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'Agreeing to Disagree': Filling Gaps in Deliberately Incomplete Contracts

Omri Ben-Shahar

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OMRI BEN-SHAHAR*

INTRODUCTION

Incomplete contracts have always been viewed as raising the following challenge for contract law: does the incompleteness—or, "indefiniteness," as it is usually called—rise to such a level that renders the agreement legally unenforceable? When the indefiniteness concerns important terms, it is presumed that the parties have not reached an agreement to which they intend to be bound. This "fundamental policy" is the upshot of the view that "contracts should be made by the parties, not by the courts."[1] When, in contrast, the indefiniteness concerns less important terms, courts supplement the agreement with gap fillers and enforce the supplemented contract.

The common law has traditionally tended towards the no-contract outcome. For example, an agreement to pay an employee "a fair share" of the profits, without specifying the precise fraction, was too indefinite to be enforced.[2] This traditional result has been weakened under the Uniform Commercial Code's (the "Code") "contract with open terms" approach that more aggressively supplements the parties' agreement with reasonable or average terms, including price terms.[3]

Many areas of contracting have witnessed significant shifts from the common law's formalist no-contract outcome to the more liberal gap filling and enforcement approach embodied in the Code. However, both the traditional common law and the Code continue to share the premise that the problem of indefiniteness is of a dichotomous nature: either a full-blown contract can be assembled with the aid of gap fillers, or no contract exists. These are the only two choices. Regimes and

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* Professor of Law and Economics, University of Michigan Law School (omri@umich.edu). I benefited from helpful comments and suggestions by Ian Ayres, Oren Bar-Gill, Nili Cohen, Ted Parson, Ariel Porat, Omri Yadlin, and workshop participants at Boston University, Georgetown, Michigan, Tel-Aviv University, Wisconsin, and Yale Law Schools, and the contracts panel at the 2004 annual meeting of the American Law and Economics Association. Manny Shachmurove provided valuable research assistance. Financial assistance from the John M. Olin Center for Law and Economics at the University of Michigan Law School is gratefully acknowledged.

1. RESTATEMENT (SECOND) OF CONTRACTS § 33(2) cmt. b (1981).
2. *See, e.g.*, Varney v. Ditmars, 111 N.E. 822, 823 (N.Y. 1916).
3. U.C.C. § 2-204(3) (2002).

jurisdictions may differ as to where the boundary between contract and no-contract lies, but they all follow the all-or-nothing methodology.

This Article proposes a different methodology. It advances the idea that *partial agreements may deserve partial enforcement*. If a deal is only partially struck, because it contains pockets of indefiniteness, the law should not be limited to choosing the polar solutions of full enforcement or no enforcement. Instead, the law should have available an intermediate solution of holding the parties accountable only to the definite parts of the agreement. The more definite the deal is, the greater the contractual liability.

This Article identifies an important category of situations in which parties intentionally drafted their agreement indefinite, leaving issues that were difficult to resolve for future completion. In these situations, contractual incompleteness is neither a result of haste nor of unforeseeability, but rather a deliberate choice to temporarily *disagree* over some matters, to sidestep difficult issues over which consensus could not be reached. It is here, in the presence of partial assent, that "partial enforcement" could be desirable.

In these setting of deliberate incompleteness, the familiar standards of filling gaps, using either reasonable hypothetical consent ("mimicking" or "majoritarian" default rules), or information-forcing one-sided provisions ("penalty" default rules), are not suitable for filling gaps in such deliberately incomplete contracts. They are not suitable because they provide *definitive* default terms, which prevent the parties from leaving their deal legally binding and incomplete. That is, under the familiar standards of gap filling, if parties recognize and anticipate the content of the gap filler, then the set of *legal obligations* governing the transaction—whether explicit or supplemented—is no longer incomplete. Effectively then, in the presence of definitive default terms, no additional assent is needed and the parties are deprived of the power—which they may have sought to maintain—to affirmatively approve or veto the missing terms.

Instead, this Article proposes a new approach to gap filling: a party who seeks enforcement of a deliberately incomplete agreement would be granted an option to enforce the transaction under the agreed-upon terms supplemented with terms that are the *most favorable* (within reason) to the defendant. I will call this gap-filling principle a "pro-defendant" default rule. If a buyer and a seller agree on many provisions but leave others, such as payment terms, "to be agreed upon," then each party should be able to enforce a deal supplemented by payment terms that are most favorable to the other party. The buyer should be able to enforce a deal in which payment is made in cash, in full, upfront; and the seller should be able to enforce a deal in which the buyer is granted the generous credit terms that the buyer sought. The incomplete contract is

supplemented by a "decoupled" default provision, either payment in cash or lenient credit terms, depending on the identity of the enforcing party. Effectively, a deliberately incomplete contract becomes the legal equivalent of *two* complete contracts, each favorable to a different party, with each party entitled to enforce only the contract favorable to its opponent.

To understand the novelty of this gap-filling approach, compare its prescription to those of other gap-filling approaches in a contract with a missing price. For example, consider a landlord and a tenant who agreed on the subject matter of the lease and all other terms, but left the price term open. Imagine that the reasonable monthly rent for such property varies from $3000 to $5000. Under the "mimicking" approach to gap filling, the court ought to set a "fair and reasonable" price, reflecting the rent in the majority of comparable leases, which is somewhere between $3000 and $5000, perhaps $4000. Under the "penalty" default-rule approach, the court might want to set the price biased against the party who drafted the agreement (contra-proferentem), to provide that party with incentives to draft the price term explicitly. If it were the landlord who drafted the vague contract, the supplemented price would be $3000. Under the pro-defendant gap-filling approach that is developed here, the price term would depend on the party seeking enforcement. If the tenant is the party trying to enforce the deal, then she can only do so at a price of $5000, most favorable to the landlord. And if it is the landlord who is suing for enforcement, then he can only get a price of $3000, most favorable to the tenant.

Of course, the selection of a gap-filling standard should not be arbitrary, but should depend on the reason for the incompleteness. Thus, the mimicking gap filler should apply when the parties wanted to save the cost of explicit agreement and intended to apply an average or market term. The penalty gap filler should apply when one of the parties—in the above example, the landlord—is responsible for the vagueness and could have resolved it cheaply by making an explicit stipulation. And, along the argument that will be developed in this Article, the pro-defendant gap filler should apply when the parties failed to reach consensus over this issue and left it deliberately indefinite. Specifically, it should apply in the common scenario in which the parties left this term "to be agreed upon," preserving mutual veto power.

This Article develops various justifications for the pro-defendant gap-filling approach. First, it suggests that, on conceptual grounds, this outcome reflects more precisely the intent of the parties who drafted a deliberately indefinite agreement or an agreement-to-agree. These parties have reached some consensus, a partial commitment, and thus a no-contract result would frustrate their achievement. But at the same

time they failed to reach consent over the missing term, rendering false the presumption of "hypothetical consent," which lies at the basis of the mimicking default rule. Further, while it is reasonable for the defendant to reject a court-imposed "compromise" term on the grounds that she explicitly reserved her right to veto such compromises in the hope of securing better-than-average terms, it would be unreasonable for the defendant to reject a deal containing her most favorable terms. Surely, when she entered the indefinite agreement, the best terms she must have intended to secure are these "most favorable" terms (although she may have soberly hoped to get terms that are less one-sided). What grounds then, does the defendant now have to reject a deal that grants her such terms? Such a one-sided deal, we can say for certain, is the one deal that does not conflict with the enforced-against party's initial intent. Although she reserved the veto power, it is not such favorable terms that she intended to veto.

This Article suggests that the pro-defendant gap-filling approach serves additional goals. First, it will be shown that this regime provides negotiating parties with greater security against unilateral retractions by their counterparts, thus enhancing the incentives to make precontractual investments. This greater precontractual investment, in turn, increases the overall contractual pie. Second, the binding nature of precontractual agreements enables parties to break down the big commitment into smaller piecemeal commitments accumulated sequentially. These two effects increase the chances that negotiations will succeed and that full agreement will eventually be achieved.

The proposed pro-defendant gap-filling approach is not merely a theoretical possibility, but rather a viable technique recognized (and occasionally applied) by courts adjudicating incomplete agreements. Part IV of this Article will survey the variety of contexts in which courts have considered pro-defendant gap fillers, and how courts managed to identify the content of the defendant's most favorable term. To briefly illustrate one such context, consider the case of *Ontario Downs Co. v. Lauppe*, which involved an agreement for the sale of 16 acres of land for $50,000, but left for further agreement where within the seller's 450-acre lot the land would lie.[4] When the seller retracted, the negotiations were not yet resumed and the lot was never identified. In the suit by the buyer, the court rejected the no-contract outcome but at the same time refused to designate a reasonable parcel. Instead, the court instructed that the contract can only be enforced with respect to a parcel that seller would designate. Effectively, the contract was supplemented with a term—the parcel of land—most favorable to the defendant.

4. 13 Cal. Rptr. 782, 782, 784, 786 (Dist. Ct. App. 1961).

Similarly, there is a substantial line of cases in which the parties left the payment terms open "to be agreed upon," where courts applied the doctrine of "cure by concession" and allowed the buyer to enforce the deal if she agrees to make a full payment in cash and with no delay, namely, in a manner most favorable to the seller.[5] When the agreement is supplemented in such a pro-defendant manner, "there is no longer any way the provision may be construed to [the defendant's] detriment,"[6] and thus it is guaranteed not to violate the defendant's original intent.

This Article develops the theory of pro-defendant gap fillers in four parts. Part I briefly reviews the law of indefiniteness and the existing theory of gap filling. Part II identifies situations in which contracts are left deliberately incomplete and demonstrates that existing standards of gap filling do not provide an adequate solution to these situations. Part III develops the concept of pro-defendant default provisions, and argues that they are suitable to fill gaps in deliberately incomplete contracts. Finally, Part IV explores, as just explained, various doctrinal uses of the pro-defendant gap-filling technique.

I. INDEFINITE AGREEMENTS AND GAP FILLING

A. The Law of Gap Filling

1. THE PROBLEM OF INDEFINITENESS

A contract is indefinite when it does not address a material aspect of the deal. Some seemingly unresolved aspects could be overcome by courts through liberal interpretation of meaning or by reference to context (e.g., prior oral agreements, course of performance). But other unresolved aspects cannot because the parties simply failed to reach agreement or to manifest any type of inferable assent over these matters. These contracts suffer from indefiniteness.

Traditionally, the common law regarded indefinite contracts as lacking mutual assent and unenforceable. The justification for this policy was often stated in terms of an absence of the intent to be bound. Because the underlying question is always whether the parties intended to contract, the more issues left unresolved, the stronger is the inference

5. RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 1, § 33 illus. 2 ("A agrees to sell and B to buy a specific tract of land for $10,000 . . . [and] to lend B the amount, but the terms of loan are not stated . . . . The contract is too indefinite to [enforce] against B, but B may [enforce it] if he offer to pay the full price in cash.").

6. Busching v. Griffin, 542 So. 2d 860, 864 (Miss. 1989).

that no such intent ripened.[7] Accordingly, if the missing terms were sufficiently material, the contract would have been unenforceable.

