

## THE FAULT THAT LIES WITHIN OUR CONTRACT LAW

*George M. Cohen\**

*Scholars and courts typically describe and defend American contract law as a system of strict liability, or liability without fault. Strict liability generally means that the reason for nonperformance does not matter in determining whether a contracting party breached. Strict liability also permeates the doctrines of contract damages, under which the reason for the breach does not matter in determining the measure of damages, and the doctrines of contract formation, under which the reason for failing to contract does not matter.*

*In my Article, I take issue with the strict liability paradigm, as I have in my prior work on contract law. In my view, the theoretical justifications for strict liability as a general paradigm for contract law oversimplify contractual intent, the relationship between intent and fault, and the nature of contractual fault. Moreover, the strict liability label is descriptively misleading, once one dips even slightly below the surface of contract doctrine. Fault shows up throughout contract law. Efforts to make contract law conform more to the strict liability paradigm and exorcize fault are wrong-headed. In any case, such efforts are doomed to fail. Fault may not be the dominant feature of contract law, but it plays an inherent, invaluable, and ineluctable supporting part. Like other contract rules, strict liability is merely a fault-based presumption. Determining the limits of that presumption means considering why parties make contracts and why they do not perform them, in other words, fault. Courts and scholars should acknowledge the role of fault and think about how to use fault more effectively within the framework of contract doctrine.*

### INTRODUCTION

The myth that contract law is a system of strict liability stubbornly persists.<sup>1</sup> I seek to debunk this myth.<sup>2</sup> In my view, the theoretical justifications

---

\* Brokaw Professor of Corporate Law, University of Virginia School of Law. Thanks to Umair Javed for research assistance and participants in the University of Virginia summer workshop for helpful comments.

1. E.g., RESTATEMENT (SECOND) OF CONTRACTS, ch. 11, introductory note (1981) (“Contract liability is strict liability. . . . The obligor is therefore liable in damages for breach of contract even if he is without fault . . .”).

2. This essay thus continues a recurrent theme in my writing on contract law. George M. Cohen, *Implied Terms and Interpretation in Contract Law*, in 3 ENCYCLOPEDIA OF LAW AND

for strict liability oversimplify contractual intent, the relationship between intent and fault, and the nature of contractual fault. Moreover, the strict liability label is descriptively misleading once one dips even slightly below the surface of contract doctrine. Efforts to make contract law conform more to the strict liability paradigm and exorcize fault are misguided. In any case, such efforts are doomed to fail. Fault plays an inherent, invaluable, and ineluctable role in contract law.

### I. STRICT LIABILITY IN CONTRACT LAW

The strict liability paradigm permeates classical contract law. Usually, however, the explicit label “strict liability” appears only in connection with the doctrines of performance and breach. Under these doctrines, failure in any way to perform a contract breaches the contract, and subjects the breaching party to liability, regardless of “fault.”<sup>3</sup> The paradigmatic case is a seller who delivers goods that fail “in any respect to conform to the contract.”<sup>4</sup> Strict liability means that the contract provides a “warranty” of results.<sup>5</sup> In short, the reason for nonperformance does not matter.

If the doctrinal irrelevance of fault is the touchstone of strict liability, then the other main areas of contract law—formation and damages—seem to fit that paradigm as well. With respect to damages, Holmes long ago articulated the strict liability view: just as the reason for nonperformance does not matter in determining breach, the reason for the breach does not matter in determining damages.<sup>6</sup> An aggrieved party who can prove breach is entitled to “compensation,” which contract law generally defines as protecting the expectation interest.<sup>7</sup> Fault seems irrelevant to determining compensation.

Finally, although contract formation doctrine does not explicitly endorse strict liability, it nevertheless also seems to comport with the strict liability view. In this case, however, it is the reason for failing to contract, rather than for failing to perform, that does not matter.<sup>8</sup> Basic formation doctrine holds

---

ECONOMICS 78 (Boudewijn Bouckaert & Gerrit De Geest eds., 2000) [hereinafter Cohen, *Interpretation*]; George M. Cohen, *The Fault Lines in Contract Damages*, 80 VA. L. REV. 1225 (1994) [hereinafter Cohen, *Fault Lines*]; George M. Cohen, *Finding Fault with Wonnell's "Two Contractual Wrongs"*, 38 SAN DIEGO L. REV. 137 (2001) [hereinafter Cohen, *Finding Fault*]; George M. Cohen, *The Negligence-Opportunism Tradeoff in Contract Law*, 20 HOFSTRA L. REV. 941 (1992) [hereinafter Cohen, *Negligence-Opportunism Tradeoff*].

3. RESTATEMENT (SECOND) OF CONTRACTS § 235 cmt. b (“[A]nything short of full performance is a breach, even if the party who does not fully perform was not at fault . . .”).

4. U.C.C. § 2-601 (2005).

5. See, e.g., RESTATEMENT (SECOND) OF CONTRACTS § 266 cmt. b, illus. 7 (contracting party who warrants merchantability of a machine is liable for incurable defect not due to fault of seller and which seller did not know about).

6. *Globe Ref. Co. v. Landa Cotton Oil Co.*, 190 U.S. 540, 544 (1903). For a critique of this view, see Cohen, *Fault Lines*, *supra* note 2.

7. RESTATEMENT (SECOND) OF CONTRACTS §§ 344 cmt. a, 347 & cmt. a.

8. Technically the doctrine is one of strict nonliability rather than strict liability, but the idea is essentially the same.

that no contractual liability exists unless and until the parties agree.<sup>9</sup> Just as fault seems irrelevant to performance and compensation, so it seems irrelevant to “agreement.”

The narrow explicit association of strict liability with contract performance and breach is puzzling. What sense would it make to call contract law a strict liability regime if strict liability merely occupies the narrow doctrinal space of performance while the reason for nonperformance matters for formation and remedy? In fact, the justifications usually offered for strict liability apply across contract law. These justifications are weak.

