

# Comparative Contract Law and Development: The Missing Link?

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## ABSTRACT

*Contract law has long been a favorite area of study among comparative law scholars. Economists have posited that contract institutions play a central role in economic development. Yet, in sharp contrast to the state of the art in other fields (such as corporate law and bankruptcy law), the possible role of contract laws in shaping economic outcomes remains largely neglected. This Essay explores the main reasons that might explain this status quo. These are: (1) the lack of meaningful variation in contract laws around the world, (2) the triviality of contract law, (3) the ample availability of choice of law, (4) the U.S.-centric bias of the law and economics literature, (5) the lack of public data on contracting practices, and (6) the boundaries of contract law. It concludes that, while important, these factors are ultimately insufficient to justify the scarcity of works on the economic consequences of contract law, which could be a fruitful area for future research.*

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## INTRODUCTION

Does contract law matter from an economic standpoint? If so, differences in the laws of contract across various jurisdictions may

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produce divergent economic outcomes. Given the centrality of contractual arrangements to the operation of modern capitalism,<sup>1</sup> one would expect this to be a major question for researchers interested in the relationship between law and economic development. Yet, this is not what we see. In fact, the inquiry into the economic consequences of different contract laws around the world has received comparatively little scholarly attention.<sup>2</sup>

Such neglect of the economic implications of different contract laws is all the more surprising given the abundance of studies in the related fields of comparative contract law and institutional economics. Comparative contract law has long commanded significant attention from scholars and practitioners, making it *the* most traditional area of comparative legal analysis.<sup>3</sup> There is a voluminous literature mapping the distinctions in contract laws across various jurisdictions and legal traditions, as well as their evolution over time.<sup>4</sup> There are also numerous efforts seeking to bridge these differences through the unification or harmonization of contract laws.<sup>5</sup> The existing analyses, however,

<sup>1</sup> For Max Weber, “A legal order can indeed be characterized by the agreements which it does or does not enforce.” MAX WEBER, *ECONOMY AND SOCIETY* 668 (Guenther Roth & Claus Wittich eds., Ephraim Fischhoff et al. trans., Bedminster Press 1968) (1956).

<sup>2</sup> Aristotelis Boukouras, *Contract Law and Development* 2 (Dec. 4, 2011) (unpublished manuscript), <https://ssrn.com/abstract=2297450> (“[T]he literature on economic growth and development has placed emphasis on the importance of property rights and their enforcement, but contract law has received disproportionately less attention.”). For representative exceptions to this broader trend, see Katharina Pistor, *Legal Ground Rules in Coordinated and Liberal Market Economies*, in *CORPORATE GOVERNANCE IN CONTEXT: CORPORATIONS, STATES, AND MARKETS IN EUROPE, JAPAN, AND THE US* 249 (Klaus J. Hopt et al. eds., 2005); John C. Reitz, *Political Economy and Contract Law*, in *NEW FEATURES IN CONTRACT LAW* 247 (Reiner Schulze ed., 2007); and Aditi Bagchi, *The Political Economy of Regulating Contract*, 62 *AM. J. COMP. L.* 687 (2014).

<sup>3</sup> See E. Allan Farnsworth, *Comparative Contract Law*, in *THE OXFORD HANDBOOK OF COMPARATIVE LAW* 899, 900 (Mathias Reimann & Reinhard Zimmermann eds., 2006) (“Of all areas of law, perhaps none has been subjected to comparative study as consistently, frequently, and intensely as contract law. . . . [I]f there is a classical subject-matter of comparative law, that title should be awarded to the law of contract.”).

<sup>4</sup> See, e.g., *COMPARATIVE CONTRACT LAW: BRITISH AND AMERICAN PERSPECTIVES* (Larry A. DiMatteo & Martin Hogg eds., 2016); *GOOD FAITH IN EUROPEAN CONTRACT LAW* (Reinhard Zimmermann & Simon Whittaker eds., 2000); 7 *INTERNATIONAL ENCYCLOPEDIA OF COMPARATIVE LAW* (Arthur von Mehren ed., 1982).

<sup>5</sup> The most prominent harmonization effort is the Vienna Convention for the International Sale of Goods (“CISG”), which is now in force in more than 80 countries. *Status: United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980)*, UNITED NATIONS COMM’N ON INT’L TRADE L., [http://www.uncitral.org/uncitral/en/uncitral\\_texts/sale\\_goods/1980CISG\\_status.html](http://www.uncitral.org/uncitral/en/uncitral_texts/sale_goods/1980CISG_status.html) [<https://perma.cc/HZ6X-CZBT>] (last visited Sept. 25, 2017). Other significant initiatives are the UNIDROIT Principles of International Commercial Contracts, the various EU Directives on consumer contracts, and the academic effort leading to the Principles of European Contract Law. UNIDROIT PRINCIPLES OF INTERNATIONAL COMMERCIAL CON-

are mostly doctrinal in nature, and generally fail to examine the economic consequences of the divergent legal regimes.

At the same time, the booming field of institutional economics has focused extensively on the economic implications of different legal institutions. Among these institutions, the so-called “contract institutions” play a central role. Nobel laureate Douglass North went so far as to argue that “the inability of societies to develop effective, low-cost enforcement of contracts is the most important source of both historical stagnation and contemporary underdevelopment in the Third World.”<sup>6</sup> The World Bank includes a specific indicator for “enforcing contracts” in its influential and controversial Doing Business Report.<sup>7</sup> Economists have undertaken numerous empirical studies to investigate the economic consequences of contract institutions.<sup>8</sup>

Nevertheless, this large body of works on “contract institutions” is surprisingly devoid of any discussion of contract *law* as the field is understood by legal scholars and practitioners. Contract institutions are equated with the existence and effectiveness of third-party enforcement mechanisms to make good on the parties’ agreement. These works evaluate the quality of contract institutions based exclusively on measures of procedure, such as the duration and cost of the enforcement process and the number of appeals involved.<sup>9</sup> There is no

TRACTS (2010); PRINCIPLES OF EUROPEAN CONTRACT LAW: PART 1 (Ole Lando & Hugh Beale eds., 1995); PRINCIPLES OF EUROPEAN CONTRACT LAW: PARTS 1–2 (Ole Lando & Hugh Beale eds., 2000); PRINCIPLES OF EUROPEAN CONTRACT LAW: PART 3 (Ole Lando, Eric Clive, André Prum & Reinhard Zimmermann eds., 2003).

6 DOUGLASS C. NORTH, INSTITUTIONS, INSTITUTIONAL CHANGE AND ECONOMIC PERFORMANCE 54 (1990).

7 THE WORLD BANK, DOING BUSINESS 2016: MEASURING REGULATORY QUALITY AND EFFICIENCY 91 (13th ed. 2016), <http://www.doingbusiness.org/~media/WBG/DoingBusiness/Documents/Annual-Reports/English/DB16-Full-Report.pdf>. For a critique of the Doing Business project, see Bénédicte Fauvarque-Cosson & Anne-Julie Kerhuel, *Is Law an Economic Contest? French Reactions to the Doing Business World Bank Reports and Economic Analysis of the Law*, 57 AM. J. COMP. L. 811 (2009).

