

UCLA

UCLA Law & Economics Series

Title

The Borat Problem In Contract Law: Fraud, Assent, And Standard Forms

Permalink

<https://escholarship.org/uc/item/0wp5r2qr>

Author

Korobkin, Russell

Publication Date

2011-08-08

Peer reviewed

THE *BORAT* PROBLEM IN CONTRACT LAW: FRAUD, ASSENT, AND STANDARD FORMS

Russell Korobkin *

Two parties reach an oral agreement. The first then presents a standard form contract, which the second signs without reading, or without reading carefully. When the second party later objects that the first did not perform according to the oral representations, the first party points out that the signed document includes different terms or disclaims prior representations and promises. I call this all-too-common occurrence the “Borat problem,” after litigation over the 2006 movie of that name based on this fact pattern.

The Borat problem exists on the blurry border between tort and contract law. This article describes the doctrinal indeterminacy and the underlying normative problem of bilateral opportunism that has caused courts to respond to the problem in a variety of inconsistent and unsatisfying ways. It then makes the case that the costs of contracting can be minimized if parties who draft standard form contracts are required to obtain “specific assent” from their counterparts in order to contradict or disclaim prior representations, and non-drafting parties are required to satisfy a heightened evidentiary standard before being permitted to challenge the enforceability of standard form terms on the grounds of fraud or misrepresentation.

INTRODUCTION

In the 2006 movie, *Borat: Cultural Learnings of America for Make Benefit Glorious Nation of Kazakhstan*,¹ English comedian Sacha Baron Cohen plays

* Professor of Law and Faculty Director of the Negotiation and Conflict Resolution Program, UCLA School of Law. This article benefited greatly from feedback at workshops at Cornell Law School, the Harvard Program on Negotiation, Hebrew University, Northwestern Law School, St. Louis University Law School, UCLA School of Law, University of Chicago Law School, and the University of Washington Law School. Steve Calandrillo, Bob Hillman, Peter Levine, Doug Lichtman and Eyal Zamir provided extremely helpful, detailed comments. Mike LaPlante, Paul McReynolds, Gina Nicholls, Nick Palatucci, Isaac Silverman, and Jonathon Townsend provided critical research assistance.

the role of an outrageously inappropriate Kazakhstani television reporter, Borat Sagdiyev, who journeys across the United States to film a documentary about American culture. In the course of his travels, the title character uses his bizarre persona to elicit offensive statements and behavior from, as well as to generally humiliate, a number of ordinary Americans who are clearly not in on the joke. The movie was a critical and box office success: *Borat* was nominated for an Academy Award for Best Adapted Screenplay,² Baron Cohen won a Golden Globe Award for Best Actor in a Comedy or Drama,³ and the movie earned nearly one-third of a billion dollars in ticket and DVD sales.⁴

One of Borat's unwitting stooges was Maryland driving instructor Michael Psenicska. In the movie, Psenicska, hired to give Borat a driving lesson, finds himself trapped in the passenger seat of a car while the volatile faux-Kazakhstani careens erratically down the local streets, endorsing rape, shouting obscenities at other drivers, and asking Psenicska to be his boyfriend. Clearly discombobulated by this unexpected behavior, an anxious Psenicska alternately ignores, deflects, objects to, or nervously chuckles at Borat's political incorrectness while trying to prevent an accident.

In Alabama, etiquette coaches were the chosen foil for Borat's peculiar brand of social obtuseness. As etiquette expert Kathie Martin attempts to gently teach the clueless Borat social graces, Borat makes vulgar sexist and anti-Semitic comments and then shows Martin nude pictures of his supposed son, leaving her visibly uncomfortable and practically speechless. Excerpts of Martin's coaching session are interspersed with scenes from a dinner party that etiquette instructor Cynthia Streit hosts for Borat with a group of her genteel friends. The boorish Borat shocks the guests with sexist comments, aggressive sexual innuendo and put downs, and repeatedly refers to one guest who indicated that he is "retired" as a "retard." When Borat returns from a trip to the restroom holding a bag of feces, Streit, in a remarkable exhibition of

¹ Borat: Cultural Learnings of America for Make Benefit Glorious Nation of Kazakhstan (Four by Two Productions, 2006).