## II. JUSTIFICATIONS FOR STRICT LIABILITY

One can posit two broad types of justifications for strict liability: traditionalist and economic. A “traditionalist” justification derives strict liability from two simple premises. First, contract law grounds liability in the mutual consent of the contracting parties.<sup>10</sup> Second, fault is a social judgment distinct from consent.<sup>11</sup> Unlike the tort law of accidents between strangers, contract law allows the parties themselves to define the scope of liability, removing, in theory, the need for social judgment (other than the social judgment to enforce agreements according to the parties’ intentions). The only relevant fault is breach of any agreement the parties intended to make. Fault thus merges with mutual intent; it is not an independent criterion of liability.<sup>12</sup>

Enforcing agreements according to mutual consent does not quite imply strict liability, however. Suppose the parties intend that the reason for nonperformance matters in determining liability under their contract. A regime that strictly enforces fault-based intent is not what we usually think of as strict liability. Thus, a traditionalist justification of strict liability must defend the proposition that the parties generally intend that the reason for nonperformance does not matter. That proposition is, however, contestable, as discussed below.

The economic justification starts from the same premise as the traditionalist justification—that courts should enforce agreements according to the parties’ mutual intentions—but grounds that premise differently. The economic justification focuses on “facilitat[ing] the efforts of contracting

---

9. *E.g.*, RESTATEMENT (SECOND) OF CONTRACTS § 17(1); E. Allen Farnsworth, *Precontractual Liability and Preliminary Agreements: Fair Dealing and Failed Negotiations*, 87 COLUM. L. REV. 217, 221–22 (1987).

10. *See, e.g.*, Curtis Bridgeman, *Reconciling Strict Liability with Corrective Justice in Contract Law*, 75 FORDHAM L. REV. 3013, 3034–35 (2007) (justifying strict liability under a theory of corrective justice focusing on the wrongful loss of entitlements determined primarily by mutual consent).

11. *See, e.g.*, CHARLES FRIED, *CONTRACT AS PROMISE: A THEORY OF CONTRACTUAL OBLIGATION* 4 (1981) (contrasting contract law, which focuses on the will of the parties, with tort law, which focuses on “fairness”).

12. For a more sophisticated philosophical approach to strict liability, see STEPHEN A. SMITH, *CONTRACT THEORY* 376–86 (2004).

parties to maximize the joint gains . . . from transactions.”<sup>13</sup> If courts do not enforce contracts according to mutual intent, but instead try to “regulate” the parties’ behavior, for example, by injecting courts’ “own notions” of “fault” that conflict with the parties’ preferences, joint gains will not be maximized; thus, parties will contract around those restrictions if they can and incur losses if they cannot.<sup>14</sup>

Even if contracting parties do not expressly state a preference for strict liability, economists would infer such a preference if it comports with efficiency, on the assumption that most parties would prefer strict liability.<sup>15</sup> Economists generally offer three reasons why strict liability in contract is efficient: superior risk bearing, litigation costs, and comparative institutional competence. First, if promisors are usually in a better position than promisees to bear risks that would make performance of their promises more costly or less valuable, then strict liability is efficient because it generally puts those risks on the superior risk bearer.<sup>16</sup> Second, fault-based liability imposes higher litigation costs on the parties than strict liability, because fault is more costly for courts to assess, and these costs outweigh the benefits of a fault-based system.<sup>17</sup> Finally, contracting parties are better equipped than the courts to make whatever fault determinations are desirable, and so prefer informal enforcement to court enforcement unless they say otherwise.<sup>18</sup>

These reasons are not persuasive. As discussed below, the superior-risk-bearer analysis actually supports a fault-based approach to contract law as a whole, because the promisor is not always the better risk bearer. Further, distinguishing cases in which the promisee is the better risk bearer is not always unduly burdensome. Moreover, the litigation-cost advantage of strict liability is far from clear. For example, courts under a fault-based approach can easily limit the kinds of fault evidence that parties could introduce; fault need not mean free-for-all. And the comparative institutional advantage argument that parties prefer that they, rather than courts, should make fault judgments merely returns us to the problem of determining mutual intent.

### III. THE UNCERTAINTY OF MUTUAL INTENT

Under both the traditionalist and economic justifications, the argument for strict liability is stronger if mutual intent is easily determined and clearly distinguishable from fault. Adopting a fault-based system of contract law in

---

13. Alan Schwartz & Robert E. Scott, *Contract Theory and the Limits of Contract Law*, 113 YALE L.J. 541, 544 (2003).

14. See, e.g., RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 99 (7th ed. 2007).

15. *Id.* at 97.

16. *Id.* at 182.

17. E.g., Robert Cooter, *Unity in Tort, Contract, and Property: The Model of Precaution*, 73 CAL. L. REV. 1, 31–32 (1985).

18. E.g., Robert E. Scott, *In (Partial) Defense of Strict Liability in Contract*, 107 MICH. L. REV. 1381, 1392–94 (2009).

those circumstances would lead to illegitimate social judgments by courts on the traditionalist view, and result in inefficient contracting around or failures to contract on the economic view.

Determining disputed mutual intent is inherently uncertain, however. Mutual intent is an ideal. Contracting parties attempt to express mutual intent, often in writing, but do so imperfectly. Contracts are largely a set of private rules, and all rules require interpretation, stories that explain their meaning in a particular situation.<sup>19</sup> As unanticipated situations arise, disputes requiring interpretation inevitably occur. Parties generally resolve these disputes on their own, often driven by reputational concerns. When these efforts fail, they bring their disputes to court. In litigated cases, the parties typically contest the requirements of mutual intent. Contract law is another set of rules, designed predominantly to help courts choose between competing versions of mutual intent. The very existence of contract law, therefore, belies an easily determined mutual intent in disputed contracts. This is especially true for doctrines of formation and remedy, matters about which contracting parties often say little.