This approach, often viewed as formalistic and harsh, was reformed under the Code. Under the Code, indefiniteness—whether inadvertent or a result of inability to agree—can be cured by filling the gaps. Indeed, the Code provides gap fillers for almost every aspect of the deal, and gives broad permission for courts to fill gaps by incorporating practices and unwritten customs.[8] Here, too, the underlying principle is that the parties' intent to contract should be the ultimate test. However, the Code's gap-filling jurisprudence is founded on a different empirical basis. The empirical premise is that agreements are intended by the parties to be binding even when they leave, as they often do, many terms open.[9]

There is some debate as to whether modern courts take the doctrine of indefiniteness seriously. On the one hand, the Code's liberal gap-filling platform, imitated by the *Restatement (Second) of Contracts* (the "Second Restatement"),[10] gives grounds for the belief that parties can nowadays enforce contracts with almost any term left open, as long as the circumstances indicate the intent to be bound. Gap fillers are available on price, payment terms, duration, delivery terms, and many others,[11] effectively constituting a standardized statutory contract.[12] On the other hand, some evidence has recently been collected that the doctrine of indefiniteness continues to play a major role in court decisions, barring the supplementation and enforcement of gap-ridden agreements.[13] However, regardless of the extent to which the doctrine of indefiniteness continues to bar enforcement, it is clear that both the traditional common law and the Code regard indefinite contracts as posing a problem of binary choice. Either a full-blown contract can be assembled with the aid of gap fillers, or the contract is unenforceable. It is an all-or-nothing choice.

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7. *See* RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 1, § 33 cmt. c ("The more terms the parties leave open, the less likely it is that they have intended to conclude a binding agreement.").

8. U.C.C. § 2-204(3).

9. *Id.* § 2-204 (stating that "commercial standards on the point of 'indefiniteness' are intended to apply").

10. RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 1, § 33.

11. U.C.C. §§ 2-304 to -310.

12. *See, e.g.*, JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE § 3-4 (4th ed. 1995).

13. *See, e.g.*, Robert E. Scott, *The Theory of Self-Enforcing Indefinite Agreements*, 103 COLUM. L. REV. 1641, 1652–61 (2003) (analyzing a sample of cases with indefinite contracts, many of which were not enforced).

2. AGREEMENTS TO AGREE

Agreements to agree are a particular type of indefinite agreement that have received special attention and have been adjudged under a more particularized set of rules. In agreements to agree, parties affirmatively acknowledge the indefiniteness of their agreement and state their intent (or hope) that further negotiations will enable them to reach a more complete agreement. When the further negotiations fail and no agreement emerges, courts are usually unwilling to apply gap fillers and enforce the contract.[14] Interestingly, the missing terms, which the parties left for further negotiation and agreement, are no more material than terms that courts readily supplement into other indefinite agreements.[15] It is not the materiality of the terms per se that prevents gap filling, but rather the fact that the parties explicitly identified them as the subject matter for further affirmative agreement. Apparently, the inference many courts draw is that when parties agree to agree, they have not yet agreed and thus they do not yet intend to be bound. Such agreements merely mark a stage in the precontractual negotiations in which certain substance has been resolved and should be memorialized.[16]

While agreements to agree are normally deemed unenforceable, other closely related forms of preliminary agreements are more regularly enforced. For example, "agreements in principle" or agreements "subject to a contract," in which parties draft the outline of their agreement and acknowledge that some details need to be worked out, are held enforceable even in cases where they are quite bare.[17]

It might appear, then, that the jurisprudence of precontractual agreements in general, and of agreement to agree in particular, exhibits that same "all-or-nothing" feature that characterizes the doctrine of indefiniteness. Either the precontractual agreement manifests sufficient intent to be bound so as to be supplemented and enforced, or it does not manifest such intent and is unenforceable. In this area of precontractual

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14. 1 ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 2.8 (Joseph M. Perillo ed., rev. ed. 1993).

15. For example, when the contract is silent about payment terms, the Code instructs that full payment "is due at the time and place at which the buyer is to receive the goods." *See* U.C.C. § 2-310(a). However, when parties agree to agree on payment terms, the agreement may be deemed unenforceable. *See* Ansorge v. Kane, 155 N.E. 683, 685 (N.Y. 1927).

16. *See, e.g.*, Empco Mfg. Co. v. Ball-Co Mfg., Inc., 870 F.2d 423, 425 (7th Cir. 1989) (stating that letters of intent and agreement to bargain are only a stage in the negotiations and do not give rise to liability).

17. Texaco, Inc. v. Pennzoil Co., 729 S.W.2d 768, 788–89 (Tex. Ct. App. 1987) (holding that the agreement-in-principle is a binding contract because there was intent to be bound).

liability, however, the all-or-nothing characteristic is eroding. In practice, even when the agreement does not rise to a full-blown contract and is deemed unenforceable for the purpose of contractual remedies, the parties' freedom to walk away from it has been somewhat limited by courts. With the emergence of the good-faith duties, courts have increasingly limited the privilege of parties, who made serious albeit partial precontractual manifestations of intent, to retract.[18] The *freedom from contract* that parties in these situations historically enjoyed was constrained. Specifically, many courts have been requiring parties who entered agreements to agree to indeed make an honest effort to reach an agreement, and have been tailoring some measure of reliance liability to a breach of this duty.[19] Accordingly, an arbitrary decision by a party to walk away from the negotiation could give rise to liability without requiring the court to supplement missing terms.

B. The Theory of Gap Filling

Filling gaps in incomplete contracts was elevated from a context-specific inquiry to a generalizable theory when it was noticed that while contractual gaps vary in contexts and in substance, there are unifying rationales to filling them. Although gaps concerning contingent voting rights in a complex merger agreement have nothing in common with gaps concerning missing payment dates in a lease contract, the formula by which the law fills these gaps—what judges have to consider in order to generate the gap filler—may have a lot in common.

The reason there can be competing theories of gap filling is the recognition that there exist different systematic sources for incompleteness. Gaps in contracts are not random holes, but arise from identified imperfections in the negotiation process. Diagnosing these imperfections yields solutions for redressing them, namely, standards for filling the gaps.

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18. *See, e.g.*, E. Allan Farnsworth, *Precontractual Liability and Preliminary Agreements: Fair Dealing and Failed Negotiations*, 87 COLUM. L. REV. 217, 223-43 (1987) [hereinafter Farnsworth, *Precontractual Liability*] (describing the different grounds for precontractual liability); Charles L. Knapp, *Enforcing the Contract to Bargain*, 44 N.Y.U. L. REV. 673, 679-81 (1969) (explaining the emergence of the obligation to negotiate in good faith as an intermediate solution between the traditional all or nothing results).

19. *See, e.g.*, Teachers Ins. & Annuity Ass'n of Am. v. Tribune Co., 670 F. Supp. 491, 498-99 (S.D.N.Y. 1987); Copeland v. Baskin Robbins U.S.A., 117 Cal. Rptr. 2d 875, 885 (2002). Some courts, while following *Tribune Co.*, assign expectation liability for the breach of "*Tribune*-duties." *See, e.g.*, Venture Assocs. Corp. v. Zenith Data Sys. Corp., 987 F.2d 429, 432 (7th Cir. 1993) (stating that unless too uncertain, expectation remedies should be awarded).

Accordingly, it is often said that there are two distinct efficiency-based theories for gap filling.[20] Each of these theories diagnoses a different reason for the contractual incompleteness, and provides gap fillers that address the diagnosed source of incompleteness. In order to succeed in developing an additional theory of gap filling, it will be necessary to identify a different source of incompleteness, one that is not addressed by existing gap-filling formula. Before doing that, however, let us briefly recall the existing theories.

1. MIMIC THE PARTIES' WILL

One reason for incompleteness is the cost of drafting a complete agreement. An agreement that addresses all possible contingencies involves costly negotiations and drafting. The underlying premise is that a complete contingent agreement can be reached, if only the parties invest sufficient effort and attention to the details. But the cost of attending to the fine details and to remote contingencies may exceed the benefit from doing so, making it rational to leave gaps in the agreement.[21]

The assumption that transactions costs are the reason for incompleteness generates a "mimicking" principle of gap filling. The law should equate the missing provisions with the hypothetical consent—the terms the parties would have agreed upon. By mimicking the parties' hypothetical will, the law is enabling the parties to save the transaction costs of drafting these very same terms expressly. Or, put differently, by *correctly* mimicking the parties' will, the law is enabling the parties to save the transaction costs of expressly opting out of the legal default rules.

The mimicking theory is based on a premise that there exists an underlying "will" or hypothetical consent. Namely, there are specific definitive terms that the parties would have rationally agreed upon had they paid sufficient attention to the matter. The only challenge is to identify these terms. Accordingly, if the judicial task of identifying the hypothetical consent is straightforward, then courts can tailor individually optimal gap fillers: ones that are rational for *these* parties.

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20. *See, e.g.*, Ian Ayres, *Default Rules for Incomplete Contracts*, *in* 1 THE NEW PALGRAVE DICTIONARY FOR ECONOMICS AND THE LAW 585 (Peter Newman ed., 1998) [hereinafter Ayres, *Default Rules*]; Richard Craswell, *Contract Law: General Theories*, *in* 3 ENCYCLOPEDIA OF LAW AND ECONOMICS 1 (Boudewijn Bouckaert & Gerrit de Geest eds., 2000). For the argument that the two gap-filling theories are merely two perspectives on one unifying approach, see Lucian Ayre Bebchuk & Steven Shavell, *Reconsidering Contractual Liability and the Incentive to Reveal Information*, 51 STAN. L. REV. 1615, 1618–19 (1999).

21. FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 3 (1991); Craswell, *supra* note 20, at 3.

And if the judicial task of identifying the hypothetical consent is more difficult, in light of the heterogeneity of contracting parties and the uncertainty concerning the circumstances, then courts could use "majoritarian" or "one-size-fits-all" default rules: ones that are rational for most similarly-situated parties.[22] Either way, the rationale for choosing the content of any default provision is to minimize transaction costs: the cost of opting into specific terms. Mimicking defaults appropriately addresses the drafting cost source of incompleteness.

2. PENALTY DEFAULT RULES[23]

Another reason for incompleteness of a contract has to do with information asymmetry. When parties are differently informed about an aspect of the deal, they may either draft provisions that are suboptimal, or neglect to address an issue that otherwise, in the presence of perfect information, would have been addressed. For example, a party may fail to alert her counterpart to the fact that she assigns idiosyncratically high value to performance, resulting in the counterpart failure to take the necessary higher precaution against breach. Since private information can be advantageous, it may not be revealed, which leaves the agreement that should optimally be tailored to the content of this information, incomplete.

If the one-sidedness of information is the cause of contractual incompleteness, gap fillers can be designed to induce information sharing. They can do so by "punishing" the informed party. If, in the presence of contractual silence, the default provision is unfavorable to the informed party, then this party will be induced to opt-out of it by drafting an express provision. In the process of reaching such an express agreement, information is shared and the information asymmetry is overcome. Thus, for example, if the default remedy for breach of contract is limited to "average" or foreseeable damages, then the party who stands to suffer high idiosyncratic profit loss from breach will have the incentive to draft a higher liquidated damage provision. This liquidated damage provision thereby communicates her private information about her expected profit. Such gap fillers are often named "information-forcing" default rules.

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22. Ayres, *Default Rules*, *supra* note 20, at 586.

23. The term "penalty default rules" was coined in Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87, 91 (1989). A similar information-cost theory of gap filling was developed contemporaneously by Lucian A. Bebchuk & Steven Shavell, *Information and the Scope of Liability for Breach of Contract: The Rule of* Hadley v. Baxendale, 7 J.L. ECON. & ORG. 284, 286 (1991).

