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# Promissory Estoppel and the Protection of Interpersonal Trust

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# PROMISSORY ESTOPPEL AND THE PROTECTION OF INTERPERSONAL TRUST

JOHN J. CHUNG\*

I.	INTRODUCTION .....	38
II.	THE NATURE AND PURPOSE OF TRUST.....	43
A.	<i>The Role of Trust in a Market Economy</i> .....	45
1.	The Importance of Trust at the Macro-Economic Level.....	46
2.	The Importance of Trust at the Micro-Economic Level.....	48
B.	<i>The Role of Trust in Contracts</i> .....	49
III.	IS THERE A DIFFERENCE BETWEEN TRUST AND RELIANCE, AND, IF THERE IS, DOES IT MATTER? .....	50
A.	<i>The Subjective Nature of Trust versus the Objective Nature of Reliance</i> .....	51
B.	<i>Reliance as an Ex Post Judicial Inquiry versus Trust as an Individual Ex Ante Process</i> .....	51
C.	<i>The Value of a Focus on Trust</i> .....	52
D.	<i>Additional Observations Concerning the Difference between Interpersonal Trust and Enforcement Trust</i> .....	55
IV.	THE ROLE OF TRUST IN PROMISSORY ESTOPPEL.....	56
V.	THE OPTIMAL LEVEL OF PROTECTION OF TRUST .....	58
VI.	THE ENDPOINT DEFINING MAXIMUM PROTECTION TRUST ....	62
A.	<i>Ames v. Employers Casualty Co.</i> .....	62
B.	<i>Prudential Insurance Co. of America v. Clark</i> .....	63
C.	<i>Drennan v. Star Paving Co.</i> .....	63
D.	<i>D &amp; G Stout, Inc. v. Bacardi Imports, Inc.</i> .....	64
VII.	THE ENDPOINT WHERE TRUST SHOULD NOT BE PROTECTED.....	66
A.	<i>Universal Computer Systems, Inc. v. Medical Services Ass'n of Pennsylvania</i> .....	66
B.	<i>Hoffman v. Red Owl Stores, Inc.</i> .....	73

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C. <i>A Fanciful Hypothetical</i> .....	75
D. <i>James Baird Co. v. Gimbel Bros.</i> .....	77
E. <i>Marker v. Preferred Fire Insurance Co.</i> .....	78
F. <i>The Role of Lawyers Concerning Promisee Self-Reliance</i> .....	79
VIII. CONCLUSION.....	81

## I. INTRODUCTION

Promissory estoppel developed in order to protect reliance on a broken promise in the absence of a contract.<sup>1</sup> Reliance lies at the core of the doctrine. However, reliance necessarily implicates another core concept—trust. The central importance of trust has been recognized by the courts, including the Michigan Supreme Court which observed, “It is the value of trust that forms the basis of the entitlement to rely.”<sup>2</sup> This paper examines the role of trust in promissory estoppel and the extent to which the law should protect trust when a promise is made. In order to do so, however, an important distinction must be drawn between two types of trust: (1) interpersonal trust between the promisee and the promisor; and (2) the promisee’s trust that the promise will be enforced (which will be referred to as “enforcement trust” in this paper).

Interpersonal trust is about the trust that one person (the promisee) reposes in another person (the promisor). It is about the personal relationship between two people. Trust in the enforceability of a promise, on the other hand, is about the trust that the promisee has in the legal system to enforce a promise.<sup>3</sup> A promisee may

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<sup>1</sup>Before the development of promissory estoppel, the law provided no remedy to plaintiffs like the widow in *Kirksey v. Kirksey*, 8 Ala. 131 (1845), who relied to her detriment on a broken promise of support from her deceased husband’s brother. No doubt in response to cases like this, the law evolved and developed into RESTATEMENT (SECOND) OF CONTRACTS § 90 (1981), which provides:

(1) A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise. The remedy granted for breach may be limited as justice requires.

(2) A charitable subscription or a marriage settlement is binding under Subsection (1) without proof that the promise induced action or forbearance.

<sup>2</sup>*State Bank of Standish v. Curry*, 500 N.W.2d 104, 107 (1993) (affirming finding of promissory estoppel in favor of borrowers against bank).

<sup>3</sup>See Sidney W. DeLong, *The New Requirement of Enforcement Reliance in Commercial Promissory Estoppel: Section 90 as Catch-22*, 1997 WIS. L. REV. 943, 953 (1997). Professor DeLong has described the two types of trust as “performance reliance” and “enforcement reliance.”

When a promisor makes a promise that the promisee recognizes to be unenforceable, the promise can induce only “performance reliance.” The promisee relies solely on her estimate of the likelihood that the promisor will perform, without any expectation of a legal remedy if the reliance is disappointed. The promisee decides whether and how much to rely by assessing the promisor’s honesty and reliability, the circumstances bearing on the probability of performance and breach, the benefits that

choose to rely on a promise even if she does not trust the promisor because she has trust that the legal system will provide a remedy for a broken promise.<sup>4</sup>

This distinction between the two types of trust is important because it frames the discussion concerning the extent to which promissory estoppel should protect a promisee. This distinction also mirrors the difference between contract and promise, which was discussed in Professor Seana Shiffrin's recent article in the *Harvard Law Review*.<sup>5</sup> Professor Shiffrin observed that a "promise establishes rules for formalizing trust in interpersonal interactions; [while] contract establishes rules that help to enable a flourishing system of economic cooperation for mutual advantage."<sup>6</sup>

The protection of interpersonal trust is closely allied with the elevation of the role and protection of promise. Those who exalt the importance of promise would argue that a promise is sacred and that a promisee's trust in a promise and the promisor is entitled to the maximum level of protection.<sup>7</sup> The protection of trust in the enforceability of a promise, on the other hand, expresses the view that a promise must rise to the level of contract in order to be enforced.

Although interpersonal trust and enforcement trust are two distinct concepts, they are inextricably bound together (even in ways that appear contradictory). For example, if the law's goal is to protect a promisee's trust in her promisor no matter what, it can be argued that the enforceability of a promise must be maximized. At the same time, if the law's goal is to encourage a promisee to rely on a promise made by someone she does not trust, the law must also provide maximum security of enforcement. On the other hand, if the law's goal is to cultivate trust and a promisee's ability to decide whom to trust, it can be argued that the law should provide something less than maximum protection in order to prevent over-reliance by promisees on untrustworthy promisors. Less than maximum protection places a burden on promisees to choose their promisors carefully. And where does this

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reliance followed by performance would confer, and the costs that disappointed reliance would impose.

If . . . the promisor makes a promise that the promisee recognizes to be legally enforceable, then the promise will induce . . . "enforcement reliance." The promisee relies both on the credibility of the promise and on the belief that she will have a legal remedy for some or all of the costs of disappointed reliance if the promise is not performed.

*Id.*

<sup>4</sup>Throughout this Article, the promisee will be a woman or a business entity and the promisor will be a man or a business entity. One commentator expressed the distinction in this manner: "The legal enforceability of promises provides a 'substitute source of reassurance' for parties who do not have a preexisting trusting relationship." Anthony J. Bellia, Jr., *Promises, Trust, and Contract Law*, 47 *AM. J. JURIS.* 25, 29 (2002).

<sup>5</sup>Seana Valentine Shiffrin, *The Divergence of Contract and Promise*, 120 *HARV. L. REV.* 708, 710-11 (2007). This work continues along the line developed by Professor Fried's landmark work. See CHARLES FRIED, *CONTRACT AS PROMISE: A THEORY OF CONTRACTUAL OBLIGATION* (1981).

<sup>6</sup>Shiffrin, *supra* note 5, at 711.

<sup>7</sup>See Bellia, *supra* note 4, at 25. The themes of morality underlying promise is expressed by statements such as the following: "By making a promise, a person invites another to trust, and to break a promise is to abuse that trust." *Id.*

balance lie or where should it lie? To what extent should the law protect interpersonal trust and trust in enforcement of a promise? Such questions are the subject of this paper.

The discussion of reliance overshadows the discussion of trust in the typical Contracts class. Nonetheless, there is a school of thought that trust is so paramount and necessary in human interaction that the law should protect and promote trust, no matter what and no questions asked. Indeed, a body of scholarly work has developed to promote the idea that the availability of promissory estoppel should be expanded in order to encourage complete trust in promisors and their promises. One of the most advanced and cited works of this kind is an article from 1985 in the *University of Chicago Law Review* by Professors Farber and Matheson, who stated, “Our proposed rule is simply that commitments made in furtherance of economic activity should be enforced.”<sup>8</sup> In proposing this rule, they argued against the need to show reliance because all that mattered in their view was the enforcement of the promisee’s trust in the promise. They went so far as to state that the protection of trust is “the core concern of contract law.”<sup>9</sup>

These are grand, sweeping statements. If a complete stranger promises a business opportunity, should the law encourage the promisee to trust the promisor no matter what? The Farber and Matheson view would answer, “Yes.” It would also brush aside questions of the following sort: What was the relationship between the promisor and the promisee? Did the promisee have any reason to trust the promisor, other than the promisor’s promise? Should the promisee have trusted the promisor? Instead of focusing on such questions, the Farber and Matheson view is that the promisee trusted the promisor, and that is that.

Surprisingly, the notion of trust as an absolutely desirable trait or state seems to have gone unchallenged in large part. It is as if trust is such an ideal virtue that it is beyond question. This exaltation of trust as an unquestionable virtue, however, is contrary to common sense and universal human experience. Parents strive to instill the notion of trust in their children. Yet, all parents tell their children not to talk to

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<sup>8</sup>Daniel A. Farber & John H. Matheson, *Beyond Promissory Estoppel: Contract Law and the “Invisible Handshake,”* 52 U. CHI. L. REV. 903, 929, 935 (1985). Of course, their proposal did not become the prevailing doctrine. Yet, despite the fact that Farber and Matheson wrote their article a generation ago, it has shown remarkable vitality. Since January 1, 2000, alone, it has been cited in at least thirty-nine law review articles and two judicial opinions. Their work can be viewed (from a historical perspective) as an effort to continue the expansion of promissory estoppel from its roots. See GRANT GILMORE, *THE DEATH OF CONTRACT* 66 (1974). Professor Gilmore described this expansion, in its early days:

In early judicial, and for that matter academic, discussions of [section] 90, there was a general assumption that the principle of [section] 90, however it should be described, should find its application mostly, if not entirely, in what might be called non-commercial situations. Judge Learned Hand once suggested that [section] 90, if it had any scope at all, which he was inclined to doubt, should be restricted to donative or gift promises. Professionals should play the game according to professional rules. If A, in a commercial context, made what could be described as an offer to B, then A’s liability to B should depend on the formal rules of offer, acceptance and consideration and on nothing else. The course of decision has, however, seen a gradual expansion of [section] 90 as a principle of decision in a good many types of commercial situations.

*Id.*

<sup>9</sup>Farber & Matheson, *supra* note 8, at 935.

strangers—notwithstanding the importance of trust. The reason is obvious. There are limits that need to be placed on trust, and trust is not a pure good that should be promoted no matter what. In fact, too much trust can be dangerous and destructive. Despite the shared intuitive understanding that trust should have its limits, there has been relatively little discussion as to where the limits should be drawn.

To be sure, trust deserves protection. However, this Article contends that the law should not engage in the maximum protection of interpersonal trust, but should instead concern itself with promoting and protecting an optimal level of trust.<sup>10</sup> Trust, no matter what and however much, should not be the focal point of judicial inquiry. A promisee should not prevail simply because she trusted the promisor. Taken to its extremes, the literature seems to encourage contracting parties to engage in self-destructive acts of casual trust. Instead, the law should ask whether the trust was reasonable and whether it was appropriate. Those who engage in a reckless level of trust should not be protected. The promotion of the optimal level can be justified on the basis of such disparate rationales as morality (at one end of a spectrum) and economic efficiency (at the other).

The obvious question raised by this approach is how to determine the level of trust that should trigger judicial protection. This Article proposes a modest solution. It attempts to establish the endpoints of the continuum along which interpersonal trust should be evaluated. At one end are the situations where trust should be entitled to maximum protection. At the opposite end are the situations where trust should not be protected, and, indeed, should be discouraged.

Part II of this Article summarizes some of the scholarship discussing the nature and role of trust. In particular, it discusses the role of trust in a market economy, and the related role of trust in Contracts law. Part III examines whether there is a difference between trust and reliance, and whether it matters. To put it differently, does a discussion of trust add anything to what has already been generated by the literature's discussion of reliance? Part III further asserts that a separate discussion of trust is beneficial because it has the potential to guide and inform internal decision-making in a way that is not possible by simply focusing on outward reliance. Part IV of this Article discusses the role of trust in the doctrine of promissory estoppel. Among other things, it reviews the scholarly literature's incorporation of trust into the promissory estoppel analysis, and examines the intertwined relationship of trust and reliance.

Part V sets forth why the law should promote an optimal level of trust, as opposed to a maximum protection of trust no matter what. It discusses the need for

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<sup>10</sup>The focus on the “optimal level of trust” requires further clarification. A necessary question is whether the optimal level refers to the level of trust within an individual promisee or whether it refers to a level of trust at a macro or societal level. This Article is based on the premise that promoting the optimal level at the individual level leads to an aggregation of effects resulting in the optimal level at the societal level. At the individual level, the level of a trust can certainly be optimized because one can choose to trust someone a lot or a little. One can choose to trust another, but have back-up plans just in case. One can choose to trust another in some matters but not in others. See Claire A. Hill & Erin Ann O'Hara, *A Cognitive Theory of Trust*, 84 Wash. U. L.Rev. 1717 (2006). By identifying the circumstances in which trust should be protected by the law from the circumstances where it should not, the goal is to provide boundaries to guide the optimum level of trust at the individual level with the goal of improving it at the societal level as well.

promisees to exercise self-reliance and self-protection in order to avoid overreliance. To guide the determination of the optimal level of trust, this Article suggests that the protection of trust should be viewed along a spectrum with one end being defined by the cases where trust should be protected to the maximum extent and with the polar opposite end being defined by cases where trust deserves no protection.<sup>11</sup> Part VI identifies the types of cases where trust should be protected. Such cases include ones where the promisee is engaged in a transaction that she cannot avoid, where she has no control over the structure of the transaction, and where she has no choice but to trust the promisor (or more accurately, trust the legal system to enforce the promise). This Part includes a discussion of cases involving insurers and insureds. Another type of case where trust should be protected includes cases where the parties have developed a long-standing, pre-existing relationship to the point where the promisee has developed a reasonable basis to trust that the promisor will act in a manner consistent with that relationship.

Part VII presents the polar end of the spectrum where trust should not be protected. This part proposes that trust should not be protected if: (1) the promisee could have determined that the promisor was untrustworthy at a low cost to the promisee; or (2) if the promisee could have avoided the harm resulting from a broken promise by taking preventive measures that cost less than the amount of the potential harm. This part includes a detailed discussion of *Universal Computer Systems v. Medical Services Ass'n of Pennsylvania*,<sup>12</sup> which this Article contends may be the most wrongly decided promissory estoppel case ever. It also includes a discussion of the role of lawyers concerning a promisee's self-reliance. Part VIII concludes the Article.

In summary, this Article does not promote or encourage trust to the maximum limits. However, trust is not the only societal interest that deserves protection under the promissory estoppel doctrine. There are other equally deserving and meritorious interests, such as: (1) an interest in discouraging naïve, self-destructive behavior—i.e., blind trust; (2) an interest in avoiding misallocation of resources caused by overreliance and misplaced trust; and (3) an interest in avoiding the waste, disappointment and rancor caused by broken promises and lawsuits—in other words,

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<sup>11</sup>This Article's approach is open to the legitimate criticism that the situations described by the endpoints comprise only a small percentage of promissory estoppel cases, and that the proposed analytical framework is of limited value for the vast majority of such cases. Nonetheless, there should be some value in setting endpoints so that comparisons can be made as to whether a particular fact situation is closer to one or the other. Whatever the limitations of the proposal, it does aspire to Llewellyn's standards for a rule of law.

The ideal rule of law in case-law will be that which

- (1) fits rather accurately the actual recorded outcome of a rather consistent body of cases examined *as cases*, on facts and result; and
- (2) is announced in those cases as the rule; and
- (3) appeals today as leading to a just result; and therefore
- (4) offers real hope of appealing to present day courts; and so of guiding them with some sureness; and so of affording a counsellor a moderately accurate prediction, and an advocate a solid basis of case-planning.