One could argue that even if intent is uncertain in general, parties at least intend courts to adopt strict liability rules. Intent about interpretive methodology, which we might call procedural or secondary, contrasts with substantive or primary intent, which is how parties should and should not behave under the contract. Contracting parties may express preferences about the methodology they want courts to use in ascertaining mutual intent. For example, merger clauses direct courts to look only at the writing. Parties do not, however, typically write “strict liability” clauses into their contracts. Thus, focusing on secondary intent merely shifts the problem of uncertain intent to a different place. Moreover, even explicit statements of secondary intent do not preempt the need for interpretation. In fact, they often create an additional interpretive question: when primary and secondary intent conflict, which takes priority?<sup>20</sup>

The difference between primary and secondary intent is just one example of a more general phenomenon: multiple intents. Contracting parties often have more than one goal. They make multiple promises. Multifaceted intent compounds the problem of contractual uncertainty. The more expressions of intent, the more likely that disputes will arise over how to reconcile or prioritize conflicting expressions.

---

19. See generally Robert M. Cover, *The Supreme Court, 1982 Term—Foreward: Nomos and Narrative*, 97 HARV. L. REV. 4 (1983).

20. See Cohen, *Interpretation*, *supra* note 2, at 96–97. Schwartz and Scott argue for the priority of secondary over primary intent on theoretical (and to me unconvincing) grounds. Schwartz & Scott, *supra* note 13, at 568–94. Similar questions arise in recent theories arguing that parties often intend to rely on “fairness norms” (primary) but they intend these norms to be enforced privately rather than by courts (secondary). See, e.g., Robert E. Scott, *A Theory of Self-Enforcing Indefinite Agreements*, 103 COLUM. L. REV. 1641 (2003). Suppose that parties do have that intention (which is contestable in many cases). If one party violates a fairness norm, the other party may, in violation of another norm, take the dispute to court. The theorists argue that courts should invariably enforce the procedural norm rather than the substantive norm. Why?

Another factor contributing to the uncertainty of intent is multiple agents. Entities are parties to most contracts, and entities can act only through agents. Different agents may negotiate a contract, draft the documents, approve the deal, and receive and evaluate the performance under the agreement. Agency law resolves some questions of how to determine contractual “intent,” under such doctrines as apparent authority<sup>21</sup> and imputed knowledge.<sup>22</sup> But the application of these doctrines is often uncertain, and in any case, they do not address all issues of contractual intent involving agents. In particular, many contract disputes arise when an entity’s agents who negotiated the contract are not the same ones seeking to enforce or escape it later.<sup>23</sup> When, for example, management changes, is the new management bound by the intent of the old management?

Thus, we should be wary of theoretical justifications for strict liability that depend on overly confident assertions of mutual intent. Otherwise, a theory that supposedly favors judicial humility and encourages efficient contracting instead fosters judicial hubris and causes inefficient interference with contract. Acknowledging the uncertainty of intent opens the door to fault.

#### IV. THE DICHOTOMY BETWEEN FAULT AND INTENT

Just as the justifications for strict liability rely on relative certainty about mutual intent, they also rely on a strong dichotomy between intent and fault. But the uncertainty of intent blurs this dichotomy. When intent is uncertain, fault can help inform intent in a variety of ways. Most obviously, parties may expressly use fault concepts in their contracts, such as best efforts<sup>24</sup> and good faith<sup>25</sup> clauses, which essentially invite courts to make fault-based judgments in the event of a dispute.

Second, parties may intend to be governed by fault standards even if they do not expressly say so. Courts often find fault standards to be implied in the contract.<sup>26</sup> Most commonly, in professional services contracts, courts presume that the professional does not intend to guarantee results, and the

---

21. See, e.g., RESTATEMENT (THIRD) OF AGENCY § 2.03 (2005).

22. See, e.g., *id.* § 5.03 cmt. d(1). U.C.C. § 1-202(f) (2005) adopts a version of imputed knowledge for organizations. Also, § 1-103 incorporates agency law.

23. See, e.g., *Nanakuli Paving & Rock Co. v. Shell Oil Co.*, 664 F.2d 772 (9th Cir. 1981) (discussing a dispute that arose when new management failed to continue prior unwritten price protection policy); *Int’l Telemeter Corp. v. Teleprompter Corp.*, 592 F.2d 49 (2d Cir. 1979) (discussing a dispute that arose when new management refused to proceed with negotiated settlement agreement).

24. See generally KENNETH A. ADAMS, A MANUAL OF STYLE FOR CONTRACT DRAFTING 88–94 (2004).

25. See, e.g., *Channel Home Ctrs. v. Grossman*, 795 F.2d 291 (3d Cir. 1986) (holding enforceable a contractual duty to bargain in good faith contained in a letter of intent).

26. The classic case is *Wood v. Lucy, Lady Duff-Gordon*, 118 N.E. 214 (N.Y. 1917) (Cardozo, J.).

client agrees to accept the professional standard of care.<sup>27</sup> In agency contracts, courts imply duties of care and loyalty.<sup>28</sup> Courts often apply similar standards to other service contracts.<sup>29</sup>

Third, contracting parties often draft terms designed to discourage certain conduct. Although these terms do not explicitly mention fault, fault may help explain the purpose behind these terms and therefore facilitate their interpretation. For example, “satisfaction clauses” in construction contracts protect owners against shoddy work by builders, but courts often limit an owner’s ability to reject a builder’s work if that purpose would not be served.<sup>30</sup> Contingency payments discourage shirking, but if satisfactory effort occurs, courts sometimes allow recovery under the *quantum meruit* doctrine even if the contingency has not occurred.<sup>31</sup>

Fourth, fault can help resolve a conflict between plausible competing interpretations of intent by focusing on narrower grounds. Courts may be more confident about whether the parties intended to prohibit specific conduct in a particular circumstance than about which of two interpretations ought to prevail more generally.<sup>32</sup>

Finally, fault may be inconsistent with contractual intent. Contracts may expressly or impliedly limit the application of fault. For example, courts interpret express and implied warranties as strict liability standards.<sup>33</sup> Similarly, courts interpret option contracts<sup>34</sup> and (more controversially and less consistently) employment-at-will contracts to give absolute discretion to one

---

27. See, e.g., RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 52 cmt. b (1998) (stating that a lawyer is not a guarantor of successful outcome).