² Borat: Cultural Learnings of America for Make Benefit Glorious Nation of Kazakhstan, The Internet Movie Database (IMDb), available at <http://www.imdb.com/title/tt0443453/awards>.

³ Nominations and Winners, Hollywood Foreign Press Association, 2006, available at <http://www.goldenglobes.org/nominations/year/2006>.

⁴ The movie grossed \$261 million in worldwide theatrical performance and an additional \$62 million in U.S. DVD sales. The Numbers (www.the-numbers.com/movies/2006/BORAT.php) (last visited July 25, 2011).

patience and self-control, attempts to explain how a toilet operates. But when a suggestively-dressed African-American female (actually an actor) knocks at the door and is introduced by Borat as a prostitute, the guests begin to flee and an exasperated Streit tells Borat that neither he nor his friend may stay for dessert.

As Borat continues his travels, he encounters a recreational vehicle populated by trio of fraternity brothers from the University of South Carolina. In the ensuing alcohol-enhanced conversation, the men profanely disparage women and mourn the fact that slavery is no longer legal.

How did *Borat's* producer, Twentieth Century Fox, convince Psenicska, Martin, Streit, the fraternity members and many others to become the victim of Baron Cohen's brand of humiliating humor? According to these victims, the studio enticed them into the transactions by way of a two-part strategy: a lie followed by a standard-form contract.⁵

In Psenicska's telling, Todd Schulman (who is identified in the *Borat* credits as an editorial assistant to Baron Cohen) called Psenicska and offered to pay him \$500 to give Borat, whom Schulman identified as a Kazakh television reporter, an on-camera driving lesson for a "documentary [film] about the integration of foreign people into the American way of life."⁶ Psenicska agreed to the bargain. On the date of filming, Schulman and a film crew arrived late with the \$500 in cash and a document labeled "Standard Consent Agreement," which they prevailed upon Psenicska to sign.⁷ The consent form, which Psenicska says he did not read,⁸ indicates the signatory's consent to appear in a "documentary-style....motion picture" using "entertaining content and formats," and includes a lengthy waiver provision whereby the signatory "agrees not to bring at any time in the future any claims against the Producer" for an assortment of claims including "fraud (such as any alleged deception or surprise about the Film or this consent agreement)."⁹ It also included a provision stating that "the Participant acknowledges that in entering into [the Agreement], the

⁵ The film spawned ten lawsuits in all. Panda Kroll, Teaching Through a Study of the Borat Litigation, 3 J. of the World Universities F. 127, 144 exh. A (2010). Only a subset are relevant to this article.

⁶ Psenicska v. Twentieth Century Fox, 07 Civ. 10972, 2008 WL 4185752 (S.D.N.Y., Sept. 24, 2008), Complaint at ¶ 13.

⁷ Id. at ¶16-17.

⁸ Id. at ¶ 17.

⁹ "Standard Consent Form" ¶¶ 1, 4 [hereafter "Borat Release"], available at http://img.slate.com/media/1/123125/123073/2133676/2150683/061020_BoratRelease_p1.

Participant is not relying upon any promises or statements made by anyone about the nature of the Film or the identity of any other Participants or persons involved in the film."¹⁰

Martin claimed that Schulman hired her over the phone to provide "etiquette training to a foreign reporter whose travel experiences were being filmed...for Belarus television" for \$350.¹¹ At the time of the session, Schulman handed Martin a document, which she signed, that he referred to as a "standard filming release form" and which was materially identical to the form signed by Psenicska.¹²

Schulman allegedly told Streit that her dinner party would "be filmed for an educational documentary made for Belarus television."¹³ At the time of the dinner party, Schulman provided Streit and her guests with written documents, which included the same terms that appeared in the Psenicska and Martin agreements. He asked each for a signature, and they too complied.¹⁴

Two of the fraternity members (identified in their lawsuit only as John Does) claimed that unnamed producers recruited them at their fraternity and offered them \$200 to appear in a film, which the producers assured the men would not be shown in the United States.¹⁵ After taking them to a bar and purchasing them alcohol, the producers then prevailed on them to sign written "Standard Consent Forms" like those procured from the other complainants.¹⁶

The *Borat* plaintiffs alleged that they were induced to participate in the video sessions by the producer's representation that the footage would be used for a documentary film about American life made for an Eastern European audience -- they neither consented to playing the straight men in a Sacha Baron Cohen comedy routine nor to having their performance used as part of a studio-produced, major motion picture, that would be shown around the world. That the producers used them for an entirely different purpose was improper, and such improper use of their likenesses should entitle them to a legal remedy.