K.N. Llewellyn, *The Rule of Law in our Case-Law of Contract*, 47 YALE L.J. 1243, 1256 (1938).

<sup>12</sup>*Universal Computer Systems, Inc. v. Med. Ass'n of Pa.*, 628 F.2d 820 (3d Cir. 1980).

parties would be better off avoiding bad situations, as opposed to trying to sort out in a courtroom the aftermath of an unfortunate act of misplaced trust.<sup>13</sup>

## II. THE NATURE AND PURPOSE OF TRUST

What is trust and what purpose does it serve? Scholars have utilized a variety of approaches to address the subject.<sup>14</sup> It has been approached from disciplines as varied as psychology,<sup>15</sup> anthropology,<sup>16</sup> evolutionary biology,<sup>17</sup> and economics.<sup>18</sup> This Article does not endorse or reject any particular approach, and instead discusses trust in an agnostic manner designed to reflect the common understanding that would be recognized in any court. With regard to interpersonal trust, the following

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<sup>13</sup>See Stanley D. Henderson, *Promissory Estoppel and Traditional Contract Doctrine*, 78 YALE L.J. 343, 383 (1969). There are undoubtedly other factors as well, and any proposed formula will necessarily be imprecise and need to be flexible.

The granting of relief under Section 90 depends ultimately upon a judgment that enforcement is necessary to avoid injustice. Such a requirement serves as a reminder that not all promisees who suffer reliance injuries are entitled to the protections of the section. More important, the notion that justice determines the limits of responsibility means that promissory estoppel is informed by a basic test of fairness. The doctrine thus allows courts wide latitude in redistributing losses resulting from unfilled promises. At the same time, it must be recognized that the very flexibility of Section 90 prevents its reduction to a precise formula or series of tests.

*Id.* See also Benjamin F. Boyer, *Promissory Estoppel: Requirements and Limitations of the Doctrine*, 98 U. PA. L. REV. 459, 497 (1950) (making a similar observation earlier in the century).

In addition, we can expect an attempt on the part of some courts to formalize the fact-situations which they will recognize as creating injustice. While judicial recognition of hardship and injustice as a reason for enforcing a gratuitous promise is necessary if promissory estoppel is to develop and mature, formalization or the confining of its use to a few specific situations is neither necessary nor desirable. Should that occur, promissory estoppel would become as mechanical as the jurisprudence of which Pound once complained. Rather, it is to be hoped that fluidity in the application of the concept will be maintained so that injustice may be avoided whenever it is encountered in connection with the gratuitous promises here discussed.

*Id.*

<sup>14</sup>This Article is not intended to serve as an in-depth examination of the nature of trust. For those interested in reviewing the scholarship in this area, the works cited in the Hill & O'Hara article, *supra* note 10, provide a good start. In addition, the entirety of Numbers 2 and 3 of Volume 81 of the Boston University Law Review is devoted to the subject of trust, with articles from scholars within and from outside the legal academy. See Symposium, *Trust Relationships*, 81 B.U. L. REV. 321 (2001).

<sup>15</sup>See, e.g., Tom R. Tyler, *Trust and Law Abidingness: A Proactive Model of Social Regulation*, 81 B.U. L. REV. 361 (2001).

<sup>16</sup>See, e.g., Russell Hardin, *Distrust*, 81 B.U. L. REV. 495, 504 (2001) (citing anthropological studies of trust in societies in Pakistan, Oman, and the American South).

<sup>17</sup>See, e.g., Margaret M. Blair & Lynn A. Stout, *Trust, Trustworthiness, and the Behavioral Foundations of Corporate Law*, 149 U. PA. L. REV. 1735, 1753 n. 35 (2001).

<sup>18</sup>See, e.g., Avner Ben-Ner & Louis Putterman, *Trusting and Trustworthiness*, 81 B.U. L. REV. 523 (2001).



definition utilized by Professors Hill and O'Hara is accessible and sensible. "Trust experts all seem to agree that trust is a state of mind that enables its possessor to be willing to make herself vulnerable to another—that is, to rely on another despite a positive risk that the other will act in a way that can harm the truster."<sup>19</sup> This definition is helpful for several reasons. It highlights the subjective, internal nature of trust. It also points out that trust involves at least two people, the self and other, and the process by which the self reaches out to another. It also emphasizes the fact that trust involves risk and vulnerability, and that trust poses the potential of a dangerous downside.

It necessarily follows that trust implicates personal judgment. Indeed, a powerful indicator of judgment is whether one is able to tell the difference between someone who should be trusted and someone who should be distrusted. The intertwined concepts of trust and judgment are so powerful that human accomplishments are measured by them. The important point is that the law should be wary and tread carefully in this area because the establishment of poor standards or misdirected incentives has the potential to interfere with the development of the most important personal qualities, and such poor standards or misdirected incentives have the potential to channel behavior toward regrettable or self-destructive ends.

Notwithstanding the potential dangers and downside of trust, it is equally and obviously true that trust provides the possibilities for benefits and advantages.

When my confidence in your assistance derives from my conviction that you will do what is right (not just what is prudent), then I trust you, and trust becomes a powerful tool for our working our mutual wills in the world. So remarkable a tool is trust that in the end we pursue it for its own sake; we prefer doing things cooperatively when we might have relied on fear or interest or worked alone.<sup>20</sup>

The benefits of trust can be explained by examining the harm caused by distrust.

Distrust in a world in which others are untrustworthy does, of course, protect one against losses that would follow from taking the risk of cooperating with others. But it can wreck one's own opportunities in a society or context in which others generally are trustworthy. The meaningful result of trust, when it is justified, is to enable cooperation; the result of distrust is to block even the attempt at cooperation. Trust is functional in a world in which trust pays off; distrust is functional in a world in which trust does not pay off.<sup>21</sup>

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<sup>19</sup>Hill & O'Hara, *supra* note 10, at 1724. Two other professors also described trust along similar lines.

First, trust involves at least two actors—the actor who trusts and the actor who is trusted. Second, the trusting actor must deliberately make herself vulnerable to the trusted actor in circumstances in which the trusted actor could benefit from taking advantage of the trusting actor's vulnerability. Third, the trusting actor must make herself vulnerable in the belief or expectation that the trusted actor will in fact behave "trustworthily" – that is, refrain from exploiting the trusting actor's vulnerability. Blair & Stout, *supra* note 17, at 1745-46.

<sup>20</sup>FRIED, *supra* note 5, at 8.

<sup>21</sup>Hardin, *supra* note 16, at 503.

Distrust is about a world marked by isolation and suspicion. In such a world, aspirations and development will necessarily be limited because people will be unwilling to pursue ventures that might lead to gains greater than the sum of the individual contributions. It is for this reason that trust is a subject of economic concern.

#### A. *The Role of Trust in a Market Economy*

There are numerous reasons why trust should be encouraged. One recurring theme in the literature focuses on the importance of trust for a modern, market economy.<sup>22</sup> As one observer put it: “[O]ne of the fundamental psychological conditions for the successful coordination of complex commercial transaction [is] interpersonal trust.”<sup>23</sup> Professors Farber and Matheson added:

Up until this point, relationships characterized by interdependence and thus by a need for trust have been described as though they were exceptional. This description could not be further from the truth. The network of interdependence in modern economic relations extends far beyond the ongoing relationship between specific parties to the very structure of the modern economy. Modern economic relations are dependent upon institutions which themselves are based on trust. The firm, an essential economic unit, can function only if employees and

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<sup>22</sup>There is also the theme based on moralistic prescriptions. See FRIED, *supra* note 5, at 16-17.

The obligation to keep a promise is grounded not in arguments of utility but in respect for individual autonomy and in trust. Autonomy and trust are grounds for the institution of promising as well, but the argument for *individual* obligation is not the same. Individual obligation is only a step away, but that step must be taken. An individual is morally bound to keep his promises because he has intentionally invoked a convention whose function it is to give grounds—moral grounds—for another to expect the promised performance. To renege is to abuse a confidence he was free to invite or not, and which he intentionally did invite. To abuse that confidence now is like (but only *like*) lying: the abuse of a shared social institution that is intended to invoke the bonds of trust. A liar and a promise-breaker each *use* another person. In both speech and promising there is an invitation to the other to trust, to make himself vulnerable; the liar and the promise-breaker then abuse that trust. The obligation to keep a promise is thus similar to but more constraining than the obligation to tell the truth. To avoid lying you need only believe in the truth of what you say when you say it, but a promise binds into the future, well past the moment when the promise is made. There will, of course, be great social utility to a general regime of trust and confidence in promises and truthfulness. But this just shows that a regime of mutual respect allows men and women to accomplish what in a jungle of unrestrained self-interest could not be accomplished. If this advantage is to be firmly established, there must exist a ground for mutual confidence deeper than and independent of the social utility it permits.

*Id.* See also Lon L. Fuller, *Consideration and Form*, 41 COLUM. L. REV. 799, 811 (1941). The focus on the moral aspect seems to have been reflected in Professor Fuller’s earlier observation that the cases under Section 90 of the Restatement of Contracts “are not ‘upholding transactions’ but healing losses caused through broken faith.” *Id.*

<sup>23</sup>G. Richard Shell, *Opportunism and Trust in the Negotiation of Commercial Contracts: Toward a New Cause of Action*, 44 VAND. L. REV. 221, 225 (1991).

employer have at least limited trust in each other. Markets for goods can exist only if sellers normally can be trusted to make future deliveries of nondefective products. Insurance, credit, and investment can exist only when the other party generally can be trusted to pay.<sup>24</sup>

The need for trust in an economy is easy to overlook because of its intangible nature. Yet without it, many transactions that are taken for granted could not be completed or even entered. People need one another because people stopped being self-sufficient centuries ago—individuals do not, as a general rule, grow their own food or make their own clothes. Trust enables economic actors to enter into transactions with each other. The ability to obtain goods and services from others is rooted in trust.

### 1. The Importance of Trust at the Macro-Economic Level

The importance of trust to a market economy can be seen at both the macro-economic level and the micro-economic level of the firm. At the macro level, trust is an essential element. Indeed, the ability to trust strangers is what distinguishes primitive, tribal-based economies from modern, free-market economies. This transition from primitive to modern economic structures was observed in the nineteenth century as it was occurring.<sup>25</sup> The ability to move beyond transactions

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<sup>24</sup>Farber & Matheson, *supra* note 8, at 927. See also DeLong, *supra* note 3, at 950, n. 23. Along similar lines, Professor DeLong added: “Most scholars agree that *bargain* promises are legally enforced in order to increase the gains available through trade. Enforceability encourages promisees to enter into bargain contracts by reducing their risk of disappointed reliance.” *Id.*

<sup>25</sup>See HENRY SUMNER MAINE, ANCIENT LAW: ITS CONNECTIONS WITH THE EARLY HISTORY OF SOCIETY, AND ITS RELATION TO MODERN IDEAS 172-73 (London, J. Murray 1920) (1866).

The movement of progressive societies has been uniform in one respect. Through all its course it has been distinguished by the gradual dissolution of family dependency, and the growth of individual obligation in its place. The Individual is steadily substituted for the Family, as the unit of which civil laws take account . . . Nor is it difficult to see what is the tie between man and man which replaces by degrees those forms of reciprocity in rights and duties which have their origin in the Family. It is Contract. Starting, as from one terminus of history, from a condition of society in which all the relations of Persons are summed up in the relations of Family, we seem to have steadily moved towards a phase of social order in which all these relations arise from the free agreement of Individuals.

*Id.*

Maine went on to state:

All the forms of Status taken notice of in the Law of Persons were derived from, and to some extent are still coloured [sic] by, the powers and privileges anciently residing in the Family. If then we employ Status, agreeably with the usage of the best writers, to signify these personal conditions only, and avoid applying the term to such conditions as are the immediate or remote result of agreement, we may say that the movement of the progressive societies has hitherto been a movement *from Status to Contract*.

*Id.* at 173-74.

limited to people who are personally known to one another to transactions with people with no prior relationship is a necessary condition of modern economic life.<sup>26</sup>

This movement away from an economy based on family or tribal relationships to a modern economy is based, in large part, on trust. Here, the discussion is more about enforcement trust rather than interpersonal trust. In the absence of an ability to trust strangers, business relationships and economic activity are confined to a tightly-circumscribed group.<sup>27</sup> Such limits obviously place significant constraints on the ability of an economy to expand. In order to move beyond trust confined to a circle of intimates, the ability to trust that the legal system will enforce promises made by strangers takes on added and obvious importance. The confidence of a promisee in enforcement trust may be the necessary catalyst to enable her to make the leap of faith to rely on a stranger's promise. The importance of trust to a modern economy provides an easy explanation as to why the legal enforcement of trust would become important in a country spanning a continent and whose citizens did not descend from

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<sup>26</sup>See Michael Trebilcock & Jing Leng, *The Role of Formal Contract Law and Enforcement in Economic Development*, 92 VA. L. REV. 1517, 1521-22 (2006). This distinction between undeveloped and advanced economies was the subject of this recent article which discussed the work of Nobel Laureate Douglass North:

North first identifies self-enforcement as the primary feature of contracts used in tribes, primitive societies, and close-knit small communities—settings in which personal knowledge of transacting parties about one another is extensive, and repeat dealings are pervasive. North then points out the limits of self-enforcing contracts in a world of increasing impersonal exchange. In such a world, simultaneous exchange and repeat dealings are no longer the prevailing norm; thus, self-enforcing contracts become insufficient because there no longer exists a dense social network of interaction to enable transacting to take place at low cost.

*Id.*

The analysis added:

One particular understanding of this assessment by North in contemporary development studies is that as developing countries' economies become more fully integrated into the larger global economy, formal contract enforcement mechanisms assume a larger significance. North explains that 'third-party enforcement' means "the development of the state as a coercive force able to monitor property rights and enforce contracts effectively."

*Id.* at 1522.

<sup>27</sup>Hill & O'Hara, *supra* note 10, at 1739. In their article, Professors Hill and O'Hara pointed to a study of Chinese rubber dealers who limited their dealings to: (in order of priority) nuclear family; extended family; clansmen; fellow villagers; other Chinese who spoke the same dialect; Chinese who spoke another dialect; and, finally, non-Chinese. *Id.* at 1739-40. They established this priority because of their inability to rely on legal mechanisms to enforce trust. *Id.* To anyone who believes that the importance of tribes is merely a matter of historical interest limited to pre-twentieth century history, a cursory glance at the daily news stories (especially from other parts of the world like Gaza, Iraq, Nigeria, and Somalia) should amply demonstrate that tribalism remains a powerful force and provides the contextual explanation for many current events. It is also interesting to note that Maine's observation is confirmed in that there is an inverse relationship between the strength of tribalism in a society, on the one hand, and the rule of law and the strength of contract law, on the other. See MAINE, *supra* note 25 at 173-74. To the extent that a reader may interpret the preceding as a value judgment, such a judgment is purely the creation of the reader and not the Author.

a common tribe, region, or religion.<sup>28</sup> Thus, trust (and the protection of trust) serves an important economic and social function.<sup>29</sup> Formal legal mechanisms are therefore necessary to encourage and protect trust as a society moves from an economy dominated by transactions between parties who know one another to an economy dominated by transactions between strangers. This ability to trust enables an economy to grow exponentially beyond the limits imposed when transactions are confined to closely-related parties.

## 2. The Importance of Trust at the Micro-Economic Level

Trust (the interpersonal kind) also serves a vital role at the micro-economic level of the firm. It serves to harmonize interpersonal dealings among actors within the firm, and between actors within the firm and those outside.

Where trust can be harnessed, it can substantially reduce the inefficiencies associated with both agency and team production relationships. Trust permits transactions to go forward on the basis of a handshake rather than a complex formal contract; it reduces the need to expend resources on constant monitoring of employees and business partners; and it avoids the uncertainty and expense associated with trying to enforce formal and informal agreements in the courts.<sup>30</sup>

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<sup>28</sup>Jay M. Feinman, *The Meaning of Reliance: A Historical Perspective*, 1984 WIS. L. REV. 1373, 1376 (1984). Professor Feinman addressed the role of social and economic needs in the development of Contracts law and the promotion of trust.