28. See, e.g., RESTATEMENT (THIRD) OF AGENCY §§ 8.01, 8.08 (2005).

29. For example, in *Milau Associates, Inc. v. North Avenue Development Corp.*, 368 N.E.2d 1247 (N.Y. 1977), the court rejected the application of the implied warranty of fitness to a contract for the installation of a sprinkler system, finding instead that “unless the parties have contractually bound themselves to a higher standard of performance, reasonable care and competence owed generally by practitioners in the particular trade or profession defines the limits of an injured party’s justifiable demands.” *Id.* at 1250. The court added that “[g]iven the predominantly service-oriented character of the transaction, neither the code nor the common law of this State can be read to imply an undertaking to guard against economic loss stemming from the nonnegligent performance by a construction firm which has not contractually bound itself to provide perfect results.” *Id.* at 1251.

30. See, e.g., RESTATEMENT (SECOND) OF CONTRACTS § 228 (1981); *Morin Bldg. Prods. Co. v. Baystone Constr., Inc.*, 717 F.2d 413 (7th Cir. 1983) (Posner, J.).

31. See, e.g., RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 40.

32. Cf. Robert S. Summers, “Good Faith” in *General Contract Law and the Sales Provisions of the Uniform Commercial Code*, 54 VA. L. REV. 195 (1968) (arguing that good faith should be defined with reference to specific acts done in bad faith).

33. See U.C.C. §§ 2-313, 2-314, 2-315 (2005); RESTATEMENT (SECOND) OF CONTRACTS § 266 cmt. b, illus. 7.

34. See, e.g., E. ALLAN FARNSWORTH, CONTRACTS § 3.23, at 176 (4th ed. 2004). Economic scholars have become enamored with analogizing many contract terms and doctrines to options. See, e.g., Avery Wiener Katz, *The Option Element in Contracting*, 90 VA. L. REV. 2187 (2004). While the analogies can be enlightening, one danger of them is that they too casually smuggle the strict liability connotation of options to other areas where plausible arguments can be made for fault-based approaches. That is, option analogies put the strict liability rabbit in the hat.

or both parties, thereby making fault irrelevant.<sup>35</sup> On the other hand, sometimes fault trumps inconsistent intent to further a different goal of contract law, especially the protection of third parties.<sup>36</sup>

The above discussion, however, suggests several caveats against too quickly assuming inconsistency between intent and fault.<sup>37</sup> Sometimes what appears to be a conflict between fault and intent may in reality reflect different interpretations of uncertain intent.<sup>38</sup> Moreover, terms limiting fault require interpretation about how far these limits extend. The parties' endorsement of fault in one part of their relationship may evidence their intent to extend fault more broadly rather than to limit its application.<sup>39</sup> Fault considerations may reappear if the reason for excluding fault does not apply.<sup>40</sup>

#### V. THE MEANING OF CONTRACTUAL FAULT

The recognition that intent is often consistent with fault does not establish whether, in the face of uncertain intent, courts ought to presume that the parties intend fault-based liability. One argument for presuming such intent is that contractual fault is inefficient conduct that parties would want to discourage. Economists have identified three types of contractual fault: failure to take precautions, failure to mitigate, and opportunism.<sup>41</sup> Precaution taking is most generally associated with the superior-risk-bearer concept, which assigns contracting risks to the party better able to bear those risks, and presumes that the parties intended this result. Though itself fault based, the superior-risk-bearer idea could, as discussed above, support strict liability if the promisor is so often the better precaution taker that the benefits of making individualized fault assessments are not worth the costs.

---

35. See, e.g., FARNSWORTH, *supra* note 34, § 7.17, at 499–500.

36. See, e.g., RESTATEMENT (SECOND) OF CONTRACTS § 178 (stating when contract terms are unenforceable on grounds of public policy).

37. Compare, e.g., Cohen, *Interpretation*, *supra* note 2, at 84–85 (discussing whether good faith is better viewed as a mandatory or default rule), with VICTOR GOLDBERG, FRAMING CONTRACT LAW (2006) (criticizing court interpretations of good faith as inconsistent with mutual intent).

38. The classic statement remains Cardozo's: "From the conclusion that promises may not be treated as dependent to the extent of their uttermost minutiae without a sacrifice of justice, the progress is a short one to the conclusion that they may not be so treated without a perversion of intention." *Jacob & Youngs, Inc. v. Kent*, 129 N.E. 889, 891 (N.Y. 1921).

39. In a recent case explicitly referencing the strict liability principle, a court found that a commercial landlord breached a contractual obligation to secure tenant consent in connection with selling the property, in part because the parties used "best efforts" clauses elsewhere in the contract but not in connection with the tenant approval obligation. *West Willow-Bay Court, LLC v. Robinobay Court Plaza, LLC*, No. 2742-VCN, 2007 Del. Ch. LEXIS 154, at \*14 (Ch. Nov. 2, 2007). An alternative interpretation would be that the "best efforts" clauses reflected the parties' view of the landlord's obligations generally rather than exceptions to strict liability.

40. Thus, insurance contracts are usually considered strict liability obligations, yet the *contra proferentem* doctrine deems the insurer at fault for drafting ambiguous contracts, see, e.g., JOHN EDWARD MURRAY, JR., MURRAY ON CONTRACTS § 88G, at 483–84 (4th ed. 2001), and the bad faith breach doctrine punishes insurers who unreasonably try to avoid their contractual obligations, see, e.g., FARNSWORTH, *supra* note 34, § 12.8, at 762.

