Old Law Is Cheap Law

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1. Introduction

The legal system has expanded enormously over the centuries. The number of rules has grown exponentially (there are millions of rules right now), and so has the capacity of the legal system (there are many more judges and lawyers than in the past). In this paper, I show that the growth of legal rules can best be understood as a function of the growth of the capacity.

A larger capacity changes the law in several ways. First, it allows the law to attack more types of undesirable behavior. When the legal system’s capacity is limited, it can attack only the most harmful acts. As capacity grows, it can also attack acts that are less harmful at the margin.

Take precontractual liability — rules that deal with bad behavior during negotiations that do not lead to a contract. An example is a window-dressing job interview with many candidates when the employer already has decided which candidate to hire. Although this act is socially harmful, its harm tends to be low — usually just the time lost by the candidates. In addition, adjudicating such cases is labor-intensive, as proving the parties’ intentions and statements during negotiations is intrinsically difficult. Not surprisingly, no court on this planet accepted precontractual liability cases before the 20th Century. Although the doctrine was “invented” in the 19th century (by the German scholar von Jhering), it was only in the 20th century that German courts started to apply it, soon followed by countries like the Netherlands, France, and the United States. Even today, precontractual liability is still underdeveloped.\(^1\)

Second, a larger capacity allows courts to use rules that are better but require more work for the courts. Consider the strict, 17th-century version of the parol evidence rule. The rule held that whenever there was a writing, no “parol evidence” (literally, “oral evidence,” for instance testimony from witnesses) was allowed. A strict parol evidence rule is cheap law: Courts only have to read within the “four corners’ of the document. On the bright side, this allows courts to decide cases in fifteen minutes, so to speak. On the not so bright side, this often leads to courts getting the facts wrong as the writing does not always reflect the true agreement. In the 19th and 20th century, American courts carved out a growing list of exceptions. Today, parol evidence is permitted in a wide range of circumstances, for instance, when the document contains an error or looks incomplete. In some American states (the so-called “Corbin jurisdictions”), parol evidence is permitted even to contradict written terms. All these exceptions lead to higher-quality outcomes (courts are more likely to discover the truth), but they also require more work from the courts. Given capacity constraints, a strict parol evidence rule may have made sense in the 17th Century.

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By “old law is cheap law,” I mean that in the past, when the economy was less developed, law was a product society spent less money on. Law was, in other words, a low-quality-low-price product. Just like low-income people buy a cheap house or a cheap car, poor societies buy cheap law. Cheap law is of lower quality in that it tolerates more harmful acts or leads to courts getting the facts wrong more often.

This paper starts from an empirical observation — that the legal system’s capacity grows as an economy grows. The paper’s contribution consists of explaining which rules will be added or changed as capacity increases. In other words, the point is not that contract law (or any other field of law) has expanded since the 11th century. My point is to explain how it has expanded, that is, to explain which rules were introduced first, and which were introduced later.

The paper offers a novel theory on legal evolution. To position the paper in the literature, it is useful to distinguish two types of costs related to operating a legal system. The first is the fixed costs of producing and promulgating the legal rule. The second is the variable costs of adjudicating and enforcing the rule. This paper focuses on the latter. (I don’t consider the fixed production costs because I believe that they tend to be much lower than the costs of implementing the rule on a daily basis.) The literature so far has primarily focused on the first type — the legal production costs. For instance, there is some literature on the optimal timing of rule production, the specificity of legal rules, accuracy in adjudication, and the depreciation of case-law over time. There is also extensive literature on rules versus standards, dealing with the question whether the detailed rule should be produced ex-ante (before the act), or ex-post (after the act).

While this paper offers the first general formulation of the “old law is cheap law” thesis, there is some literature on the economics of old law, focusing on specific applications. For instance, Posner has argued that tribal law uses strict liability rather than negligence because strict liability is easier to prove (as it requires only proof of harm and causation and no discussion on culpability.) Relatedly, Schaefer has argued that developing countries prefer rules over standards to minimize adjudication cost.

Note that when (vague) standards are used instead of precise rules, the first task of defining the rules is done at the second stage, during adjudication. But even then, the specification of the standard is a fixed cost, that applies irrespective of how often the specification will be used.


2. The Mechanism

The “old law is cheap law” hypothesis is based on two assumptions. The first is that, as GDP per capita grows, the capacity of the legal system will grow as well, i.e., relatively more resources and personnel will be devoted to the legal system. The second is that, as the capacity expands, courts add the rules that maximize the net social benefits, i.e., the benefits of the improved behavior minus the cost of adjudication needed to obtain that behavior. In principle, both assumptions could be considered “black boxes” for the sake of the theory. Nonetheless, this section will briefly reflect on the underlying mechanisms.