8 See, e.g., Daron Acemoglu & Simon Johnson, *Unbundling Institutions*, 113 J. POL. ECON. 949 (2005); Holger Spamann, *Legal Origins, Civil Procedure, and the Quality of Contract Enforcement*, 166 J. INSTITUTIONAL & THEORETICAL ECON. 149 (2010). For an excellent review of this literature, see Michael Trebilcock & Jing Leng, *The Role of Formal Contract Law and Enforcement in Economic Development*, 92 VA. L. REV. 1517 (2006).

9 See THE WORLD BANK, *supra* note 7, at 20 (measuring contract enforcement in terms of the “[t]ime and cost to resolve a commercial dispute and the quality of judicial processes”); see also Acemoglu & Johnson, *supra* note 8, at 951 (using three procedural proxies to measure contract institutions: (1) the number of procedures necessary to collect on an unpaid check, (2) an “index of procedural complexity,” and (3) the number of procedures necessary to resolve a court case on commercial debt); Spamann, *supra* note 8 (employing mostly measures of civil procedure to compare the enforceability of contracts in common and civil law jurisdictions). According to Acemoglu & Johnson, even an “ideal proxy” for contract institutions would simply “measure the

consideration of the substance of what is actually enforced. This approach thus fails to give any weight to the fundamental questions of contract law, namely (1) how to determine the content of the parties' agreement, which is often not self-evident, and (2) which agreements courts should enforce, since no legal system in the world offers state support to any and all promises that the parties write, sometimes for good economic reasons.<sup>10</sup>

To be sure, the existing literature on institutional economics has produced equivocal results, even on the economic importance of formal contract institutions in general.<sup>11</sup> A significant number of those works suggest that extralegal mechanisms—such as reliance on kinship, social norms, and reputation—can serve as effective substitutes for formal judicial enforcement of contracts by the state.<sup>12</sup> Other studies, by contrast, find that the need for formal enforcement increases with economic growth and the rising complexity of economic exchange.<sup>13</sup> Despite the existence of academic disagreement on the importance of contract institutions, it still does not explain the lack of interest in investigating the possible role of contract laws in shaping contract design and the choice of organizational form.<sup>14</sup> Moreover, the

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costs of enforcing private contracts,” as if the substance of what is actually enforced did not at all matter or vary across jurisdictions. See Acemoglu & Johnson, *supra* note 8, at 951.

<sup>10</sup> See MICHAEL J. TREBILCOCK, *THE LIMITS OF FREEDOM OF CONTRACT* 2 (1993). The related concept of freedom of contract is also not self-explanatory, and instead exhibits significant variation across capitalist economies. See Duncan Kennedy, *Law-and-Economics from the Perspective of Critical Legal Studies*, in *THE NEW PALGRAVE DICTIONARY OF ECONOMICS AND THE LAW* 465, 467 (Peter Newman ed., 1998) (“The actual legal systems of developed capitalist societies may: (a) refuse to enforce many contracts by (i) categorically excluding some, (ii) excluding others on grounds of defects in formation, and (iii) excusing performance for one reason or another based on subsequent events; (b) provide very different levels of support for people trying to enforce contracts, with consequences for how meaningful or valuable the promise will turn out to be; (c) require contracts in many situations; and (d) impose terms in many kinds of contracts regardless of the agreement of the parties.”).

<sup>11</sup> See Trebilcock & Leng, *supra* note 8, at 1573.

<sup>12</sup> See *id.* at 1537–54.

<sup>13</sup> See, e.g., *id.* at 1543 (citing Daniel Berkowitz et al., *Legal Institutions and International Trade Flows*, 26 MICH. J. INT'L L. 163, 164 (2004)).

<sup>14</sup> As Claude Ménard and Mary Shirley have noted, this future agenda would allow New Institutional Economics to integrate the contributions of Douglass North and Oliver Williamson. Claude Ménard & Mary M. Shirley, *The Contribution of Douglass North to New Institutional Economics*, in *INSTITUTIONS, PROPERTY RIGHTS, AND ECONOMIC GROWTH: THE LEGACY OF DOUGLASS NORTH* 11, 28 (Sebastian Galiani & Itai Sened eds., 2014). In outlining this line of inquiry, they note:

A foremost issue will be: How do the (Northeastern) rules that determine the security and functioning of property rights or the laws that affect contractual credibility and enforcement shape the choice of (Williamsonian) modes of governance and of the ways to organize transactions? A related question is: What are the comparative

presence of general skepticism about the law's actual contribution to economic development has coexisted with the expansion of the field.<sup>15</sup>

There is no question that measuring differences in legal regimes and evaluating their actual effects are no easy tasks.<sup>16</sup> These challenges, however, have not prevented the emergence of a robust empirical literature that attempts to determine the economic consequences of different regimes of corporate law and bankruptcy.<sup>17</sup> The scarcity of studies on the relationship between contract law and development is even more surprising given that some of the most prominent contemporary scholars in the field of "law and development" are also contract law scholars.<sup>18</sup>

This Essay examines this apparent puzzle by analyzing various reasons that might explain such assumed disregard for the possible role of contract law in shaping economic outcomes. The reasons examined are (1) the lack of meaningful variation in contract laws around the world, (2) the triviality of contract law, (3) the ample availability of choice of law, (4) the U.S.-centric bias of the law and economics literature, (5) the lack of public data on contracting practices, and (6) the problem of defining the boundaries of contract law. This Essay concludes that, although important, these factors are ultimately insufficient justifications for the scarcity of works on the economic consequences of contract law. Therefore, those economic consequences remain a fruitful area for future research.

## I. DOES CONTRACT LAW MATTER?

### A. *Inexistence of Real Differences*

Comparative law would not matter from an economic perspective if there were no actual differences in the outcomes produced by different countries' laws. A central theme of comparative scholarship is

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costs of different institutional schemes, such as different judicial systems for implementing contractual laws?

*Id.*

<sup>15</sup> See generally Kevin E. Davis & Michael J. Trebilcock, *The Relationship Between Law and Development: Optimists Versus Skeptics*, 56 AM. J. COMP. L. 895 (2008).

<sup>16</sup> For a discussion of the promises and limitations of the use of quantitative methods in this area, see Holger Spamann, *Empirical Comparative Law*, 11 ANN. REV. L. & SOC. SCI. 131 (2015).

<sup>17</sup> For a few representative examples, see John Armour & Douglas Cumming, *Bankruptcy Law and Entrepreneurship*, 10 AM. L. & ECON. REV. 303 (2008); Rainer Haselmann, Katharina Pistor & Vikrant Vig, *How Law Affects Lending*, 23 REV. FIN. STUD. 549 (2010); and Rafael La Porta, Florencio Lopez-de-Silanes, Andrei Shleifer & Robert W. Vishny, *Law and Finance*, 106 J. POL. ECON. 1113 (1998).

