THREE PICTURES OF CONTRACT: DUTY, POWER, AND COMPOUND RULE

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H.L.A. Hart, following others before him, draws our attention to the difference between duty-imposing and power-conferring rules. Duty-imposing rules require persons "to do or abstain from certain actions, whether they wish to or not."[1] The law of theft, for example, instructs persons not to steal, no matter what their personal preferences are. Power-conferring rules "provide that human beings may by doing or saying certain things introduce new [duties], extinguish or modify old ones, or in various ways determine their incidence or control their operations."[2] Thus constitutions provide procedures whereby legislatures can act to create new laws or extinguish old ones when a majority of their members so desire.

Some theories of contract law characterize it as a private power-conferring rule, others as a duty-imposing one. Hart suggests contract is a legal power:

> Legal rules defining the ways in which valid contracts or wills or marriages are made . . . provide individuals with *facilities* for realizing their wishes, by conferring legal powers upon them to create, by certain specified procedures and subject to certain conditions, structures of rights and duties within the coercive framework of the law.[3]

On this picture, the point of contract law is to grant persons the power to modify, within limits, their legal obligations to one another. As Ernest Weinrib puts it, the "contract effects a voluntarily assumed change in the pre-existing legal relationship between the contracting parties . . . ."[4] Or in Randy Barnett's words, to "make a contract . . . a party must explicitly or implicitly manifest an intent to be legally bound."[5] According to the alternative, duty-imposing picture, contract law is concerned with extralegal wrongs such as breaking a promise, causing reliance harms, or unjustly enriching oneself at the expense of another. Consider, for example, Charles Fried's claim that "since a contract is first of all a

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1 H.L.A. HART, THE CONCEPT OF LAW 81 (2d ed. 1994).

2 *Id.*

3 *Id.* at 27–28; *see also id.* at 96, 250.

4 Ernest J. Weinrib, *Punishment and Disgorgement as Contract Remedies*, 78 CHI.-KENT L. REV. 55, 66 (2003).

5 Randy E. Barnett, *The Sound of Silence: Default Rules and Contractual Consent*, 78 VA. L. REV. 821, 861 (1992).

promise, the contract must be kept because a promise must be kept,"[6] or Patrick Atiyah's arguments that contract law is designed to compensate for reliance-based harms and prevent unjust enrichment.[7] While Fried and Atiyah make very different claims about the point of contract law, they agree that it is meant to impose duties on persons who enter into agreements for consideration.

This variety among contract theories is remarkable. It is usually easy to tell whether a law is duty imposing or power conferring. While there are many possible points of disagreement with respect to, for example, the criminal law or Article I of the U.S. Constitution, no one doubts that the point of the one is to impose duties and the other to confer powers. Why such deep disagreement in the case of contract law?

The answer requires a more general account of the difference between power-conferring and duty-imposing rules and of how we identify a given law as of one or the other type. The function of a duty-imposing law is to give persons subject to it a new reason to act in accordance with the rule—in Hart's words, "whether they wish to or not."[8] The function of a power-conferring law, by contrast, is to enable persons to determine, within bounds, what the law is or requires. As Joseph Raz puts it, power-conferring laws attach legal consequences to certain acts because "it is desirable to enable people to affect norms and their application in such a way if they desire to do so for this purpose."[9] These different functions impose different design requirements on duty-imposing and on power-conferring rules.

Consider power-conferring rules. A rule can give legal actors the ability to effect normative change, when they wish, only if it is structured such that those actors commonly satisfy the rule's requirements because they want the resulting change. More precisely, the distinctive function of laws that create powers entails two features that together distinguish them from laws that impose duties. First, a law that creates powers must be designed in a way that underwrites an expectation of its purposive use—an expectation that persons will satisfy the law for the sake of the legal consequences. Second, that expectation must be the law's reason for attaching those legal consequences to acts of that type. Evidence of this second feature can be found in rules that facilitate or enable the law's purposive use. To identify whether any given law is power creating, we can look to see whether it exhibits these characteristic features.