3. DEFINITIVE DEFAULT RULES

The mimic-the-parties'-will approach and the penalty defaults approach share at least one important common feature: they both supplement the parties' obligation with a definitive provision. To the extent that the parties can anticipate what the gap filler would be—and both theories rely on the parties' ability to anticipate the gap fillers[24]—the set of *legal obligations* governing the transaction is fully determined. Whether the obligations are based on express provisions or on legally supplied default terms, they are definitive.[25]

But definitive default terms are not the only conceptual way to deal with ambiguity. Consider by analogy computer software. Programs always start with preset defaults that usually represent the average user's preferences—what most people would have selected if they had the chance to try and experience different settings. These are definitive majoritarian defaults. One can also imagine penalty defaults, utilizing settings that most users would not want, eliciting setting reversals and "preference revelation." But some features are set such that no prior setting is selected; requiring that the user will make an affirmative selection (e.g., click one of several buttons) or else the feature will not be activated and the process will be stalled. These are nondefinitive defaults: the settings are not fully determined (although they might be narrowed down to several popular choices), but as a result of the different selections made by different users, the program will eventually run with each user's most favorable setting. In the analysis below, I will argue that contractual ambiguity could potentially be dealt with in a similar manner, utilizing nondefinitive default options.

II. DELIBERATE INCOMPLETENESS

A. When Do Parties Prefer Indefiniteness?

Once it is concluded that the parties entered into a binding agreement, default rules—whether mimicking or penalty defaults—supplement any incompleteness in the agreement with *definitive* and predictable terms. This basic feature of gap-filling law has the implication that parties cannot create liability while leaving any of their *obligations* legally blank. If they want to create liability, then whatever

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24. *See generally* Craswell, *supra* note 20; E. ALAN FARNSWORTH, CONTRACTS §§ 1.10, 7.15, at 36, 495 (3d ed. 1999) (stating that courts assume that parties recognize the default provisions and can opt out of them).

25. Indeed, by its legal definition a "contract" cannot be incomplete. U.C.C. § 1-201(12) (2003) (defining "contract" as "the total legal obligation that results from the parties' agreement as determined by [the Code]," and including all the gap fillers).

obligation they leave unresolved the law would eventually supply. True, it might be unclear at the time of the agreement how the law would supplement the missing term, but it is clear that if the agreement would be held binding, it would be supplemented. Thus, imagine a situation in which parties who negotiate over an aspect of the deal cannot reach consent. If they leave this issue open, and if the gap is not too severe to render the contract unenforceable due to indefiniteness, a gap filler will kick in to resolve the issue. But the parties would anticipate this and realize that leaving a blank is equivalent to agreeing to a definitive term that is identical to the gap-filler. That is, when gaps are filled by definitive default provisions, parties are effectively precluded from leaving an issue unresolved.

This feature of contract law could, at times, conflict with the parties' interests. In the discussion to follow, I will argue that there is both a theoretical and an empirical basis for the claim that parties have an interest in unresolved agreements. In a nutshell, the parties may want to leave an issue unresolved when they want actual, rather than inferred consent to govern. That is, each party may seek to maintain a veto power over the specific term to avoid having to surrender to a compromise which she never embraced. Parties may seek to maintain the power to *reject* any undesired term. At the same time, they want the other issues that were already agreed upon not to be reopened unilaterally. Once this claim is established, it will provide the necessary foundation for a different approach to gap filling, one that does not utilize definitive defaults.

1. CONCEPTUAL GROUNDS

Can rational parties choose to leave part of their agreement deliberately incomplete? One way to think about this, which was offered in a thought-provoking and influential paper by mathematician Robert Aumann, is to characterize situations in which parties may *agree to disagree*.[26] Aumann showed this agree to disagree situation to be possible by identifying the conditions for the *opposite* to be true: when it is that parties *cannot* agree to disagree. The logic of his claim is, roughly, the following: if one party knows that the other party's view is different from his own, she should revise her own view so as to take into account the fact that the other party may have some different information justifying her view.[27] The other party would follow the

26. Robert J. Aumann, *Agreeing to Disagree*, 4 ANNALS STATS. 1236, 1236 (1976).

27. More precisely, a player's updating should occur only if the player shares common "priors," such that a player can attribute the opponent's differing view to "new information," rather than a "bias." It also requires that the shared priors be common

same updating process. Thus, for example, if two doctors have differing views or predictions on how a certain medical procedure would affect the patient, each basing her view on her own prior experience, then each would rely on the other doctor's position as a valid reason to update her own. As long as their views are different, this convergence-by-inferences dynamic will remain in action. In equilibrium, the parties' views will converge.

The lesson from Aumann's insight is not that disagreements are impossible, but rather that different opinions or views among rational parties can be maintained only in the presence of initial *biases* or *prejudices*. In the doctors example, they may remain in disagreement if, say, each considers her own training as superior (a "prejudice"), or if each is influenced by the salience of her own prior experience (a "bias"). Disagreements cannot be solely attributed to one-sided information. Information-based differences in views "wash out."[28]

Aumann's theorem, by articulating the conditions under which disagreement would be overcome also tells us the flip side, namely, when a disagreement *cannot* be overcome—when parties will agree to disagree. It suggests that even rational parties who are willing to update their own views in light of the views of others may fail to reach consensus, if they either have different priors (biases or prejudices), or if their private information is not sufficiently well communicated to trigger the inference process.

When an "agreement to disagree" results from different initial beliefs on what is going to happen, there is little reason to expect that the parties would eventually be able to resolve their differences. If parties attribute the gap in their positions not to private information but to a preference-based divergence, they would not reach consensus. If a buyer and a seller negotiating the sale of a firm have different probability assessments concerning the future profitability of the firm that are not based on private information but rather on psychological factors, prejudices, or tastes, then agreement may permanently elude them.

On the other hand, an "agreement to disagree" may also occur even when parties are not influenced by such biases, but instead find it difficult to credibly communicate views and information. For example, the buyer of the firm may be ready to infer that the firm is worth more than she thought if she figures out why the seller is asking for a high price. While the seller's information cannot be directly conveyed, his

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knowledge. *See, e.g.*, DREW FUDENBERG & JEAN TIROLE, GAME THEORY § 14.3.2, at 548–49 (1991).

28. *See* Moriss H. DeGroot, *Reaching a Consensus*, 69 J. AM. STAT. L. ASS'N 118, 118 (1974).

assessments can. As long as the buyer cannot reliably infer all that the seller knows, disagreement may persist.

Interestingly, disagreement that arises from a difficulty to communicate the underlying information between the parties may be short lived. Over several rounds of communicating each other's opinions the parties would eventually revise their views, infer each other's information, and reach agreement.[29] An interim negotiation stage may exhibit an agreement to disagree, to be resolved later as more updating takes place.

In real-life negotiations, this interim stage might be a long one. Parties may be unable to agree on an issue, but still recognize that their inability to agree could eventually be overcome as more of their private information is credibly shared. This perceived "temporariness" of the disagreement could manifest itself in a phased agreement, whereby parties postpone the resolution of some term of their agreement. While the decision-theoretic model of agreeing to disagree explains the paradoxical logic of such agreements, one may still wonder why parties bother to enter into an initial partial agreement. Why do they not wait until negotiations reach a more advanced state and enter into the full blown agreement then? One answer to this puzzle, which will be discussed below, focuses on incentives to rely. It will be shown that "agreeing now to agree later"[30] could be an optimal approach for the parties to focus their precontractual investments by ruling out other possible terms. But before turning to the utility of phased agreements, let us first briefly discuss the prominence of this practice.

2. NEGOTIATION PRACTICES

Parties to complex negotiations may deliberately choose to leave parts of their agreement incomplete. This incompleteness is not an oversight but a strategy aimed at increasing the chance for success. To begin with, in complex deals it is not possible to tackle all issues simultaneously. Consensus is achieved piecemeal as different aspects of the transaction are brought up. There usually comes a point in the negotiations when sufficient issues are resolved that some commitment between the parties becomes desirable. The arrival at partial agreement does not represent a conclusion or a negotiation peak, but rather a

29. For a model in which agents need several rounds to revise their opinions and to reach consensus, see generally John D. Geanakoplos & Heraklis M. Polemarchakis, *We Can't Disagree Forever*, 28 J. ECON. THEORY 192 (1982).

30. This term is the title of an intriguing discussion paper. Oliver Hart & John Moore, *Agreeing Now to Agree Later: Contracts that Rule Out but Do Not Rule In* (Nat'l Bureau of Econ. Research, Working Paper No. w10397, 2004), *available at* http://papers.nber.org/papers/w10397.pdf.

necessary stage toward a more complete agreement. At this stage, parties expect that the remaining issues will be resolved through continued negotiations.

Agreements are not achieved at once because the resolution of various issues involve different degrees of difficulty. The parties may believe that the obstacles to agreement for some issues may subside after most of the transaction is determined, or that future negotiations may succeed where present negotiations failed. For instance, change in external conditions or the identity of the negotiating agents may remove a roadblock to agreement. Parties may also set aside sticky issues in the hope that they might be able to sidestep them, as when the likelihood of a relevant contingency declines.

Specifically, it is commonly recognized in negotiation manuals that contentious issues should be avoided in initial stages of the negotiation as they might "place unbearable strain on the overall settlement process."[31] Parties are encouraged to tackle easier issues first to reach as much consensus as possible, thereby increasing their own motivation and incentive to find ways to resolve the contentious issues.[32] Or each may believe that delay will result in a more favorable resolution.[33] The effort spent to reach partial agreement, the dynamic of goodwill from this effort, and the increased awareness of the potential surplus from a complete agreement may create a context amenable to the resolution of the remaining issues.[34]

This "agreeing-to-disagree" strategy, it should be noted, is different than the negotiation strategy of resorting to a third party's neutral arbitrational authority. The latter strategy exposes each party to greater risk by removing their veto power. Such third-party resolution is appropriate for parties who are willing to accept a compromise, but have conflicting views on what is fair. But in the situations discussed above, parties are not yet ready to commit to a compromise and prefer to

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31. DAVID A. LAX & JAMES K. SEBENIUS, THE MANAGER AS NEGOTIATOR 97 (1986) (noting that parties should avoid contentious issues that may render agreement impossible).

32. FRED CHARLES IKLÉ, HOW NATIONS NEGOTIATE 1, 18 (1964) ("If there is a conflict about many issues, the less controversial ones should be solved first because agreement will lead to further agreement . . . . [and a]greements on disagreement . . . . can be used to isolate unsettled issues so as to facilitate agreement on other matters."); GEOFFREY R. WATSON, THE OSLO ACCORDS 309 (2000) ("One puzzle-solving heuristic is to solve the easy part of the puzzle first; once that part is solved, the harder parts of the puzzle may seem easier.").

33. *See, e.g.*, LAX & SEBENIUS, *supra* note 31, at 96–97 ("Negotiations often leave much ambiguity with the tacit understanding that a definite resolution of the issue perhaps strongly favoring one party will later become necessary.").

34. *Id.* at 222; ROBERT H. MNOOKIN, SCOTT R. PEPPET & ANDREW S. TULUMELLO, BEYOND WINNING: NEGOTIATING TO CREATE VALUE IN DEALS AND DISPUTES 251 (2000).

maintain their veto power over a nonconsensual resolution. If anything, "agreeing to disagree" is similar to *nonbinding* mediation agreements. In such situations, parties believe that a procedure of incremental commitments would increase their chances of success.