<sup>18</sup> A few prominent examples are Michael Trebilcock and Kevin Davis.

that, despite apparent differences in doctrinal formulations, the laws of different jurisdictions often lead to the same outcomes. While differences in doctrinal routes may captivate legal scholars, they are less likely to make an impression on businesspeople structuring their transactions if the practical results are identical. Prominent comparatists Konrad Zweigert and Hein Kötz have gone so far as to advocate for the existence of a “*praesumptio similitudinis*” in comparative law, which assumes the absence of actual differences in the various jurisdictions’ approaches to the same problems.<sup>19</sup>

If the contract laws of different jurisdictions are always equivalent from a functional perspective, one will not expect differences in the formulation of legal rules to produce distinct economic consequences. As in other areas of law, it is indeed the case that divergent contract law rules and doctrines address the same economic problems and frequently lead to the same results. To take just one prominent example, the volume on *Good Faith in European Contract Law* by Reinhard Zimmermann and Simon Whittaker is rife with hypothetical fact patterns showing how different jurisdictions reach the same outcomes through different doctrinal arguments.<sup>20</sup>

One could go further and argue that the observed distinctions in contract law doctrines are particularly nuanced. Consequently, although not unique to contract law, the pattern of functional equivalence is more pronounced in contract law than in other legal fields. Despite significant functional convergence, corporate laws are marked by substantial formal distinctions that appear to be practically relevant. For instance, most countries lack the strong version of employee board representation (or “codetermination”) in company boards, as mandated under German law.<sup>21</sup>

Existing distinctions in the laws of contracts, by contrast, are generally ones of degree. To take a prominent example, a classical difference in comparative law is that specific performance is, as a formal

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19 K. ZWIEGERT & H. KÖTZ, AN INTRODUCTION TO COMPARATIVE LAW 40 (Tony Weir trans., 3d ed. 1998). For a discussion of critiques to this presumption and to the functional method generally, see Ralf Michaels, *The Functional Method of Comparative Law*, in THE OXFORD HANDBOOK OF COMPARATIVE LAW, *supra* note 3, at 339.

20 See generally GOOD FAITH IN EUROPEAN CONTRACT LAW (Reinhard Zimmermann & Simon Whittaker eds., 2000) (finding, however, significant convergence in the outcome of various hypotheticals).

21 Luca Enriques, Henry Hansmann, Reinier Kraakman & Mariana Pargendler, *The Basic Governance Structure: Minority Shareholders and Non-Shareholder Constituencies*, in REINIER KRAAKMAN ET AL., THE ANATOMY OF CORPORATE LAW: A COMPARATIVE AND FUNCTIONAL APPROACH 79, 102 (3d ed. 2017).

matter, more widely available in civil law jurisdictions than in common law jurisdictions, even though civil law jurisdictions deny, and common law jurisdictions grant, specific relief in various circumstances.<sup>22</sup> This permits a significant, though not complete, overlap in terms of practical results.<sup>23</sup>

Yet the very prominence of unification and harmonization efforts in the law of contracts suggests that existing legal differences can be consequential from a practical standpoint.<sup>24</sup> Formal differences that produce identical results are unlikely to constitute a costly impediment to international commerce. Although one cannot rule out the personal benefits to participants (through, e.g., increased prestige) in driving these processes, the persistent emphasis on harmonization of contract laws implies that real-world outcomes are at stake.

To be sure, and in part because of the success of such harmonization efforts, there is an important sense in which the laws of contract of various jurisdictions have been converging over time, to the effect that differences may be less pronounced than they once were. Beyond efforts in the international arena, the recent revisions to the German and French Civil Codes aim, at least in part, to emulate some of the elements of the common law of contracts. Nevertheless, even if differences in legal treatment are always relative<sup>25</sup>—and may be smaller than in the past—they certainly persist. Whether they matter from an economic standpoint should be an open question, not a foregone conclusion.

### B. *Triviality of Contract Law*

Even if differences exist, one would not expect them to matter if it is clear, from a theoretical standpoint, that contract law is wholly

<sup>22</sup> See RUDOLF B. SCHLESINGER, HANS W. BAADÉ, PETER E. HERZOG & EDWARD M. WISE, *COMPARATIVE LAW* 739 (6th ed. 1998) (“[T]he civilians’ recognition of the obligee’s right to specific performance (so long as such performance is not shown to be actually impossible) stands in marked contrast to the common law’s preference for non-specific remedies.”); JAN M. SMITS, *CONTRACT LAW: A COMPARATIVE INTRODUCTION* 10–11 (2014).

<sup>23</sup> JAMES GORDLEY & ARTHUR TAYLOR VON MEHREN, *AN INTRODUCTION TO THE COMPARATIVE STUDY OF PRIVATE LAW: READINGS, CASES, MATERIALS* 534 (2006) (“Claims for performance may not be very frequent in practice . . . .”); Henrik Lando & Caspar Rose, *On the Enforcement of Specific Performance in Civil Law Countries*, 24 *INT’L REV. L. & ECON.* 473, 486 (2004) (“The remedy is available but rarely sought in Germany and France, and has been (virtually) abolished as a remedy for production contracts in Denmark.”).

<sup>24</sup> See *supra* note 20 and accompanying text.

<sup>25</sup> James Q. Whitman, *The Two Western Cultures of Privacy: Dignity Versus Liberty*, 113 *YALE L.J.* 1151, 1163 (2004) (“But the issue is not whether there is an absolute difference. Comparative law is the study of *relative* differences.”).

trivial. For our purposes, the “triviality hypothesis” means that contract law does not in any way prevent the parties from structuring exactly the deal they want.<sup>26</sup> If this is the case, variations in contract law should not affect the form of economic organization in society—which would explain why scholars may not be inclined to study this theme.

One reason why contract law is instinctively deemed to be trivial is the notion that most, if not all, rules of contract law have the nature of default rules. Default rules apply, as their name suggests, “in default” of the parties’ agreement, but parties are free to adopt a different regime if they so choose. For instance, the U.S. Uniform Commercial Code implies a warranty of merchantability in every contract, but the parties are free to exclude it if they so wish.<sup>27</sup>

There is no question that many rules in the laws of contract have the nature of default rules. Yet, the prevalence of default rules does not render contract law necessarily trivial for at least two reasons. First, the existence and choice of default rules is not devoid of economic consequences. If the law provides a rule that the parties do not want, this will increase transaction costs—whose magnitude, in turn, will depend on the particular mechanism that the law requires for the parties to opt out of the default regime.<sup>28</sup> Moreover, by imposing a default rule that most parties would like to avoid (what Ian Ayres and Robert Gertner have dubbed a “penalty default” rule), the law can enhance efficiency by bridging the information asymmetry between the parties and the informational burden imposed on courts.<sup>29</sup>

This means that some default rules will be more efficient than others, and can thereby potentially affect contract design and the cost of doing business. Germany has explicitly advertised that its statutory default rules for specific types of contracts, as well as the “catch-all provisions that apply in cases where the contractual parties have not agreed otherwise,” make German contracts “more cost-effective and reliable than contractual agreements under English or US law.”<sup>30</sup> Some continental scholars have even advanced the quixotic claim,

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<sup>26</sup> For a slightly different articulation of the triviality hypothesis in the context of corporate law, see Bernard S. Black, *Is Corporate Law Trivial? A Political and Economic Analysis*, 84 Nw. U. L. REV. 542, 544, 551 (1990).

<sup>27</sup> U.C.C. §§ 2-314, 2-316 (AM. LAW INST. & UNIF. LAW COMM’N 2014).

<sup>28</sup> For a typology of these different mechanisms, see Ian Ayres, *Regulating Opt-Out: An Economic Theory of Altering Rules*, 121 YALE L.J. 2032, 2045 (2012).

<sup>29</sup> Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87, 91 (1989).