2.1. Maximize the Net Social Benefit (Benefit per Case Times Multiplier minus Adjudication Costs per Case)

As legal systems expand, rational legal systems will add those rules that maximize the net social benefit. The net benefit is the difference between the (gross) benefit of better behavior and the adjudication costs. This means that the legal system should look at two parameters: how harmful the behavior is and how much court time it would cost for a court to verify violations.

In theory, there is a third parameter: the multiplication effect. The reason is that the legal system produces sticks that are meant not to be applied.\(^\text{10}\) Rational citizens tend to settle their disputes in the shadow of court decisions, or, even better, simply follow the rules. Suppose that citizens violate the law 1% of the time and that the legal disputes that arise out of the violation are settled 99% of the time so that only 1% of the legal disputes end up in court. In this example, for every 1 case that is brought to the court, there are 10,000 cases in which behavior is altered by the law. Because of this multiplication effect, an expanding legal system should give more weight to the benefits than to the adjudication costs of a new rule.

Contra-intuitively, this does not mean that the frequency of undesirable behavior should matter — as long as the multiplication effect is the same. Suppose that each bank robbery causes $100 harm, and each burglary causes a harm of 80. Now, suppose there are 5 times more burglaries than bank robberies. Should the legal system attack burglaries before it attacks robberies? No. While the social benefit of stopping burglaries is nearly five times higher than that of stopping bank robberies, doing so would cost the court five times more work (as there will be five times more cases). The act with the highest marginal social cost is a bank robbery. In short, courts should not consider how often a type of undesirable behavior happens in society, but how many cases will show up in court compared to the behavioral changes. In the absence of specific indications, courts may assume that the multiplication effect will be the same.

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The multiplication effect depends, however, on the predictability of court decisions. If court decisions are harder to predict, the multiplication effect may be smaller. When evidence is harder to interpret, or when courts apply more complicated tests, the predictability may drop, and courts may get more cases.

2.2. Why Does Legal Capacity Increase in GDP per Capita?

At the outset, the correlation between economic development and relative legal expenditures is simply an empirical fact. We now have more judges, attorneys, and law professors than in the 1960s, even if we control for population growth. In the 1960s, there were, in turn, more judges and lawyers than — say — in the 19th century. For instance, in 1867, when the landmark case Hadley v Baxendale was decided, there were only 15 common law judges in the entire United Kingdom. Today, there are many more judges.

Why would legal expenditures grow faster than the GDP itself? At first glance, the answer seems obvious: A wealthy society can afford it because it has more money. Indeed, if the legal system does no more than producing a luxury good — the satisfaction of a taste of fairness — demand for law would increase when more essential needs (like food or housing) are satisfied.

Still, when the legal system’s primary goal is not to satisfy a taste for fairness but to reduce socially harmful behavior, the answer is no longer obvious. Why poor societies would be less interested in reducing harmful behavior. Why would they care less about incentives or risk allocation? After all, good incentives may mean more food produced, and better risk allocation may mean higher survival chances in bad times.

A different explanation is that wealthy societies have more human capital. Professional adjudication requires trained professionals. When human capital is scarce, the legal system cannot expand because there is not enough personnel available on the market. Of course, this begs the question why human capital increases over time. A first answer is that investments in human capital become more rewarding as life expectancy increases. A second answer is that the invention of book printing increased the productivity of education. A third answer is that self-development is a luxury good that is bought more as more people get wealthy. Still, the human capital hypothesis does not explain why human capital would be used disproportionally for one industry — the legal services industry. After all, human capital can also be used in agriculture (better-trained farmers), manufacturing (more highly skilled workers), or trade.

The best explanation for the expansion of legal capacity, in my view, is Baumol’s Cost Disease. This theory holds that, when the productivity of one job rises faster than that of another, more people will move to the less productive job. Baumol attributes the fact that most people are now working in the services industry to the sharp productivity rise in the agricultural and manufacturing industry. A few centuries ago, agriculture required the vast majority of the labor force. Now it is 1%. A modern farmer is able to feed maybe 80 times more people than in the past — a productivity growth of 8,000 percent.