Evidence that power-conferring laws anticipate and facilitate their purposive use can often be found in rules that condition an act's legal consequences on evidence of the actor's legal purpose. Many power-conferring laws require for their exercise the performance of conventional

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6 CHARLES FRIED, CONTRACT AS PROMISE: A THEORY OF CONTRACTUAL OBLIGATION 17 (1981).

7 P.S. Atiyah, *Contracts, Promises and the Law of Obligations*, 94 LAW Q. REV. 193 (1978).

8 HART, *supra* note 1, at 81.

9 JOSEPH RAZ, PRACTICAL REASON AND NORMS 102 (Princeton Univ. Press 1990) (1975).

legal speech acts or legal formalities. Legislators use ritualized procedures to vote, judges use special words and writings to announce holdings, a will must be witnessed and delivered, a power of attorney must be in a proscribed form. Such conventional speech acts function, among other things, to ensure that the legal actor who performs them expects and intends the relevant legal consequences. Other power-conferring laws require other sorts of evidence of legal purpose. Thus the effectiveness of a deed depends on an expression of the right legal intention, "which is found upon examination of the whole instrument to be plainly though untechnically expressed."[10] Along similar lines, the Office of Legal Counsel has opined that the effectiveness of a presidential order does not depend on "the form or caption of the written document" but on the substance of what is said.[11] Here a requirement that the actor perform an act with the right meaning—that she express the right illocutionary intent—ensures, *inter alia*, that she intends the legal consequences of her act.

Contract law contains no such rules. With the decline of the seal, there are no longer any purely formal conditions of contractual validity. In fact, as a result of the rules that govern implied-in-fact contracts, acceptance by performance, battles of the forms, the use of course of performance evidence, and the like, parties need not even express their agreement in so many words. Nor do courts commonly look for other evidence of the parties' legal purpose. The Second Restatement of Contracts provides that "[n]either real nor apparent intention that a promise be legally binding is essential to the formation of a contract," and the comments imagine a contract being formed despite both parties' mistaken belief that their agreement is not legally enforceable.[12] And while the black-letter rule in England states that "[a]n agreement, though supported by consideration, is not binding as a contract if it was made without any intention of creating legal relations,"[13] English courts adopt in most cases so strong a presumption of such intent that Atiyah concludes it is "more realistic to say that no positive intention to enter into legal relations needs to be shown, and that 'a deliberate promise seriously made is enforced irrespective of the promisor's views regarding his legal liability.'"[14]

All of this is to say that if contract law is a power-conferring law, it is an odd one. Most power-conferring laws employ rules that clearly condition the legal consequences of an action on the actor's legal purpose. Such laws wear their power-conferring function on their sleeve: Validity conditions that sort for legal purpose anticipate and enable the law's

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10 Waller v. Brown, 149 S.E. 687, 688 (N.C. 1929).

11 Legal Effectiveness of a Presidential Directive, as Compared to an Executive Order, Op. Off. Legal Counsel (Jan. 29, 2000), http://www.usdoj.gov/olc/predirective.htm.

12 RESTATEMENT (SECOND) OF CONTRACTS § 21 & cmt. b, illus. 2 (1981).

13 GUENTER TREITEL, THE LAW OF CONTRACT 149 (10th ed. 1999).

14 P.S. ATIYAH, AN INTRODUCTION TO THE LAW OF CONTRACT 153 (5th ed. 1995) (quoting 1 SAMUEL WILLISTON, A TREATISE ON THE LAW OF CONTRACTS 39 (3d ed. 1957)).

purposive use. In fact, validity conditions that sort for legal purpose are strong evidence that the law's *only* function is to establish a legal power. If a law serves no purpose but to allow persons to effect legal change when they wish, it is not merely senseless but also counterproductive to apply it to acts not done for the sake of their legal consequences. To allow a person's actions to effect a legal change she neither expects nor wants is not to grant her control over the law but to take it away. Consequently, where a law is meant only to give persons the ability to effect legal change, we should expect it to include validity conditions that sort for legal purpose. By the same token, the presence of conditions of legal validity that sort for legal purpose indicates that this is the law's sole function.