<sup>30</sup> LAW MADE IN GERMANY 7 (3d ed. 2014), [http://www.lawmadeingermany.de/Law-Made\\_in\\_Germany\\_EN.pdf](http://www.lawmadeingermany.de/Law-Made_in_Germany_EN.pdf) [<https://perma.cc/DAL4-MB6J>] (emphasis removed).

based on questionable empirical evidence, that the type of statutory default rules found in civil law jurisdictions makes a positive contribution to economic development.<sup>31</sup>

Second, a variety of factors make it exceedingly difficult for parties to opt out of default rules, making them effectively “sticky” in practice. Judges may regard the legal defaults as embodying a superior ideal of fairness, and thereby refuse to recognize voluntary deviations from the default regime.<sup>32</sup> Taiwanese courts, for instance, have insisted on applying the statutory rules to private contracts that would appear to have opted out of the default scheme.<sup>33</sup>

In addition, the very presence of default rules may trigger behavioral biases that distort the parties’ preferences. Endowment effects and the status quo bias discourage deviations from the legal default, making their existence and content far more consequential.<sup>34</sup> Precisely because their existence matters, some law and economics scholars have strongly advocated against the provision of default rules by statutes and restatements, maintaining that they hinder, rather than help, the adoption of efficient contracting practices by commercial parties.<sup>35</sup>

Despite the prominence of default rules, contract law also contains a fair number of mandatory rules.<sup>36</sup> Where they exist, the doctrines of good faith and unconscionability, the ban on penalty clauses, and restrictions on specific performance—to name just a few examples—are all mandatory rules.<sup>37</sup> This means that they are immutable from the perspective of the contract parties, who cannot provide for a different regime in their agreement.

31 See Raouf Boucekkiné et al., *Contract Rules in Codes and Statutes: Easing Business Across the Cleavages of Legal Origins*, in *INSTITUTIONAL COMPETITION BETWEEN COMMON LAW AND CIVIL LAW: THEORY AND POLICY* 41, 43–44 (Michèle Schmiegelow & Henrik Schmiegelow eds., 2014).

32 See Alan Schwartz & Robert E. Scott, *Contract Theory and the Limits of Contract Law*, 113 *YALE L.J.* 541, 596 (2003).

33 Wen-Yeu Wang, *The Evolution of Contract Law in Taiwan: Lost in Interpretation?*, in *PRIVATE LAW IN CHINA AND TAIWAN: LEGAL AND ECONOMIC ANALYSES* 100, 101 (Yun-chien Chang et al. eds., 2017).

34 See Marcel Kahan & Michael Klausner, *Path Dependence in Corporate Contracting: Increasing Returns, Herd Behavior and Cognitive Biases*, 74 *WASH. U. L.Q.* 347, 359, 361–62 (1996); Russel Korobkin, *Inertia and Preference in Contract Negotiation: The Psychological Power of Default Rules and Form Terms*, 51 *VAND. L. REV.* 1583, 1584 (1998); Russell Korobkin, *The Status Quo Bias and Contract Default Rules*, 83 *CORNELL L. REV.* 608, 631 (1998).

35 See Alan Schwartz & Robert E. Scott, *The Common Law of Contract and the Default Rule Project*, 102 *VA. L. REV.* 1523, 1572 (2016).

36 See Black, *supra* note 26, at 545–46.

37 *Id.* at 573.

Even if unavoidable, a mandatory rule could still be trivial if it invariably mimics market outcomes—that is, it always provides parties with the rule they would have chosen.<sup>38</sup> If no party would ever want to stipulate a contractual penalty or prevent the application of the duty of good faith, then their mandatory character becomes irrelevant. However, this is not necessarily the case. The mandatory rules mentioned above, for instance, are the object of both intense scholarly controversies about their efficiency and fairness, as well as significant variation across jurisdictions.<sup>39</sup> The number of mandatory contract terms can be quite substantial in different countries, further suggesting that contract law is unlikely to be trivial.<sup>40</sup>

### C. Choice of Law

Even if jurisdictional differences in contract law are not trivial, they are unlikely to matter from an economic standpoint if the parties can avoid a suboptimal regime and pick the most efficient one for their purposes at low or no cost.<sup>41</sup> It turns out that many legal systems have converged in recognizing party autonomy as to choice of law in contracts, even though various exceptions continue to apply.<sup>42</sup> This means that parties enjoy considerable leeway in picking the law of their choosing to govern the terms of their agreement.

Choice of law is not just a theoretical possibility, but also a recurrent feature of modern business practice. Choice-of-law clauses are routine in commercial agreements, with most international contracts specifically providing for them.<sup>43</sup> Indeed, their existence has induced the phenomenon of “regulatory competition” in contract law, as different jurisdictions strive to attract contract parties based on the ad-

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<sup>38</sup> *Id.* at 544 (arguing that mandatory rules may be trivial if they are “market mimicking,” that is, they “would be universally adopted anyway”).

<sup>39</sup> See Mariana Pargendler, *The Role of the State in Contract Law: The Common-Civil Law Divide*, 43 *YALE J. INT’L L.* (forthcoming 2017), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2848886](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2848886).

<sup>40</sup> *Id.* at 15.

<sup>41</sup> Choice of legal regime is a prominent development strategy. For examples from the corporate law context, see Ronald J. Gilson, Henry Hansmann & Mariana Pargendler, *Regulatory Dualism as a Development Strategy: Corporate Reform in Brazil, the United States, and the European Union*, 63 *STAN. L. REV.* 475 (2011).

<sup>42</sup> Mathias Reimann, *Savigny’s Triumph? Choice of Law in Contract Cases at the Close of the Twentieth Century*, 39 *VA. J. INT’L L.* 571, 576 (1999). For the United States, see RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 187 (AM. LAW INST. 1971). For the European Union, see Convention on the Law Applicable to Contractual Obligations 1980 O.J. (L 266) 23.

<sup>43</sup> Giesela Rühl, *Party Autonomy in the Private International Law of Contracts: Transatlantic Convergence and Economic Efficiency*, in *CONFLICT OF LAWS IN A GLOBALIZED WORLD* 153, 157 (Eckart Gottschalk et al. eds., 2007).

vantages of their contract regime—an effort that, incidentally, reinforces the notion that contract law matters.<sup>44</sup>

The desire to attract contracting parties (and, ultimately, legal work) has elicited, among other things, a “battle of the brochures” in which countries advertise the benefits of their legal system.<sup>45</sup> While England emphasizes the absence of a duty of good faith, Germany highlights the role of statutory terms and other gap-fillers in enhancing legal certainty and reducing transaction costs.<sup>46</sup> Unlike corporate charters, which are filed with the state and publicly available, contracts are typically private documents, making it difficult to ascertain the winner of this particular form of competition. The limited empirical evidence available on this issue, based on data from the International Court of Arbitration, shows English and Swiss law as the most popular governing laws.<sup>47</sup>

Still, the fact that sophisticated parties often opt into foreign laws in large commercial transactions does not mean that such choice is (1) costless and (2) always available. If these conditions do not hold, then choice of law does not eradicate the possible negative effects of any country with inefficient contract laws. In practice, it turns out that choice of a foreign law to govern a domestic contractual dispute is often either (1) too costly or (2) unavailable as a matter of law.

Avoiding domestic contract laws by opting into a foreign legal regime entails costs both in the front and back end of the contracting process.<sup>48</sup> In the front end, during the parties’ negotiation and drafting stage, it will often require the retention of foreign legal counsel in addition to domestic counsel. This arrangement, however, possibly leads not only to unnecessary duplication of efforts, but also to greater

<sup>44</sup> Stefan Vogenauer, *Regulatory Competition Through Choice of Contract Law and Choice of Forum in Europe: Theory and Evidence*, 21 EUR. REV. PRIV. L. 13, 30 (2013).