The functional approach, on the other hand, posits a strong causal relation between social needs and legal development. The interests and needs of a society, especially in its economic aspects, generate strong pressure on the form and content of contract law. Without necessarily resorting to crude determinism, advocates of this approach stress the extent to which contract law responds to forces external to the legal system and downplay its purely internal intellectual development.

The functional approach contemplates that, in any society in which economic exchange is significantly developed, a large number of transactions will occur without the precision envisioned by the classical formation/bargain consideration model. In an economic exchange, the absence of the discrete bargain or the precise agreement required by the classical model should not prevent the enforcement of a promise that induces foreseeable reliance. Enforcement in those cases serves a variety of social needs, such as the promotion of trust and of transactional security, and therefore facilitates exchange.

*Id.*

<sup>29</sup>*Cf.* Larry E. Ribstein, *Law v. Trust*, 81 B.U. L. REV. 553, 555 (2001). From a different angle, Professor Ribstein argues that laws designed to enforce trust may actually undermine trust because they substitute reliance on formal, legal mechanisms to regulate behavior over a stronger form of trust developed through personal relationships. *Id.*

<sup>30</sup>Blair & Stout, *supra* note 17, at 1757. *See also* Farber & Matheson, *supra* note 8, at 928. Professors Farber and Matheson made similar observations:

Because trust is essential to our basic economic institutions, it is a public good. One individual breaking trust in a dramatic way, or many individuals breaking trust less dramatically, can lead to short-run benefits for those individuals but create negative externalities. The willingness of others to trust is impaired, requiring them to invest in precautions or insure themselves against the increased risk of betrayal. Such

Interpersonal trust also serves to reduce transaction costs – a holy grail of economic efficiency theories. It overcomes the barriers of wariness and suspicion, and permits transactions to proceed on their merits.

The awkwardness or expense of more formal means of assuring reciprocal exchange motivate parties to seek other ways of constructing cooperative bargaining relationships. The basis of all alternatives is one of the most fragile, yet powerful human dispositions—interpersonal trust. Parties prefer to deal on trust because it lowers the transaction costs inherent in the alternative approach of bargaining based on mutual suspicion. Moreover, trust signals that postcontractual relationships with the same or future partners can be based on mutually beneficial understanding and flexibility rather than on strict adherence to legal rights and contract terms.<sup>31</sup>

Thus, trust reduces financial costs and delays in time. While the benefits may be difficult to measure, their existence is intuitive and obvious.

### B. *The Role of Trust in Contracts*

Because of the role of trust in social and economic relationships, the Law of Contracts encourages and enforces trust. In addition to describing the protection of trust as “the core concern of contract law,”<sup>32</sup> Professors Farber and Matheson also stated: “[T]he underlying legal policy is to protect the ability of individuals to trust promises in circumstances in which that trust is socially beneficial.”<sup>33</sup> If the law did not protect trust, contracts would be undermined. “For if losses were truly to be allowed to lie where they fall, then no contract would ever be enforced. If somebody ended up losing because he trusted in the promise of another, why the more fool he!”<sup>34</sup> The bottom line is that the role and presence of trust (interpersonal trust and enforcement trust) is intertwined with the law of Contracts and cannot be separated.

A further and more important set of questions (for purposes of this Article) is how does trust develop and how should trust develop? Common understanding tells us that trust develops over time and over a course of dealing between people. As a general matter, people do not say or think, “Hello, I’m so and so. It’s nice to meet you. You just made me a promise. I will trust you.” Usually, it requires more for

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externalities exist because of asymmetrical information: the promisor necessarily has better information about his own trustworthiness than does the promisee. For example, in the short run employers can profit by making commitments to employees, obtaining the resulting benefits, and then reneging. But in the long run, enforcement benefits promisors as a group by fostering the reliance from which they seek to benefit. Conversely, trustworthy individuals confer a social benefit by increasing the general perception of trust, thereby allowing others to decrease such costs.

*Id.*

<sup>31</sup>Shell, *supra* note 23, at 255.

<sup>32</sup>Farber & Matheson, *supra* note 8, at 935.

<sup>33</sup>*Id.* at 905. *See also* FRIED, *supra* note 5, at 83. Along similar lines, Professor Fried added, “In general we can get the social, collective benefits of trust only if we are faithful for the sake of trust itself, not just for the sake of the resulting benefits.” *Id.*

<sup>34</sup>*Id.* at 65.

trust to build. If one accepts this description, should the law reflect common behavioral practice or should the law intervene to accelerate the development of trust? Should the state intervene to push private conduct in a direction it might not otherwise go? The advocates of maximum trust protection would answer yes. This Article takes a contrary view.

### III. IS THERE A DIFFERENCE BETWEEN TRUST AND RELIANCE, AND, IF THERE IS, DOES IT MATTER?

At this point, a few foundational questions should be addressed: Is there a difference between trust and reliance, or are they interchangeable? Even if there is some difference in meaning, does it matter for Contracts? What, if anything, is gained by focusing on trust in the application of promissory estoppel, as opposed to reliance alone? Despite the synonymous relationship between the words, this Article submits that there is a difference and that the difference is important because it is about a party's ability to make appropriate decisions and to choose beneficial relationships.<sup>35</sup>

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<sup>35</sup>See Farber & Matheson, *supra* note 8, at 945. The Farber and Matheson article draws a distinction between trust and reliance:

Based on our survey of recent promissory estoppel cases, we believe that promissory estoppel is losing its link with reliance. In key cases promises have been enforced with only the weakest showing of any detriment to the promisee. Reliance-based damages are the exception, not the rule. With the decline of reliance, promissory estoppel is moving away from tort law. It has become a means of enforcing promises differing in doctrinal detail from traditional contract law but sharing a common goal. That goal, we have argued, is to foster trust between economic actors. Trust is a moral good, but it is also an economic asset. It allows coordination and planning between economic actors and fosters the formation of valuable economic institutions.

Perhaps in an earlier age traditional contract law was adequate to foster the degree of trust society needed in economic activities. Today, an increasingly interdependent society needs to foster trust in a variety of relationships not readily organized through the device of the formal contract. Promissory estoppel is one of several mechanisms courts have used to try to close what we have called the "relational gap" in contract law.

*Id.*

This passage illustrates the decoupling of trust from reliance. It suggests that trust should be encouraged and protected without regard to reliance. This view, of course, places the weight of the law behind the enforcement of the promise, and is consistent with Professor Fried's views as expressed in his book, *Contract as Promise*. See generally FRIED, *supra* note 5. See also Edward Yorio & Steve Thel, *The Promissory Basis of Section 90*, 101 YALE L.J. 111, 121 (1991).

Fried explains much of contract law in terms of the moral obligation of promise. His primary focus is on the promisor, who has an interest in requiring that promises be kept so that others will take her at her word. By enforcing contracts, the legal system supports principles of trust and integrity.

*Id.*

Thus, the use of the word "trust" in the literature is not synonymous with "reliance." Indeed, trust is used to urge the primacy of promise over reliance.

A. *The Subjective Nature of Trust versus the Objective Nature of Reliance*

Some dictionary definitions suggest the absence of any difference between trust and reliance. For example, the online version of the Oxford English Dictionary uses one to define the other. It defines trust as: “Confidence in or reliance on some quality or attribute of a person or thing, or the truth of a statement.”<sup>36</sup> The online version of the American Heritage Dictionary suggests a more nuanced distinction, however. It provides: “*Rely* implies complete confidence. . . . *Trust* stresses confidence arising from belief that is often based on inconclusive evidence.”<sup>37</sup>

This latter definition suggests several layers of difference between the two. Trust can be viewed as an internal, subjective state of mind, while reliance can be viewed as an objectively verifiable act. This observation also leads to the corollary proposition that trust and reliance occupy different positions on a temporal continuum. It may be the case that the development of trust must precede reliance. Accordingly, trust might be viewed as a precursor or condition to reliance.<sup>38</sup> Thus, the movement from trust to reliance is (in part) a movement in time and a movement from internal to external, subjective to objective. Moreover, the existence of trust can only be proven to the extent that it manifests itself in reliance.

B. *Reliance as an Ex Post Judicial Inquiry versus Trust as an Individual Ex Ante Process*

The observation that the movement from trust to reliance is a movement in time and a movement from subjective to objective leads to a further observation that is central to the legal analysis. The focus on reliance is exclusively about the *ex post* judicial inquiry as to whether the promisee’s conduct was reasonable. In other words, the examination of reliance is about a court reviewing a record after the fact. At that point, the individual has been removed from the process; the process has been thrown into the hands of the lawyers and the court. The conduct constituting the reliance has already occurred, and the court is determining whether such conduct was reasonable under an objective standard.

An examination of trust focuses on a different moment in time and a different stage in the process. It is about the *ex ante* decision made by the individual before reliance occurs. The formation of trust is a private matter. It is the point when the promisee, alone in her conscience, decides whether to engage in conduct that objectively constitutes reliance. There is no judicial involvement at that point, and no external inquiry imposing objective, judgmental standards. The promisee has not yet crossed the point of no return between the subjective/objective divide. Thus, the examination of trust takes place at a different stage than an examination of reliance.

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<sup>36</sup>See OXFORD ENGLISH DICTIONARY, 402 (2d ed. 1989), available at <http://dictionary.oed.com>.

<sup>37</sup>See THE AMERICAN HERITAGE DICTIONARY OF THE ENGLISH LANGUAGE 1475 (4th ed. 2000), available at <http://www.bartleby.com/61>.

<sup>38</sup>This Article does not assume or suggest that trust must always and necessarily accompany reliance. It is, of course, possible for reliance to occur without trust. As an extreme example, a prisoner must rely on his jailer—whether trust exists is another matter. Nonetheless, because this Article is about the law of Contracts, it deals with consensual relationships.



*C. The Value of a Focus on Trust*

Because trust is about the individual *ex ante* decision-making process, an examination of trust presents the opportunity to guide and inform behavior. Nonetheless, a focus on trust presents its own set of unique analytical challenges. As learned by many students in their first week of law school, the law of Contracts is based on the “objective theory of contract.”<sup>39</sup> Given the law’s emphasis on objective standards, it may seem a bit surprising that trust, a subjective state of mind, has been (or should be) the subject of judicial and scholarly attention. Despite the law’s emphasis on objective criteria, trust merits examination because of its relationship to conduct.

Under ideal circumstances, the decision to trust is about the full exercise of personal autonomy. It is at the heart of the moment when one decides to move beyond oneself to reach out to another. It should be the result of a reflective and deliberate internal calculus informed by experience. To the extent the law encourages trust no matter what, it undermines this process and removes the cautionary burden of self-reliance and self-restraint from a promisee. The focus on trust is therefore, in part, about the appropriate level of the law’s influence on, involvement with or interference in personal, private decision-making. By concentrating on the moment when the decision is being made whether to act in reliance, the law can influence whether trust, a subjective state of mind, ripens into reliance or an enforceable transaction, both objective acts. This would add more incentive for the law’s need to examine trust because it is at that formational stage where the decision to rely is made.

A different way to analyze the importance of trust is to ask whether there is any point to discussing anything other than reasonable reliance. After all, Section 90 is concerned with reasonable reliance, so why move beyond that to examine trust? However, if one accepts the premise that law should guide, affect or improve behavior, then there are theoretical and practical benefits to examining trust. To that end, an understanding of a person’s internal state is helpful, and perhaps necessary, to guiding external conduct. Although stated in the context of examining the role of emotion in the law, the following observation is equally applicable to a discussion of trust: “Understanding the nature of emotion has practical, not merely theoretical, value. Emotions motivate behavior. Accordingly, if we have an interest in affecting the behavior of another person—whether a child, a student, or a fellow citizen—we should also take an interest in that person’s emotional life.”<sup>40</sup> There is little

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<sup>39</sup>*See, e.g.*, CHARLES L. KNAPP ET AL., PROBLEMS IN CONTRACT LAW, CASES AND MATERIALS 27 (5th ed. 2003) (“[B]oth the rhetoric and the actions of courts and writers have stressed an ‘objective theory’ of contract obligation, by which one is ordinarily bound or not bound, not by her ‘secret intent’ to that effect, but by the reasonable interpretation of her words and actions.”). The objective theory of contract is, of course, traceable back to the articulation of the theory by Oliver Wendell Holmes, Jr., that the “making of a contract depends not on the agreement of two minds in one intention, but on the agreement of two sets of external signs—not on the parties’ having *meant* the same thing but on their having *said* the same thing.” Oliver Wendell Holmes, Jr., *The Path of the Law*, 10 HARV. L. REV. 457, 464 (1897).

<sup>40</sup>Dan M. Kahan & Martha C. Nussbaum, *Two Conceptions of Emotion in Criminal Law*, 96 COLUM. L. REV. 269, 297-98 (1996).

educational value to telling someone to engage or not engage in certain outward behavior without also explaining the underlying reasoning. There is a moral and educational emptiness to an approach that only addresses conduct.

There is a great deal of room for debate as to how and whether public education and public policy should be used to shape the emotional evaluations that citizens form; many people do think that the only correct focus for law is behavior, and that, so far as the law is concerned, the person who effectively suppresses hatred is on a par with the person who ceases to hate . . . . Most of us would not be very satisfied with teachers who ruled racist behavior off-limits but failed to teach the falsity of the beliefs about African-Americans that underlie much racial prejudice and hatred, allowing their students to persist in those appraisals.<sup>41</sup>

To borrow this thought, the person who is concerned only with reasonable reliance, without an understanding of trust, is not necessarily on a par with the person who knows whom to trust and when to trust. It is more likely that the latter will be better able to avoid unfortunate situations. This is why trust, by itself, merits examination and discussion.

With specific reference to the law of Contracts, Professor Shiffrin observed:

For instance, *if* contract law's aim were to protect against harm suffered from breach of promise, measured in terms of reasonable reliance, what

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<sup>41</sup>*Id.* at 300. Professors Kahan and Nussbaum laid the foundation for their views by highlighting the difference between the mechanistic view of emotion as opposed to the evaluative view:

The mechanistic conception sees emotions as forces that do not contain or respond to thought; it is correspondingly skeptical about both the coherence of morally assessing emotions and the possibility of shaping and reshaping persons' emotional lives. The evaluative conception, in contrast, holds that emotions express cognitive appraisals, that these appraisals can themselves be morally evaluated, and that persons (individually and collectively) can and should shape their emotions through moral education.

*Id.* at 273.

Whether one holds one view or the other determines whether one believes in the possibility of improvement or not. Those with a mechanistic view hold a pessimistic view of improvement. "But most versions of the mechanistic view hold out little hope that conditioning will render the emotions governable: thus they always focus on the need to cultivate mechanisms of suppression and indulgence as the primary devices to control emotion." *Id.* at 298. Those with an evaluative view hold an optimistic belief in the possibility of improvement, and the possibility of improvement is closely bound to the notion of the efficacy of education.

The evaluative view, in contrast, considers emotional education to be closely bound up with moral education. Because cognitive appraisals are integral to emotions, the educator of emotions must address herself to her pupil's beliefs, especially about matters of value. . . . Those who subscribe to the evaluative view are also much more likely to view moral education as a matter of public concern. The inculcation of correct values plays no necessary role in the mechanistic program, which purports to focus only on behavior. But if the evaluative view is correct, then any program of emotional education that disregards moral belief is destined to fail.

*Id.* at 298-300.

counts as a reasonable form of reliance might depend on the cultural context and the degree to which trust is encouraged; the degree to which trust is encouraged might, in turn, be a matter settled partly by the norms of morality and not merely by cultural customs.<sup>42</sup>

In other words, the law has the potential to guide and shape behavior.<sup>43</sup>[jic1]

The need for the law to serve an educational role is further underscored by the limitations of knowledge and risk-assessment that impair contracting parties.<sup>44</sup> Empirical studies have shown that prospective contracting parties tend to be overly and unrealistically optimistic of the potential outcome of transactions, and fail to fully understand or assess the risks involved.<sup>45</sup> However, the law of Contracts is based on the principle that autonomous parties are fully capable of choosing and deciding their respective goals or wants, determining how to attain or obtain them, and accurately assessing the costs and benefits.<sup>46</sup> In other words, the coherence of Contracts law depends on the ability of parties to make rational choices (or the ability of the law to assume rationality on the part of the actors). Thus, it is in the law's interest, and the interest of society's reliance on law, to encourage people to make thoughtful, rational decisions and choices. Promoting trust no matter what encourages the wrong, ill-advised sort of conduct that undermines the foundation of Contracts. At a minimum, the law should at least refrain from encouraging inappropriate conduct (if it is too much to look to the law to promote appropriate conduct).