In any event, when parties leave their agreement deliberately incomplete, they are making a commitment to be bound to the agreed upon terms, conditional on the remaining terms being resolved in a manner satisfactory to them. While this is *not* a commitment to the full-blown contract that was not yet finalized, it is a commitment to the relationship and to refrain from unilateral departure.[35] A complete freedom to walk away would conflict with the subtle dynamics of the negotiation and indicate that even resolved issues can be unilaterally reopened, thus diminishing the value of initial understandings. Since this value generates further agreement, a norm of unrestricted freedom to retract would be detrimental to the successful resolution of a negotiation.

For example, in the context of negotiations between states a bargaining norm of no-retraction-from-preliminary-understandings is recognized. When a negotiating party manifests its position, it is considered improper to "revert to a harder position from a more conciliatory one."[36] Treaties are negotiated article-by-article and

> [w]hile it is understood that the parties are not bound by their acceptance to individual articles in the way they are bound by the conclusion of a final agreement, each party expects that its opponent will generally preserve agreed parts as the building blocks for the overall agreement. The very fact that the parties laboriously negotiate with each other to settle their issues point by point constitutes an implied promise that yesterday's work will not be destroyed tomorrow by reopening these partial agreements.[37]

In fact, international negotiators do not share private law's legalistic view that agreements to agree are not enforceable. In treaty law, "there

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35. LAX & SEBENIUS, *supra* note 31, at 279–80 (emphasizing the informal sanctions of breaking contingent agreements); ROY J. LEWICKI ET AL., NEGOTIATION: READINGS, EXERCISES, AND CASES 100 (2d ed. 1993) (advocating that negotiators strategically make only tentative commitments until an entire agreement is reached).

36. IKLÉ, *supra* note 32, at 22–23.

37. *Id.* at 99. This argument does not conflict with the common practice of "issue trading," whereby concessions already made can be traded away to win agreement over a stalemated issue. In fact, the only reason that a party might have the power to *trade* away a concession is the informal recognition by the other party that this concession is otherwise not freely retractable. *See* G. RICHARD SHELL, BARGAINING FOR ADVANTAGE 170 (1999).

is little doubt that parties can enter in legally binding 'agreements to agree.'"[38]

3. THE BENEFITS OF GRADUAL COMMITMENT

The argument thus far suggests that agreements to disagree are both logically possible and are regularly used to embody a mild form of commitment in practice, but it has yet to explore the reasons why such intermediate forms of commitment should *not* be freely retractable under the law. Shouldn't parties be free to walk away anytime prior to full agreement without suffering legal consequences? In thinking about what negotiating parties gain from constraining their mutual ability to walk away before full agreement is reached, there are various sources of value that might be recognized. One type of benefit has to do with psychological and cognitive effects that are associated with a gradual compromise. Concessions that may be hard to make if framed as a lumpy, measurable departure from the ideal terms may be easier to digest in small portions.[39] Here, the value of entering into partial commitments in the intermediate stage is the fragmentation of the otherwise hard to swallow large commitment. (Is this not the major reason why premarital commitments grow gradually as a common feature preceding the full-blown marriage?) Thus, if parties were free to walk away anytime prior to a full formal agreement, these partial understandings would amount to naught, and the potential for a gradual progression of the commitment would be forfeited.

Another benefit arising from the existence of a precontractual commitment has to do with the integrity of the negotiation process. It is increasingly recognized by legal writers that when the risk of parties walking away is diminished, the ritual of contract negotiation is taken more seriously. Greater trust emerges when parties enter the bargaining when they are ready to do business and refrain from making misleading gestures.[40] Put differently, the signal that an entrance into negotiations transmits with respect to the propensity of a party to work towards a deal is more powerful the greater is the sanction for walking away.[41]

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38. WATSON, *supra* note 32, at 65.

39. *See, e.g.*, ROBERT C. CIALDINI, INFLUENCE: SCIENCE AND PRACTICE 15 (2d ed. 1988) ("The trick is to bring up the options independently of one another so that each small price will seem petty when compared to the already-determined much larger price.").

40. *See, e.g.*, Hoffman v. Red Owl Stores, 26 Wis. 2d 683, 687-88, 696-97, 699, 133 N.W.2d 267, 269, 274-75 (1965); Farnsworth, *Precontractual Liability*, *supra* note 18, at 220.

41. This "signaling" effect is recognized in the international negotiations literature. *See, e.g.*, Lloyd Jensen, *Soviet-American Behavior in Disarmament Negotiations*, *in* THE 50% SOLUTION: HOW TO BARGAIN SUCCESSFULLY WITH HIJACKERS,

Why is some form of interim commitment useful for the parties? We might worry that the opposite is true, that any form of precontractual commitment—any limitation of the *freedom from contract*—might cause parties to think twice before entering negotiations. Such precontractual commitments, if backed up by legal liability, might chill incentives to bargain and reduce the incidence of surplus-creating negotiations.[42]

One explanation for the value-enhancing effect of precontractual liability focuses on the incentives to invest in the relationship.[43] In the same manner that contractual liability is instrumental in promoting reliance on the contractual promise, precontractual liability can be instrumental in promoting reliance on the partial, precontractual commitment. Such precontractual reliance on negotiations can take many forms. It may involve the forgoing of opportunities to negotiate with other partners,[44] loss of job offers and promotions,[45] training and investment in relationship-specific assets,[46] aequisition or sharing of information,[47] investment in the real estate by a potential tenant,[48] and many more. These are costly activities that parties undertake in order to increase the size of the "pie" that any agreement would subsequently divide.

In the absence of some kind of commitment, parties will apply greater caution and expend less in precontractual reliance, in fear that such investment might be wasted if the other party walks away, or that

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STRIKERS, BOSSES, OIL MAGNATES, ARABS, RUSSIANS, AND OTHER WORTH OPPONENTS IN THIS MODERN WORLD 289 (I. William Zartman ed., 1976).

42. *See* 1 E. ALLAN FARNSWORTH, FARNSWORTH ON CONTRACTS § 3.64, at 384 (3d ed. 2004) (describing "an undesirable chilling effect" discouraging parties from entering negotiations); Jason Scott Johnston, *Communication and Courtship: Cheap Talk Economics and the Law of Contract Formation*, 85 VA. L. REV. 385, 416–17, 445–46 (1999) (arguing that liability for pretrade representations in the event of negotiation breakdown would "cause the market to shrink" and force parties to utilize more cautious bargaining strategies, thus wasting opportunities for efficient trade).

43. Several scholars have argued that liability can enhance precontractual reliance. Richard Craswell, *Offer, Acceptance, and Efficient Reliance*, 48 STAN. L. REV. 481, 482–83 (1996); Avery Katz, *When Should an Offer Stick? The Economics of Promissory Estoppel in Preliminary Negotiations*, 105 YALE L.J. 1249, 1308–09 (1996). For a formal analysis of the particular rules of liability that can induce efficient reliance, see generally Lucian A. Bebchuk & Omri Ben-Shahar, *Precontractual Reliance*, 30 J. LEGAL STUD. 423 (2001).

44. *Tribune Co.*, 670 F. Supp. at 498–99.

45. Grouse v. Group Health Plan, Inc., 306 N.W.2d. 114, 115 (Minn. 1981).

46. *Hoffman*, 26 Wis. 2d at 696–97, 133 N.W.2d at 274–75.

47. Venture Assoc. Corp. v. Zenith Data Sys., 96 F.3d 275, 278 (7th Cir. 1996) ("[Complex negotiations] often [are] costly and time-consuming. The parties may want assurance that their investments in time and money and effort will not be wiped out by the other party's footdragging or change of heart or taking advantage of a vulnerable position created by the negotiation.").

48. Hammond v. Ringstad, 10 Alaska 543, 544 (D. Alaska 1945).

reliance will make them vulnerable to hold-up by the other party. The benefits a party can enjoy from any reliance investment are diminished by the chance that the deal will fall through or by the ability of the other party to expropriate some of the surplus created by the investment. Indeed, this is one reason why parties who enter complex and costly negotiations are careful to first agree on some precontractual arrangements for cost reimbursement in the event that negotiations fail.[49]

Accordingly, parties enter into partial agreements and agreements to agree in the hope that they will have some binding force to provide some measure of security and encourage each other to keep investing in the success of the relationship. Because it is costly to invest in negotiations, each party must sacrifice some freedom to walk away in order to encourage the other party to negotiate. The precontractual commitment enables a party to commit to a specific *partner* and a specific negotiation protocol without committing to specific *terms*. In the presence of such a commitment, the risk each party faces of her counterpart's unilateral abandonment of the relationship is diminished. Greater relationship-specific investment emerges with this added confidence, and with greater investment a profitable full-blown contract is more likely to arise.

Another way to think about the value of a partially binding agreement to agree is to recognize the "self-fulfilling prophecy" that it embodies: when parties are faced with issues that are difficult to resolve, the memorialization of the resolved issues and an agreement to agree over the unresolved issues—if coupled with some liability for breakdown—helps the parties resolve the remaining issues. The notion that an agreement to agree is a "contradiction in terms"[50] and that a contract to make a contract is conceptually impossible overlooks this self-fulfilling effect. A contract to make a contract, if it is associated with some liability, can make the subsequent contract more likely. Part III will explore an intermediate liability regime that creates this gradual commitment effect.

B. The Inadequacy of Standard Gap Fillers

Having argued that contractual gaps can arise from the transactors' deliberate choice to phase the agreement process, the next step of the

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49. *See, e.g.*, Ronald J. Mann, *Contracts—Only with Consent*, 152 U. PA. L. REV. 1873 (2004) (surveying a variety of self-imposed precontractual liability schemes); Russell J. Weintraub, *A Survey of Contract Practice and Policy*, 1992 WIS. L. REV. 1, 27 (showing that most firms make irrevocable offers).

50. Shepard v. Carpenter, 55 N.W. 906, 906 (Minn. 1893) (finding that "an agreement that they will in the future make such contract as they may then agree upon amounts to nothing"); Ridgway v. Wharton, 6 Eng. Rep. 237, 268 (1857); *see also* 1 CORBIN, *supra* note 14, § 2.8, at 134.

argument is to demonstrate that standard approaches to gap filling are ill-equipped to address the needs and concerns that give rise to such deliberate gaps. Standard gap-filling techniques provide a single definitive provision that the parties are assumed to anticipate. When the parties take into account the legally supplied default term, they cannot effectively leave portions of their deal unresolved for future negotiation and agreement. Whether it is the express agreement or the background default rules that define the totality of obligations, there is a fully determined set of legal obligations. No further stipulation of terms by the parties is required.[51]

For example, if an explicit agreement over price is absent but the law supplements the contract with a definitive term, either the reasonable majoritarian price or a contra-proferentem (penalty) price provision, then the parties would recognize this default provision and consider the deal to be obligationally complete.[52] Contracting in the shadow of this definitive default term is equivalent to explicitly drafting this term into the contract. Any desire that the parties might have had to reach a binding commitment and to leave the price term open for future voluntary resolution would be frustrated by a court-imposed compromise.