<sup>45</sup> *Id.* at 30–33.

<sup>46</sup> See THE LAW SOCIETY OF ENGLAND AND WALES, ENGLAND AND WALES: THE JURISDICTION OF CHOICE 5 (2007), <http://www.eversheds-sutherland.com/documents/LawSocietyEnglandAndWalesJurisdictionOfChoice.pdf> [<https://perma.cc/9CRH-39WP>]; LAW MADE IN GERMANY, *supra* note 30, at 7.

<sup>47</sup> Gilles Cuniberti, *The International Market for Contracts: The Most Attractive Contract Laws*, 34 NW. J. INT’L L. & BUS. 455, 472 (2014) (finding that English and Swiss law are chosen three times more frequently than their closest competitors); Stefan Voigt, *Are International Merchants Stupid? Their Choice of Law Sheds Doubt on the Legal Origin Theory*, 5 J. EMPIRICAL LEGAL STUD. 1, 15 (2008) (“The results seem to indicate that Swiss law is most attractive, followed by English law . . .”). Admittedly, however, the use of International Chamber of Commerce arbitrations as the sole source of the data introduces important biases into these studies’ findings.

<sup>48</sup> For a distinction between front- and back-end costs, see Robert E. Scott & George G. Triantis, *Anticipating Litigation in Contract Design*, 115 YALE L.J. 814 (2006).

legal fees—as sophisticated foreign counsel in “in-demand” jurisdictions likely face higher demand for their services, and can therefore command higher compensation.

Moreover, the choice of a foreign governing law will likely also affect the choice of the back-end mechanism of contract enforcement. It will be far more difficult for a local judge to enforce a foreign-law governed agreement in an accurate manner. To the extent accurate enforcement is possible, it will typically require significant expenditure in translations and expert opinions to educate the local court, adding significantly to both the costs and duration of the enforcement process. At the same time, legal obstacles relating to jurisdiction and enforcement hinder the ability of domestic parties to litigate their contract disputes in foreign courts.<sup>49</sup>

An attractive alternative would be to choose arbitration as the preferred mode of dispute resolution, since parties can pick arbitrators who are trained in, or otherwise familiar with, the governing law of the contract. Indeed, choice of foreign laws is a recurrent feature of international commercial arbitrations.<sup>50</sup> Yet, this does not make the flight to arbitration necessarily efficient.

Arbitrations, which are not subsidized by the state, are more expensive than judicial proceedings in a number of countries.<sup>51</sup> Moreover, a number of factors—most notably the tendency to “split the difference”—may make arbitration an imperfect substitute to state-sponsored courts.<sup>52</sup> One empirical study has found that parties to large transactions in the United States—a country that is deemed to have an efficient system of contract law and enforcement—are far more likely to pick judicial resolution over arbitration of disputes.<sup>53</sup> This suggests that choice of law, if available, may lead to the adoption of second-best mechanisms of contract enforcement, and, potentially, to suboptimal contracting practices. When it comes to transactions of lower value between small businesses, the costs associated with the

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<sup>49</sup> See Jens Dammann & Henry Hansmann, *Globalizing Commercial Litigation*, 94 CORNELL L. REV. 1, 18–31 (2008) (describing the challenges discouraging the extraterritorial litigation of commercial disputes).

<sup>50</sup> See *supra* note 47 and accompanying text.

<sup>51</sup> See Dammann & Hansmann, *supra* note 49, at 37.

<sup>52</sup> *Id.* at 31–39.

<sup>53</sup> Theodore Eisenberg & Geoffrey P. Miller, *The Flight from Arbitration: An Empirical Study of Ex Ante Arbitration Clauses in the Contracts of Publicly Held Companies*, 56 DEPAUL L. REV. 335, 350–52 (2007) (finding that only about 11% of the contracts in their sample had arbitration clauses, representing roughly 10% of the domestic contracts and 20% of the international contracts).

application of foreign laws are likely to be prohibitive in most circumstances.

Beyond the cost considerations that often make the choice of foreign law impracticable or unattractive, such a choice is often simply unavailable as a matter of law. First, the embrace of private autonomy in the determination of the applicable law is still incomplete in many jurisdictions, many of which are developing countries with less than ideal legal systems. Brazilian law, for instance, arguably continues to deny the contracting parties the ability to choose the applicable law to the contract outside of the arbitration context.<sup>54</sup> Other Latin American countries also follow a similarly restrictive approach to choice of law.<sup>55</sup>

Second, and more importantly, party autonomy is far from absolute, even in jurisdictions that most strongly embrace it. Instead, a number of exceptions restrict the parties' ability to elect a law of their choosing. First, choice of law is typically unavailable in purely domestic cases.<sup>56</sup> This is a major limitation for countries that have inefficient contract laws, and one that could have serious economic implications. Second, most jurisdictions require that the chosen law have a sufficient relationship to the parties or the transaction,<sup>57</sup> which represents another constraint on parties from jurisdictions with suboptimal laws. Third, jurisdictions severely constrain, though to varying degrees, the ability of contract parties to choose foreign laws that negatively impinge on consumers' and workers' rights.<sup>58</sup>

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<sup>54</sup> Nadia de Araujo & Fabiola I. Guedes de C. Saldanha, *Recent Developments and Current Trends on Brazilian Private International Law Concerning International Contracts*, in 1 PANORAMA OF BRAZILIAN LAW 73, 81–83 (Jacob Dolinger et al. eds., 2013).

<sup>55</sup> María Mercedes Albornoz, *Choice of Law in International Contracts in Latin American Legal Systems*, 6 J. PRIV. INT'L L. 23, 43–48 (2010).

<sup>56</sup> Rühl, *supra* note 43, at 159–60.

<sup>57</sup> *Id.* at 160. New York law is a prominent exception, as section 5-1401 of the General Obligations Law (“GOL”) dispenses with the requirement of a reasonable relation in contracts involving at least US \$250,000. N.Y. GEN. OBLIG. LAW § 5-1401 (McKinney 2017). Section 5-1402 of the GOL permits any party to sue a foreign party in New York courts for contracts governed under New York law whose obligations amount to at least US \$1 million. *Id.* § 5-1402.

<sup>58</sup> Jurisdictions adopt different approaches in this respect, with the European Union being more restrictive than the United States in constraining choice of law in the consumer context. See James J. Healy, *Consumer Protection Choice of Law: European Lessons for the United States*, 19 DUKE J. COMP. & INT'L L. 535, 557–58 (2009) (finding that U.S. courts have inconsistently applied public policy considerations to guarantee consumer protections afforded by home state laws).

Finally, all jurisdictions deny enforcement to foreign laws that violate the state's *ordre public* or fundamental public policy.<sup>59</sup> For example, a recent German decision refused to enforce the choice of the laws of Virginia in a commercial agency contract because Virginia did not recognize the generous post-termination indemnity rights enjoyed by agents under German law.<sup>60</sup> To the extent that these core public policies differ across jurisdictions—and they certainly do—the availability of foreign laws does not eliminate the potential shortcomings of a given country's laws.