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The productivity of lawyers may have grown a little bit, but not that much. Lawyers may work a little faster now because they have more and better books. They also may be a little better trained, as law schools have become a little more efficient. Copy-editing documents definitely goes faster since the invention of word processors. But the core tasks — preparing persuasive arguments, listening to counter-arguments, deliberating — are not done much faster. Overall, the productivity in the legal services industry may have increased, but not as much as in agriculture or manufacturing.

One interpretation of Baumol’s Cost Disease is that the abundance of food and manufactured goods has reduced a worker’s marginal utility in those industries. In other words, the opportunity cost of spending time to legal disputes has decreased. In poor economies, time spent to a dispute meant less time for producing food. In wealthy economies, it means less time for luxury goods.

2.3. The Assumption that Courts Maximize Net Benefits when Expanding Law.

If courts receive more resources, why would they use it in ways that help society most? Why would courts balance the benefits of improved behavior and the costs of adjudication?

The simplest (and in my view strongest) explanation is that judges are human beings. Human beings are used to balancing interests all the time. Human beings balance costs and benefits whenever they decide what to eat, what products to buy, where to spend a vacation, how much to work, and which kid to give extra attention. In a broader sense, balancing advantages and disadvantages is a fundamental feature of any living creature with a pain and pleasure centrum in the brain. Decision making is balancing pain impulses and pleasure impulses. So, when courts are put in a non-self-interested position and forced to make a decision, they tend to do what they are doing as human beings all the time — balance interests.

What if courts are not interested in maximizing efficiency but in maximizing court fees? Most courts on this planet are financed by plaintiffs. The history of common law courts is partly the history of an enterprise competing for lucrative fees with manorial, merchant, and church courts. Still, if courts maximize court fees, the outcome may resemble the results of the model. Plaintiffs are the ones who suffer the harm of the socially undesirable behavior. The larger the harm compared to the court fee, the more likely victims are willing to go to court. (See also the more general literature on the efficiency of the common law. E.g., Rubin (arguing that inefficient rules are more likely to be challenged because the losses of inefficient rules are higher than the gains.)

What if new rules are the result of political lobbying? While the short-term effect of lobbying may be “noise,” the long-term trend may go in the same direction. The more harmful behavior is, the stronger the victim’s incentive to lobby for legal intervention.

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2.4. *Social Norms as Super Cheap Law*

Another question is why poor societies would leave socially undesirable behavior unpunished. If there is no money to pay professionally trained lawyers, why not have a super-cheap procedure, because a cheap solution seems to be better than none at all. The answer is that poor countries do use such a super cheap mechanism — it is called social norms.

A social (or “moral”) sanction system is cheaper than a legal sanction system because it is not done by professionals, but by ordinary people during their daily conversations. Victims tend to express their frustration to family and friends, who listen to stories and form a judgment. The cost of this activity is close to zero, as human beings have a strong need to talk to others anyway. They can talk about the weather, about the latest hunt, or about someone’s undesirable behavior. Social norms adjudication is a free by-product of social interactions.

Unfortunately, the lack of professionalism also leads to less accurate decisions. The evidence is of lower quality (often hearsay only, and rarely is there any written evidence), evidence-weighing is done less systematically, and norms can’t be nuanced because they are transmitted orally. As a result, innocents may be punished, and violators may remain unpunished. Moreover, social sanctions (like reputation sanctions) may not be strong enough to stop undesirable behavior; or, they may be too strong, out of proportion to the harm. It is hard to create optimal doses of incentives in a non-organized system. In short, social norms are an extreme form of a low-quality-low-price good. In this respect, the cheapest law is not law but social norms. As societies become wealthier, they can afford it to have more of these tasks taken over by professionals.

3. *Criminal Law, Tort Law, and Antitrust Law*

I now illustrate the “old law is cheap law” principle with examples from criminal law, tort law, antitrust law, and bankruptcy law.

3.1. *Criminal Law*

Consider four types of harmful behavior: murder, rape, sexual harassment, and bullying. While harm may vary in individual cases, people will likely agree that, usually, murder is more harmful than rape, rape more harmful than harassment, and harassment more harmful than bullying. Therefore, expanding legal systems will criminalize these four types in that order. Rules against murder are as old as the law. Rules against rape are old as well.  