¹⁰ Id. ¶ 5.

¹¹ Martin v. Mazer, 08 Civ. 1828 (S.D.N.Y., Sept. 24, 2008), Complaint at ¶¶ 28-32.

¹² Id. ¶¶ 39-41.

¹³ Streit v. Twentieth Century Fox, 08 Civ. 1571 (S.D.N.Y., Sept. 24, 2008), Complaint at ¶ 26.

¹⁴ Id. ¶ 11.

¹⁵ California Superior Court, Case #SC091723, Filed Nov. 9, 2006, Complaint at ¶¶ 11-12 (available at http://cdn.digitalcity.com/tmz_documents/110906_borat_wm.pdf).

¹⁶ Id. at ¶¶ 13-14.

Twentieth Century Fox responded that the complete agreements between the studio and the various parties was reflected in the written consent forms, duly signed by each plaintiff, and that the content of any prior communication between the parties was legally irrelevant.

The claims raised by the *Borat* plaintiffs illustrate a complex doctrinal and normative puzzle that lurks in the muddy interstices between contract and tort law and extends in significance far beyond the particular context of a comedian attempting to trick hapless individuals into being the butt of a grand joke. Should the law privilege the text of a signed, written contract over prior inconsistent oral statements or promises? Or should the law permit non-drafting parties to sustain tort or breach of contract claims by proving the content of such earlier representations? The issue arises frequently, and courts have struggled mightily, and reached inconsistent outcomes, when forced to confront what I call the "*Borat* problem."

This article both explains why the *Borat* problem is a difficult one and provides a framework for addressing it that (1) recognizes the root problem of bilateral opportunism, (2) attempts to minimize the social costs of strategic exploitation plus exploitation avoidance maneuvers, and (3) does this within the confines of doctrinal categories familiar to the courts.

Part I describes the present confusion among courts. Courts in different jurisdictions – and even, on occasion, courts in the same jurisdiction – have adopted quite different doctrinal strategies of responding to the *Borat* problem.

Part II assesses the normative tension raised by the *Borat* problem, which underlies the judicial ambivalence. A legal rule protecting non-drafting parties from the type of exploitation alleged by the *Borat* plaintiffs subjects drafters to intentional and unintentional exploitation by non-drafting parties, largely as a consequence of the risk of judicial error in distinguishing true from false claims, and also by their own agents. But a legal rule protecting drafting parties has its own attendant costs resulting from the direct costs of reading and understanding standard-form contracts, the deleterious effect that reading in this context can have on trust in contractual relationships, and the psychological costs felt even by non-drafting parties who identify false representations before signing written documents.

Part III provides a two-pronged approach to minimizing the social costs caused by the *Borat* problem, measured as the joint costs of exploitation plus the joint costs of avoiding exploitation. To reduce the risk of judicial error, and thus protect drafting parties, courts should require non-drafters to meet a heightened clear and convincing evidence standard before admitting evidence that drafters made prior representations that are inconsistent with signed writings. To reduce the cost of comprehending terms in signed writings that are

inconsistent with prior representations, and thus protect non-drafting parties, courts should require drafters to obtain “specific assent” to written terms that contradict or disclaim prior representations. This specific assent requirement is satisfied by both a “clear statement” of the extent of disclaimer and “realistic notice” of its presence in the writing. Not only is this outcome normatively appealing because it promises to maximize contractual efficiency under the circumstances, it can be promulgated within the boundaries of traditional doctrinal categories, and so falls squarely within the judiciary’s realm of authority to accomplish.