In sum, choice of law is no panacea for the possible inefficiencies of a given country's contract laws. It is often costly and limited in scope, and fails to come to the rescue of parties in critical circumstances, such as purely domestic transactions. Nor is choice of law unique to the contract realm. While entrepreneurs may incorporate their businesses abroad—thereby mitigating the possible shortcomings of local laws—the agenda of improving national corporate laws as a development strategy has not weakened, given the costs of opting out of the domestic legal regime.<sup>61</sup>

#### D. *The Dominant Approach in U.S. Law and Scholarship*

Another factor explaining the lack of interest in contract law from a development standpoint has to do with the particular contours of the field in the United States. Studies in comparative law works are inevitably shaped by the particular lenses of the researcher, which determine the object of investigation. The dominant perspective in the U.S. environment is key, given that the country is the source of the vast majority of works both in law and economics and in institutional economics. Quite naturally, scholars interested in institutional work are more likely to focus on issues that seem important to them. This factor has at least three distinct, though complementary, dimensions.

First, the nature of U.S. contract law is such that most of the factors identified above appear to be more persuasive there than in other countries. Although this is a relative difference—as are all differences

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<sup>59</sup> See generally Kent Murphy, Note, *The Traditional View of Public Policy and Ordre Public in Private International Law*, 11 GA. J. INT'L & COMP. L. 591 (1981).

<sup>60</sup> Franco Ferrari, *Forum Shopping: A Plea for a Broad and Value-Neutral Definition* 31–32 (N.Y.U. Sch. of Law, Pub. Law & Legal Theory Research Paper Series, Paper No. 14-39, 2014), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2474181](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2474181) (citing Bundesgerichtshof [BGH] [Federal Court of Justice] Sept. 5, 2012, VII ZR 25/12 (Ger.)).

<sup>61</sup> For the existence of choice on corporate law, as well as the continued relevance of domestic legal reform to the development agenda, see Gilson, Hansmann & Pargendler, *supra* note 41, at 507–12.

in comparative law<sup>62</sup>—the common law of contracts generally grants the parties greater leeway in determining the substance of contract terms, as well as in choosing the law applicable to their agreement.<sup>63</sup> The relatively greater freedom of contract afforded by U.S. law helps substantiate the belief of contract law’s irrelevance. Compared to other jurisdictions, the lesser degree of state intervention in U.S. law contributes to the sense that contract law is trivial, either on its own terms or because undesirable restrictions can be easily avoided through choice of law. This naturally discourages the analysis of the economic consequences of legal variation, which is generally assumed away.

Second, not only is there a general perception that contract law is trivial from a descriptive perspective, but there is also a growing sense that such an “empty” version of contract law is desirable from a normative standpoint. To be sure, the debate about the role of contract law in promoting efficiency and distribution objectives is an old one and remains unresolved. Yet, aside from various influential noninstrumental analyses by legal philosophers,<sup>64</sup> the increasingly prevalent view in contemporary contract scholarship is that contract law’s primary mission is to further efficiency, and that it can best do so if its role is minimal with as few mandatory rules (and, for some authors, as few default rules) as possible.<sup>65</sup> In the last few decades, U.S. scholars interested in using substantive laws to further distributional or macroeconomic goals have largely gravitated towards bankruptcy law.<sup>66</sup> Yet, this “empty” view of contract law is far stronger in the U.S. context than elsewhere, with European scholars insisting that a “socially infused” law of contracts should remain high on the agenda.<sup>67</sup>

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<sup>62</sup> See *supra* note 25 and accompanying text.

<sup>63</sup> Pargendler, *supra* note 39, at 26.

<sup>64</sup> See generally CHARLES FRIED, *CONTRACT AS PROMISE: A THEORY OF CONTRACTUAL OBLIGATION* (1981); Daniel Markovits, *Contract and Collaboration*, 113 *YALE L.J.* 1417 (2004).

<sup>65</sup> Schwartz & Scott, *supra* note 32, at 544, 548; Schwartz & Scott, *supra* note 35, at 1526.

<sup>66</sup> See, e.g., Zachary Liscow, *Counter-Cyclical Bankruptcy Law: An Efficiency Argument for Employment-Preserving Bankruptcy Rules*, 116 *COLUM. L. REV.* 1461, 1466–68 (2016); David A. Skeel, Jr., *Vern Countryman and the Path of Progressive (and Populist) Bankruptcy Scholarship*, 113 *HARV. L. REV.* 1075, 1078 (2000).

<sup>67</sup> See, e.g., Udo Reifner, ‘Thou Shalt Pay Thy Debts’: *Personal Bankruptcy Law and Inclusive Contract Law*, in *CONSUMER BANKRUPTCY IN GLOBAL PERSPECTIVE* 143, 143 (Johanna Niemi-Kiesiläinen et al. eds., 2003) (“The reflexive learning model of contract law, which, using good faith and good morals, created labour, tenants and consumer protection law and many other corrective measures guaranteeing its survival in the industrialised society, is gradually given up within legal procedures where judges no longer care about the terms of contracts that have failed.”).

Third, contract law has not been viewed as particularly salient or problematic in the U.S. context. This is in contrast to corporate law. After a period of intellectual and practical stagnation,<sup>68</sup> corporate law has, since the 1970s, been ridden with normative controversies that appear to be highly relevant from an economic standpoint.<sup>69</sup> Strong unease about the U.S. economic performance in the early 1980s—and its perceived relationship to then-prevailing corporate governance structures—helped spur a strong interest in comparative corporate governance.<sup>70</sup>

Of course, the very devaluation of contract law is also a function of one's lenses, driven by the existing legal regime as well as normative convictions or ideology. One could argue that contract law may have a relevant policy role to play under U.S. law as well. To illustrate this problem, take one of the main objects of policy controversies and legal reforms in recent times: the financial crisis of 2008. One natural reading of the crisis is that it fundamentally resulted from a variety of problems in a large chain of private contracts: consumers did not understand the contract terms that assigned disproportionate risks to them,<sup>71</sup> changes in real estate market prices that were not anticipated by the parties,<sup>72</sup> obstacles to the renegotiation of mortgage contracts that no longer served the parties' interests,<sup>73</sup> the exponential rise in the number of over-the-counter derivative contracts after legal changes guaranteed their enforceability,<sup>74</sup> and investment bankers

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<sup>68</sup> Roberta Romano, *Metapolitics and Corporate Law Reform*, 36 *STAN. L. REV.* 923, 923 (1984) ("Until recently, corporate law has been an uninspiring field for research even to some of its most astute students.").

<sup>69</sup> The strong normative debates cover, for instance, the proper balance of power between shareholders, directors, and managers and the need for mandatory state regulation—themes which arguably affect the firms' cost of capital, the competitiveness of U.S. markets, the rate of hostile acquisitions, the protection of stakeholders, and the time horizon of investors and managers.

<sup>70</sup> See Mariana Pargendler, *The Corporate Governance Obsession*, 42 *J. CORP. L.* 359, 379 (2016).

<sup>71</sup> See, e.g., Oren Bar-Gill & Elizabeth Warren, *Making Credit Safer*, 157 *U. PA. L. REV.* 1, 8–9 (2008) (proposing a solution to this problem through the imposition of comprehensive safety regulations of consumer credit).

<sup>72</sup> See Ryan Bubb & Prasad Krishnamurthy, *Regulating Against Bubbles: How Mortgage Regulation Can Keep Main Street and Wall Street Safe—From Themselves*, 163 *U. PA. L. REV.* 1539, 1553–55 (2015) (proposing a regulatory solution to this problem).

<sup>73</sup> Manuel Adelino et al., *Why Don't Lenders Renegotiate More Home Mortgages? Redefaults, Self-Cures and Securitization*, 60 *J. MONETARY ECON.* 835, 836 (2013).