Put differently, once it is recognized that the gap in the agreement is due neither to drafting costs nor to one-sided superior information, there is no prima facie reason to expect that either a mimicking or a penalty-default provision would be desirable. Often, parties endure long and costly negotiations before deciding to leave a term open. In these cases, parties search for ways to explicitly state the incompleteness of their agreement, which is probably more costly to draft than a definitive reasonable provision. That is, the saving of drafting costs—the rationale of the mimic-the-parties'-will theory—cannot explain the gap. Similarly, the failure of the parties to agree on a term is not necessarily due to one party's superior information. True, nonagreement may arise as a result of each party safely hiding his or her private information or reservation value. However, this is not the type of one-sided information that the law is necessarily interested in forcing out of the parties by means of a penalty default. In these deliberate incompleteness

51. The law recognizes interim forms of agreement, under which the obligations are not fully determined but the parties are required to negotiate them in good faith. *See Tribune Co.*, 670 F. Supp at 498. Here, however, the incomplete agreement is wholly unenforceable. A breach of the good-faith duty usually does not give rise to contract damages.

52. True, the parties would have to be able to anticipate what price the court would supplement, but their ability to do so is the foundation of standard default rule theories. Without it, parties cannot be assumed to opt out of non-mimicking defaults and cannot be incentivized to reveal private information in opting out of penalty defaults.

cases, the underlying justifications for standard gap-filling techniques are not valid.

C. The Inadequacy of the No-Enforcement Approach

When a contract is recognized to be deliberately incomplete, it is usually thought that the correct legal response is to refrain altogether from filling the gap due to absence of assent. After all, each party had a different term in mind, and they manifested a preference to have an incomplete set of obligations and to postpone further agreement until a later date. Contract enforcement requires an objectively manifested meeting of the minds and here we have an indication of the opposite, of an absence of consent.

The problem with this no-supplementation regime is that it implies nonenforcement of the entire (albeit partial) agreement reached by the parties.[53] If the court does not supply a definitive term, then it is impossible to determine the plaintiff's expectation interest, and thus the remaining solution is to deem the contract too indefinite to be enforced. If the parties left the price intentionally undetermined, then a policy *not* to supply a price term renders the whole deal unenforceable.[54] But such nonenforceability implies that the parties can freely walk away from the agreed-upon terms, and later reenter negotiations to revise these terms. In that case, nonenforceability of the precontractual agreement frustrates the ability of the parties to "rule out" terms.

One way to defend the no-supplementation approach is to recognize that parties often prefer their agreement to be governed by norms other than legal sanctions. This account has been developed recently by Robert Scott, who notes that indefiniteness is often a deliberate drafting choice of the parties, who "appear to prefer the indefinite agreement they concluded to the more explicit and verifiable alternative that they ignored."[55] Deliberate gaps make room for subsequent informal agreement, which in turn is driven by reciprocal fairness. Agreements to agree, under this view, should be unenforceable in order to enable the parties to utilize informal methods of self-enforcement such as reciprocity.

While Scott's explanation for the existence of indefinite agreements and of agreements to agree is different than the one offered in this

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53. *See* Drees Farming Ass'n v. Thompson, 246 N.W.2d 883, 886 (N.D. 1976) (finding that nonsupplementation of an option of renewal under "terms to be negotiated" would make the option meaningless); 1 FARNSWORTH ON CONTRACTS, *supra* note 42, § 3.8a, at 213–14.

54. *See, e.g.*, Joseph Martin, Jr., Delicatessen, Inc. v. Schumacher, 417 N.E.2d 541, 544 (N.Y. 1981); 1 CORBIN, *supra* note 15, § 4.1, at 532.

55. Scott, *supra note* 13, at 1657.

Article, it shares the fundamental observation of the existence of deliberately incomplete agreements. Scott also observes that one of the strategies available to parties negotiating an agreement is to leave some terms unresolved in the expectation that their resolution will become possible in the future course of their relationship, and in the expectation that the law will not fill the gaps with a mid-range compromise. But while Scott argues that there should be no legal sanction on a party who retracts from such an agreement, to leave room for informal negotiations, the account developed in this Article focuses on settings in which such informal negotiations failed.

Moreover, the premise that parties may not want the court to interfere with the resolution of the remaining issues does not imply that the parties also consider the formally drafted portions of the agreement nonbinding. Why else did they draft them into "legal" language? While the agreement is incomplete, it does contain some elements of consent that the parties did draft into a formal format. Making the agreement wholly unenforceable, even in those cases where norms of reciprocity failed to provide a resolution, and allowing the parties to walk away freely, would frustrate this accomplishment. It would undermine the more subtle notions of commitment that emerge in the wake of partial agreements. If the law were to enforce only the memorialized parts of the agreement and not intervene in the unresolved parts, then the commitment can be maintained and extralegal norms of reciprocity could continue to regulate the missing terms.

It might seem that, presented with a deliberately incomplete contract, the court's adjudicative choices include either aggressive supplementation of terms with a definitive default provision or nonenforcement of the contract entirely. The court is faced with an all-or-nothing choice, and can either supplement the gaps and enforce the deal as if it were complete ("all"), or consider it a preliminary, nonbinding deal ("nothing"). In particular, this dichotomy suggests that the court cannot apply a partial enforcement approach, and enforce only the agreed upon terms.

In the next Part, I will argue that this all-or-nothing feature, although it fairly describes many areas of the law, is not optimal and not necessary. When the parties affirmatively choose to leave a matter open for further negotiation and yet manifest an intent to be bound to the resolved issues, a legal regime different than the current all-or-nothing regime is called for. In these situations, an intermediate regime that supplements and enforces such deliberately incomplete deals without writing the missing elements of the contract over for the parties is preferable and, indeed, available.

III. PRO-DEFENDANT GAP FILLERS

A. Decoupling the Default Rule

Consider a situation in which parties negotiate a contested issue (say, a contingent price), with each insisting on a term that is favorable to her. If the parties deadlock over this issue, yet proceed to draft an agreement on the remaining issues, then each party can be deemed to manifest consent to a complete contract that contains the agreed upon terms and the term she demanded concerning the stalemated issue. That is, assent by a party to the incomplete agreement that contains a "to-be-agreed-upon" gap eliminates any reasonable grounds she might have to reject the complete agreement when supplemented by the term she has been openly seeking all along. This manifested consent is, of course, "constructive." There is actual assent only to the part of the deal that includes the expressly agreed-upon terms. But there is implied intent to be bound to the part of the deal that was contested, as long as it is resolved with the term that this party vied for.

In this situation where a contested issue is left deliberately open, each party can be seen as manifesting assent to a different deal. It is as if they drafted two contracts, identical in the components that contain all the agreed-upon issues, but different in the components that contain the contested issues. Each party wants to be bound to the contract that contains her favorable terms. Thus, if one of these hypothetical contracts were to be enforced against a party, it can only be the one to which she assented, the one containing her favorable terms.

This interpretation of the deliberately incomplete agreement is consistent with the parties' choice to address their differences by entering into a partial understanding, rather than remaining silent or walking away. If the parties recognize their deadlock and nevertheless draft a partial agreement, they are indicating that some assent has been obtained. They are also indicating, however, that each is seeking different content to fill the remaining gap. Accordingly, the only way to give efficacy to their intent is to decouple the remaining gap from the agreed-upon terms.

How could that be done? Of course, neither party can enforce a contract containing her own favorable terms, terms to which the other party never surrendered. Instead, the power that each party would have is to enforce upon her opponent a deal that, with respect to the contested issues, includes the *opponent's* favored terms. A party can, of course, choose not exercise this option, in which case—if the other party does not exercise her own option—the "no contract" outcome remains. If the incomplete contraet is supplemented in such a manner, the enforced-against party, being granted the terms she either agreed to or unilaterally

sought, cannot legitimately claim that she never intended to be bound to it. Isn't this the deal she pursued all along? Liability here is grounded not on what a party affirmatively or hypothetically assents to, but rather on a reasonable restriction over what a party may reject.[56]

This gap-filling approach transforms the incomplete contract into a set of *two* complete contracts. Essentially, the gap filler is "decoupled": it is equal to the term favored by the party against whom enforcement is sought. For example, if the seller demanded no less than $1000 and the buyer was willing to pay no more than $800, and if every other term of the transaction was agreed upon, then the seller can enforce a deal supplemented by the buyer's price of $800 and the buyer can enforce a deal supplemented by the seller's price of $1000. Hence, each party receives an *option* to enforce a deal containing the term the other requested. The precontractual agreement is transformed into a "double option."[57]

Thus, unlike standard gap-filling approaches that trace a single definitive term to best supplement the deal and apply this term regardless of the identity of the party seeking enforcement, this approach provides a *pair* of gap fillers. The majoritarian mimicking approach to gap filling would supplement the missing price term in the example above with one that is "reasonable," generally somewhere between $800 and $1000. Such a term, however, forces a compromise on the parties to which they did not assent, and perhaps affirmatively rejected. But under the pro-defendant gap-filling approach, the plaintiff asks the court to fill the gap with the defendant's terms, leaving no possibility that an undesired contract is being imposed upon either of the parties.

Note that filling the gap in a manner favorable to the defendant does not force the plaintiff to transact under terms to which she does not assent. The pro-defendant terms are enforced only if the plaintiff prefers such a deal to the no-contract alternative. Essentially, the question is not whether a party will want to enforce a contract supplemented with the other party's terms (she often may not), but whether the other party should be entitled to reject such favorable deal.

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56. For the moral basis of this principle of obligation, resting on the nonrejectability of an individual's own representations, see generally T.M. Scanlon, *Contractualism and Utilitarianism*, *in* UTILITARIANISM AND BEYOND 103, 117 (Amartya Sen & Bernard Williams eds., 1982).

57. *See* 1 DANIEL FRIEDMAN & NILI COHEN, CONTRACTS 289 (in Hebrew) (mentioning the technique of double option and arguing that "a substitute to no supplementation can be found in the willingness of the plaintiff to acquiesce to the other party's maximal demand with respect to the missing element.").

B. "Most Favorable" to the Defendant

In choosing as a default the term that is favorable to the enforced-against party, the example above identified this term by reference to the party's express proposal. It was assumed that the parties exchanged explicit communications, each stating her favored term, and failed to strike a compromise. To complete the deal, each party was given an option to incorporate the term proposed by the other. In that example, the content of the gap filler—the term that is known to be desired by the enforced-against party—was not hypothetical, but rather evidenced by reference to her own affirmative representations.

In general, however, parties may leave a contract deliberately incomplete without first going through the motions of making explicit proposals and without marking their respective favorable terms. For example, the parties to a lease contract may agree on a renewal period, but leave the renewal price indefinite, "to be agreed upon," in the expectation that it might be easier for them to reach assent at a later stage. In these situations, there is no affirmative statement by any party from which an inference can be drawn as to her favorable term. How would the decoupled gap filler operate in this more general setting?

Supplementing the deal with the term the enforced-against party proposed is a way to assure that the defendant is not subject to a transaction laden with terms that she did not will. When a party affirmatively proposes terms, it provides a strong basis to infer that the party assents to those terms. The task to identify nonrejectable terms is made straightforward. In the absence of an express proposal, a similar principle of assent can be satisfied if the gap is supplemented by terms that fulfill an equally powerful nonrejectability standard—terms that are most favorable (within the set of reasonable terms) to the defendant. While this party never expressly stated what these most favorable terms are, the court would have to imagine the most that this party reasonably hoped to gain when entering into the incomplete agreement and how this party hoped, ex ante, to resolve the missing provisions. Instead of using a majoritarian or an "average" term, the court would apply a biased term, favorable to the defendant. Thus, the only difference between situations in which the defendant made a proposal versus situations in which he did not is the difficulty of ascertaining what are the defendant's most favorable terms.