Such aspirations are at odds with those who advocate the enforcement of promises without regard to whether the promisee's trust or reliance is reasonable or desirable. The problem with such a view is that it assumes all contracting parties possess a certain (high) level of information, wisdom, judgment and analytical ability, which leads them to make contracting decisions that should be enforced by the courts. In a hypothetical world, promisees might possess all of these qualities in abundance, but the real world is populated by ordinary humans.<sup>47</sup> If one accepts the

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<sup>42</sup>Shiffrin, *supra* note 5, at 716.

<sup>43</sup>*Id.* at 741 ("Namely, a great deal of morally virtuous behavior depends upon cultivating sound instincts and habits and allowing these to guide one's behavior.").

<sup>44</sup>See Melvin Aron Eisenberg, *The Limits of Cognition and the Limits of Contract*, 47 STAN. L. REV. 211, 211 (1995). Professor Eisenberg has described such limitations as "limits of cognition." *Id.*

<sup>45</sup>*Id.* at 216,223.

<sup>46</sup>*Id.* at 213.

<sup>47</sup>See Charles L. Knapp, *Rescuing Reliance: The Perils of Promissory Estoppel*, 49 HASTINGS L.J. 1191, 1314-5 (1998). In a somewhat different context, Professor Knapp described these conflicting views in this manner:

In one view of the world, things should function tidily. People should think before they act, seek advice when out of their depth, know what they are getting into, read all documents, and write down all their agreements. If they do not, the law will see that they suffer the consequences. People may be hurt, but they—and others who learn of their misfortune—will profit from the experience, and the world will become tidier. The drawback of this approach is that it fails to recognize the human side of the law, the need for fairness. If we expect formality every time, there is no humanity.

premise that contracting parties are subject to human mistakes, misjudgments, and miscalculations, then there may be a role for the law to guide and educate to help people to make better decisions and to develop better judgment. Providing guidance concerning when, how and whom to trust might be one such role. As stated by Professors Goetz and Scott: “Appropriately calibrated enforcement rules can be used to achieve the optimal number and type of promises based on the degree and form of adaptation by promisor and promisee.”<sup>48</sup>

*D. Additional Observations Concerning the Difference between Interpersonal Trust and Enforcement Trust*

As described, there is a difference between a promisee’s trust in the promisor as opposed to a promisee’s trust that the promise will be enforced. In other words, a promisee may have no faith in the promisor, but may nonetheless rely on the promise because she knows and trusts that the law will enforce the promise. Alternatively, a promisee may know that the promise is legally unenforceable, but relies on the promise anyway because she trusts the promisor to perform. More likely is the scenario where the promisee has no idea whether the promise is enforceable or not (because she is not a lawyer), but relies on the promise because she trusts the promisor.

This Article contends that trust in the promisor is more deserving of attention, for a couple of reasons. First, it seems intuitively true that the universe of cases involving trust in the promisor is larger than the set of cases involving trust that the promise will be enforced. “Enforcement reliance” cases require the involvement of a promisee who knows the difference between an enforceable versus an unenforceable promise—i.e., a sophisticated party. A sophisticated party represented by lawyers will decide whether to trust the other party or not, but will also have a basis to know whether a promise can be enforced. A less sophisticated party who is less familiar with the law will only have trust in the promisor as a basis for reliance.<sup>49</sup>

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In the other view of the world, people screw up. They grope their way through a complex and demanding world, doing the best they can, which is often not good enough, and they fall into traps. When they do so, the law will examine the route they followed and the nature of the particular trap. If the particular story is compelling enough, they will be rescued. Whether others will also be rescued cannot be predicted—it is a function of how compelling their story is. The drawback of this approach is that it fails to recognize the stable side of the law, the need for predictability. If we look to context every time, there is no rule of law.

*Id.*

<sup>48</sup>Charles J. Goetz & Robert E. Scott, *Enforcing Promises: An Examination of the Basis of Contract*, 89 YALE L.J. 1261, 1266 (1980). The need for care and deliberation is necessary because “[c]ontracts enable persons who are not intimates nevertheless to cease to be strangers; and breaches do not just reinstate persons’ prior status as strangers but instead leave them actively estranged.” Daniel Markovits, *Contract and Collaboration*, 113 YALE L.J. 1417, 1463 (2004).

<sup>49</sup>See DeLong, *supra* note 3, at 996. Along these lines, Professor DeLong observed: “Indeed, the more legally sophisticated the parties are, the less reason a promisee has to infer consent from a non-bargain, informal commercial promise.” *Id.* He further noted, “In light of common commercial practice, legally sophisticated commercial promisees have no reason to believe that a non-bargain promise made by a commercial promisor is legally enforceable in the absence of a manifested intention that it be so.” *Id.* at 961.

More importantly, if the goal is to guide and inform the conduct of contracting parties, the analysis should focus on the point of interpersonal contact—the point where judgment is formed. This is where the law can have the greatest effect in promoting beneficial behavior and discouraging self-destructive behavior. Any attempt to promote trust in enforceability over interpersonal trust would likely push promisees toward conduct that should be avoided. The reason is because trust in enforceability offers comparatively little reliability.<sup>50</sup> By relying on the enforceability of a promise, a promisee is relying on the inherent uncertainties of the litigation process (including the indeterminacy of the law, the respective skill of her lawyer compared to opposing counsel, and the vagaries of judicial decision-making) and must be willing to delay certainty for the months or years it might take for the litigation process to work itself out.<sup>51</sup>

In other words, encouraging trust in enforceability encourages promisees to place their trust in matters over which they have no control. On the other hand, a promisee has complete control over whether she will trust a promisor or not. By actively focusing on and guiding trust in the promisor, the law can play an educational and enriching role to help promisees avoid bad situations (which also would result in overall societal gains by the avoidance of resource-wasting transactions and lawsuits).

#### IV. THE ROLE OF TRUST IN PROMISSORY ESTOPPEL

This is surely an obvious point, but the word “trust” appears nowhere in Section 90. It does not appear in the widely-accepted hornbook definition of promissory estoppel.<sup>52</sup> It does not appear in the various state law formulations of the elements.<sup>53</sup> Nevertheless, the role of trust is an undeniable part of the doctrine. “The principle that a trust reasonably reposed and voluntarily accepted should not be violated

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<sup>50</sup>Moreover, parties enter into contracts with expectations of performance, not with expectations of enforcement. To illustrate, Comment 1 to the Uniform Commercial Code section 2-609 makes the observation that “the essential purpose of a contract between commercial persons is actual performance and they do not bargain merely for a promise, or for a promise plus the right to win a lawsuit . . .” U.C.C. § 2-609 cmt. 1 (2001).

<sup>51</sup>This is admittedly a dark view of the nature of enforcement reliance, but this view is a luxury that can be held by one who lives in a society reliably governed and organized under the rule of law. From a global, bird’s-eye perspective and in comparison to some other legal systems, there is no doubt that the American legal system is based on the rule of law, offers predictability, and is free of systemic corruption. Despite these fundamental truths, a litigant can never be assured of any particular outcome, and this is why enforcement reliance is less than ideal. Nonetheless, it is indisputable that parties need to be able to trust in the enforcement of promises and contracts, especially at the fragile stage when a society is transitioning to a modern economy. Even today, there are examples of countries being held back by the absence of a reliable judicial system.

<sup>52</sup>See E. ALLAN FARNSWORTH, *CONTRACTS* 94-95 (4th ed. 2004). “First, there must have been a promise. Second, the promisor must have had reason to expect reliance on the promise. Third, the promise must have induced such reliance. Fourth, the circumstances must have been such that injustice can be avoided only by enforcement of the promise.” *Id.*

<sup>53</sup>See, e.g., *Katz v. Danny Dare, Inc.*, 610 S.W.2d 121, 124 (Mo. Ct. App. 1981) (stating elements of promissory estoppel as: “(1) a promise; (2) a detrimental reliance on such promise; and (3) injustice can be avoided only by enforcement of the promise”).

without remedy is a very old one; [S]ection 90 is but one of its formulations.”<sup>54</sup> The role of trust in the doctrine is present and undeniable because of the requirement of reliance.<sup>55</sup> “Reliance doctrine is a means of affirming the existence of trust and cooperation among the members of that community.”<sup>56</sup>

Despite the existence and importance of trust, it should not be surprising that the doctrinal formulations focus on reliance rather than trust.<sup>57</sup> Because of the internal,

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<sup>54</sup>Charles L. Knapp, *Reliance in the Revised Restatement: The Proliferation of Promissory Estoppel*, 81 COLUM. L. REV. 52, 79 (1981). See also Farber & Matheson, *supra* note 8, at 928-2. Professors Farber and Matheson added:

Seen in this light, the cases in which courts have pushed the doctrine of promissory estoppel beyond its stated justification and technical limitations are characterized by a strong need both by the parties and society for a high level of trust. They involve relationships in which one party must depend on the word of the other to engage in socially beneficial reliance. In the employee cases, the socially beneficial reliance takes the form of higher job performance and lower turnover. In subcontracting cases, that reliance takes the form of a more efficient bidding process in which general contractors are able to give bids directly reflecting the information they receive from subcontractors. The point in these cases is not that reliance has taken place in a particular instance, but rather that reliance should be encouraged among participants in a class of activities. To restate our initial observation, the role of reliance in establishing liability and determining damages *in individual cases* is on the decline—but reliance, in the form of trust, is on the rise as the *policy* behind legal rules of promissory obligation.

*Id.*

<sup>55</sup>FARNSWORTH, *supra* note 52, at 95. The plaintiff must show “actual reliance on the promise,” and the “reliance itself must be reasonable.” *Id.*

<sup>56</sup>Feinman, *supra* note 28, at 1386. Trust could perhaps be viewed as the element that addresses a conundrum posed by another commentator. See Randy E. Barnett, *The Richness of Contract Theory*, 97 MICH. L. REV. 1413, 1423-24 (1999).

But the problem for advocates of a “reliance theory” of promissory estoppel has always been distinguishing reasonable, justified, or foreseeable reliance from unreasonable, unjustified, or unforeseeable reliance, for no contracts theorist thinks that any and all detrimental reliance justifies a promissory estoppel claim. In other words, in addition to a promise, the plaintiff needs “reliance [key] something” to get a recovery under any reliance theory of promissory estoppel. Whatever that “something” is, it cannot be reliance, which is present in any event. Thus, all reliance theories of promissory estoppel require appeal to some factor apart from reliance to distinguish enforceable promises (which are accompanied by reliance) from unenforceable ones, and this is an element that reliance theorists have been unsuccessful in identifying.

*Id.*

Perhaps, the optimal amount of trust is the “reliance [key] something”. However, any attempt by this Article, or any other, to exalt the role of trust should heed the following: “Commentators sometimes seem too zealous to find the ‘key’ element of one law or another and seem unwilling to admit how complex the law may be.” Robert A. Hillman, *Questioning the “New Consensus” on Promissory Estoppel: An Empirical and Theoretical Study*, 98 COLUM. L. REV. 580, 619 (1998). It is due to such caution that this Article favors an admittedly modest approach to the treatment of trust.

<sup>57</sup>At one time, there was a school of thought that promissory estoppel did not require a showing of reliance. “Despite the contrary position of leading commentators and both

subjective nature of trust, its existence can not be demonstrated and verified without something more. Trust can only be observed and verified once it objectively manifests itself, and reliance is, of course, the objective manifestation of trust. It is for this reason that it makes sense for the doctrine to focus on reliance. It would have been more surprising if Section 90 had been drafted in terms of trust, rather than reliance, because that would have been inconsistent with the objective theory of contract.<sup>58</sup>

#### V. THE OPTIMAL LEVEL OF PROTECTION OF TRUST

Instead of protecting blind trust, the law should encourage and protect the optimal level of trust.<sup>59</sup> In a persuasive display of sense and realism, Professors Hill and O'Hara stated:

“[A]lthough there are situations where legal policy should work to either maximize or minimize interpersonal trust, in general, the law should seek to *optimize* interpersonal trust. Individuals can be too trusting or not trusting enough. Undertrust results in foregone beneficial opportunities, paranoia, and unnecessary tensions, but overtrust leads to ineffective monitoring, fraud, reduced efficiency and incompetence. As with most problems in life and law, the challenge lies in finding the appropriate balance.<sup>60</sup>

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Restatements, courts do not require actual inducement under Section 90. Nor do they insist that the promisee suffer a detriment by relying on the promise.” Yorio, *supra* note 35, at 152. Their article argued that “the prominence of reliance in the text of Section 90 and in the commentary on the section does not correspond to what courts do in fact. Judges actually enforce promises rather than protect reliance in Section 90 cases.” *Id.* at 111. However, that assertion was quickly rebutted. *See* DeLong, *supra* note 3, at 1003.

Many of the opinions reported in 1995 and 1996 lend support to the thesis that, in order to prevail on a promissory estoppel claim, a commercial promisee must now demonstrate not only that her reliance was reasonable in light of the likelihood that the promisor would perform, but also that she had a reasonable belief that the promise was legally enforceable when made.

*Id.* *See also* Hillman, *supra* note 56, at 580-81.

Contrary to the accepted wisdom, the data and analysis presented here (1) demonstrate that the theory seldom leads to victory in reported decisions, (2) underscore the immense importance of reliance as a substantive element of the theory, and (3) suggest the willingness of courts to grant reliance damages to successful litigants.

*Id.* As a practical matter, it would seem highly unlikely that a plaintiff could survive a responsive pleading like a California demurrer or a Fed. R. Civ. P. 12(b)(6) motion without alleging reliance.

<sup>58</sup>*See* O.W. HOLMES, JR., THE COMMON LAW 324 (Little, Brown, and Company 1881). The law “necessarily ends in external standards not dependent on the actual consciousness of the individual.” *Id.* *See also* FARNSWORTH, *supra* note 52, at 95. “The standard for testing expectation [of reliance] is an objective one, under which the promisor is bound if the promisor had reason to expect reliance, even if the promisor did not in fact expect it.” *Id.*

<sup>59</sup>This is not a universal view. *Compare* Hill & O'Hara, *supra* note 10, at 1719. “Scholars outside of the criminal law typically assert that trust should be maximized.” *Id.*

<sup>60</sup>*Id.* at 1720 (emphasis added).

There is no dispute that promissory estoppel should protect a promisee's trust and resulting reliance, but the more interesting issue is determining the level or amount of trust to protect.

Those who advocate the view that a promise is a promise and that a promisee should be absolutely entitled to trust both the promisor and his promise suffer from an idealistic, perhaps naïve view. People make promises for all sorts of reasons. Some promises are genuine and well-intentioned. Others are fraudulent and designed to deceive. Moreover, many promises are made, then regretted. The regret can be due to miscalculation, imperfect information, misjudgment, or a variety of other reasons. Given that promises are made by imperfect people laboring under imperfect conditions, there should be a role for the law to require the promisee to exercise some judgment and restraint before relying on the promise. Otherwise, the law simply encourages promisees' rash behavior and vulnerability.

Other commentators have recognized the need to impose some sort of burden on promisees to exercise prudence and judgment before trusting the promisor.

[T]he promisee might be aware that the promisor acted foolishly or without deliberation and that he may later regret having made the promise. It may then be unreasonable for the promisee to rely, at least without asking the promisor to do something that shows deliberation such as seeing a lawyer or making delivery.<sup>61</sup>

By ignoring a promisee's duty to guard her own interests, the law creates a moral hazard and encourages undesirable behavior. A promise may be a promise, but those who attach moral significance and consequence to it should acknowledge a corresponding moral duty on the part of promisees to act in a responsible manner (assuming that one wants to view this issue through the lens of morality).

The issue of the promisee's own conduct can also be examined from an angle far removed from morality, the law and economics angle.<sup>62</sup> If the law does not impose

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<sup>61</sup>James Gordley, *Enforcing Promises*, 83 CAL. L. REV. 547, 581 (1995). See also Todd D. Rakoff, *Contracts of Adhesion: An Essay in Reconstruction*, 96 HARV. L. REV. 1173, 1201 (1983). Along similar lines, Professor Rakoff made the following observation in the context of discussing adhesion contracts:

Moreover, even assuming that adherents often do mean to express their trust in the drafting party's good faith, we would still need to be shown that the law should respect that trust. The law cannot unquestioningly uphold one person's trust in another; that would legitimate a great many frauds. Absent the elements of personal knowledge and intimate relationship that might lead us to respect one person's decision to repose rather blind confidence in another, the adherent should be held to the consequences of his "assent" only if there is reason to believe that the drafting party will regularly provide fair and reasonable terms.