<sup>74</sup> Lynn A. Stout, *Derivatives and the Legal Origin of the 2008 Credit Crisis*, 1 *HARV. BUS. L. REV.* 1, 3–4 (2011).

selling financial products designed to fail and marketing them to unsuspecting buyers.<sup>75</sup>

Having a complex, though malfunctioning, web of contractual relations at its root, the financial crisis could have easily sparked a renaissance of contract law. However, this did not happen. The potential promise of contract law to address at least some of the issues raised by the financial collapse was largely neglected.<sup>76</sup> Legal scholars and policymakers have interpreted the crisis as primarily a problem of corporate governance and government (de)regulation.<sup>77</sup>

### *E. Access to Data*

Perhaps the most important hurdle to the investigation of the economic consequences of contract law concerns access to data on contracting practices. Ideally, researchers undertaking comparative work should not only examine the implications of different contract law regimes from a theoretical standpoint, but also test them against empirical evidence. However, it is difficult to obtain data on contracting practices because they are typically private, proprietary, and subject to confidentiality provisions.<sup>78</sup> This is an important distinction between contract law, on the one hand, and corporate and bankruptcy law, on the other. While corporate charters, bankruptcy filings, resolutions, and stock prices are all publicly available, information on contract

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<sup>75</sup> For a discussion of this issue, see Steven M. Davidoff, Alan D. Morrison & William J. Wilhelm, Jr., *The SEC v. Goldman Sachs: Reputation, Trust, and Fiduciary Duties in Investment Banking*, 37 J. CORP. L. 529, 532–33 (2012).

<sup>76</sup> A lonely voice calling for the role of contract law in fixing the foreclosure mess, George Cohen has argued that the doctrines of assignment, modification, restraint of trade, mistake, and impracticability, among others, had a relevant role to play. George M. Cohen, *The Financial Crisis and the Forgotten Law of Contracts*, 87 TUL. L. REV. 1, 2–3 (2012) (“At the bottom of the financial crisis lie failed contracts. Failed contracts are the stuff of contract law. Yet, to date, most discussions of possible responses to the financial crisis ignore contract law.” (footnote omitted)).

<sup>77</sup> For a description of the view attributing the financial crisis (as so many other contemporary problems) to a corporate governance failure warranting a corporate governance response, see Pargendler, *supra* note 70, at 386–87. For examples of works attributing the financial crisis to deregulation and regulatory failure, see RICHARD A. POSNER, *A FAILURE OF CAPITALISM: THE CRISIS OF '08 AND THE DESCENT INTO DEPRESSION* 45–46 (2009); and Patricia A. McCoy et al., *Systemic Risk Through Securitization: The Result of Deregulation and Regulatory Failure*, 41 CONN. L. REV. 1327, 1329, 1332–33 (2009).

<sup>78</sup> See Russell Korobkin, *Empirical Scholarship in Contract Law: Possibilities and Pitfalls*, 2002 U. ILL. L. REV. 1033, 1040–41 (discussing problems with gathering empirical evidence on contracting practices and the relative rarity of such studies).

terms, business practices, and the incidence of out-of-court disputes is far harder to come by.<sup>79</sup>

In the United States, scholars seeking a glimpse into real-world contracting practices have relied on the “material contracts” that public companies must disclose under U.S. securities laws, which are made electronically available on the Electronic Data Gathering, Analysis, and Retrieval (“EDGAR”) database of the Securities and Exchange Commission (“SEC”).<sup>80</sup> This has enabled a number of studies into contracting patterns and their determinants.<sup>81</sup> Nevertheless, this being a U.S. database, its international component is relatively small.<sup>82</sup> Unfortunately, the securities laws in other jurisdictions generally do not require full disclosure of material contracts, hindering the design of comparative studies.<sup>83</sup>

Consequently, comparative studies of contracting practices across jurisdictions require the collaboration of industry participants in sharing the relevant documents. Although such access is not always easy to come by given the competitive information involved, a few studies have successfully obtained access to contracting documents and uncovered interesting results that confirm the promise of this line of study.<sup>84</sup> For instance, a study of private equity investments in 210 developing countries found important differences in the transaction structures used in common law and civil law jurisdictions, though the

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<sup>79</sup> See Richard E. Mendales, *Looking Under the Rock: Disclosure of Bankruptcy Issues Under the Securities Laws*, 57 OHIO ST. L.J. 731, 735, 797 (1996).

<sup>80</sup> See *Important Information About EDGAR*, U.S. SEC. & EXCHANGE COMM’N, <https://www.sec.gov/edgar/aboutedgar.htm> [<https://perma.cc/S9BU-P2ZF>] (last visited Sept. 25, 2017).

<sup>81</sup> See, e.g., Theodore Eisenberg & Geoffrey P. Miller, *Damages Versus Specific Performance: Lessons from Commercial Contracts*, 12 J. EMPIRICAL LEGAL STUD. 29, 30–31 (2015); Eisenberg & Miller, *supra* note 53, at 335; Colleen Honigsberg, Sharon Katz & Gil Sadka, *State Contract Law and Debt Contracts*, 57 J.L. & ECON. 1031, 1031–32 (2014).

<sup>82</sup> Even the U.S. EDGAR database provided by the SEC suffers from omissions and may not be sufficiently representative of real-world contract practices. By definition, it focuses only on public companies. Moreover, it may also fail to take into account the contracting practices of large companies, whose agreements are less likely to be deemed material under current securities regulations. George S. Georgiev, *Too Big to Disclose: Firm Size and Materiality Blindspots in Securities Regulation*, 64 UCLA L. REV. 602, 606 (2017).

<sup>83</sup> Under Brazil’s securities laws, for instance, shareholder agreements are the only contracts that public companies must disclose in full. For a comparative analysis of U.S. and Brazilian shareholder agreements filed with the respective securities regulators, see Helena Masullo, *Shareholder Agreements in Publicly Traded Companies: A Comparison Between the U.S. and Brazil*, 12 BRAZILIAN J. INT’L L. 402 (2015).

<sup>84</sup> See, e.g., Josh Lerner & Antoinette Schoar, *Does Legal Enforcement Affect Financial Transactions? The Contractual Channel in Private Equity*, 120 Q.J. ECON. 223, 223–24 (2005).

only legal variable used to explain the results was “time-to-contract-dispute-resolution.”<sup>85</sup>

Even more ambitious comparative studies would look not only at formal contract documents, but also at informal business practices. The practical difficulties in accessing data are even more acute in this case, and, precisely for this reason, the payoff to this type of inquiry is especially high. Within the U.S. context, studies on real-world contracting behavior beyond the text of the agreements, such as those conducted by Stewart Macaulay and Lisa Bernstein, are few, but highly cited and influential.<sup>86</sup>

### F. *The Boundaries of Contract Law*

A final obstacle to the recognition of the possible role of contract laws in shaping economic outcomes is subtler, and relates to the very definition of the field. While all fields raise definitional and boundary questions, this problem is especially acute with respect to the law of contracts. There is a visible trend: whenever regulation of contractual relations becomes too consequential, the field is no longer called contract law, but something else, such as labor law, financial regulation, consumer protection, insurance law, landlord-tenant law, franchise law, etc. The result is that contract law becomes, as Lawrence Friedman suggests, a law of leftovers.<sup>87</sup>

Nevertheless, even though this definitional hurdle greatly erodes the apparent significance of the law of contracts, it is not enough to eliminate it. Despite the observed trend of externalizing to other areas major policy considerations, contract law retains an important and identifiable core. These are the topics that continue to be covered in a typical contracts course—such as remedies, rules of interpretation, and the various forms of limitation to freedom of contract. And, as discussed above, these areas continue to be the object of nontrivial differences.