This generous pro-defendant supplementation guarantees that the deal to be enforced is no worse than what the defendant could have intended. It is the only deal to which it can confidently be said that the defendant manifested her constructive intent to be bound. What reasonable grounds would the enforced-against party have to reject such a favorable deal? Only opportunistic motives or a retraction from

previous manifested intent can underlie a refusal to transact under such favorable terms.

Surely, the notion of assent even to "most favorable" terms is a fiction. It is less of a fiction, however, than the notion of assent to mimicking defaults. Mimicking default rules—whether tailored or "one-size-fits-all"—are based on the premise that a mutual will of the parties exists. This premise is problematic in incomplete contracts, particularly ones in which the parties have reached a stalemate. As the court in *Walker v. Keith* conceded, "[i]t is pure fiction to say the court . . . is enforcing something the parties agreed to."[58] But the ideal of basing the obligation on the party's will can nevertheless be fulfilled by gap fillers that mimic the will of one party at a time—the terms this party favored.

Thus, in the presence of a deliberately incomplete contract, the mimic-the-parties'-will default metamorphoses into a decoupled set of mimic-one-party's-will terms, of which a single one is chosen according to the identity of the party seeking enforcement. Assent to this term is no more, and arguably less, fictitious than assent to standard gap fillers. There is every reason to presume that when parties leave terms to be agreed upon, they truly intend to permit enforcement of the deal on the terms most favorable to them, and that each has granted the other party an option to enforce the deal supplemented by such terms.

C. Scope

Pro-defendant gap fillers, whether derived from explicit proposals the defendant made or from the constructive exercise of inferring the defendant's most favorable terms, are likely to prescribe different gap-filling content than mimicking or reasonable terms. As emphasized throughout this Article, this technique is not a substitute for standard gap-filling standards, but rather should be viewed as complementary. Pro-defendant gap fillers are an appropriate solution to indefiniteness only when the gaps are left deliberately and the parties aim to resolve them through negotiations. Before turning to doctrinal illustrations of the proposed technique, two additional remarks concerning the conceptual reach of pro-defendant gap fillers are in order.

The first remark concerns the size of the gaps that the proposed technique can fill. Normally, when using standard majoritarian defaults, courts are wary not to "write the contract over" for the parties. That is, supplementation is conducted only when the gaps in the contract are not too wide. Otherwise the presumption of hypothetical assent becomes

58. 382 S.W.2d 198, 203 (Ky. Ct. App. 1964).

strained.[59] The same caution should apply to the application of the pro-defendant default terms. True, when utilizing most favorable terms, the notion of hypothetical one-sided assent can plausibly be stretched. A party may be deemed to assent to terms most favorable to her even if the set of agreed upon terms is small or even nonexistent. However, absent a serious manifestation by this party that she intends to be bound to some transaction with *this* counterpart, it would be dangerous to give the other party an option to enforce a transaction, even one containing terms that are very favorable to the enforced-against party. Such an option would relinquish the freedom *from* contract and thus undermine the security of property rights and the autonomy embedded in the voluntariness of transfers. To avoid this result, gap filling under the proposed theory can be restricted to instances when the express assent by the enforced-against party is sufficiently substantial.

The second remark concerns the nature of assent to most favorable defaults. By its definition, the concept of "assent" in contract law embodies a tension between the true "factual" intent of the parties and legally binding contractual terms. The set of binding consensual terms does not always conform to what the parties truly intended, discussed, and agreed upon. Doctrines such as the parol evidence rule, the battle of the forms, and more generally the objective theory of assent, drive a wedge between consent-in-fact and its legal translation—mutual assent. As long as there are good conceptual and instrumental justifications for this wedge, it serves a useful purpose.[60] Accordingly, the notion of assent to most favorable default rules, to the extent that it is fictional, would have to be defended on these bases. The conceptual basis—the argument that most favorable default terms are consistent with assent in deliberately incomplete contracts—has been developed thus far. I will now turn to examine the instrumental defense.

D. Increasing the Contractual Surplus

Parties may seek to form partially binding commitments for several reasons. As argued above, such precontractual commitments help parties digest concessions gradually, protect the integrity of the negotiation arena, and promote investments in the relationship.[61] Does the particular form of commitment proposed here, in which a retracting party is bound to terms most favorable to her, suffice in achieving these goals?

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59. *See* RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 1, § 33(3) & cmt. c (explaining that the more the terms that the parties leave open, the less likely it is that they actually intended to conclude a binding agreement).

60. *See* FARNSWORTH, *supra* note 24, § 3.6, at 116–18.

61. *See supra* Part II.A.3.

The conceptual analysis above showed that pro-defendant supplementation of deliberately incomplete contracts is a way to create contractual liability in a gradual manner. The more terms remain to be agreed upon the more pro-defendant terms will be utilized as gap fillers, and thus the smaller is the burden of liability to the defendant. While the complete freedom to walk away is restricted, the practical cost of this restriction is a function of the terms the defendant must put up with, which, in the case of pro-defendant gap filling, is somewhere between zero burden of no-contract and the high burden of a majoritarian contract.

This intermediate form of liability fragments an otherwise hard-to-swallow full contractual commitment into sequential small steps. When a precontractual agreement is binding but can only be enforced with terms most favorable to a party, each party knows that by entering this agreement she is effectively surrendering only the terms that are covered by the partial agreement. While she is not guaranteed to get the most favorable terms with respect to the unresolved issues, she *is* guaranteed that nothing worse than these terms can be unilaterally enforced against her. That is, any additional compromise from this "most favorable" benchmark can only be consensual. The unresolved matters would never be the reason to exit the relationship. Thus, a party can make incremental concessions, spared from a moment in which an entire large concession is to be yielded.

The guarantee that the other party cannot *freely* walk away is valuable in that it diminishes the ability of the other party to engage in hold-up games. If the other party is threatening to walk away unless some terms already agreed upon are changed, the threatened party has some remedy. True, this remedy is not as potent as full-blown contractual liability would provide because it only inflicts a partial burden on the threatening party. Still, this intermediate remedy makes it less likely that retractions from the precontractual agreement would occur or that the relationship will completely unravel. And with greater security in the longevity of the relationship and against the risk of retraction, any investment made to enhance the value of the relationship is more likely to bear fruit. Each party has an increased incentive to invest in the relationship and to rely on the precontractual understandings.[62]

62. For formal proof that incentives to invest under this regime will be optimal, see Bebchuk & Ben-Shahar, *supra* note 43, at 443–49. As the formal proof shows, for the plaintiff to have optimal incentives to invest, the defendant must be precluded from extracting any value that arises from this investment. Thus, the definition of the defendant's most favorable terms must exclude value that came about as a result of the plaintiff's precontractual reliance investment. See generally Hart & Moore, *supra note* 33, who demonstrate that the value of precontractual commitments is in enabling the parties to fine-tune their reliance. In Hart & Moore's model, the precontractual

Stated differently, we saw that under the proposed gap-filling regime, the deliberately incomplete contract is decoupled in accordance with the identity of the enforced-against party. From the perspective of party *A*, there are two enforceable contracts, each addressing a different concern this party might have (the same applies for party *B*). The first contract is the one that can be enforced against party *A*. The fact that this contract includes gap fillers that are so favorable to her guarantees that no additional concessions beyond those already made would be forced on her. This fact gives her the peace of mind to make partial concessions one step at a time. The second contract is the one that party *A* can enforce against party *B*, if the anticipated further negotiations are abandoned. The fact that party *A* has this power to enforce a contract on the other party is sufficient in providing her with the needed assurance against opportunistic hold-up by party *B*. While party *A* might prefer to negotiate the remaining terms and not yield right away to those most favorable to party *B*, she at least has the option to preclude party *B* from abandoning the relied-upon relationship.

E. The Effect of Pro-Defendant Gap Fillers on Negotiations

Would the existence of the "double option" affect the ability of the parties to reach an explicit agreement? Intuitively, it might be conjectured that each party would be inclined to act strategically: hold back or imitate a retraction, so as to trigger the exercise of the option by the opponent. Thus, a party who is genuinely ready to compromise may nevertheless engage in hawkish bargaining strategies and even withdraw from partial understandings, in the hope that her opponent would view this as a genuine breakdown and exercise his enforcement option, and thereby concede more favorable terms. If both parties act this way, bargaining that might otherwise succeed would, in the shadow of pro-defendant gap fillers, tend to fail.

It is not clear, however, that a party indeed gains anything by faking a negotiation breakdown or by hardening her position. First, if such an incentive were to exist, the other party would recognize it and would not hurry to concede the pro-defendant terms. Thus, to succeed in this strategy of inducing the opponent to cave-in, one has to demonstrate that it is not a fake by making a *credible* irreversible act of withdrawal from the bargaining. This, however, is a dangerous strategy. A party who is willing to compromise but walks away strategically in order to get better terms is taking the risk that the opponent will decide not to exercise her option and not to concede the

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agreement is not legally enforceable; however, given the investment that follows the precontractual agreement, it is against the interest of the parties to retract.

terms that are most favorable to the retracting party. If the act of walking away is irreversible, it might undermine the deal altogether. In other words, the upside for the "strategic" party, that she might get better terms, is offset by the downside, that she might end up with no deal at all.

Further, there is no reason to think that the risk that such strategic bargaining poses is any greater under the proposed pro-defendant default rules. Even in the absence of the double option, in the traditional regime that assigns no liability to retractions from agreements to agree, each party might be tempted to hold back strategically, in the hope that the other party would concede some of the terms. Indeed, negotiators are universally known to engage in such bargaining bluffs, in the hope that their opponents would "surrender." The existence of the option that their opponents now have, to force a deal, does not change the behavior of negotiators who are all the more eager to deal under their own favorable terms. So this "hold-out-to-get-better-terms" strategy has nothing to do with pro-defendant gap fillers. The fact that each party is granted a default option to concede does not affect the tendency to utilize such bargaining techniques. This last remark suggests that the double-option regime is redundant in those situations in which a party is actually interested in the deal but is vying for more favorable terms. This party would, of course, be happy to deal under her most favorable terms, and a legal rule that subjects her to such a burden is mandating an option that this party would eagerly give her opponent. The double-option regime is constraining, then, only in situations in which a party prefers to abandon the deal altogether and to retract even from the version of the deal most favorable to her.

