, relational contract theory has been a highly important factor in the formulation of modern contract law.

What relational contract theory has not done, and cannot do, is to create a law of relational contracts. Because there is no significant difference between contracts as a class and relational contracts, relational contracts must be governed by the general principles of contract law, whatever those should be. Of course, certain categories of contracts present special kinds of problems. These problems, however, derive not from the fact that the contracts in these categories are relational, but from more specific attributes. Long-term contracts, contracts to govern thick relationships, contracts that are both especially interactive and especially not well-specifiable, and other categories of contracts may each present special problems that stem from their special features. Even in these cases, for the most part the law of contract should be able to solve the relevant problems by the formulation of general principles that apply to all contracts, but are responsive to intentions and circumstances in particular cases. But relational contracts, as such, are not a special category of contract, because all or virtually all contracts are relational. That is why we do not have, and should not have, a law of relational contracts.