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<sup>85</sup> *Id.* at 224–25, 232. This measure comes from Simeon Djankov, Rafael La Porta, Florencio Lopez-de-Silanes & Andrei Shleifer, *Courts*, 118 Q.J. ECON. 453, 510 (2003).

<sup>86</sup> See, e.g., Lisa Bernstein, *Opting Out of the Legal System: Extralegal Contractual Relations in the Diamond Industry*, 21 J. LEGAL STUD. 115 (1992); Lisa Bernstein, *Private Commercial Law in the Cotton Industry: Creating Cooperation Through Rules, Norms, and Institutions*, 99 MICH. L. REV. 1724 (2001); Stewart Macaulay, *Non-Contractual Relations in Business: A Preliminary Study*, 28 AM. SOC. REV. 55 (1963).

<sup>87</sup> See LAWRENCE M. FRIEDMAN, *CONTRACT LAW IN AMERICA: A SOCIAL AND ECONOMIC CASE STUDY* 193 (1965).

## II. HOW CONTRACT LAWS MIGHT MATTER: PRELIMINARY EVIDENCE FROM BRAZIL

I conclude by pointing to some recent developments in the Brazilian context to illustrate the potential of this line of comparative inquiry. Just as the lenses used by U.S. scholars have suggested that contract law may not amount to an important development topic, those accompanying a Brazilian scholar suggest that it might. In contrast to the U.S. context, where contract law does not appear to be particularly problematic to most observers, both lawyers and economists in Brazil have warned that the courts' use of contract law to police—and thereby deny enforcement to—the terms of an agreement produce negative economic incentives with potentially serious consequences to the relevant markets.

The relevant background of the Brazilian debate is one in which, despite improvements in recent times, the country has boasted relatively small private credit markets as a proportion of GDP as well as interest rates and banking spreads which are very high by international standards.<sup>88</sup> Even though the relevant literature in Brazil is small and does not cover the minutiae of contract law and doctrine, it differs from the prevailing international perspective in suggesting that the *substance* of courts' approach to contract enforcement—as opposed to the procedural measures of time and cost, as emphasized by the literature—may well matter.

The most influential work in the Brazilian literature dates back to the early 2000s, when three prominent economists with significant experience in academia, government, and business argued that “jurisdictional uncertainty”—arising from the courts' conspicuous “anti-creditor bias”—explained the absence of a market for long-term debt in Brazil.<sup>89</sup> Subsequent studies came to suggest that the courts' bias in contract interpretation and enforcement ran in the opposite direction

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<sup>88</sup> See THE WORLD BANK, REPORT NO. 67332-BR, *THE REAL PARADOX: UNTANGLING CREDIT MARKET OUTCOMES IN BRAZIL 1* (2012), <http://documents.worldbank.org/curated/en/462701468019761562/pdf/673320ESW0P1170t0Outcomes0in0Brazil.pdf>; Guilherme Jonas Costa da Silva & Livia Abrão Steagall Pirtouscheg, *Basic Interest Rate, Bank Competition and Bank Spread in Personal Credit Operations in Brazil: A Theoretical and Empirical Analysis*, 16 *ECONOMIA* 32, 33 (2015).

<sup>89</sup> Persio Arida, Edmar Lisboa Bacha & André Lara-Resende, *Credit, Interest, and Jurisdictional Uncertainty: Conjectures on the Case of Brazil*, in *INFLATION TARGETING, DEBT, AND THE BRAZILIAN EXPERIENCE, 1999 TO 2003*, at 265, 271–73 (Francesco Giavazzi et al. eds., 2005) (“In the Brazilian case, jurisdictional uncertainty may thus be decomposed, in its anti-creditor bias, as the risk of acts of the Prince changing the value of contracts before or at the moment of their execution and as the risk of an unfavorable interpretation of the contract in case of a court ruling.”). The authors argue that this is “an anti-creditor bias, and not an anti-business bias,” and

(favoring the rich over the poor<sup>90</sup>), or denied the existence of any explicit bias in favor of creditors or debtors.<sup>91</sup> Although these studies are plagued by methodological challenges, they highlight a heated debate on the contours and merits of the courts' approach to private contracts.

Another study examined the effects of judicial decisions by courts in the State of Goiás in cases involving soybean forward contracts. The disputes date back to the crop seasons of 2003 and 2004, when market prices at the time of delivery exceeded the contract price by approximately 70%.<sup>92</sup> This change in market conditions created an incentive for farmers to breach the contract, and numerous lawsuits seeking enforcement followed. A small majority of decisions by lower courts granted farmers relief of their contract obligations, in view of the change in circumstances since the date of the agreement and the "social function of the contract."<sup>93</sup>

The probability of the Court of Appeals of the State of Goiás enforcing the contract increased from 25% in 2003 to 69% in 2007, as Brazil's Superior Court of Justice ruled in favor of the contracts' enforceability in 2006.<sup>94</sup> Although it is hard to ascertain causality, the authors found a significant decrease in the use of forward contracts in subsequent harvests.<sup>95</sup> Other works have attributed the significant increase in vertical integration of McDonald's stores in Brazil—which far exceeds the international average—to a wave of litigation in the early 2000s, in which franchisees successfully challenged the validity of certain contract clauses under Brazilian law.<sup>96</sup>

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was at least in part attributable to the emphasis that Brazil's constitution of 1988 places on the social function of property. *Id.* at 272–73.

<sup>90</sup> Ivan Ribeiro, *Robin Hood vs. King John Redistribution: How Do Local Judges Decide Cases in Brazil?* 4 (Mar. 13, 2007) (unpublished manuscript), <https://ssrn.com/abstract=938174>.

<sup>91</sup> Luciana Luk-Tai Yeung & Paulo Furquim de Azevedo, *Neither Robin Hood nor King John: Testing the Anti-Creditor and Anti-Debtor Bias of Brazilian Judges*, 6 *ECON. ANALYSIS L. REV.* 1, 1 (2015).

<sup>92</sup> See Christiane Leles Rezende & Decio Zylbersztajn, *Pacta Sunt Servanda Versus the Social Role of Contracts: The Case of Brazilian Agriculture Contracts*, 50 *BRAZILIAN J. RURAL ECON. & SOC.* 207, 208–09 (2012).

<sup>93</sup> See *id.* at 212–14.

<sup>94</sup> See *id.* at 217–18.

<sup>95</sup> See *id.* at 219–20.

<sup>96</sup> See Vivian Lara dos Santos Silva & Paulo Furquim de Azevedo, *Contratos Interfirmas em Diferentes Ambientes Institucionais: O Caso McDonald's França Versus Brasil*, 41 *R. ADM.* 381, 382, 389–90 (2006).

## CONCLUSION

The foregoing discussion explored the various reasons why there has been comparatively little interest in the economic consequences of contract law differences. With the exception of the real challenges in accessing data, the substantive reasons offered for the disregard of contract law are not persuasive. Contract is a central institution to capitalism, and contract law does not seem to be nearly as empty or immaterial as economists have assumed. Whether and how these differences may matter, however, remains an open question that is well worth pursuing, despite the practical obstacles.