F. Implementation

Can courts identify pro-defendant gap fillers? It might seem that the judicial task of identifying a party's most favorable terms is more difficult than identifying reasonable gap fillers, usually evidenced by "market" terms. But that might not necessarily be so. For one, the nature of adversarial proceedings is already such that each party provides evidence favorable to herself. For example, in adjudicating a missing price, the defendant-seller will likely bring expert testimony supporting a price in the higher end of the reasonable spectrum. In fact, it would be easier to apply a pro-defendant gap filler than to try and figure out from the parties' polarized evidence the proper balance that would adequately reflect majoritarian terms. Further, courts can instruct defendants to designate the term that they favor, and induce defendants' compliance by threatening that if the designation is

unreasonable, the court would supply a term.[63] Finally, recall that courts are already accustomed in applying another biased supplementation regime. Under the doctrine of contra-proferentem, courts are instructed to interpret an ambiguous term not along its most reasonable meaning, but rather in a one-sided fashion—least favorable to the drafter of the term.[64]

To illustrate how pro-defendant terms can be identified, consider the celebrated case of *Walker v. Keith*, the Kentucky decision that ruled that agreements to agree are unenforceable.[65] Parties entered into a 10-year lease of $100 per month with an option to extend that lease for an additional 10-year term at a rental price "to be agreed upon."[66] Holding that the parties' minds have never met on a criterion to determine the rent, the court refused to fill the gap or to enforce the extension of the lease.[67] At the trial, however, each party explicitly stated its most favorable term. The lessor demanded a price reflecting the relatively high increase in rent *locally*. The lessee sought to prove price changes *nationally* and thereby enjoy the lowest plausible rent adjustment.[68] Since both demands were within reason, the court could have given the lessee the option to extend the lease under the term identified to be favorable to the lessor. At least as a matter of conceptual logic, the "biased" supplementation is no less—and arguably better—reflective of the lessor's incompletely manifested intent than the result of no renewal.

In fact, the logic underlying this decoupled supplementation approach is already recognized and applied in contract doctrine, suggesting that implementation is not impossible. The Second Restatement, for example, recognizes that when an agreement is indefinite, it may be possible to provide one remedy but not another.[69] It may also be possible to grant a remedy only to one party, not another. For example, when payment terms are not specified in the sale agreement, "[t]he contract is too indefinite to support a decree of specific performance against [the buyer], but [the buyer] may obtain

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63. *See, e.g., Ontario Downs*, 13 Cal. Rptr. at 786–87.

64. *See* RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 1, § 206; *see also* 5 CORBIN, *supra* note 14, § 24.27.

65. 382 S.W.2d at 201.

66. *Id.* at 199.

67. *Id.* at 201. A minority of courts have decided, in identical circumstances, to protect the lessee's reliance and to fill in a rental term and enforce the agreement. *See, e.g.*, Fuller v. Mich. Nat'l Bank, 68 N.W.2d 771, 772 (Mich. 1955); *see also* FARNSWORTH, *supra* note 24, § 3.29, at 218 & nn.5–6. The Code also "rejects in these instances the formula that an agreement to agree is unenforceable." *See* U.C.C. § 2-305 cmt. 1 (2003) (internal quotations omitted).

68. *Walker*, 382 S.W.2d at 203.

69. RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 1, § 33(2) cmt. b (stating that "uncertainty may preclude one remedy without affecting another").

such a decree if he offers to pay the full price in cash."[70] Since it is possible to identify a gap filler that is most favorable to the seller, the contract can be enforced only against the seller.

This is not to say that the problem of identifying a party's most favorable terms is trivial. Even if the defendant made express proposals at some point in the negotiations, these prior proposals may have become stale, no longer representing the best the defendant can hope for. New information, changed market conditions and subsequent concessions the defendant made on other issues might all render the defendant's earlier proposal less favorable to her. In those cases, the defendant's most favorable terms should be inferred not from her proposal, but from the relevant circumstances. Any factor that materialized prior to the time designated by the parties for resolution of the open issue is relevant for ascertaining the defendant's most favorable terms, with the exclusion of the plaintiff's reliance investment. As explained in Part III.D above, the defendant must be precluded from extracting the value generated by the plaintiff's precontractual investment.

These factors suggest that the pro-defendant gap-filling regime may indeed pose problems of implementation. This might explain, perhaps, the relative scant application of this regime in practice. But, as the discussion below will demonstrate, courts have chosen to overlook the pro-defendant solution even when its implementation was straightforward.

IV. DOCTRINAL APPLICATIONS

The analysis thus far has studied the desirable properties of a regime that supplements indefinite agreements with terms that are favorable to the defendant. Such a regime has been shown to create an intermediate level of liability, deviating from the traditional all-or-nothing approach of the mutual assent doctrine—a regime that reflects more accurately the intent of parties who deliberately left an agreement incomplete. This Part turns to examine with more detail whether and how the proposed regime is already part of, or can be infused into, the law of indefinite agreements. It shows that the seeds of the proposed gap-filling regime are already planted in contract doctrine. That is, courts and commentators recognize both the technique of filling gaps with terms most favorable to the defendant, and the rationale underlying this technique, although they do so without embracing the full implications and the generality of this approach. This Part also shows that existing doctrines and practices traditionally part of the all-or-

70. *Id.* § 33(2) cmt. b, illus. 2.

nothing approach can be conceptualized to provide the infrastructure for pro-defendant gap filling. When contracts are left deliberately incomplete with the intent to be further negotiated, such expansion of the doctrine is desirable.

A. Cure by Concession

Supplementing incomplete contracts by terms most favorable to the defendant is a technique already recognized in contract law doctrine. Under the doctrine of "cure by concession," when the contract is silent over a material term the indefiniteness is overcome by granting the plaintiff the option to concede the missing term in accordance with in the defendant's most favorable arrangement.[71] As Corbin recognizes, "[w]here the parties intend to contract but defer agreement on certain essential terms until later, the gap can be cured if one of the parties offers to accept any reasonable proposal that the other may make."[72]

Cure by concession is often applied in cases in which the parties agreed on a price but left the payment terms "to be agreed upon." In these situations, if the buyer agrees to pay in a manner most favorable to the seller—full payment in cash and with no delay—then the indefiniteness is cured.[73] It is not that courts perceive the full payment in cash as the reasonable term that the parties hypothetically intended, or would have agreed upon had they continued to negotiate. In fact, oftentimes it is quite clear that the parties hoped to agree on installment or credit terms, something less favorable to the seller. Rather, courts regard the buyer's willingness to make full payment in cash as a waiver that "obviate[s] any need to come to any agreement as to the manner and form of payment."[74] Since "there is no longer any way that the provision may be construed to [the defendant's] detriment," any resistance to the contract on the ground that it is ambiguous should be eliminated.[75]

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71. *See* 1 FARNSWORTH ON CONTRACTS, *supra* note 24, § 3.29, at 219.

72. 1 CORBIN, *supra* note 14, § 4.1, at 532.

73. RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 1, § 33(2) illus. 2 ("A agrees to sell and B to buy a specific tract of land for $10,000 . . . . [and] to lend B the amount, but the terms of the loan are not stated . . . . The contract is too indefinite to . . . [enforce it] against B, but B may . . . [enforce it] if he offer[s] to pay the full price in cash.").

74. Morris v. Ballard, 16 F.2d 175, 176 (D.C. Cir. 1926) (finding that if the terms of payment were not agreed upon, the purchaser can enforce the deal if he is ready to pay the agreed price under such terms as the vendor might impose.); Shull v. Sexton, 390 P.2d 313, 318 (Col. 1964); Matlack v. Arend, 63 A.2d 812, 817 (N.J Super. Ct. Ch. Div. 1949) (finding that if the buyer "waives all credit and offers to pay cash, the defense that the agreement is too indefinite is untenable").

75. Busching v. Griffin, 542 So. 2d 860, 864 (Miss. 1989). Many courts, however, reject this view and hold that agreements that leave the terms of payment to be

Cure by concession can also apply to issues more central to the agreement than payment terms, such as identification of the subject matter of the contract or the price. In *Ontario Downs*, the parties entered agreement for the sale of 16 acres of land for $50,000, but did not specify which 16 acres within the seller's 450-acre lot were being sold.[76] The buyer offered to accept any 16-acre tract that the seller might designate, but the seller refused. The court held that the parties viewed the agreement to agree as binding, and that the gap should be filled in a way favorable to the seller.[77] Not knowing which 16-acre tract would satisfy this criterion, the court instructed that if the buyer waived his right of selection and was willing to accept any parcel, then the seller would be required to designate an "appropriate parcel" that the buyer would have to accept. If the seller failed to make such a selection, then the buyer would be entitled to designate a parcel himself. Under this scheme, the buyer can in effect force the seller to supplement the contract with a term most favorable to the seller, and the information as to what term is most favorable to the seller is extracted out of the seller by the threat that if he fails to designate it appropriately, then he will have to accept a less favorable term.

There are other situations, however, in which courts can readily overcome indefiniteness with the aid of pro-defendant gap fillers and yet refuse to do so. For example, in *Wilhelm Lubrication Co. v. Brattrud*, the parties agreed to on a sale of 5000 gallons of motor oil of a particular brand, leaving the buyer the right to determine which viscosity type he required.[78] Because there were seven possible types of motor oil each priced differently, the court refused to hold the retracting buyer to damages. The court reasoned that in the absence of a designated single type, the purchase price could not be ascertained, and thus there was no basis for the computation of damages.[79] The contract failed for indefiniteness. This was a case, however, in which the court could easily have applied a pro-defendant default, requiring the buyer to do that which he was entitled to under the agreement—namely, to specify the precise oil type. In the absence of an affirmative designation by the buyer, the court could have computed the damages on the basis of the type least costly to the buyer.

Another illustration of pro-defendant gap fillers in practice involves lease contracts that leave the duration of the renewal indefinite. For example, parties who use standard form leases that provide an extension

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agreed upon are fatally defective. *See* Roberts v. Adams, 330 P.2d 900, 906 (Cal. Dist. Ct. App. 1958); 1 CORBIN, *supra* note 14, § 4.3, at 579.

76. 13 Cal. Rptr. at 784; *see supra* note 63 and accompanying text.

77. 13 Cal. Rptr. at 787.

78. 268 N.W. 634, 635 (Minn. 1936).

79. *Id.* at 637.

clause "for ____ years" occasionally fail to fill in the blank. This might not be a deliberate case of incompleteness but rather a result of neglect or haste. Nevertheless, courts facing such indefiniteness have generally construed these terms "to be for the shortest period for which the lease could be renewed or extended."[80] This, as one court explains, guarantees that the landlord will not be held to a longer period than the agreement stated.[81]

When parties leave the price term to be agreed upon later, the option to cure the indefiniteness by conceding the other party's most favorable price is less commonly recognized. Usually, the court would fill in a price term only if the parties explicitly provided a "methodology" for determining it, but would hold the agreement fatally defective otherwise.[82] Alternatively, even in the absence of any explicit methodology courts occasionally fill in the blank with a fair and reasonable market term.[83] Other times a plaintiff who prefers a contract with the conceded price to the no-contract outcome will offer to make such a concession and to accept a pro-defendant gap filler. In his landmark decision in *Sun Printing & Publishing Ass'n v. Remington Article & Power Co., Inc.*, Cardozo makes reference to such a technique:

> If price and nothing more had been left open for adjustment, there might be force in the contention that the buyer would be viewed, in the light of later provisions, as the holder of an option. . . . [The buyer] would have the privilege of calling for delivery in accordance with a price established as a maximum.[84]

Cardozo, however, rejects the application of this approach in his decision.[85] But there are circumstances in which even a price term can

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80. 49 AM. JUR. 2D *Landlord and Tenant* § 158 (1995). Similarly, a general covenant to renew without stating the number of renewals is construed to entitle the tenant one renewal.

81. Starr v. Holck, 28 N.W.2d 289, 292–93 (Mich. 1947).

82. *Joseph Martin, Jr., Delicatessen, Inc.*, 417 N.E.2d at 543–44 (proffering a methodology for determining the price has to be found within the four corners of the agreement).