*Id.* Excessive protection of trust also generates other types of negative effects. "Legal regulation designed to deter bargaining opportunism could produce another undesirable side effect: encouraging parties who are overly cooperative or naïve to choose careers in business." Shell, *supra* note 23, at 272.

<sup>62</sup>See Juliet P. Kostritsky, *The Rise and Fall of Promissory Estoppel or Is Promissory Estoppel Really as Unsuccessful as Scholars Say It Is: A New Look at the Data*, 37 WAKE FOR. L. REV. 531, 367 (2002). The broad application of law and economics to the doctrine was summed up by this commentator's observation that the "scope of promissory estoppel in Contract and the success or failure of a promissory estoppel claim are determined by a desire



any limits on trust, the result is overreliance on a promise. Although stated in the context of examining expectation damages, the following definition of overreliance is helpful to this analysis: “By *overreliance*, we mean reliance by a promisee that inefficiently disregards the promisor’s rate of breach or, to put it differently, that inefficiently treats the promisor’s performance as insured.”<sup>63</sup> In other words, overreliance is about a promisee relying on a promise without adequately weighing whether the promisor should be trusted. The view that a promise is a promise removes the burden from the promisee to analyze whether the promisor is reliable and trustworthy and/or capable of performance. It encourages trust without analysis and without fear of consequences. Simply put, it encourages promisees to enter transactions they should avoid.<sup>64</sup>

This analysis begins with the following observation:

In non-legal understanding, a promisee’s reliance on a promise can be defined as any choice she makes because of a belief that the promise will be performed under circumstances in which the performance of the promise will be beneficial to her interests or desires. In the paradigmatic case, the promisee will be better off if she relies and the promise is performed, and worse off if she relies and the promise is breached, than she would be if she did not rely at all. Given the uncertainty about whether the promise will be performed, therefore, a promisee who relies on a promise takes a risk in order to obtain a benefit.<sup>65</sup>

The promisee’s position can be described in economic terms.

Reliance is a form of “relation-specific investment.” More specifically, it is any choice, be it action or inaction, which will (1) make S’s [the

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to promote optimal interactions between a promisee and a promisor and to promote efficient reliance.” *Id.*

<sup>63</sup>Melvin A. Eisenberg & Brett H. McDonnell, *Expectation Damages and the Theory of Overreliance*, 54 HASTINGS L.J. 1335, 1339 (2002). Professors Eisenberg and McDonnell made this observation in the context of discussing expectation damages: “The theory is that the expectation measure insures the promisee’s reliance, and therefore may cause the promisee to overrely—that is, to invest more heavily in reliance than efficiency requires.” *Id.* at 1335. See also Richard Craswell, *Offer, Acceptance, and Efficient Reliance*, 48 STAN. L. REV. 481, 494 (1996). On a similar note, Professor Craswell observed: “In some cases, an enforceable commitment on the part of S may create the opposite problem by inducing B to choose *more* than the efficient level of reliance.” *Id.* (emphasis added).

<sup>64</sup>See, e.g., IAN AYRES & GREGORY KLASS, *INSINCERE PROMISES: THE LAW OF MISREPRESENTED INTENT* 64 (2005). This problem was recognized by Professors Ayres and Klass.

The problem of creating the right incentives for optimal investment is a familiar one. It is commonly recognized that perfect expectations damages lead to inefficient promise reliance. The problem is that perfect compensation does not require a promisee to internalize the costs of his behavior, since the promisor will pay those costs if she doesn’t perform. Knowing that he will be fully covered in the case of nonperformance, the promisee has an incentive to underinvest in precautions against nonperformance (since he will be compensated for his losses in the case of breach).

*Id.*

<sup>65</sup>DeLong, *supra* note 3, at 952-53.

promisor's] performance more valuable to B [the promisee] if S does in fact perform, but (2) make B worse off than if he had not relied if S fails to perform. The second element of this definition means that reliance always involves some risk to the relying party.<sup>66</sup>

Professor Craswell added:

Since reliance involves both potential losses and potential gains, the efficient level of reliance—that is, the level of reliance that will maximize the total expected value of the proposed transaction—can be defined by the balance of the potential gains and losses. More specifically, the efficient level of reliance depends on (1) the potential upside from the reliance, or the amount by which the reliance will increase B's gain if S does perform; (2) the potential downside from the reliance, or the amount by which the reliance increases B's losses if S fails to perform; and (3) the probability of each of these two outcomes (i.e., the probability that S will or will not perform). Thus, the efficient level of reliance is determined by a sort of cost-benefit analysis, analogous to the "Learned Hand" test for defining the efficient level of precautions in a negligence case.<sup>67</sup>

To put it another way, this cost-benefit analysis is one approach to calculate the optimal amount of reliance. Whether or not one subscribes to the law and economics view of the world, it informs the analysis in this Article because of its pursuit of optimality.

So, what is the optimal amount of trust that the law should protect? This Article proposes a modest framework in response. The protection of trust should be analyzed along a continuum. One endpoint is defined by the cases where trust deserves maximum protection. This endpoint includes cases where the promisee is engaged in a transaction that she cannot avoid, where she has no control over the structure of the transaction, and where she has no viable choice but to trust the promisor (or at least trust that the promise will be enforced). It also includes cases where the parties have developed a long-standing, pre-existing relationship to the point where the promisee justifiably trusts that the promisor will act in a manner consistent with that relationship. In such situations, the law should fully protect the promisee's trust.

The opposite endpoint is occupied by the cases where trust is misplaced and should not be protected. This endpoint consists of instances involving a promisee who has entered into a transaction that she is not required to enter and where she has a choice as to whether and to what extent she should trust the promisor. As a definitional matter, the type of transaction described would encompass almost every type of business, for-profit transaction. No one is forced to seek a profit, and (typically) business people are not forced to trust the people on the other side of the bargaining table. Admittedly, this is a large subset of transactions, and needs to be further defined to mark the endpoint. Trust should not be protected if: (1) the promisee could have determined that the promisor was untrustworthy at a low cost to the promisee; or (2) if the promisee could have avoided the harm resulting from a

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<sup>66</sup>Craswell, *supra* note 63, at 490.

<sup>67</sup>*Id.* at 491.

broken promise by taking preventive measures that cost less than the amount of the harm. Admittedly, there will be a large gray area separating the endpoints, and most cases that arise are probably located in this area. Nonetheless, the setting of boundaries for the analysis through the use of these endpoints may be helpful.

#### VI. THE ENDPOINT DEFINING MAXIMUM PROTECTION OF TRUST

Two types of cases present what can be viewed as easy situations for the protection of trust. The first type of case involves situations where the promisee is engaged in a transaction that she cannot avoid, where she has no control over the structure of the transaction, and where she has no viable choice but to trust the promisor (or at least trust that the promise will be enforced). The case of *Ames v. Employers Casualty Co.*<sup>68</sup> illustrates this principle. The second type of situation is where the parties have developed a long-standing, pre-existing relationship to the point where the promisee has developed a reasonable basis to trust that the promisor will act in a manner consistent with that relationship. The case of *D & G Stout, Inc. v. Bacardi Imports, Inc.*<sup>69</sup> illustrates this second principle.

##### A. *Ames v. Employers Casualty Co.*

In *Ames*, the defendant was an insurance company that issued automobile liability policies. Its insured was a J.W. Heldoorn who was covered under a policy that included liability insurance in favor of any person injured through the use of Heldoorn's automobile. Heldoorn collided with another automobile in which plaintiff Frank Ames was a passenger. Ames, who was injured in the accident, sued Heldoorn and won a judgment against him. The defendant insurance company refused to cover the loss on the ground that Heldoorn was driving the automobile for his personal use (which was allegedly not covered), as opposed to a business use (which was covered). Heldoorn asserted that the defendant's agent had represented that he was covered for all uses of his automobile. Heldoorn won in the trial court, and the Court of Appeal affirmed. It stated, "But where, as here, the insurer makes a promise to write a certain specific coverage, the insured is entitled to rely thereon and the insurer is estopped from taking a different position."<sup>70</sup>

Protection of trust and reliance is justifiable in these types of situations. Anyone who owns an automobile is required by law to have a liability policy.<sup>71</sup> The insured has no choice but to enter into a transaction with an insurance company; it is consensual only because the insured has the choice of selecting from more than one insurer. The insurer also occupies a superior position of knowledge and bargaining (as evidenced by the prevailing use of adhesion contracts to bind consumers). In the universe of consensual transactions, the promisee is at her most vulnerable in these types of situations. She should be entitled to trust the promisor or trust the enforcement mechanism, and that trust should be protected by law.

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<sup>68</sup>60 P.2d 347, 352 (Cal. Dist. Ct. App. 1936).

<sup>69</sup>*D & G Stout, Inc. v. Bacardi Imps, Inc.*, 805 F. Supp. 1434 (N.D. Ind. 1992).

<sup>70</sup>*Ames*, 60 P.2d at 352.

<sup>71</sup>This Article does not represent that automobile insurance was mandatory in California at the time of Mr. Heldoorn's accident. The material point is that such insurance is mandatory today.

*B. Prudential Insurance Co. of America v. Clark*

If *Ames* defines part of the endpoint, the case of *Prudential Insurance Co. of America v. Clark*<sup>72</sup> lies just next to it. In that case, Steve Clark was a young Marine who was killed in Vietnam when his helicopter crashed. Before he was deployed, Clark purchased a life insurance policy issued by a Prudential competitor, which policy had no war risk or aviation exclusion clauses. Prudential's agent contacted Clark and urged him to drop the competitor's policy and purchase a Prudential policy instead. The agent represented that Prudential would issue the same type of coverage. In reliance on the agent, Clark dropped his existing coverage and purchased a Prudential policy. However, Prudential issued a policy that excluded coverage for death as a result of war or aviation accidents. Clark had no opportunity to correct the mistake because he was in Vietnam.

Clark's parents submitted a claim under the Prudential policy. Notwithstanding the exclusions, Prudential paid out \$10,000 pursuant to the policy. After Clark's parents received the money, Prudential realized its mistake and demanded the return of the money on the grounds that Clark's death was not covered under the policy. When the parents refused, Prudential sued them. The Fifth Circuit ruled against Prudential and allowed the parents to keep the money. In its decision, the court recognized the applicability of promissory estoppel to the parents' defense.

[Promissory estoppel] requires affirmative action indicative of a desire to be contractually bound. In the case at bar, that affirmative action manifested itself when the agent, Brumell, promised to obtain a policy without the exclusion clauses and thereby induced Steve to drop his other policy in reliance upon that promise.<sup>73</sup>

For purposes of the present analysis, the major difference between *Ames* and *Clark* is that, unlike automobile insurance, no one is required to purchase life insurance. Nevertheless, the fact remains that the insured occupies the weak and vulnerable position when dealing with insurers, and the need of the weak and powerless to trust the stronger party and/or the enforcement mechanism should be protected. Clark trusted Prudential's agent to arrange the agreed upon policy. Promissory estoppel protected this trust.

*C. Drennan v. Star Paving Co.*

If one accepts cases like *Ames* and *Clark* as marking the endpoint where trust should be protected, a case like *Drennan v. Star Paving Co.*<sup>74</sup> can be analyzed to determine where it lies along the continuum. Under this analysis, it occupies a point closer to the midpoint of the continuum but still within the half of the continuum where trust should be protected. The defendant subcontractor submitted a bid in the amount of \$7,131.60 for paving work to the plaintiff general contractor. The plaintiff relied on this bid in preparing his own bid for work on a school project, and was awarded the contract. Afterward, the defendant told the plaintiff that it had

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<sup>72</sup>*Prudential Ins. Co. of Am. v. Clark*, 456 F.2d 932 (5th Cir. 1972).

<sup>73</sup>*Id.* at 936.

<sup>74</sup>*Drennan v. Star Paving Co.*, 333 P.2d 757 (Cal. 1958).

made a mistake in computing its bid for the subcontract and that it could not do the work for less than \$15,000.

Justice Traynor's opinion upheld the right of the general contractor to rely on the subcontractor's bid, and cited Section 90 to support the Court's ruling.

Plaintiff testified that it was customary in that area for general contractors to receive the bids of subcontractors by telephone on the day set for bidding and to rely on them in computing their own bids. Thus on that day plaintiff's secretary, Mrs. Johnson, received by telephone between fifty and seventy-five subcontractors' bids for various parts of the school job. As each bid came in, she wrote it on a special form, which she brought into plaintiff's office. He then posted it on a master cost sheet setting forth the names and bids of all subcontractors. His own bid had to include the names of subcontractors who were to perform one-half of one per cent or more of the construction work, and he had also to provide a bidder's bond of ten per cent of his total bid of \$317,385 as a guarantee that he would enter the contract if awarded the work.

Late in the afternoon, Mrs. Johnson had a telephone conversation with Kenneth R. Hoon, an estimator for defendant. He gave his name and telephone number and stated that he was bidding for defendant for the paving work at the Monte Vista School according to plans and specifications and that his bid was \$7,131.60. At Mrs. Johnson's request he repeated his bid. Plaintiff listened to the bid over an extension telephone in his office and posted it on the master sheet after receiving the bid form from Mrs. Johnson. Defendant's was the lowest bid for the paving.<sup>75</sup>

These facts are significant because the business practice forced the general contractor to trust and rely on the subcontractor's bid. Given the nature of the bidding process and the relationship between general contractors and subcontractors, there was no realistic alternative business practice for the parties. Either the parties conducted themselves in the described manner or the parties did not do business at all. In this sense, a general contractor and the subcontractors are roughly analogous to an insured and her insurer. The circumstances and structure of the transaction force the promisee to trust the promisor. Under such circumstances, the trust should be protected.

*D. D & G Stout, Inc. v. Bacardi Imports, Inc.*

A second type of situation where trust should be protected is where the parties have developed a long-standing, pre-existing relationship to the point where the promisee has developed a reasonable basis to trust that the promisor will act in a manner consistent with that relationship.<sup>76</sup> In *D & G Stout, Inc. v. Bacardi Imports*,

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<sup>75</sup>*Id.* at 758.

<sup>76</sup>See Farber & Matheson, *supra* note 8, at 925. This point is consistent with the following observation by Professors Farber and Matheson:

Two factors appear to coalesce in cases in which promissory obligation has been expanded beyond its traditional boundaries. First, as suggested above, the promisor's primary motive for making the promise is typically to obtain an economic benefit.

*Inc.*,<sup>77</sup> the plaintiff was a wholesale distributor of liquor in Indiana. At the start of 1987, plaintiff was a distributor for four major suppliers including Bacardi Imports, Inc., the defendant (“Bacardi”). As the year progressed, however, the plaintiff’s future as a profitable business was placed in doubt when two of its major suppliers terminated their relationship with the plaintiff (for reasons unrelated to performance). This left the plaintiff with only two major suppliers (Bacardi and Hiram Walker) and one minor supplier (Canandagua). Due to the loss of the major suppliers, the plaintiff was forced to evaluate a variety of options, including going out of business. It determined, however, that it could remain a profitable business if it could retain its three remaining suppliers, and downsize its operations. It also concluded that it would be forced out of business if it lost another supplier. Given this precarious situation, the plaintiff sought verbal commitments of its relationships with its suppliers, and obtained such commitments from Hiram Walker and Canandagua.<sup>78</sup>

On July 9, 1987, plaintiff attended a meeting with several Bacardi representatives to discuss a variety of topics. Bacardi had its own concerns about the plaintiff’s continuing viability, and inquired into the plaintiff’s condition and prospects. The plaintiff told Bacardi that it could stay in business as long as it maintained its three remaining suppliers, and sought Bacardi’s assurance that Bacardi would remain a supplier. The plaintiff made clear that Bacardi’s continued business was necessary for the plaintiff’s future. Bacardi’s vice-president of marketing responded by telling the plaintiff not to worry. He assured the plaintiff that if it continued to meet Bacardi’s sales expectations and if there were no changes in market conditions, plaintiff would remain a Bacardi distributor.<sup>79</sup>

After this meeting, the plaintiff nonetheless pursued negotiations with another distributor regarding the sale of all of its assets to the other distributor. By the end of July, however, the plaintiff decided to remain in business for itself, based on its belief that Bacardi would remain a supplier. Bacardi, on the other hand, continued to harbor doubts about the plaintiff’s viability. On July 30, Bacardi informed the plaintiff that their relationship would terminate at the end of the year. Realizing that it could not remain in business, the plaintiff revived the negotiations with the other distributor for the sale of its assets. But given the dramatic change in circumstances, the plaintiff lost whatever leverage it had in prior negotiations. As a result, the plaintiff sold its assets for \$1.956 million in August. If it had concluded the negotiations in July, it would have received \$3.109 million.<sup>80</sup>

The plaintiff sued Bacardi under a theory of promissory estoppel, and won. The basic fact of the case was that “Bacardi simply changed its mind, and [the plaintiff]

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Second, the enforced promises generally occur in the context of a relationship that is or is expected to be ongoing rather than in the context of a discrete transaction. These relationships are characterized by a need for a high level of mutual confidence and trust.