41. See Cohen, *Negligence-Opportunism Tradeoff*, *supra* note 2, at 944–61.

In many cases, the promisor is in a good position to take cost-effective precautions that would reduce or eliminate the risk of nonperformance. These precautions range from quality control to backup supplies to purchasing insurance to not promising in the first place. In many other cases, however, the promisee is better able to take precautions, for example by restraining reliance or assisting the promisor.<sup>42</sup>

But precaution taking is merely one aspect of contractual fault, and not always the most important.<sup>43</sup> For example, the parties may be equally able to take precautions or there may be no cost-effective precautions that either party can take. Precaution taking matters most when contract failures most resemble unintentional torts: accidental contracts and accidental contingencies.<sup>44</sup> An accidental contract is one the parties should not have made; that is, it was jointly unprofitable at the time of formation, but one or both parties did not know that. An accidental contingency is an event arising after contract formation that makes the contract jointly unprofitable and therefore one that, from an economic perspective, the parties should no longer perform. Both cases naturally raise the question whether the contracting parties could have taken reasonable precautions to prevent the contract or the contingency, for example by investing more in information.

On the other hand, if the contract is jointly profitable at the outset and remains so, but a “regret contingency” occurs that makes the contract less profitable for one side, then mitigation and opportunism often become more important than precaution taking.<sup>45</sup> Mitigation is an action, taken after a contingency occurs, that reduces the losses caused by that contingency, such as obtaining substitute performance. Contract doctrine focuses solely on promisee mitigation as a limitation on damages.<sup>46</sup> Often, however, the promisor is the superior mitigator. For example, promisors can repair or replace their defective performance, or purchase market substitutes. Just as the case for strict liability is stronger when the promisor is more likely the superior risk bearer, so it is stronger when the promisor is more likely the superior mitigator (the superior mitigator concept being merely a variation on superior risk bearer). If, however, the promisee is often the superior mitigator, as the mitigation of damages doctrine recognizes, the case for strict liability is weakened.

---

42. See, e.g., Ariel Porat, *A Comparative Fault Defense in Contract Law*, 107 MICH. L. REV. 1397, 1398–1403 (2009).

43. See, e.g., U.C.C. § 1-201(b)(17) (2005) (defining “fault” broadly as “a default, breach, or wrongful act or omission”); *id.* § 2-613 cmt. 1 (fault includes both negligence and willful wrong). See generally Cohen, *Negligence-Opportunism Tradeoff*, *supra* note 2.

44. See Cohen, *Fault Lines*, *supra* note 2, at 1245–52 (discussing accidental contracts); *id.* at 1258–65 (discussing accidental contingencies).

45. See Charles J. Goetz & Robert E. Scott, *The Mitigation Principle: Toward a General Theory of Contractual Obligation*, 69 VA. L. REV. 967, 972–73 (1983).

46. See RESTATEMENT (SECOND) OF CONTRACTS § 350 (1981). The Restatement recognizes the “willful failure to mitigate” as a form of bad faith. *Id.* § 205 cmt. e.

Apart from precautions and mitigation, there is another form of contractual fault that plays a large role in contracts and contract law: opportunism.<sup>47</sup> One party in a contractual relationship often takes, or fails to take, some action that creates the possibility of loss to the other; that is, one party becomes vulnerable to opportunistic expropriation by the other, with “opportunistic” defined as contrary to the parties’ agreement, contractual norms, or conventional morality.<sup>48</sup> In the paradigmatic case, one party makes a relationship-specific investment, leaving the investing party vulnerable to threats by the other to deprive him of his investment.<sup>49</sup> Specific investments can occur before or after contract formation.<sup>50</sup> Similarly, a party may intend to act opportunistically from the outset or form the intent after the specific investment occurs.

Opportunistic behavior can occur even absent specific investments. All opportunism requires is some change in position (“reliance”) growing out of the contractual relationship that exposes one party to loss that the other party can intentionally impose. This vulnerability can arise in various ways. If performance is sequential, one party may provide a benefit to the other party who then tries to keep that benefit without performing his reciprocal obligations.<sup>51</sup> Or one party may forego other contracting opportunities, which then become unavailable when market conditions change.<sup>52</sup> Or one party may provide information to the other party, who then uses the information to the first party’s disadvantage.<sup>53</sup> Or one party may act negligently and the other party knowingly tries to exploit rather than correct the problem.<sup>54</sup> Finally, contract terms and contract law doctrines often create the potential for opportunistic exploitation by a party seeking to apply those rules to unintended situations.<sup>55</sup>

As with the other forms of fault, strict liability makes sense if the promisor is almost always the most likely opportunist. But that is not the case. Moreover, as I have argued in previous work, the better precaution taker and

---

47. See, e.g., POSNER, *supra* note 14, at 93–94; Timothy J. Muris, *Opportunistic Behavior and the Law of Contracts*, 65 MINN. L. REV. 521 (1981).

48. Cohen, *Negligence-Opportunism Tradeoff*, *supra* note 2, at 957.

49. See, e.g., Schwartz & Scott, *supra* note 13, at 559–62.

50. See, e.g., Cohen, *Negligence-Opportunism Tradeoff*, *supra* note 2, at 960–61.

51. POSNER, *supra* note 14, at 93–94.

52. See, e.g., RESTATEMENT (SECOND) OF CONTRACTS § 19 cmt. a, illus. 1 (1981); *id.* § 90 cmt. d, illus. 10.

53. See, e.g., Cohen, *Finding Fault*, *supra* note 2, at 150.

54. See, e.g., RESTATEMENT (SECOND) OF CONTRACTS § 49 (stating that an offeree cannot accept beyond deadline if offeror negligently delayed in communicating the offer but offeree knows or has reason to know of the delay); *id.* § 153 (allowing relief for unilateral mistake if the other party had reason to know of the mistake or his fault caused it).

55. I disagree with the argument that formalist approaches to contract law create less possibility for opportunistic behavior than alternative approaches. See Schwartz & Scott, *supra* note 13, at 585–89, 601–05.

the most likely opportunist are often different parties.<sup>56</sup> Contract disputes, then, present questions not only about which party is the best precaution taker, but also which party is the best mitigator and which is the most likely opportunist. The case for strict liability is strongest when the promisor is all three. In my view, however, the likelihood that the promisee is more at fault on one or more of these criteria is high enough in litigated cases that strict liability is not generally justified.