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13 For instance, rape was a crime in Ancient Egypt. See Reynolds, James Bronson (1914), “Sex Morals and the Law in Ancient Egypt and Babylon,” 5 Journal of the American Institute of Criminal Law and Criminology, 20–31. Rape was also a crime under the code of Hammurabi, although the rape of a married woman was considered adultery so that both the rapist and the victim receive the death penalty. Under Ancient Hebrew law, both rapist and the victim were executed under the assumption that the victim could
Still, the criminalization of rape happened later in some legal systems. In the old Roman Kingdom (753-509 BC), murder was criminalized but not rape. This is illustrated by the event that lead to the overthrow of the monarchy: the rape of Lucretia by one of the king’s sons. While the rapist did not violate formal law, the citizens were shocked and established the republic. Cicero later used this to illustrate that there is such a thing as natural law: the rapist should have known raping is wrong.\textsuperscript{14} A different interpretation is that the rapist should have known this because he was violating social norms. As the Roman economy had become more developed, it was time to add rape to the list of offenses attacked by the legal system.

Sexual harassment became a legal wrong only in the 1970s.\textsuperscript{15} Bullying had to wait until the 21\textsuperscript{st} century. Between 1999 and 2015, all 50 American states have passed anti-bullying legislation; in some states, bullying is a crime.

3.2. Tort Law

Tort liability can be strict or negligence-based. If it is strict, courts must check whether there is harm and who caused it. If it is negligence-based, courts must also check whether the injurer was negligent (or “at fault”). The last demands more work, as it requires determining what is optimal care (balancing care costs and expected accident costs) and what level of care the injurer exercised. Not surprisingly, old legal systems used strict liability. This is well-documented for tribal law. If a horse hit a pedestrian, the rider had to pay, even if he did nothing wrong. In Ancient Rome, strict liability was the normal rule until the Lex Aquilia (286 BC) introduced negligence-based liability.

Or consider the evolution from contributory negligence to comparative negligence in the 20\textsuperscript{th} century. Contributory negligence means that, when both the injurer and the victim are negligent, the victim must bear the full loss (as she “contributed” to the accident). Comparative negligence means that, in such cases, both parties must bear a part of the loss, proportional to (“compared to”) their culpability. Comparative negligence is considered fairer and has some economic benefits as well, but it requires extra work from the courts as they have to determine the relative culpability (50/50? 30/70?).\textsuperscript{16} Not surprisingly, old law used contributory negligence. (The underlying moral justification was that one should not blame another if one is guilty himself; don’t throw a stone if you have sins yourself. But this does not explain the later move to comparative negligence later when Christian morality remained unchanged). The switch to comparative negligence gradually happened

\textsuperscript{14} Marcus Tullius Cicero’s (106-43 BCE) De Legibus, II, iv, 10.

\textsuperscript{15} Barnes v. Train (1974) is often cited as the first sexual harassment case under Title VII of the Civil Rights Act of 1964. Sexual harassment forms a crime in some cases, depending on state law (and often under the label assault).

in American states only in the 20th century, quickly followed by European countries.

3.3. **Antitrust Law**

Antitrust law is *very* expensive law. It requires complicated fact-finding, including calculating market shares, price elasticities, potential consumer benefits. Cases take weeks or even years and require teams of highly specialized lawyers and economists.

The benefit of more competition may be high, though. Cartels and monopolists distort prices and significantly reduce allocative efficiency. So, the reason why antitrust law was virtually nonexistent is not that the benefits per case are low; the reason is that these cases require an incredible amount of work.

This may explain why competition law was virtually nonexistent before the American Sherman Act in 1890.\textsuperscript{17} The fact that antitrust law is very expensive law may explain why some developing countries don’t have antitrust authorities. Given the limited capacity of the legal system of these countries, courts must focus on cases with a higher net benefit.

One way to keep adjudication costs under control was to work with strict rules rather than vague standards. This explains why early antitrust law heavily relied on *per se rules*. In recent decades, as the United States became wealthier, antitrust law moved from rules to standards. More and more *per se rules* have been replaced by “rules of reason.” A similar, though less pronounced evolution can be observed in the EU.\textsuperscript{18}

Even now, the legal system (and the FTC) has only capacity to go after the largest players. Microsoft, Google, and Apple have to fear antitrust law, not your local plumber of sprinkler company, even if they engage in anticompetitive behavior in their small local market.

3.4. **Bankruptcy Law**

Old law was harsh for insolvent debtors. Debts were never forgiven. In many cases, debtors were pushed into slavery. In other cases, debtors risked criminal sanctions—even the death penalty.

Harsh punishment makes sense when debtors have obtained by fraudulently misrepresenting the risk, or when they have moved assets to friends or family on the eve of bankruptcy. However, harsh sanctions discourage risk-taking and entrepreneurship when insolvency was a matter of bad luck. Cheap law is unable to distinguish the two. Therefore, it treats all debtors alike, punishing them all harshly. As the capacity of legal systems increased, bankruptcy became softer.