One way to try to rescue a power-conferring picture of contract is to argue that the consideration requirement is a validity condition of this sort. Thus Lon Fuller's suggestion that consideration is a "natural formality,"[15] separating out for legal enforcement agreements in which "a legal transaction was intended."[16] But this is hardly the only, or the most obvious, interpretation of the consideration rule. Fuller himself observed that exchange also marks agreements "of sufficient importance to our social and economic order to justify the expenditure of the time and energy necessary" for enforcement.[17] Other explanations of consideration include the special moral qualities of exchange relationships, doubts about judicial competence to assess when to enforce gratuitous promises, and the argument that the rule is a historical anomaly, a myth created by Holmes and Williston that does not accurately describe how contract law functions. The consideration requirement provides, at best, equivocal support for an interpretation of contract law on the model of most power-conferring laws. More generally, it is simply not obvious that the conditions of contractual validity are designed to sort for legal purpose.

There is, however, another way to understand contract as a legal power, one that suggests an important difference between contract law and most power-conferring laws, and which expands our understanding of normative powers in general. The core thought is that it is possible for a law to anticipate and enable its purposive use without conditioning the legal effect of a person's actions on evidence of her legal purpose. I suggest reserving the term "power-conferring" for laws that include validity conditions that sort for legal purpose, such as those discussed in the previous paragraphs. I use the term "compound law" for laws that do not condition the legal consequences of an act on evidence of the actor's legal purpose but are structured in a way that both ensures that a significant proportion of actors subject to them are likely to have such a purpose and recognizes and facilitates that purposive use. As distinguished from power-conferring laws, the structure of compound laws suggests that they function

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15 Lon L. Fuller, *Consideration and Form*, 41 COLUM. L. REV. 799, 815 (1941).

16 *Id.* at 801.

17 *Id.* at 799.

both to impose duties and to create powers.

Compound laws so defined have four characteristic features, each of which contract law exhibits. First, because compound laws do not include conditions of validity that sort for legal purpose, we can expect persons sometimes to commit legally relevant acts for reasons other than their legal consequences. Contract law satisfies this condition because of the many reasons, independent of a desire to undertake a legal obligation, for entering into an agreement for consideration. Second, it must be possible to tell a story about why the law would want to attach legal consequences to acts of that sort, a story that does not involve empowering persons purposively to effect legal change. In the case of contract law, this will be a story about why we would want to hold parties legally liable for the nonperformance of exchange agreements regardless of whether they intended legal liability. A brief tour through contract theory suggests many possible stories of this sort. Third, while the law does not sort for legal purpose, the legal consequences must be such that a significant proportion of legal actors want to bring them about. Even if the conditions of contractual validity do not require a legal purpose, it is obvious that many parties do enter into contracts expecting and wanting legal enforcement.

Finally, a compound law must include rules that anticipate and enable its purposive use. It is not enough that some actors use the law instrumentally. A legal power exists only if the law is designed for such uses—only if it both expects and facilitates them. Many contract doctrines appear to work on the assumption that parties normally want or expect legal liability. Consider, for example, the statute of frauds, which requires that certain agreements be in writing to be enforceable.[18] A familiar explanation of the rule is that it is meant to give parties a new reason to create written evidence of their agreements: Only by doing so can parties get the advantages of legal enforcement.[19] The explanation assumes that many parties expect and want legal liability: Only if this is so does the rule give them a reason to write down their agreements. Other doctrines are designed to give parties greater ability to manipulate their legal obligations. The parol evidence rule, for example, provides that the parties can agree as to which of their prior agreements or communications will have a legal effect and which will not, increasing their control over the scope of their legal liability. These and other contract doctrines exemplify how a law can anticipate and enable its purposive use without conditioning an act's legal effect on the actor's legal purpose.

The design of contract law suggests that it is a multipurpose tool. Contract law functions to give persons the power to effect change in their legal duties toward one another when they wish. But unlike pure power-

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[18] RESTATEMENT (SECOND) OF CONTRACTS § 110 (listing types of contracts commonly covered by statutes of frauds).