83. *See* Daniel E. Feld, Annotation, *Validity and Enforceability of Provision for Renewal of Lease at Rental to Be Fixed By Subsequent Agreement of the Parties*, 58 A.L.R.3D 500, 515–19 (1974).

84. 139 N.E.2d 470, 470 (N.Y. 1923) (citations omitted).

85. *Id.* at 471. Commentators raise doubts as to the validity of the outcome in *Sun Printing* based on the same logic developed in this article. *See, e.g.*, FARNSWORTH, *supra* note 24, § 3.29, at 220 ("On the court's own reasoning, had the buyer offered to pay the Canadian supplier's *highest* price . . . there would appear no reason to refuse to enforce the agreement."). However, many other examples in line with *Sun Printing* can

be supplemented by picking a value most favorable to the defendant. The following Section explores these circumstances.

B. Agreements with an Explicit Range of Terms

Oftentimes the parties, while failing to specify a definite term such as price, do specify a *range* from which they expect to pick out a definite term in the course of subsequent negotiations. This situation presents courts with an intermediate form of indefiniteness. There is no formula or methodology that can yield a certain "resolution of ambiguity," but there is more than "an inkling that either of the parties assented" to some figure.[86] Since courts are reluctant to split the difference and name a price in the mid-range, a result more loyal to the parties' agreement is sometimes achieved by granting each party an option to concede the other party's most favorable price within the range. As Corbin explains the law in this situation:

> The exact price may be left for future negotiation within a specified maximum and a specified minimum. In such a case it may be intended that the buyer shall have a binding option to buy at the maximum, or the seller shall one to sell at the stated minimum, or both may have such options.[87]

Thus, when the parties explicitly state that the price to be agreed upon "shall not exceed p," courts have overcome the problem of indefiniteness by granting the buyer an option to buy at the stated maximum, p.[88] The explicit rationale for this solution is similar to the one invoked in this Article. A seller's agreement to agree on a price not exceeding p can be view as containing two separate components: to continue good faith negotiations over a the price, and to forgo his prerogative to demand a price greater than p. If the buyer were willing to pay p, the seller would be considered retracting from the latter component of this agreement if he refused to accept p.[89] The seller's

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be found in adjudication of incomplete lease contracts, where parties leave the rent to be agreed upon later, and the plaintiff is seeking enforcement under the best possible terms for the defendant. Knapp, *supra* note 18, at 698–703 (surveying this line of cases).

86. *Schumacher*, 417 N.E.2d at 544.

87. 1 CORBIN, *supra* note 14, § 2.8, at 138–39.

88. *See, e.g.*, Denny v. Jacobson, 55 N.W.2d 568 (Iowa. 1952) (stating that the lease's option to renew was at price to be agreed upon "'not less than Forty-seven and 50/100 dollars ($47.50) or more than Seventy-seven and 50/100 dollars ($77.50)'" is enforceable at the maximum rent); *see also* cases cited in 1 CORBIN, *supra* note 14, at 578 n.27.

89. "When a bargained-for term of a renewal provision sets a range within which negotiations for a rental rate must take place, the lessor may not render the

own acceptance of the *range* negates any reasonable grounds for him to reject the best term within the range.

In cases in which parties agree to agree on a term but fail to specify an explicit range, the same result of granting each party an option to concede the other party's favorable term could be obtained if courts were to supplement the agreement with an *implied range*. True, this interpretation of the agreement takes us further from the parties' actual will, to the domain of implied or hypothetical will. But as one court explained:

> A court may not close its eyes to the truism that a landlord's proper objective should be and is to obtain the highest rent that a tenant under all the circumstances can afford to pay . . . . When, therefore, a tenant's option extension clause in a lease contains a ceiling (*implied or constructive in this instance*) upon the rent to be charged for the extended period and the tenant is willing to pay that ceiling price, the landlord may not be heard to challenge that option clause otherwise void for uncertainty.[90]

Given that the parties explicitly postponed the negotiation over the renewal price, it is fictitious to say that the parties reached hypothetical consent. This is why courts by and large rejected the "reasonable" price gap fillers, which are so closely linked to the notion of mimicking the parties' will. But it is less fictitious to presume that the landlord hypothetically consented not to demand more than the maximal plausible rent. It may well be that the tenant hoped for a better outcome and would not be interested in exercising the renewal option under such terms. But if the tenant *is* interested and is suing to renew the lease under the "ceiling" price, is there any good reason to prefer the standard non-enforcement outcome?

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renewal provision unenforceable simply by . . . insisting on rent exceeding the maximum allowed by the contract." *See* Little Caesar Enters., Inc. v. Bell Canyon Shopping Ctr., 13 P.3d 600, 603 (Utah 2000).

90. Huber v. Ruby, 65 N.Y.S.2d 462, 465 (Gen. Term 1946) (emphasis added).

C. *Options for Renewal of Lease*

One of the main areas in which the doctrine of indefiniteness has been well tested is a lease contract with a tenant option to renew at rental to be agreed upon at the time of renewal. While the majority of courts still view these contracts as indefinite and unenforceable, a growing trend is to allow the tenant to exercise the option even if the negotiations over the renewal price fail, by using the fair market price as gap filler.[91] This solution clearly violates the landlord's immunity, which he explicitly secured in the contract, from nonconsensual designation of the rental price. Accordingly, courts have occasionally considered a policy of allowing the tenant to renew under the landlord's maximal obtainable price. In such cases, the tenant's exercise price is sometimes equated with "the highest rent which a responsible bidder is apt to offer."[92]

To be sure, this solution is not without difficulty. It suggests that an option to renew under a price to be agreed upon would automatically become an option to renew under the landlord's maximal price. But if the parties already thought about granting the tenant an option (to renew), doesn't their reluctance to state a renewal price indicate that they did not seek to grant the tenant a one-sided power to effectuate renewal? Indeed, the pro-defendant supplementation of the option strains the language of the explicit agreement. But it surely does less of injustice to the parties' original intent than the polar solutions usually reached of either average market price or invalidation of the option altogether. While the landlord did not grant the tenant an explicit option to renew at the maximal price, it is unreasonable for him to defend by saying that he did not intend to be bound to such an interpretation.

One way the maximal price can be inferred by a court is by looking at other bids the landlord received from potential tenants, and equating the renewal price to the highest rentable value.[93] Like a right of first refusal, the price is set at the highest value the landlord is offered elsewhere. True, the proposed gap-filling standard is more than an "implied" right of first refusal. Here, the tenant can compel the transaction and does not have to wait for the landlord to initiate one. But both an implied right of first refusal and an option to concede the

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91. *See* Feld, *supra* note 83, § 2[a], at 503–06.

92. *See, e.g.*, Moolenaar v. Co-Build Cos., 354 F. Supp. 980, 984 (D.V.I. 1993) (restricting this formula to the highest value under the original zoning restrictions).

93. Dietrich v. J.J. Newberry Co., 19 P.2d 115, 117 (Wash. 1933); DiMaria v. Michaels, 455 N.Y.S.2d 875, 877 (App. Div. 1982).

maximal price address the problem of indefiniteness by reference to the highest "market value of the premises at the time of renewal."[94]

Another way to implement the "highest-value" formula is for the court to pick the valuation assessed by the landlord's expert witness.[95] In many of these suits, the tenant, while asking the court to supplement the deal with a fair or reasonable rental price, provides some testimony concerning the market price, usually on the lower end of the market distribution. The landlord, trying to show that there does not exist one "market price" and that the agreement is thus indefinite, provides testimony concerning the high end of the market distribution. The fact that both the landlord's and the tenant's information is valid does not neeessitate an outcome of no enforcement. Rather, and eonsistent with the courts' stated purpose to protect the tenant's bargain, the tenant should be entitled to concede the landlord's price.

These intermediate solutions, of enforcing an agreement to agree while supplementing it with terms more favorable to the enforced-against party, are the exception. More often courts restrict their attention to "all-or-nothing" solutions. Even when a tenant is willing to pay the maximal rent, "as much as any other responsible party would pay," the court may refuse to enforce the renewal option.[96] But often the underlying reason for the rejection of this supplementation formula is not a rejection of the pro-defendant gap-filling logic, but rather a recognition that the highest price alone does not exhaust the defendant's concern. For example, a landlord may be unhappy even with the highest market price in light of the conduct of the tenant. In these situations, the correct implementation of a pro-defendant gap filler would require the impractical judicial task to ascertain such non-price concerns, which perhaps explains some of the judicial resistance to the rule.

V. CONCLUSION

Building on an assortment of existing doctrines and gap-filling practices, and seeking justification both on conceptual and economic grounds, this Article has developed a pro-defendant standard of gap filling in incomplete contracts, potentially contributing to the general theory of default rules in contract law.

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94. *Diettrich*, 19 P.2d at 117; 49 AM. JUR.2D *Landlord and Tenant* § 156, at 165 & n.30 (citing Arnot v. Alexander, 44 Mo. App. 25, 28 (1869) (holding that the view that a fair rentable value is "different and may be 'something more' that its full or highest rentable market value" is erroneous)).

95. Lassiter v. Kaufman, 581 So. 2d 147, 148 (Fla. 1991).

96. *Diettrich*, 19 P.2d at 115.

There are several ways to think about the underpinnings of the proposed approach. One way, which I explored in a previous essay, is to think of contractual liability as arising, not from consensus between the parties, but from each party's separate and unilateral representation of serious intent to be bound.[97] Under this approach, a party cannot freely retract from the terms and proposals she indicated would be acceptable to her. If the basis of liability is divorced from consensus, each party could be accountable for a different unilateral representation. And when a party's unilateral representation is incomplete, this ground of liability is consistent only with supplementation that is favorable to the liable party since it is only to such terms that her intent to be bound can be safely presumed.

The pro-defendant gap-filling approach can also be viewed as a beginning of a challenge to the general idea of reasonable, or mid-range, resolutions of disputes in contract law. Much of the law of remedies, for example, is aimed at reaching reasonable, unbiased assessments of damages, often as a prerequisite to granting any remedy at all. For example, expectation damages are awarded only if the assessment of lost profits can be made reasonably accurately.[98] Applying the logic developed in this Article, this all-or-nothing approach—either damages are proven with certainty, or no damages will be recovered—can be questioned. In the context of damages, even if the plaintiff failed to prove the lost expectation with sufficient certainty, the default outcome should not be a complete bar against recovery of expectation damages. Instead, the plaintiff should be entitled to a recovery of such damages as prescribed by the formula most favorable to the defendant.[99] While this remedial burden may fail to accurately reflect the plaintiff's true loss, it is more accurate than the denial of expectation damages altogether and it guarantees that the defendant is not held accountable for more than the loss he caused.

The analysis in this paper focused on conceptual and economic justifications for the pro-defendant default rules. A more complete inquiry into the merits of this approach would have to address additional aspects. For example, it would have to explore in greater depth bargaining practices and the extent to which they are consistent with the fundamental no-going-back norm underlying the proposed regime. Additionally, the inquiry can extend to other areas of legal doctrine in which default rule theory proved useful, and explore the value of gap filling in the manner most favorable to the liable parties.

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97. *See* Omri Ben-Shahar, *Contracts Without Consent: Exploring a New Basis for Contractual Liability*, 152 U. PA. L. REV. 1829 (2004).

98. *See* RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 1, §§ 33(2), 35(2).

99. *See Wilhelm*, 268 N.W. at 637.