## VI. FAULT IN CONTRACT DOCTRINE

If, as I have argued, mutual intent and efficiency often support fault-based rather than strict liability, contract doctrine does not stand in the way. In fact, the language and architecture of contract doctrine strongly reflect the pervasive influence of fault.

Contract doctrine contains numerous direct expressions of fault. The Restatement and UCC include the following terms, all of which naturally invite a fault inquiry: best efforts,<sup>57</sup> diligence,<sup>58</sup> fault,<sup>59</sup> fraudulent,<sup>60</sup> good (and bad) faith,<sup>61</sup> injustice (and justice and unjust),<sup>62</sup> justified,<sup>63</sup> know and reason to know,<sup>64</sup> mitigate,<sup>65</sup> negligent,<sup>66</sup> precaution,<sup>67</sup> reasonable,<sup>68</sup> unconscionable,<sup>69</sup> and willful.<sup>70</sup> The ubiquity of fault terms strongly suggests a vital role for fault in contract doctrine, though the bewildering and seemingly ad hoc variety of terms scattered across the doctrinal landscape obscures the extent and nature of that role.

Two prime examples of rules in the Restatement expressly incorporating fault standards are section 20 on misunderstanding and section 201 on interpretation.<sup>71</sup> Interestingly, these two sections not only directly link mutual intent to fault but adopt a relative fault standard. Under these essentially

---

56. In my earlier work, I argued that deterring opportunism should take priority over deterring negligence in contract law when one party is the least-cost avoider and the other is the most likely opportunist. See Cohen, *Negligence-Opportunism Tradeoff*, *supra* note 2.

57. See, e.g., U.C.C. § 2-306 (2005).

58. See, e.g., RESTATEMENT (SECOND) OF CONTRACTS §§ 54(2)(a), 56, 67.

59. See *infra* note 90 and accompanying text.

60. See, e.g., U.C.C. § 2-702(2).

61. See, e.g., *id.* § 2-103(j).

62. See, e.g., RESTATEMENT (SECOND) OF CONTRACTS § 90.

63. See, e.g., *id.* § 164.

64. See *infra* text accompanying notes 71–74.

65. See, e.g., RESTATEMENT (SECOND) OF CONTRACTS § 350 cmt. b.

66. See, e.g., *id.* § 19 cmt. c.

67. See, e.g., *id.* § 66.

68. See, e.g., *id.* § 228.

69. See, e.g., U.C.C. § 2-302 (2005).

70. See RESTATEMENT (SECOND) OF CONTRACTS § 261. cmt. d.

71. *Id.* §§ 20, 201.

similar doctrines, if the parties agree on a meaning, that meaning prevails. If they attach “different meanings” to their agreement, no contract exists if neither is at fault or both are equally at fault.<sup>72</sup> If, however, one party’s fault exceeds the other’s, a contract exists and the meaning of the party whose fault is greater loses.<sup>73</sup> Fault is determined by whether a party “knows” or has “reason to know” of the other’s meaning. One might be tempted to dismiss sections 20 and 201 as minor and uniquely fault-based doctrines. But the fact that they address how courts should handle uncertain intent makes them foundational.

One might also ask how these doctrines square with the objective theory of contract. The objective theory is based on manifestations that have “objective” meanings.<sup>74</sup> The “attached meanings” of sections 20 and 201 seem subjective rather than objective. Nevertheless, sections 20 and 201 are consistent with the objective theory, if that theory is understood in fault terms. The objective theory presumes that when one party manifests some intent and then later asserts a different intent, either he negligently or intentionally misled the other party originally, or is acting opportunistically now.<sup>75</sup> That is, the party manifesting intent, i.e., the promisor, “knows or has reason to know that the other party may infer from his conduct that he assents,”<sup>76</sup> precisely the standard of sections 20 and 201. If, on the other hand, the promisee’s fault exceeds that of the manifesting promisor, the justification for the objective theory disappears.<sup>77</sup>

Even when a doctrine is not expressed in fault language, its purpose may be to discourage opportunistic or negligent behavior. For example, the statute of frauds,<sup>78</sup> the parol evidence rule,<sup>79</sup> and the consideration doctrine<sup>80</sup> all aim, at least to some extent, to deter assertions of false promises. Similarly, the market damage rule discourages opportunistic breaches to take

---

72. *Id.* §§ 20(1) & cmt. d, 201(3).

73. *See, e.g.*, *Hub Recycling, Inc. v. Louis Usdin Co.*, 106 B.R. 372 (D.N.J. 1989) (applying § 201 to interpret Pollution Exclusion Clause against insurance company on ground that it knew insured’s intended meaning). The Restatement rules on trade and other usages also incorporate a “knows or has reason to know” standard. RESTATEMENT (SECOND) OF CONTRACTS §§ 220, 221, 222; *see also* U.C.C. § 1-303(d) (stating that trade usage of which the parties “are or should be aware” can be used to interpret the agreement); RESTATEMENT (SECOND) OF CONTRACTS § 211(3) (excluding term of standardized agreement if party who drafts it “has reason to believe” that other party would not have agreed to a particular term if he knew about it).

74. RESTATEMENT (SECOND) OF CONTRACTS § 2 cmt. b.

75. Cohen, *Negligence-Opportunism Tradeoff*, *supra* note 2, at 979–80.

76. RESTATEMENT (SECOND) OF CONTRACTS § 19(2). The objective theory also uses the term “justify” to incorporate fault considerations. *See id.* § 2 (“A promise is a manifestation of intention . . . so made as to justify a promisee in understanding that a commitment has been made.”); *id.* § 24 (similar definition of offer).

77. For a recent critique of the objective theory sounding some similar themes, see Lawrence M. Solan, *Contract as Agreement*, 83 NOTRE DAME L. REV. 353 (2007).