[19] *See, e.g.*, Karl N. Llewellyn, *What Price Contract?—An Essay in Perspective*, 40 YALE L.J. 704, 747 (1931).

conferring rules, it does not include mechanisms to sort for a contractual purpose. That fact requires explanation. One can easily imagine a contract law that employs formal conditions of validity or that requires parties to perform a legal speech act or to state their intent to be bound. As Karl Llewellyn observed, "a business economy demands a means of quick, not one of 'informal' contracting."[20] The fact that the contract law we have includes none of these mechanisms suggests that its purpose is not only to confer powers but also to impose duties.

Moreover, contract rules that allow parties to control the scope or effect of their legal obligations also limit that power in ways consistent with a duty-imposing function. Thus while the parol evidence rule allows parties to define the scope of their legal obligations, courts will permit extrinsic evidence to determine whether a document is integrated, to resolve the meaning of ambiguous terms, and, in some jurisdictions, even to determine whether there is an ambiguity.[21] The Restatement provides that "a manifestation of intention that a promise shall not affect legal relations may prevent the formation of a contract"[22] but observes that partial performance by one side or a finding of unconscionability can render such a term unenforceable.[23] Courts will enforce a liquidated damages clause, giving the parties greater control over the legal consequences of a breach, but only if the amount is "reasonable in the light of the anticipated or actual loss,"[24] preventing parties from opting for the protection of supercompensatory damages. While contract law gives parties many tools for controlling the legal consequences of their agreements, those tools are limited in ways that prevent radical departures from the extralegal obligations they owe one another.

While compound rules share characteristics of both duty-imposing and power-conferring rules, they are not a simple mix of the two. Rather, as the above account is meant to show, they form a distinctive category of rules with a structure all their own. The appearance of this structure in contract law casts new light on the familiar tension between formalism and anti-formalism, as well as the historical battle between law and equity in contract. With respect to the practice of contract law, the compound picture explains and, in individual cases, can help resolve these tensions. With respect to contract theory, the empirical plausibility of the compound

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20 *Id.* at 741.

21 *See, e.g.*, Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co., 442 P.2d 641, 645–46 (Cal. 1968) (holding that court may consider extrinsic evidence in determining whether term is ambiguous); RESTATEMENT (SECOND) OF CONTRACTS § 209 (1981) (describing rule for determining when agreement is integrated); *id.* § 212 (describing rule for use of extrinsic evidence in interpreting ambiguous terms).

22 RESTATEMENT(SECOND) OF CONTRACTS § 21 (1981).

23 *Id.* § 21 cmt. b; *see also* Wendell H. Holmes, *The Freedom Not To Contract*, 60 TUL. L. REV. 751, 780–86 (1986) (describing cases in which agreements are enforced despite no-enforcement clauses).

24 RESTATEMENT(SECOND) OF CONTRACTS § 356(1) (1981).

picture provides an argument for pluralist interpretations, theories that view the contract law we have as animated by multiple, sometimes conflicting normative commitments.

The analysis of contract as a compound rule does not yet say what those normative commitments are. To know a law's function is not yet to know the principles that justify it. Thus, to say that contract law has a duty-imposing function is not yet to say whether the legal duty is grounded, for example, on the duty to perform, on a duty to compensate for harms caused, or if it is meant to protect and support the social practice of undertaking and performing voluntary obligations more generally. Similarly, to say contract law is also designed to create legal powers is not yet to say whether the law's reason for doing so is to increase autonomy, to achieve greater efficiency or is based on some other principle or principles.

The compound picture does explain, however, why the duty-power distinction deserves a place at the center of contract theory. Contractual relationships coincide with a constellation of similarly structured extralegal practices, such as agreement, exchange, cooperation, and promise. With the decline of the seal, contracts are not marked out by formal or other conditions of validity that unequivocally sort for a legal purpose, rules that would clearly identify contract law as power conferring. Yet there is no doubt that many parties expect and want legal enforcement and that the law is designed to facilitate such uses—characteristics that distinguish contract law from other, purely duty-imposing rules. Together, these distinctive features render both pure power-conferring and pure duty-imposing theories of contract law inherently contestable. They provide support for the idea that contract law partakes in characteristics of both and for the picture of contract law as a compound rule.