\textsuperscript{17} Occasionally, rules against usury, price gauging, and the just price doctrine may have had an antitrust effect, but they were not deliberately designed for this purpose.

\textsuperscript{18} Van den Bergh, Roger (2017), *Comparative Law and Economics*, Cheltenham, Edward Elgar. One of the themes in Roger Van den Bergh’s work was the fight for a better antitrust law, more based on economic expertise, with more attention to the business logic of certain practices. In other words, Van den Bergh wanted better law, but also more expensive law.
4. Contract Law

So far, I have given examples from criminal law, tort law, and antitrust law. From a scholarly viewpoint, however, there is a danger that I have cherry-picked examples that fit into my framework. As we now turn to contract law, I will discuss all the major changes, not just a few hand-picked ones.

Let us first look at the general evolution of the English common law of contracts. In the early 12th century, courts didn’t take any contract cases at all (only property and tort cases). It would take until the 17th century until courts generally accepted contracts cases.

It is easy to explain why low-capacity courts may decide not to take contract cases. While contract breaches can be as harmful as torts or property violations, they are more subject to reputation sanctions. Reputation is a strong mechanism in contracting, as contracts are voluntary transactions and most people who do trade do so repeatedly. Also, potential victims can protect them against opportunistic breaches by demanding simultaneous performance or periodic payments.

In the late 12th century, common law courts started to take one type of contract cases—debts that had not been paid back.

Next, they also accepted refusals to pay for completed performance (for instance, a builder having finished a complete house and not being paid at all). At first glance, the potential loss for the victim is the same. Whether a $100,000 debt is not paid back, or the $100,000 price for a construction job is not paid, in both cases the promise risks losing $100,000. Yet in the second case, the potential victim can more easily protect himself by demanding installments, for instance for installments of $25,000 to be paid each time a fourth of the job is finished. (This increases transaction costs, but at least it reduces the vulnerability of the first to perform.). In the case of debt, no such protection is possible. Of course, the lender could not lend $100,000 but only $25,000 but that would defeat the purpose of the contract which is to temporary provide $100,000 capital.

From the early fifteenth century on, courts also accepted cases of defective performance. If the house was built and the $100,000 was paid, but later the house turned out to be defective, the victim could now go to court and demand compensation (technically, by extending tort law to “trespass on the case,” which later became known as “assumpsit”). While defective performance can lead to significant losses, these losses are usually lower than the contract price. Moreover, determining to what extent performance was defective demands more of the courts time than determining whether performance was complete. Therefore, the net benefit for allowing defective performance cases was likely lower than the net benefit for unpaid contract price cases.

By the second half of the fifteenth century, reliance damages could be awarded when no party hadn’t even started performance. Reliance damages are harder to prove than damages caused by defective performance, and they are usually lower.

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19 A concise summary of history of the common law of contracts can be found in on Farnsworth, E. Allen, (2003), *Farnsworth on Contracts*, Aspen, §1.5-1.6.
20 Note that law merchant courts took contract cases in the medieval fairs and markets, and Church courts enforced sworn promises, although this was prohibited in 1164.
By the end the sixteenth century (and especially since Slade’s case in 1602), common law courts also accepted purely executory contracts (that is, contracts in which neither party had started performance). Here, the potential loss is only a foregone profit. The profit is nearly always smaller than the contract price. Moreover, it is harder for the court to know for sure that an agreement has been formed when performance hasn’t even started. Therefore, the next benefit of this extension was lower than that of the three previous extensions.

It took until the 20th century, however, before precontractual liability was a ground for compensation in English courts. As explained earlier, it makes sense why no legal system intervened at the pre-contractual stage before the 20th century. The harm to the victim is usually modest, for instance lost time. Moreover, it was often hard for courts to find out who said what during negotiations, or what were the true motives of the parties. This does not mean that such strategies are cause no social harm, but that expensive law is needed to correct this behavior.

4.1. From Formalism to Mutual Assent

Mutual assent seems like an obvious condition for a contract. Nonetheless, older legal systems, like old Roman law, didn’t consider it a condition for the validity of a contract. Old Roman law was formalistic. A contract was formed when a ritual was undergone, in which certain words had to be uttered, and certain symbolic acts (like the seller of land literally handing over some dirt of the land to the buyer) had to be performed. One implication was that there was a numerus clausus for contracts: only contracts for which such a ritual existed were legally valid. Only in late medieval times, formalism was abandoned, the numerus clausus principle was given up, and the basic requirement for a contract became mutual assent.