78. *See, e.g.*, FARNSWORTH, *supra* note 34, § 6.1, at 356.

79. *See, e.g.*, Eric A. Posner, *The Parol Evidence Rule, the Plain Meaning Rule, and the Principles of Contractual Interpretation*, 146 U. PA. L. REV. 533 (1998).

80. *See, e.g.*, POSNER, *supra* note 14, at 100.

advantage of a change in market price while encouraging mitigation.<sup>81</sup> Many contract doctrines, then, incorporate fault-based presumptions, even if not obviously directed at fault. Exceptions or alternative doctrines cover situations that do not fit the presumptions. Flexibility in doctrinal choice presents opportunities for courts to make relative fault assessments. In what follows, I offer some representative examples of fault in each of the main doctrinal areas of performance, damages, and formation.

With respect to performance, the doctrine of impracticability invariably crops up as a counterexample to strict liability. This is somewhat surprising.<sup>82</sup> The traditional presumption of impracticability, that neither party anticipated and protected against some risk,<sup>83</sup> emphasizes mutual innocence of the parties, not fault.<sup>84</sup> The traditional approach, however, takes an unduly narrow view of fault. Impracticability reflects a concern with promisee fault other than precaution taking. Specifically, courts tend to excuse a promisor from bearing some risk if the promisee is the superior mitigator,<sup>85</sup> or perhaps the superior insurer.<sup>86</sup>

Even if one disagrees that the impracticability doctrine itself is fault based, fault inevitably influences the doctrine. Because of uncertainty in determining what relevant risks the parties assumed when contracting, impracticability doctrine gives promisors a vehicle for claiming excuse opportunistically—for example, by falsely alleging that performance was truly impracticable. The doctrine tries to reduce the risk of promisor opportunism that it introduces. For one thing, courts tend to reject promisor claims of excuse when the promisor can easily mitigate by providing a substitute performance.<sup>87</sup> On the other hand, courts are more willing to grant excuse when the changed circumstances are less subject to promisor manipulation, such as in cases involving the promisor's death<sup>88</sup> or destruction of a particular thing.<sup>89</sup> Moreover, the doctrine allows the promisee to challenge the application of the doctrine by proving promisor "fault."<sup>90</sup>

---

81. Cohen, *Fault Lines*, *supra* note 2, at 1319–20.

82. A more apt example is the substantial performance doctrine and *Jacob & Youngs, Inc. v. Kent*, 129 N.E. 889 (N.Y. 1921), discussed in Cohen, *Negligence-Opportunism Tradeoff*, *supra* note 2, at 990–1000, as well as in a number of papers in this Symposium.

83. RESTATEMENT (SECOND) OF CONTRACTS § 261 (1981).

84. See SMITH, *supra* note 12, at 383.

85. See GOLDBERG, *supra* note 37, at 334–39 (arguing that excuse is justified to encourage promisee to economize on getting nonfungible substitute).

86. See POSNER, *supra* note 14, at 105–08. For a critique of the superior insurer theory, see MICHAEL J. TREBILCOCK, *THE LIMITS OF FREEDOM OF CONTRACT* 130–36 (1993).

87. See, e.g., U.C.C. § 2-614(1) (2005).

88. RESTATEMENT (SECOND) OF CONTRACTS § 262.

89. *Id.* § 263.

90. See U.C.C. § 2-613 (“Where . . . goods suffer casualty without fault of either party . . . the contract is avoided . . .”); RESTATEMENT (SECOND) OF CONTRACTS § 261 (“Where . . . a party’s performance is made impracticable without his fault . . . his duty to render that performance is discharged . . .”); *id.* § 265 (“Where . . . a party’s principal purpose is substantially frustrated without his fault . . . his remaining duties to render performance are discharged . . .”). Somewhat

The existence and structure of excuse doctrine are neither accidental nor aberrational. The pattern found here recurs throughout contract doctrine. Some rule aims to deter faulty behavior by one party, but in doing so creates an incentive for faulty behavior by the other party. Contract law then creates an exception or limitation to deter that behavior, and so on. Regardless of whether the doctrine uses express fault terms, the doctrine as a whole contains both fault-based presumptions and doctrinal vehicles by which the parties can introduce fault assessments to overcome those presumptions.

With respect to contract damages, I have previously argued that the choice among different measures of damages (expectation, reliance, and restitution), as well as the limitations on expectation damages, are best understood as doctrines enabling courts to make relative fault assessments.<sup>91</sup> In fact, damages doctrines are best suited to dividing liability when both parties are at fault. In light of this crucial role of damages in facilitating relative fault assessments, the resistance of courts to “penalty clauses,” which preclude such assessments, is eminently sensible, despite the continued objection of many economic scholars.

Finally, formation doctrine seems to mirror performance doctrine in that it presumes promisee fault in failing to secure an agreement, just as performance doctrine presumes promisor fault in failing to perform. But various formation doctrines allow fault considerations when this presumption does not hold. For example, the “know or has reason to know” standard of sections 20 and 201 appears in several offer and acceptance rules.<sup>92</sup> The “acceptance by silence” doctrine, for example, uses the standard both to encourage precaution taking by promisor-offerees in acquiring relevant information and to discourage opportunistic ignorance of potentially harmful information.<sup>93</sup> By the same token, a promisee cannot forestall the other party’s ability to acquire further information necessary to evaluate the deal by opportunistically insisting on the deal’s closure and enforceability when the promisee has reason to know the other party is still investigating.<sup>94</sup>

Strict liability theorists might point to the absence of a duty of good faith in contract formation.<sup>95</sup> One reason contract law excludes the duty of

---

surprisingly, the term “fault” appears in the Restatement and UCC almost exclusively in connection with excuse doctrines.