*Id.*

<sup>77</sup>D & G Stout, Inc. v. Bacardi Imps, Inc., 805 F. Supp. 1434 (N.D. Ind. 1992).

<sup>78</sup>*Id.* at 1437-38.

<sup>79</sup>*Id.* at 1438-39.

<sup>80</sup>*Id.* at 1439-44.

was not unreasonable in failing to anticipate that.”<sup>81</sup> The crucial part of the court’s decision was the following:

As emphasized throughout the trial, the liquor distribution business traditionally had operated on an informal basis. Long term relationships were formed based on nothing more than a handshake. Bacardi and [the plaintiff] had done business in this environment for years to the satisfaction of both, making it all the more reasonable for Bacardi to have expected [the plaintiff] to rely on Bacardi’s word, and for [the plaintiff] to actually rely on it. By 1987, the market was in the midst of a wholesale change, not only in terms of the number of players and the names of those players, but in the way in which business was done. Nothing in the changes sweeping the liquor market, however, suggested that the old rules were out the window, particularly with respect to a relationship of such long standing.<sup>82</sup>

The plaintiff trusted Bacardi, and made a crucial business decision based on that trust. Given the long-standing relationship between the parties and the nature of their dealings with each other over time, the plaintiff had reasonably developed a trust in Bacardi. Under such circumstances, trust should be protected.

*Bacardi* did not involve a rash decision based on an isolated encounter. The parties’ relationship and expectations developed over years, in accordance with the common practice of their industry. This is the way trust between contracting parties should develop, and trust developed in this manner deserves maximum legal protection.

#### VII. THE ENDPOINT WHERE TRUST SHOULD NOT BE PROTECTED

At the opposite end of the spectrum lie the cases where trust should not be protected, and indeed should be discouraged. The challenge here is to identify the criteria for such cases. To this end, the discussion will turn to what may be the most wrongly decided promissory estoppel case ever (in this author’s opinion, of course): *Universal Computer Systems, Inc. v. Medical Services Ass’n of Pennsylvania*.<sup>83</sup>

##### A. *Universal Computer Systems, Inc. v. Medical Services Ass’n of Pennsylvania*.

In July 1975, the defendant Medical Services Association of Pennsylvania (referred to as “Blue Shield” in the opinion) solicited bids for the lease of a computer. Plaintiff Universal Computer Systems, Inc. (“Universal”) prepared a bid proposal. Blue Shield was located in Camp Hill, Pennsylvania, which is approximately 3.5 miles from Harrisburg. Universal was located in Westport, Connecticut. The solicitation required that bids be received by Blue Shield no later than noon on Monday, August 18, 1975 at Harrisburg. Joel Gebert, a Blue Shield employee, served as the liaison between Blue Shield and all prospective bidders. On or about August 15, the president of Universal, Warren Wilson, called Gebert to tell

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<sup>81</sup>*Id.* at 1449.

<sup>82</sup>*Id.* at 1451.

<sup>83</sup>*Universal Computer Sys. v. Med. Servs. Ass’n of Pa.*, 628 F.2d 820 (3d Cir. 1980), *reversing* *Universal Computer Sys, Inc. v. Med. Servs. Ass’n of Pa.*, 474 F.Supp. 472 (M.D. Pa. 1979).

him that Universal would be sending a bid on an Allegheny Airlines flight to Harrisburg. He asked if Gebert could arrange for someone to pick up the bid at the Harrisburg airport on Monday morning. Gebert assured Wilson that the bid would be picked up and brought to Blue Shield by the deadline. On the 18th of August, Universal dispatched its bid, and Wilson called Gebert again that morning to give him further information. Gebert, however, informed Wilson that he had changed his mind and that the bid would not be picked up at the airport. Universal was unable to make alternative, timely arrangements for delivery of its bid to Blue Shield. Blue Shield rejected the bid as untimely.<sup>84</sup>

Universal sued Blue Shield and the jury returned a verdict in the amount of \$13,000 against Blue Shield. The jury found that Universal would have won the contract if its bid had been timely, and the amount represented Universal's lost profits under the contract. The trial court granted Blue Shield's motion for judgment *non obstante veredicto*, and Universal appealed. The appellate court reversed the order granting j.n.o.v. and remanded the case with directions to reinstate the jury's verdict. In so ruling, the Third Circuit held that Universal had established its right to recovery under promissory estoppel.<sup>85</sup> "Here it is clear that plaintiff incurred a substantial detriment as a result of relying upon defendant's promise. Plaintiff has suffered an injustice in being deprived of the service promised by Blue Shield's employee, Gebert."<sup>86</sup>

At its core, this case is about the fact that Universal's agent trusted Blue Shield's agent. The existence of trust and reliance is undisputed. The Third Circuit chose to protect this trust (even though the trial judge thought it did not deserve protection).<sup>87</sup> But why did this trust deserve protection? Should it have deserved protection? And what does this case say to anyone else in Universal's position? This Article submits that the case was wrongly decided. The trust should not have been protected. The Third Circuit should have gone the other way to explicitly discourage trust in this type of situation.

A key fact should be noted. There is nothing in the record to show or even suggest that there were ever any prior dealings between Wilson and Gebert, or Blue Shield and Universal. The only fair reading of the case leads to the conclusion that Wilson and Gebert spoke for the first time ever on August 15, 1975, and that this was the first time Blue Shield and Universal had attempted to do business with each other. In other words, the two people and the two businesses involved were complete strangers to one another prior to August 15. Moreover, there is no answer in either the appellate or trial court opinion to any of the following questions: What did Wilson know about Gebert's personal trustworthiness? What did Wilson know about Gebert's personal ability to arrange the pick-up? What did Wilson know about Gebert's authority or power within Blue Shield to arrange or order the pick-up? What did Wilson know about Gebert's work demands that might interfere with Gebert's ability to arrange the pick-up? Because none of these factual issues is addressed in the two opinions, a reasonable inference is that these facts were either

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<sup>84</sup> *Universal Computer Sys.*, 628 F.2d at 822.

<sup>85</sup> *Id.* at 825.

<sup>86</sup> *Id.*

<sup>87</sup> *Id.*



not developed in discovery or not presented at trial. Despite the stated and missing facts, the Third Circuit held that Wilson acted reasonably in trusting Gebert.<sup>88</sup> Should the law encourage people to trust complete strangers?

For those who would cite a moral prescription or societal benefits to justify the Third Circuit's decision, there are equal or more compelling reasons based on the same grounds to reach the opposite conclusion. Trust should be the product of care and deliberation. It is difficult to identify the moral or societal justifications for the protection of casual encounters with strangers.<sup>89</sup>

From the framework of an economic analysis approach, the *Universal Computer* decision is difficult to justify. The quantitative downside to Universal's trust was \$13,000, the amount of the lost profits from the contract.<sup>90</sup> This amount merits examination in some context. How much would it have cost Universal to avoid this loss? The facts of the case state that the bid was placed on an 8:30 a.m. flight from LaGuardia to Harrisburg. Suppose Universal had arranged for a paralegal (say, from one of its local law firms) to start the day at 7:00 a.m. Starting at that time, the paralegal could proceed with package to the airport, fly to Harrisburg, deliver the bid, and return to New York by 5:00 p.m. That would represent a total of 10 hours of paralegal billable time. Additional costs would include the cost of airfare and local transportation. In 1975, a paralegal might have been billed at \$25 per hour (as a very rough estimate), and the roundtrip airfare might have cost \$250. Add in a generous \$50 for local transportation, and the total cost of delivery of the bid might have been roughly \$550. For \$550, Universal could have avoided a \$13,000 loss.<sup>91</sup>

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<sup>88</sup>*Id.* at 824. It also clear from the record that it was not the usual business practice for bids to be handled in the manner described. The trial court's opinion emphasized the fact that the bidding process was governed by federal procurement regulations, and that such regulations prohibited any preference or favoritism in the process. The trial court ruled that picking up the bid at the airport would have violated the regulations. It also held that Universal knew or should have known about the regulations, and concluded that Universal's reliance was unjustified. The Third Circuit, however, disagreed, and ruled that it was error for the trial court to rule that Universal should have been aware of the regulations.

Quite apart from the legal effect of the regulations, the Third Circuit's decision can be viewed as an encouragement of the type of business conduct described. It is another matter entirely, though, whether any such conduct should be encouraged. Based on a lengthy career in the world of big law firm practice, the author would guess that any junior lawyer who missed a deadline by trusting someone other than the firm's hired agent to file a document in court or with a regulatory agency would quickly find himself or herself unemployed.

<sup>89</sup>And what about Gebert? Critics of this Article may argue that Gebert's perfidy should be punished. To those who are quick to conclude that there was bad faith in Gebert's conduct, it is equally plausible that Gebert was simply trying to be an accommodating, nice guy to a stranger asking for a favor. Unfortunately, he had committed himself to do something that he was unable to do (possibly for reasons out of his control). Gebert may be a living example of the maxim, "No good deed goes unpunished."

<sup>90</sup>*Universal Computer Sys.*, 628 F.2d at 825.

<sup>91</sup>This hypothetical utilizes a paralegal to contrast it with the fact that Universal ultimately resorted to a law firm after the damage had been done. The point is to illustrate that an ounce of prevention is worth a pound of cure.

Instead of approaching it this way, the Third Circuit said it was right for Universal to trust a stranger, take the risk of a \$13,000 loss, hire a lawyer to seek recovery, and then bear the uncertainties of litigation and trial, when Universal could have avoided the whole mess for about \$550. Economic efficiency analysis under the law and economics approach may not provide the answer to every legal problem, but it certainly suggests a compelling result here.

For those who favor this kind of analysis, it suggests a formula to evaluate promissory estoppel cases. Where the cost of self-reliance or self-protection is less than the potential quantitative downside resulting from misplaced trust, the law perhaps should not protect trust and instead encourage self-reliance.<sup>92</sup> Going back to the *Universal* case, suppose it would have cost Universal \$13,000 to arrange delivery of its bid to Harrisburg. Under those hypothetical facts, it is at least understandable (from an economics point of view) why Universal would trust Blue Shield to take care of the delivery. This formula could also explain (in part) cases like *Ames*, *Clark* and *D & G Stout*. In each of those cases, the promisee was in no position to engage in self-reliance. The promisees in those cases were at the mercy of their promisors. Given those circumstances, the cost of their self-reliance would be closer to infinity rather than to zero, and therefore the cost of self-reliance or self-protection greatly exceeded the potential downside.<sup>93</sup>

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<sup>92</sup>A similar approach was proposed by Professor Gordley, who wrote:

A second thesis of this Article is that courts enforce such promises because they can be performed without significant cost to the promisor. . . . [T]hese promises raise neither the fear that the promisor acted foolishly to his detriment, nor that the exchange was unfair. Moreover, the enforcement of these promises is desirable because, nearly always, while the promisor can confer the benefit at a negligible cost, the promisee either cannot obtain the benefit otherwise or can do so only at a significantly greater cost.

Gordley, *supra* note 61, at 582.

Also along somewhat similar lines, Professor Katz proposed:

In the foregoing examples, my suggested rule of thumb generally implies holding large, informed, wealthy repeat players to their precontractual offers and representations, while excusing small, uninformed, liquidity-constrained novices from theirs. This favoring of weak parties over strong ones comports with the traditional norms of equity out of which the estoppel doctrine originally grew and may for some readers seem appealing for that reason. It is important to remember, however, that my analysis here is not focused on distributional fairness, but on allocative efficiency. Whether or not it is fairer to favor weak parties over strong ones, it is necessary to do so in order to give the weak appropriate incentives to make reliance investments—investments that increase the social value of exchange for strong and weak alike. It is in the private interests of the strong to enter into contractual arrangements whereby they bind themselves not to use their bargaining power to expropriate the investments of the weak. Who is strong and who is weak, however, and whose investment incentives need protection, may be a matter for individualized and decentralized determination.

Avery Katz, *When Should an Offer Stick? The Economics of Promissory Estoppel in Preliminary Negotiations*, 105 YALE L.J. 1249, 1302 (1996).

<sup>93</sup>Any *ex ante* use of this formulation may require the amount of potential downside to be adjusted by the probability of the loss occurring so that amount of potential downside represents an expected value. If, for example, there had been a fifty-fifty chance that Blue Shield would not pick up the Universal delivery, the potential downside would equal .5 x

In other words, there are some transactions where the cost of self-protection or self-reliance is so high that it is not economically feasible to engage in such measures. In such circumstances, there are only two choices—avoid the transaction or trust. This stark, “either/or” choice demonstrates why seeking the optimum level of trust protection should be the aim of the law. The law should not encourage or protect ill-advised behavior or poor judgment, but the law also should not stifle beneficial activity. If the law does not protect the optimal level of trust, the set of avoided transactions will certainly include transactions that would have otherwise benefited the promisee and society as a whole. This is the reason why trust should be protected where self-reliance or self-protection exceeds the potential downside.<sup>94</sup>

The utility of this formulation lies in its analysis of the enforceability of promises through the prism of the promisee’s calculations.<sup>95</sup> Such an approach makes sense as

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\$13,000 or \$6,500, which would still be significantly greater than the \$550 cost of self-reliance. Even if the risk of Blue Shield’s failure had been an unrealistically low 10%, the potential downside would have equaled .1 x \$13,000 or \$1,300. Thus, even if Universal could have counted on a 90% chance of reliability, it still would have made more sense to arrange for its own delivery (and it is baffling why anyone would assign such a high probability of reliability to a complete stranger).

<sup>94</sup>This need for the protection of trust was recognized by one commentator who wrote: Courts seem more willing to apply promissory estoppel where significant barriers prevent the negotiation of an explicitly reciprocal contract because, in such cases, permitting an estoppel claim may be the most efficient means of fostering reliance and increasing gains from trade. It seems appropriate to apply promissory estoppel when private bargains may be unlikely to arise and yet it would seem optimal for the reliance to be protected.

Kostritsky, *supra* note 62, at 577-78.

<sup>95</sup>Other commentators have engaged in compelling economic analyses of the enforcement issue by focusing on the promisor. For example, Prof. DeLong wrote: “Rational commercial promisors will make non-bargain promises only when their expected benefit from the promisee’s anticipated reliance exceeds the expected cost of making the promise, including the expected cost of performance and any potential liability for breach.” DeLong, *supra* note 3, at 952.

In fact, the scholarship on promissory estoppel seems to have been marked by pendulum-type swings from articles focusing on the promisor to articles focusing on the promisee, with the Farber and Matheson article representing a high point of promisor-focused scholarship. The following passage evidences another example.

The critical and difficult question about Section 90 in the courts is not whether to protect reliance, but whether to enforce the promise at issue. It is neither sufficient nor necessary that the promise induce the promisee to rely to her detriment. Every promise may influence the promisee’s behavior, and yet not every relied-upon promise is enforceable. What distinguishes enforceable from unenforceable promises is the quality of the commitment made by the promisor.