Formalism can easily be seen as an example of “old law” that is “cheap law.” Verifying whether certain rituals had been followed takes less times for the court than finding out whether there was a true meeting of minds.

4.2. Statutes of Fraud and Parol Evidence

In the 17th Century, when the majority of the population became literate, the English Statute of Frauds started to demand written evidence for many types of contracts. Combined with a strict parol evidence doctrine, this reduced the time courts needed to spend on contracts cases. Courts only needed to quickly read the (usually short) document; they did not need to listen to witnesses or consider other information such as past transactions or customary practices.

Over time, as the courts’ capacity increased, courts started to carve out exceptions to the Statutes of Fraud. Anything that resembles a signature, such as a printed name of a form, is fine now. A few words on the back of a restaurant bill is enough. If one of the parties has started performance, the requirement for written evidence is dropped. Since the late 20th century, a name printed in an email serves as a valid signature.

All these relaxations of the Statute of Fraud resulted in higher-quality law — courts are more likely to find out what was truly agreed upon. At the same time, they mean more
work for the courts. They are expensive law.

4.3. **Economic Duress Instead of the Preexisting Duty Rule**

Consider the facts of *Alaska Packers v. Domenico*. Fishermen were hired in San Francisco to sail to Alaska and work there for a cannery during the salmon season. When they arrive in Alaska, they refused to work unless they would receive $100 instead of the agreed-upon $50. The employer agreed because it was not possible to bring other workers over to Alaska before the end of the salmon season. Afterwards, the court decided that the employer had to pay only the originally agreed $50, not the $100.

There are two techniques that attack opportunistic renegotiations like this. The first is the consideration doctrine. The fishermen received more to do exactly the same they had to do under the original contract; in other words, they had a preexisting duty. Therefore, there was no rational motive (“consideration”) for the employer’s promise to pay more. As a result, the second promise was not binding, and the first contract was still governing.

The second technique is applying the economic duress doctrine. When courts take a careful look at the circumstances (analyzing whether the “threat” was “improper,” and whether the victim had a “reasonable alternative”), they may conclude that the second promise was induced under duress, and therefore not binding.

The consideration doctrine is cheaper law. All the courts need to do is compare the two contracts. If the wage differs but not the amount of work, there is no consideration. Unfortunately, the consideration doctrine is easy to evade. If the fishermen promise to work 15 minutes longer, they can make the second contract valid, even if it was the outcome of an opportunistic renegotiation.

The economic duress doctrine is more expensive law because it requires an investigation into the circumstances of the renegotiation. But it can’t be evaded by formalistic tricks like promising to work 15 minutes longer. It is expensive law, but better law, increasingly applied in the 20th century.

4.4. **From Fraud (and Caveat Emptor) to Far-Reaching Disclosure Duties**

In a perfect market, there is no asymmetric information. In practice, that is often not the case. Better-informed parties have an incentive to keep information for themselves to exploit informational advantages. Better-informed parties may, therefore, flat-out lie, conceal information (deliberately make it harder for the other party to discover the truth), tell half-truths (which are literally true but still misleading because they suggest something untrue), or simply not disclose certain information.

Though asymmetric information is socially harmful, attacking its exploitation is costly for the legal system. It takes time to investigate what statements have been made, whether these statements are false, whether the other party knew the same, and which party was in the best position to produce the information.

Old legal systems were governed by caveat emptor. Caveat emptor means literally that the buyer needs to beware. Although caveat emptor is sometimes interpreted as a legal rule
that permits dishonesty, it can better be interpreted as the absence of a rule about honesty.\footnote{21 Walton H. Hamilton, "The Ancient Maxim Caveat Emptor," \textit{Yale Law Journal} 40: 1113-1187 (1931).}

As legal systems increased capacity, they started to carve out exceptions to caveat emptor. First, they prohibited plain fraud (cases in which words were said that were literally untrue). Then they attacked more subtle forms of fraud, such as concealment (cases in which no words were uttered) and half-truths (cases in which uttered words were misleading though not literally false). Later, they intervened whenever there was negligent misrepresentation (cases in which statements were carelessly made). Eventually, they developed far-reaching duties to disclose.

This chronological order makes sense. Fraud is likely the most harmful form of creating asymmetric information. After all, the lie is deliberately chosen to obtain the largest possible benefit to the maker of it (while the benefit of negligent misrepresentation to the maker is more like a lucky shot). Fraud is also harder to detect because it is deliberately constructed not to be detected. The only way victims can protect themselves against lies is to never believe any statement whatsoever made by the other.