91. See Cohen, *Fault Lines*, *supra* note 2.

92. See RESTATEMENT (SECOND) OF CONTRACTS §§ 26, 54, 69. The “reason to know” standard also appears in other contexts. For example, a party with reason to know of another party’s special needs may have an obligation to take special precautions to protect the other party. See U.C.C. § 2-315 (stating that reason to know creates implied warranty of fitness); *id.* § 2-715(2)(a) (stating that seller’s reason to know of buyer’s general or particular requirements and needs makes seller potentially liable for consequential damages); *cf.* RESTATEMENT (SECOND) OF CONTRACTS § 351(1) (“reason to foresee” standard).

93. See, e.g., *McGurn v. Bell Microproducts, Inc.*, 284 F.3d 86 (1st Cir. 2002) (remanding for factual findings on whether employer accepted employee’s counteroffer by silence under § 69 because it knew or had reason to know that employee had written counteroffer on employer’s original offer and returned it to employer).

94. See RESTATEMENT (SECOND) OF CONTRACTS § 26.

95. See U.C.C. § 1-203; RESTATEMENT (SECOND) OF CONTRACTS § 205 cmt. c.

good faith from formation is to allow parties to misrepresent certain information about themselves to protect their private information and their investment in that information, thereby enabling them to obtain a larger share of the contractual surplus.

Once again, however, a rule that seems designed to preclude fault considerations instead merely defines the boundaries of such considerations. Other doctrines deter parties from opportunistically abusing other kinds of information in the contract formation process. For example, one party cannot mislead the other about the likelihood of a deal to obtain more time to evaluate the deal.<sup>96</sup> Nor can one person use negotiations to extract and then expropriate beneficial information from another without paying for it.<sup>97</sup>

A final example from formation doctrine is the concept of “justice” in reliance doctrines.<sup>98</sup> Reliance doctrines developed to thwart what courts perceived to be opportunistic attempts by promisors to escape liability through strict interpretations of various formation doctrines: consideration, offer and acceptance, and the statute of frauds.<sup>99</sup> But as is well understood, promisee reliance does not itself prove promisor opportunism. And reliance-based liability itself can lead to opportunistic investments in or assertions of reliance by promisees. So once again, contract doctrine provides an outlet for making relative fault assessments, by limiting the application of reliance doctrines to situations in which “justice” requires enforcement.

## VII. THE INEVITABILITY OF FAULT

Even if one disagrees with my conclusions that fault often comports with mutual intent and believes that contract doctrine should be revised to reduce further or eliminate entirely the role of fault in contract law, there is an additional problem with a systematic strict liability regime: it cannot work. Law is an inherently normative enterprise of which judges are a part. Judges are not automatons; they exercise judgment, which includes making normative assessments like fault. Fault is a metric by which courts assess the gap between formalist concepts and normative reality.

Coase emphasized that parties can often contract around unwanted legal rules.<sup>100</sup> But we sometimes forget the parallel legal-realist lesson (the Court

---

96. See, e.g., *Markov v. ABC Transfer & Storage Co.*, 457 P.2d 535 (Wash. 1969) (involving a tort action of misrepresentation based on promise of lease renewal made while promisor was looking to sell the premises).

97. See, e.g., *Reeves v. Alyeska Pipeline Serv. Co.*, 56 P.3d 660 (Alaska 2002) (finding implied contract where promoter disclosed idea for visitor center in return for confidentiality or participation in project).

98. See RESTATEMENT (SECOND) OF CONTRACTS §§ 84(2)(b), 87 cmt. e, 89, 90, 129, 139(1). In performance doctrine, the rules regarding conditions and material breach speak of “forfeiture” rather than reliance, but the idea is similar. *Id.* §§ 227, 229, 241. In remedy doctrine, the foreseeability limitation on expectation damages also contains a “justice” limitation, *id.* § 351(3), as do the remedial provisions for mistake, *id.* § 158(2), and impracticability, *id.* § 272(2).

99. See generally Charles L. Knapp, *Reliance in the Revised Restatement: The Proliferation of Promissory Estoppel*, 81 COLUM. L. REV. 52 (1981).

100. See R.H. Coase, *The Problem of Social Cost*, 3 J.L. & ECON. 1 (1960).

Theorem, perhaps?): courts can often find ways to exercise discretion. In contract cases, courts can incorporate fault judgments by interpreting contract terms, manipulating contract doctrine, or using legal doctrines outside of contract, such as tort. Game theorists fail to capture this phenomenon because they model courts as setting the rules the parties play by and then largely disappearing from the scene.<sup>101</sup> In reality, courts as well as contracting parties are players in an ongoing game. Different judges (and the same judge in different cases) will of course vary in their inclinations toward strict liability or fault approaches. But sooner or later, fault will out.

#### CONCLUSION: A ROLE FOR STRICT LIABILITY, AND FAULT

Although I have argued that the strict liability view of contract law needs to be significantly qualified, I recognize the source of the strict liability impulse. That impulse is strongest when a persuasive story of presumptive promisor fault exists. For example, strict liability seems natural in debt contracts and contracts for the sale of goods. We are comfortable interpreting these contracts as allocating the risk of changes in financial circumstances or market price, or requiring perfect tender, in large part because of the assumption of easy promisor substitutability. These situations are certainly not trivial in contract law. Nevertheless, they are far from describing the full spectrum of contract disputes. Even in goods cases, the conditions for strict liability are often not satisfied. In those situations, we should expect to see, and do see, courts incorporating fault standards into contract law.

In short, calling contract law a strict liability system emphasizes its commitment to deterring promisor fault. But strict liability, like other contract rules, is merely a fault-based presumption. We may reasonably disagree about how strong the presumption is or ought to be. But determining the limits of that presumption inevitably means considering why parties do not perform their contracts, in other words, fault.

Scholars and courts should embrace and help shape the fault that lies within our contract law, rather than theorize as if it does not or should not exist.

---

101. See generally Eric A. Posner, *Economic Analysis of Contract Law After Three Decades: Success or Failure?*, 112 *YALE L.J.* 829 (2003) (summarizing game theoretic models of contract).