Yorio, *supra* note 35, at 162. Professors Yorio and Thel continued:

Courts enforce promises under Section 90 when they view the promises as serious and deserving of enforcement *qua* promise; they do not enforce them out of solicitude for promisees. The promisor’s commitment may be shown to be sufficiently serious by her contemplation of particular and substantial reliance, by the formality of the promise, by the situation of the promisee, or by a chance of benefit to the promisor. The importance to courts of promise explains why the remedy for breach of a Section 90 promise is invariably expectancy relief (if measurable); why the absence of

a matter of economic analysis. “[B]ecause a promisee can control reliance costs more easily than can a promisor, the risk of detrimental reliance is lower if borne by the promisee rather than the promisor.”<sup>96</sup>

This type of cost-benefit analysis also suggests an alternative way to view Universal’s decision. This alternative confirms that Universal made a rational business decision by trusting Blue Shield, but still leads to the conclusion that the Third Circuit was wrong. Under this analysis, Universal may have made the following calculation: The potential profit from the contract is \$13,000, but the chance of winning the bid is only 5% so the expected value is \$650. It will cost about \$550 to arrange for delivery, but that will almost wipe out the expected value of winning. At that point, it almost makes no sense to bid. That cost, however, can be eliminated by trusting and relying on Blue Shield to pick up the bid at the airport.

If this thinking reflects the decision-making process, it would have been a perfectly rational decision for Universal to trust Blue Shield. It is difficult to criticize that business judgment. The economy looks to business executives to make those sorts of decisions. However, it is one thing to recognize a good business decision, but it is another thing entirely for the state to guarantee the desired result if events do not turn out as planned. Universal may have made a perfectly sound judgment, but things do not always turn out well. The risk of the downside is always present, and a major part of any business executive’s job is risk management. Despite best efforts and best-laid plans, things happen and the downside becomes real. But that is business, and the state does not ordinarily intercede to unwind the loss after things go bad. However, that is exactly what the Third Circuit did. The Third Circuit exercised its power to save Universal from a business decision that did not turn out as hoped.<sup>97</sup>

It should be noted that this Article’s view of the *Universal* case is not shared by others. In particular, the Farber and Matheson article points to this case as an

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inducement and detriment is irrelevant; why some promises are not enforced despite detrimental reliance; and why the outcome (in terms of both liability and remedy) generally turns on some aspect of promise.

*Id.* at 166.

<sup>96</sup>Goetz, *supra* note 48, at 1295.

Critics may point out that the proposed formulation only takes into account the potential downside of trust and fails to incorporate the potential upside. It fails to do so because it is a natural and universal tendency for promisees to incorporate the potential upside into their analyses. The problem seems to be a reluctance to consider the downside risks. The point is that promisees will only trust and rely if the cost to do so is less than the potential upside. This calculation is so obvious and embedded that most promisees probably engage in this calculation at an almost subconscious level. Focusing on downside and risk, on the other hand, probably comes less naturally, and that is why the formulation focuses on that aspect of trust.

<sup>97</sup>This point is not intended to provoke a political debate with those who may favor strong state involvement and intervention in the market. But even those who disagree with this Article’s point of view would probably agree that the doctrine of promissory estoppel is probably not the ideal mechanism to achieve their goals.

exemplar of correct promissory estoppel analysis.<sup>98</sup> There is obviously considerable room for disagreement over the wisdom of the decision.<sup>99</sup>

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<sup>98</sup>Farber & Matheson, *supra* note 8, at 930-932. That article proposed a hypothetical Restatement (Third) of Contracts, complete with comment and illustrations. It proposed a new Section 71A:

§ 71. Enforceability of Commercial Promises

A promise is enforceable when made in furtherance of an economic activity.

Comment:

a. *Rationale and relation to other rules.* This section deals with what has traditionally been called consideration—namely, the legal conclusion that a promise is enforceable. Prior rules tested every promise or modification to determine whether the promise was conditioned on some tangible bargained-for exchange. The present section eliminates the need for finding a specific bargained-for promise or performance for each promise or modification. Rather, the key determination is whether the promise is designed to induce the creation of or to aid in the continuation of economic activity. The rule posits the social and economic utility of promises made in furtherance of economic activity.

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Illustrations:

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4. Corporation A prepared a bid for leasing a computer to Corporation B. A was running behind schedule and asked an agent of B to pick up the bid at the airport. The agent, after agreeing to pick up the bid, declined to do so and the bid arrived too late for consideration. Assuming the agent acted within his actual or apparent authority, B is bound by the agent's representation. If A can show that it would have been awarded the lease, it can recover lost profits."

*Id.* Illustration 4 is, of course, based on the *Universal* case. *See id.* at 932 n.103.

<sup>99</sup>The reasoning underlying the Farber and Matheson article's approval of the *Universal* case and the role of the courts in protecting trust is reflected in the work of other leading scholars. For example, Professor Hillman proposed the following hypothetical problem and solution.

Problem 3: MDM Enterprises produces the television series "Why Spy?" for XYZ Television Network and later begins negotiations with XYZ for the production of a spin-off series, "Journey." The parties tentatively agree on a licensing fee of \$750,000 per episode for twenty-two episodes of the new series. They discuss a five-year license, with the network to have the right to cancel at any time. They also discuss a ten percent escalation of the licensing fee over the five-year period. Before signing any documents or reaching a final agreement on any terms, the network offers MDM \$1.5 million to produce two episodes of "Journey." Without accepting XYZ's offer, MDM produces the episodes at a cost of \$1 million. Thereafter, negotiations over the full deal break down. MDM seeks \$1.5 million in compensation when no other network shows interest in the new series.

We will see in Problem 3 that MDM may recover under the doctrine of promissory estoppel even though MDM and XYZ have not signed a contract for the production of "Journey," and MDM did not formally accept XYZ's offer to purchase two episodes of the series.

The problem with *Universal* is that the court, in effect, made Blue Shield the guarantors of Universal's success even though Blue Shield received nothing in return and even though Universal could have protected itself at minimal cost. This was certainly a case of court-enforced "overinsurance" as described by Professors Goetz and Scott, who wrote: "Legally mandated 'overinsurance' induces a moral hazard because the promisee will not exercise optimal self-protection."<sup>100</sup> The court further ignored the following principles:

Whatever the reasons for the riskiness attached to the performance prospects of any promise, the promisee can protect himself against prospective losses from detrimental reliance by limiting his behavior adjustments. In practice, the attempt to do this is frequently manifested in intermediate courses of action taken by promisees who do not completely ignore the implications of a promise in their planning but do not react as fully as if performance were certain.<sup>101</sup>

Universal was a sophisticated party that could (and should) have protected itself. Yet, the court ignored that reality.

*B. Hoffman v. Red Owl Stores, Inc.*

The issue of overreliance and ill-considered conduct on the part of promisees can be further developed by an examination of one of the best known promissory estoppel cases, *Hoffman v. Red Owl Stores, Inc.*<sup>102</sup> Joseph Hoffman wanted to acquire a Red Owl grocery store franchise. Red Owl assured him that he would be granted one if he took certain steps to gain experience in the business and if he invested \$18,000 into the franchise. Over the course of more than two years, Hoffman relied on Red Owl's assurances by selling his bakery, and by buying, operating and then selling a smaller grocery store in another town to gain experience. After all this, Red Owl increased the required \$18,000 investment amount to \$24,100, increased it again to \$26,000, and increased it yet again to \$34,000. Hoffman was unable to come up with the increased amount, and Red Owl never granted him a franchise. Hoffman sued and won on a promissory estoppel theory.

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ROBERT A. HILLMAN, THE RICHNESS OF CONTRACT LAW: AN ANALYSIS AND CRITIQUE OF CONTEMPORARY THEORIES OF CONTRACT LAW 48-49 (1997).

The issue here is why should the courts protect MDM's decision? Under the terms of the hypothetical, it appears that MDM made a business decision to proceed with the production of "Journey" without a contract in hand. The motivation for the decision would likely be a desire to test the market to see if there are higher bidders for the project, with assumption of the risk that nothing turns up. When things do not turn out well for MDM, why should the court protect it from the consequences of its decision? Moreover, by asserting promissory estoppel, MDM converted XYZ's offer into an irrevocable option even though that was never XYZ's intent (with MDM using the option period to shop its project around town). This does not appear to be a simple matter of trust and reliance by the promisee. Rather, it looks like opportunistic conduct by MDM.

<sup>100</sup>Goetz, *supra* note 48, at 1285.

<sup>101</sup>*Id.* at 1270.

<sup>102</sup>*Hoffman v. Red Owl Stores, Inc.*, 133 N.W.2d 267 (1965).

The innocent, blameless victim of a broken promise prevailed. This is the accepted story.

However, a recent re-examination of *Hoffman v. Red Owl* requires a fundamental re-thinking of the case.<sup>103</sup> According to Professor Scott, the key to understanding the actual events in that case lies in Hoffman's statement that he had \$18,000 in cash to invest in the franchise.<sup>104</sup> Hoffman alleged that Red Owl assured him that was all he would need to invest. The real story emerges through the following questions:

What was the understanding as to the composition of the \$18,000? Was it supposed to be all equity, or was it to be cash composed of some equity and some debt? If the latter, from what sources was Hoffman to obtain his encumbered cash? Finally, how reasonable was Red Owl's reaction to the changing sources of Hoffman's prospective \$18,000 contribution as he moved his assets around between September 1961 and January of 1962?<sup>105</sup>

It turns out that Hoffman was unable to answer these questions, and that is where the problem was. Hoffman assumed that his \$18,000 contribution could be composed of equity and borrowed cash, but Red Owl was looking for a pure equity contribution.<sup>106</sup> The basic problem was that Red Owl was focused on the amount of pure equity, while Hoffman was focused on the amount of cash he would need regardless of whether it was borrowed or not. In fact, a substantial portion of Hoffman's cash was borrowed, and this explains why Red Owl's required contribution changed.<sup>107</sup> When it realized that Hoffman was looking to invest borrowed cash, Red Owl had to change the structure of the transaction to ensure that the level of equity contribution remained the same. In other words, the crucial number in Red Owl's eyes – the amount of pure equity – remained substantially unchanged throughout the negotiations.

At a basic level, Hoffman did not understand the transaction he was trying to negotiate. So, whose fault is that? Some might be quick to blame the big, heartless corporation who took advantage of the weaker party. This makes no sense, however. Hoffman initiated contact with Red Owl, not the other way around. Plus, what possible benefit did Red Owl gain by not granting the franchise? Some might also argue that Red Owl had some sort of duty or obligation to better inform Hoffman of what was required. However, the law of Contracts does not require a party to educate or provide business schooling to the person on the other side of the table.

Hoffman apparently trusted and relied on the various Red Owl representatives with whom he dealt. But on what was his trust based? It appears to have been based, in large part, on his own misunderstandings regarding the deal he sought. With this new re-examination, it appears that Hoffman bears a great deal of the responsibility for the failed outcome of his efforts. Therefore, the *Hoffman* case may not be a shining example of the doctrine of promissory estoppel.

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<sup>103</sup>See Robert E. Scott, *Hoffman v. Red Owl Stores and the Myth of Precontractual Reliance*, 68 OHIO ST. L.J. 71 (2007).

<sup>104</sup>*Id.*

<sup>105</sup>*Id.* at 75.

<sup>106</sup>*Id.*

<sup>107</sup>*Id.*

Referring back to the continuum along which trust should be enforced, it appears that the *Hoffman* case lies closer to the *Universal* case and that the court should not have protected Hoffman's trust and reliance. Should the law protect those who develop their trust based on their own misjudgments and poor information? If the law were to do so, it would certainly remove incentives to form better judgments and obtain better information. That would hardly improve moral posture or advance societal goals. With regard to the formula comparing the cost of self-reliance or self-protection to the potential downside, Hoffman's downside could be measured as \$10,600, the amount of his settlement after the decision.<sup>108</sup> Compared to this amount, how much would it have cost to obtain the advice of an accountant or business lawyer at the outset of negotiations? In the early 1960's, one would suppose that \$500 would have purchased sufficient advice (at least enough advice to point out the difference between debt and equity). Thus, for \$500, Hoffman could have saved himself from a considerable amount of personal difficulty, lost time and financial loss. It seems that the law should encourage that kind of conduct, as opposed to misplaced or poorly formed trust.

### C. A Fanciful Hypothetical

The promisee's responsibility in response to a promise can be further illustrated by the following hypothetical. Ms. Trusting owns a horse farm. Mr. Slick enters into a contract to purchase an abandoned meat processing plant in town. Mr. Slick is new to the area. Neither Ms. Trusting nor anyone else in town has ever met or heard of Mr. Slick. Mr. Slick drives into town in his Hummer, leaves \$100 tips for the waitresses at the diner, and tells everyone he meets about his big plans to export pork products to overseas markets. The townsfolk are eager to hear about his plans because the town has been in decline for many years, and is sorely in need of economic development. One day, Mr. Slick sees Ms. Trusting in the diner and takes her aside. "You know, my plant's gonna need product. Now, you're probably wondering what's this got to do with you. Here's the deal. You could start raising pigs on your farm, and I'll buy your supply of pigs once my plant is ready to open in fourteen months. I'll pay top dollar, and I'll guarantee to buy from you for ten years." For Ms. Trusting, this is the deal of a lifetime because the cost of raising horses has exceeded her revenues for a few years, and she immediately accepts the offer. Upon hearing her acceptance, Mr. Slick turns to everyone in the diner and yells out, "I just locked in my first supply of pigs! Ms. Trusting is gonna be one of my pig suppliers!" The other diners cheer at the good news of even more business activity in their town.

Although Ms. Trusting is trusting by nature, even she wonders whether she should get Mr. Slick's promise in writing. But she decides that Mr. Slick must have been serious because he announced the deal to everyone in town. Plus, the big story on the front page of her local newspaper was about the new law of promissory estoppel and how all promises in furtherance of economic activity were now enforceable. Armed with this knowledge, Ms. Trusting starts raising pigs on her farm.

A little over a year later, she contacts Mr. Slick who has since returned to the other side of the country. At first, Ms. Trusting has to remind Mr. Slick who she is.

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<sup>108</sup>*Id.* at 98.



The conversation then goes from bad to worse, and Mr. Slick denies any obligation to buy any pigs. Unfortunately for Ms. Trusting, the market value of her farm has dropped considerably because no one wants to own a pig farm.<sup>109</sup> Ms. Trusting therefore sues Mr. Slick in the local court. She loses on her breach of contract theory because the promise is unenforceable due to the Statute of Frauds.<sup>110</sup> However, she prevails on her claim under a promissory estoppel theory, and wins judgment on the promise. However, Ms. Trusting learns that Mr. Slick is judgment-proof.

Several scenarios can account for why Mr. Slick made his promise.

1. Mr. Slick is a convicted felon who lies and cheats for a living. He duped gullible investors to give him millions of dollars to invest in his project. He would bring the investors to town, show them the pigs on Ms. Trusting's property, and offer that as proof that the project was underway and on track. The investors' money was gambled away in Vegas; or
2. Mr. Slick is a starry-eyed optimist who comes up with one pie-in-the-sky scheme after another. He always believes he is just one deal away from the big-time. The pork processing plant was just the latest scheme that amounted to nothing. His business plans, such as they are, are an exercise in hope and hype. Despite his delusions, he honestly thought the plant would be his ticket to fortune, and he honestly thought that he was doing Ms. Trusting a favor by offering her a way to participate in the project. As Mr. Slick likes to say, "you can't blame a guy for trying;" or
3. Mr. Slick is an honest, hard-headed businessman, but a very bad one. He completely miscalculated the demand for pork in foreign markets, and miscalculated the cost of financing the project. As a result, he was unable to convince any lenders to finance the project.

Because of Ms. Trusting's inherent nature and because she knew of the laws in her state designed to maximize trust in business transactions, Ms. Trusting never did any due diligence before starting a pig farm. Suppose, however, any person could have learned any one of the following facts from a search of public records at minimal cost:

- a) Mr. Slick had two prior felony convictions for embezzlement and wire fraud.
- b) Local zoning ordinances did not permit the operation of a meat processing plant, and it would take at least two years to get a decision on the proposed use with no assurance of a favorable outcome.
- c) A town in the next county was already one year into the development of a competing pork processing plant, and a study by a local college showed that the area could only support one.

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<sup>109</sup>For those unfamiliar with pig farming, the smell is ever-present and overpowering. This hypothetical was constructed this way as a reminder that it will often be the promisee alone who must live with the consequences of the broken promise.

<sup>110</sup>U.C.C. § 2-201 (2001) (or the one-year provision of the Statute of Frauds, if the U.C.C. does not apply for some reason).