Within the fraud family, plain fraud involves the least work for the courts: courts have to check whether the statement was false, and whether the maker of the statement likely knew the falsehood. Concealment (like putting a pot of flowers on top of a wooden floor damaged by termites) requires more work for the courts, because it may be less obvious whether the concealer had the intent to mislead. Half-truths require even more work for courts, as the statements are literally true so that the court needs to examine the context in which they were made.

Negligent misrepresentation is highly complicated because it requires cost-benefit balancing — court have to decide whether the factual mistake could have been corrected at reasonable costs. Duties to disclose involve even more balancing — whether information was worth being produced, which party was in the best position to produce it, and whether the information was worth being communicated. Also, parties can protect themselves to some extent by asking questions (so that the other party’s lack of a response may signal that he has something to hide, or so that the other party has to make a deliberate statement, which can be actionable if fraudulently made). In short, the “old law is cheap law” thesis can explain the gradual movement from fraud prohibitions to disclosure duties.

4.5. \textit{From All-or-Nothing Incapacity to Exploitation of Irrationality}

Old law worked with all-or-nothing rules: either someone had full capacity to make contracts or no capacity at all. Minors were categorically incapable of making contracts. If a merchant sold a good to a minor, there was no discussion — the parents could unwind the transaction. Drunken adults, on the other hand, were fully capable of entering contracts. Again, no discussion.

All-or-nothing rules make life easy for courts. All the courts have to check is the status of the plaintiff. Cheap law, however, is also low-quality law. It was impractical that minors could not participate in market transactions without their parents. It was also undesirable that drunken people could be exploited by letting them sign one-sided contracts.
Modern law has largely abandoned categorical thinking. Minors can enter into binding contracts for necessities at the normal price. In other words, minors can participate on the market, but adults cannot exploit their lack of experience by selling them goods they don’t need or making them pay a higher price. Contracts can also be avoided if a non-drunken party exploited the drunkenness of the other party.

All these nuances mean more work for courts. They may have to examine the necessity of the goods, their market price, or the circumstances in which the transaction took place. Yet it is also higher-quality, as it avoids false negatives (denying binding force to good contracts) and false positives (enforcing exploitative contracts).

4.6. The Shrinking of Definiteness Requirements

Contracts are never complete. There are always unanticipated circumstances. If contracts are incomplete, courts may have to fill the gaps. Courts limit the amount of work they are willing to do, though, by requiring contracts to be sufficiently “definite.” Originally, definiteness meant defining on all major terms, such as the type of contract, price, quantity, and quality. As the courts’ capacity expanded over time, the definiteness requirement was relaxed. Section 2 of the UCC does not even require a price. All that the parties need to agree on is the type of good and the quantity. If no price is stipulated, courts will fill the gap by inserting market price. Outside the UCC, courts sometimes do the same, especially in relational contracts (in which one party became vulnerable by making a relation-specific investment). In Oglebay Norton v. Armco, a transportation company had bought special vessels for a long-term contract with a steel factory. The contract stated a price formula for the duration of the contract. When a price index on which the formula was based disappeared, the court indicated it would determine the price if parties did not reach an agreement. More work for the courts, but better law.

4.7. From No Excuses via Impossibility to Impracticability

Consider the evolution from no excuses, to impossibility excuses, to impracticability excuses. In 1863, the highest English court created a major legal change in Taylor versus Caldwell. A concert hall had burned down, just before a concert series had to take place. The court decided that the owner of the hall didn’t have to pay damages to the concert organizer, as the performance was excused because of impossibility. Since the concert organizer did not have to pay either, the decision let both parties share the loss, in that both lost their expected profit. Before this precedent, the owner would have had to pay damages to the concert organizer, which meant that the owner would have absorbed the entire loss (by losing not only his own profit but also by serving as the de facto profit insurer of organizer’s profit). Taylor v. Caldwell meant a better risk allocation, but also more work for the court in that the court had to determine whether performance had become impossible.

In the 20th century, impossibility was replaced by impracticability. Promisors are excused when the cost of performance clearly exceeds the value to the promisee, even if performance has not become literally impossible. Again, this is an even better risk allocation (by hedging the promisor’s risk) but at the expense of even more work for the
4.8. Mutual Mistake

Mutual mistake means that both parties relied on the same, incorrect information. In the iconic case of *Sherwood v. Walker* (1887), a cow was sold for a low price, both parties believing the cow was barren. Before delivering the cow, however, the rancher discovered the cow pregnant and worth ten times more. The court allowed rescission of the contract after asking a philosophical question: is a pregnant cow a different object than a non-pregnant cow. A century later, the highest court of the same state (Michigan) overruled the old, philosophical test and installed a new test that defines mutual mistake as a risk problem (*Lenawee County Board of Health v. Messerly*, 1982). The new test requires courts to ask asking how parties allocated this, or how rational parties would have allocated the risk.