Under facts like these, should the law concern itself solely with the promisor's wrongful or misguided conduct, without any questions raised about the promisee's own involvement in the matter? What purpose is served by leaving the promisee's conduct unexamined? As fanciful as this hypothetical may be, the world has an abundant share of Mr. Slicks, and it seems that all would be better served if the Ms. Trustings of the world were encouraged to protect themselves. Any movement toward exalting trust, no matter what, would undermine this encouragement.

This hypothetical also illustrates the difference between reasonable reliance and optimal trust. A panel of judges, like the ones in the *Universal* case, might view Ms. Trusting's reliance as reasonable. After all, Mr. Slick had a contract to purchase the meat processing plant, and projected the appearance of (flashy) success. It would also be no problem to prove the promise because of all the eyewitnesses in the diner. These facts could arguably support a finding of reasonableness. However, should Ms. Trusting have trusted Mr. Slick? Is that the level of trust the law should encourage or protect? Would any competent lawyer have advised Ms. Trusting to trust Mr. Slick? The important point is that an *ex post* judicial inquiry into whether reliance was reasonable is something entirely different from an individual's *ex ante* decision to trust.

This Article does not suggest that the courts have overlooked the promisee's conduct. However, it seems there has been a tendency in the courts and the scholarly literature to focus more on the promisor's conduct. This observation does not imply that such a focus is misplaced. If anything, the promisor's conduct is more inviting for examination and interesting because it often involves morally reprehensible conduct.<sup>111</sup> A couple of notable instances where the court did focus on the promisee's conduct add more texture to the understanding of the protection of trust.

#### D. *James Baird Co. v. Gimbel Bros.*

It is instructive to examine the case often regarded as the companion to *Drennan—James Baird Co. v. Gimbel Bros.*<sup>112</sup> Just like its California counterpart, *Gimbel Bros.* involved a subcontractor who withdrew a mistakenly-computed bid submitted to a general contractor. Just like *Drennan*, *James Baird Co.* relied on the subcontractor's bid and was awarded the general contract. Unlike *Drennan*, however, Judge Learned Hand refused to protect the general contractor's trust and reliance. Indeed, the judge was keen to criticize the promisee's conduct in the transaction. "The contractors had a ready escape from their difficulty by insisting upon a contract before they used the figures; and in commercial transactions it does not in the end promote justice to seek strained interpretations in aid of those who do not protect themselves."<sup>113</sup>

With all due respect to Judge Hand, he got it wrong and Justice Traynor got it right.<sup>114</sup> If it can be assumed that the nature of contractor-subcontractor interactions

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<sup>111</sup>For example, Professor Kostritsky identified the presence of opportunistic conduct by the promisor as a key element in successful promissory estoppel cases. See Kostritsky, *supra* note 62, at 542.

<sup>112</sup>*James Baird Co. v. Gimbel Bros.*, 64 F.2d 344 (2d Cir. 1933).

<sup>113</sup>*Id.* at 346.

<sup>114</sup>Subsequent case law made this clear.

for Pennsylvania projects in the 1930's was similar to California projects in the 1950's, the use of the analysis comparing the cost of self-reliance to the potential downside would weigh against the result in *Gimbel Bros.* Given the need for speed and informality in the bid submission process, it would be impractical for a contractor to gum up the process by insisting on and negotiating a formal contract, as Judge Hand would require. Such self-help or self-reliance would add crippling costs to the transaction in the form of lost time, managerial distraction, and perhaps attorneys' fees to the point where cost of self-protection would outweigh the potential downside. Thus, it would be unreasonable to expect a contractor to act in the manner demanded by Judge Hand. If that were the law, the contractor might not have any choice, except to cease business.

*E. Marker v. Preferred Fire Insurance Co.*

Another example of a court looking at the promisee's conduct was in the case often regarded as a companion to *Clark—Marker v. Preferred Fire Insurance Co.*<sup>115</sup> Clinton Marker was a lawyer and a licensed agent of the Preferred Fire Insurance Company, the defendant. In other words, the plaintiff was one of the defendant's insurance agents. Marker owned real property in Topeka, which was destroyed by a tornado on June 8, 1966. The property had been insured for this type of loss under a policy issued by the defendant, but the policy had expired on February 27, 1966. The lawsuit arose out of the circumstances surrounding the failure to renew the policy.

In late 1965, Marker was in the process of purchasing the property and became aware of the fact that the policy at issue was due to expire in February 1966. However, Marker expressly instructed the agent who had arranged the coverage (a Mr. Johnson, who was also a co-defendant) not to renew the policy. Marker told Johnson that he (Marker) would take care of the renewal (the reason for the instruction was apparently related to the commission). Marker alleged that Johnson had promised him that he (Johnson) would remind Marker of the expiration date. Marker alleged that Johnson failed to do so, and that is why the policy was not renewed (even though Marker was in actual possession of the policy which stated the expiration date). Marker sought recovery under a theory of promissory estoppel (in addition to breach of contract). The court rejected all of Marker's arguments and affirmed the grant of summary judgment in defendants' favor.

Also we again wish to stress the fact that Marker was an attorney and was himself a licensed agent for Preferred Fire Insurance Company. . . . The terms of the policy were always within the knowledge of the plaintiff and if he failed to remember that the policy expired at a certain time before the

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Traynor's analysis in *Drennan* won out over Hand's analysis in *Baird* in subsequent contractor-subcontractor cases. More importantly, however, the drafters of the Restatement (Second) of Contracts subsequently adopted and extended the logic of *Drennan*. Restatement (Second) section 87(2) today provides that "[a]n offer which the offeror should reasonably expect to induce action or forbearance of a substantial character on the part of the offeree before acceptance and which does induce such action or forbearance is binding as an option contract to the extent necessary to avoid injustice."

Katz, *supra* note 92, at 1263.

<sup>115</sup>Marker v. Preferred Fire Ins. Co., 506 P.2d 1163 (Kan. 1973).

tornado, it was his own negligence and not that of Johnson which prevented the plaintiff from renewing his policy.<sup>116</sup>

Even though *Marker* and *Clark* both involved a failure to arrange promised insurance coverage, the different nature of the plaintiffs led (correctly) to opposite conclusions.<sup>117</sup> In terms of the comparison of the cost of self-protection to the potential downside, the cost of self-protection for *Marker* was almost negligible due to the fact that he was both a lawyer and an agent for the defendant. His situation was unlike *Clark's*, who was in no position to exercise feasible self-reliance or self-protection.

#### F. The Role of Lawyers Concerning Promisee Self-Reliance

So how does one exercise self-reliance or self-protection? *Marker* points to one method: the hiring of a lawyer. The fact that *Marker* was a lawyer was a crucial factor in the decision. It was important, of course, because *Marker* was in a position to protect himself. Thus, in determining the cost of self-reliance or self-protection, a helpful question is to ask whether the promisee should have hired a lawyer. In *Red Owl*, as discussed, Hoffman could probably have avoided his loss by spending a modest amount on professional advice. The use of lawyers was also alluded to in *Gimbel Bros.* when Judge Hand sharply criticized the plaintiff for not protecting itself.<sup>118</sup> This was likely Judge Hand's way of saying that the plaintiff should have hired a lawyer.

It would be wrong, however, to conclude that the law should refrain from protecting trust if a promisee fails to hire a lawyer. The inquiry should focus on whether the nature of transaction allows for the hiring of a lawyer, and, if the answer is yes, then on whether the promisee should have hired a lawyer. *Clark* and *Drennan* illustrate this analytical process. In the typical insured-insurer situation, the cost of the transaction would be prohibitive if the insured is required to hire a lawyer to protect her interest. The economics of insurance purchase would be so costly for the insured that the only rational decision would be not to obtain insurance. In the subcontractor-contractor situation, the lack of available time in the bidding process is one reason why it would not be feasible for the contractor to protect itself by hiring counsel. In sum, the law should respect the real world constraints of common transactions and recognize that there are severe limits to which a promisee can

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<sup>116</sup>*Id.* at 1170.

<sup>117</sup>This is certainly not an original observation.

The different results in *Clark* and *Marker* were determined not so much by differences in the ways the doctrine was applied as by differences in the ways the underlying facts were perceived—differences that placed the cases in disparate “situation-types.” A key distinction was the difference in the characteristics of the respective insureds. *Clark* involved an unsophisticated insured who relied on the representations of a commercially responsible agent. The court understood *Marker* to involve commercial parties of equal stature and the offer of a gratuitous courtesy by Johnson. In the courts' views, the facts demanded liability in the first case but not in the second. Jay N. Feinman, *Promissory Estoppel and Judicial Method*, 97 HARV. L. REV. 678, 702 (1984).

<sup>118</sup>James Baird Co. v. Gimbel Bros., 64 F.2d 344, 346 (2d Cir. 1933).

protect herself in certain transactions. In such instances, it would be foolish to require the promisee to hire a lawyer.

In other transactions, however, protecting oneself by hiring a lawyer would be the prudent course of action, and the law should refrain from protecting those who do not take that step.<sup>119</sup> As mentioned, the *Red Owl* case represents a situation where promisee would have been well-served by hiring a lawyer or an accountant. It follows that claims for promissory estoppel should face particularly tough scrutiny when the promisee is (or should have been) represented by counsel, and the courts have recognized legal representation as an important factor in cases where such claims have been denied.<sup>120</sup>

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<sup>119</sup>A reader may wonder why the *Bacardi* case does not fall into the category where the promisee should have hired a lawyer. After all, the promisee was a sophisticated business entity with ample resources and was in discussions concerning its continued existence. That sounds like a situation where the court should have criticized the promisee for not protecting itself.

This Article submits, however, that the promisee acted rationally and prudently by not bringing a lawyer into the situation. The promisee had a long-standing, pre-existing relationship with Bacardi in which mutual actions were taken and decisions made in an informal manner without the involvement of lawyers. This is the context out of which the trust developed. If the promisee had brought a lawyer into this situation, it would have been tantamount to a declaration that it did not trust Bacardi and that the existing relationship had moved to a different, more unfriendly level—an escalation in tension, in other words. The risk of jeopardizing and irreparably harming the relationship with Bacardi was too great.

As Professor Hillman observed:

Business people are usually comfortable with their contracting partners, familiar with the subject matter of their deals, and eager to do additional business in the future.

They believe that deals should be honored and that “*legalese*”—symbolizes distrust and selfishness. Business people also want to establish and maintain good reputations.

They are therefore generally content with informal arrangements.

HILLMAN, *supra* note 99, at 243 (emphasis added).

<sup>120</sup>*See, e.g.,* W.R. Grace & Co. v. Taco Tico Acquisition Corp., 454 S.E.2d 789 (Ga. Ct. App. 1995). In that case, Taco Tico attempted to acquire the Del Taco restaurant business. The parties executed a non-binding letter of intent and a management services agreement under which Taco Tico actually began operating the Del Taco business pending consummation of the transaction. Circumstances changed, however, and the transaction fell apart. Taco Tico sued on several theories. One of its claims asserted promissory estoppel because the seller had represented that the transaction would be completed. The court rejected the claims. It noted that the letter of intent expressly stated that neither party may rely on any representations made by the other party regarding whether the transaction would be consummated. It therefore ruled that, as a matter of law, Taco Tico could not have reasonably relied upon any alleged representations by Del Taco, and ordered that a directed verdict be entered against Taco Tico.

In this appeal, both parties to the negotiations were experienced, successful businessmen who were advised by capable attorneys. Therefore, it cannot be reasonably maintained that they did not comprehend the terms of the letter of intent that they signed or that they did not understand the possibility that the transaction would not be completed. Under these circumstances, Taco Tico cannot avoid the responsibility for its actions taken in preparation for the acquisition of Del Taco based on the assumption that the transaction would be completed.

*Id.* at 791.

## VIII. CONCLUSION

There are, of course, obvious disadvantages to anything less than maximum protection of trust. Identifying the type of trust that should be protected from the type that should not is a difficult task with no clear guidelines yielding consistent results. As noted by two scholars:

But the problem is quite simply that policies that reduce the reliability of promises are likely to reduce both beneficial and detrimental reliance. Thus, legal rules that encourage self-protective adaptation by the promisee achieve desired reductions in detrimental reliance only at the cost of concomitant reductions in beneficial reliance.<sup>121</sup>

Moreover, the approach seems to give free rein to the “bad man” to lie and mislead.<sup>122</sup> After another of his broken promises, he would say, “You trusted me? That is entirely your problem. You should have known better.” The advocates of expansive trust protection would argue that such a policy is necessary to protect the virtuous from the bad man.

Unless, however, the law can legislate away the existence of bad promisors, the law should pursue a complete approach to the problem of bad promises by also encouraging promisees to avoid them. There are simply numerous types of promises that should not be relied upon and transactions that should not be pursued. In many such instances, the promisee will be the party who is in a better position to avoid the situation.<sup>123</sup>

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<sup>121</sup>Goetz, *supra* note 48, at 1271.

<sup>122</sup>This is a reference to Holmes’ “bad man.”

If you want to know the law and nothing else, you must look at it as a bad man, who cares only for the material consequences which such knowledge enables him to predict, not as a good one, who finds his reasons for conduct, whether inside the law or outside of it, in the vaguer sanctions of conscience.

Holmes, *supra* note 39, at 459.

The “bad man” was one of the concerns of the Farber and Matheson article. “Rather, promises are enforced in order to foster a society in which people can confidently rely on each other. Such a society is morally superior to the state of constrained avarice depicted by ‘bad man’ theories of legal obligation.” Farber & Matheson, *supra* note 8, at 942.

<sup>123</sup>These principles are also consistent with sound legal practice.

This seems as good a place as any to point out that the promisee might also be relying on her knowledge of a rule of law, in this case the rule of promissory estoppel. This is a difficult factor to assess. On the one hand, [S]ection 90 has been around at least since 1932 (citations omitted). One might with justification take the position that reliance on these rules is no less reasonable or significant than reliance on the rules of non-liability, such as the consideration requirement or the rules of form. But there is a problem here, nonetheless. It is one thing to counsel a client, “If you can get the other party to sign a formal ‘contract,’ you will probably be protected.” It is—at least it seems to me to be—a different thing to counsel the client, “You should go ahead and rely on the promise that was made to you, because then you will be protected.” I have never advised a client in these circumstances, but given the risks involved, it has always seemed to me that I would counsel the promisee to change position only if she would do so anyway, because of her trust in the promisor—not just for the sake of binding someone to a promise that she fears may not be performed, and could not otherwise be enforced. I have refrained from putting forth the promisee’s conscious

To this end, this Article has proposed a framework to protect trust to a certain degree and yet promote self-reliance and self-protection. The overall approach is to recognize and honor existing business practices in order to avoid a situation where the law forces contracting parties to act in ways inconsistent with the actual realities and restraints of transactions.<sup>124</sup> Within this general framework, however, the law can act to inform the analysis and process by which trust develops.

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reliance on [S]ection 90 (or some other similar rule) as an independent argument for enforcement in this discussion, because a main thrust of my argument is that individuals rely on promises not primarily (if at all) because of their expectations of legal enforceability, but because of their expectations of performance.

Knapp, *Rescuing Reliance*, *supra* note 47, at 1294 n.420.

On a similar note, another commentator observed:

Second, proving the existence of such passive, subtle reliance or the amount of damage suffered was “administratively baffling,” and something to be avoided. Indeed, Llewellyn contended that the problems of proving substantial reliance meant that businesspeople should not build their transactions with it in mind. He pointed out that it would be folly for an attorney to advise a client to rely on an otherwise unenforceable agreement, because if the court found insufficient proof of reliance, the client would be out a considerable sum.

Michael Gibson, *Promissory Estoppel, Article 2 of the U.C.C., and the Restatement (Third) of Contracts*, 73 IOWA L. REV. 659, 673 (1988).

<sup>124</sup>This approach is like the following.

Novices in business, such as the franchise applicants in *Hoffman*, may not know the formal legal doctrines, and more experienced parties, such as the general contractor in *Drennan*, may view legal doctrine as subordinate to prevailing social norms or business exigencies. For both kinds of parties, these norms and exigencies may constitute the real conventions in force. In this view, because offerors know about and knowingly benefit from offerees' reliance on such social and business understandings, it would be unfair to allow one party to evade the obligations of such understandings while it reaps the benefits of the other's compliance. Rather than trying to preserve the elegant and official conventions that parties do not really use, the law should try to reflect the messy but realistic conventions that the parties do actually follow.

Katz, *supra* note 92, at 1265.