The philosophical “what is a cow” test is cheap law. It takes only fifteen minutes and a good cup of coffee to decide a case. Risk analysis requires a more difficult factual and empirical investigation, but also leads to better risk allocation.

4.9. Self-Help Rules

Even in developed legal systems cannot perfectly enforce all promises. Promisors may be insolvent, or damages may be hard to prove. Therefore, self-help rules remain important. One such rule is the right to withhold performance in response to the other party’s breach (in civil law systems, this is better known under the Latin term *exceptio non adempleti contractus*.) Suppose that Preston promises to transfer his business to Kingston in return for money. If Kingston does not come up with security that the money will be paid, Preston may want to protect himself by postponing the transfer. This way, Kingston receives stronger incentives to get the deal financed, and Preston is better protected against Kingston’s possible insolvency.

Before *Kingston v Preston* (1773), English courts did not allow withholding performance. They considered all promises independent of each other. Preston had to deliver the business and Kingston had to provide security. If Kingston breached, that did not give Preston the right to breach. This was cheap law because courts did not have to look at the circumstances. All they had to was check whether the defendant had kept his own promise. A right to withhold performance requires more work than a categorical “always do what you have literally promised” rule. Courts have to make sure that the right to withhold performance is justified and not a cheap excuse to get out of an uninteresting deal.

4.10. Contract Content Regulation

Here, we can see a general evolution from relatively simple, specific rules (forbidding penalty clauses, forfeiture, covenants not to compete, or exemption terms) to standards (unconscionability, good faith). More court intervention, more circumstantial evidence, more types of bad behavior attacked, but more work for the courts.
5. Concluding Remarks

Older legal systems had lower capacity. They had fewer judges, attorneys, police officers, bailiffs, and prison guards. Therefore, the rules were so chosen that they required less work for the legal system. This meant faster procedures, simpler rules, and less tailor-made solutions. Unfortunately, it also meant more mistakes, and more forms of socially undesirable behavior tolerated.

Over time, capacity increased, and legal systems started to address more issues. Courts also became more perfectionist, reducing errors by spending more time on each case.

To what extent is our current law cheap law? Are there still forms of undesirable behavior that are tolerated because of capacity constraints? Yes, there are. For instance, aggressive behavior on social media is still largely tolerated. Also, subtle forms of fraud are often tolerated. To give an example, businesses rarely set the price at $10; instead, they set it at $9.99. That is about the same, but it looks different, as consumers subconsciously see this as $9. Though this causes minor distortions to markets, the legal system does try to prevent this practice, as it would require loads of information (on all goods sold, and on all quantities sold) to prove that prices have a number bias. In other words, attacking a number bias is expensive law. It is possible, however, that 30 years from now such deceptive practices will no longer be tolerated. Relatedly, predatory pricing is rarely attacked because proving that a price is too low is too difficult in an economy full of fixed costs. I can imagine, however, that predatory pricing will again be prosecuted in a few decades when courts have a larger capacity.

One implication of the “old law is cheap law” theory for comparative law is that it warns us for overhasty cultural explanations. Often, differences exist because one country is still using cheap law when more expensive law makes sense. For instance, French courts were using, until recently, the impossibility criterion instead of the impracticability criterion. In 2005, the highest French court held that a contractor, who had built a house 33 cm lower what was stipulated, could be forced to demolish the house and build a new one.\(^{22}\) As explained, impracticability is better, but more expensive law. Given the fact that economic development is about the same in France as in the U.S. or Germany, there was no reason why only France was stuck in the old impossibility doctrine. And yes, in 2016, the new civil code moved to impracticability.\(^ {23}\) As it turns out, there was nothing inherently “cultural” about the use of impossibility in France. There is no reason why a modern, wealthy country should continue to use cheap law.

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\(^{23}\) Technically, the term “impracticability” is not used, though the criterion is implicitly applied under the heading of “imprévision” and limitations to specific performance. The new art. 1195 CC permits termination when an unforeseeable change of circumstances renders performance excessively onerous for a party. The new art. 1221 CC holds that specific performance cannot be asked if the costs would be clearly disproportionate to the benefits.