I. JUDICIAL APPROACHES

The *Borat* problem arises when one or more of four types of clauses in standard form agreements create inconsistencies between the signed writing and alleged prior representations made by the drafting party: (1) the written document states a representation or promise that substantively contradicts or is inconsistent with the alleged oral statement;¹⁷ (2) the written document states that one or both signatories are not relying on any prior representation (no-reliance clause)¹⁸; (3) the written document states that one or both parties are making no representations other than what is explicitly contained in that written document (no-representation clause)¹⁹; or (4) the written document states that one or both signatories waive any legal claims they might have against a counterparty for fraud, deceit, or misrepresentation (waiver clause).²⁰ In the *Borat* litigation itself, the signed writing at issue includes examples of the first, second, and fourth variety of terms.²¹ This Part describes the problem of doctrinal classification raised by the *Borat* problem that has led to inconsistent judicial treatment.

¹⁷ See, e.g., *Williams v. Spitzer Autoworld Canton*, 913 N.E. 2d 410, 417 (Ohio 2009) (car buyer alleges dealer promised him \$1,500 greater trade-in allowance than specified in the writing); *Evenson v. Quantum Industries, Inc.*, 687 N.W. 2d 241 (N.D. 2004) (alleged oral representation by defendant that he would not sell a product line directly contradicted writing); *Ungerleider v. Gordon*, 214 F.3d 1279, 1283 (11th Cir. 2000) (alleged oral promise to grant an investor additional shares of stock directly contradicted by written agreement).

¹⁸ See, e.g., *Rissman v. Rissman*, 213 F.3d 381, 383 (7th Cir. 2000); *MBIA Ins. Corp. v. Royal Indemnity Co.*, 426 F.3d 204, 214 (3d Cir. 2005).

¹⁹ See, e.g., *Danann Realty Corp. v. Harris*, 157 N.E.2d 597, 598 (N.Y. 1959);

²⁰ See, e.g., *Puro v. Neil Enterprises, Inc.*, 987 A.2d 935, 936 (2009).

²¹ *Borat* Release, *supra*, ¶¶ 1, 4, 5.

A. Contract Law vs. Tort Law

The *Borat* problem exists on the border between contract and tort law, creating confusion for courts and leading to inconsistent rulings. Simply put, treating the problem as one of contract law leads to one doctrinal solution, while treating the problem as one of tort leads to a contrary solution.

1. The Contract Approach: Parol Evidence Rule

According to the parol evidence rule, the law presumes that if parties assent to a written agreement, the writing supersedes any inconsistent or contradictory terms expressed in prior oral (or even written) exchanges.²² The rule follows logically from the fact that contracting parties may modify or cancel their deals through mutual consent and, consequently, an agreement that has been superseded is no longer legally in force.²³

The parol evidence rule has the virtue of providing predictability concerning how a court will interpret an agreement when there are plausible competing claims, which reduces both the risk of disputes and the cost of dispute resolution. Furthermore, it does so by adopting what is probably the majoritarian²⁴ (and thus efficient²⁵) interpretive rule; that is, enforcing later-in-

²² Restatement (Second) of Contracts § 213; Corbin on Contracts § 573. Parol evidence may be used to prove the existence of terms that are additional to but not in conflict with the final written document, as long as the document is not intended to reflect the parties' complete agreement (that is, is not "completely integrated"). Restatement (Second) Contracts 209, 216 cmt. d. Courts in different jurisdictions take different positions as to when terms are additional rather than different and what evidence should be considered when judging the level of integration of a written document.

²³ See generally Arthur L. Corbin, The Parol Evidence rule, 53 Yale L. J. 603, 606 (1944) (describing this effect of the parol evidence rule as "the ordinary substantive law of contracts"); accord *Patton v. Mid-Content*, 841 F.2d 742, 745 (1988) (observing that an integrated signed writing makes any prior agreement unenforceable).

²⁴ See Ian Ayres, Preliminary Thoughts on Optimal Tailoring of Contractual Rules, 3 S. Cal. L. Interdisciplinary L. J. 1, 5 (1993).

²⁵ See, e.g., Robert A. Hillman, The Richness of Contract Law: An Analysis and Critique of Contemporary Theories of Contract Law 225 (1997) (the "efficient" default rule is "what most parties would want"); Charles J. Goetz & Robert F. Scott, The Mitigation Principle: Toward a General Theory of Contractual Obligation, 69 Va. L. Rev. 967, 971 (1983) (default rules of contract should be determined by asking "what arrangements would most bargainers prefer?").

time writings when they conflict with prior (often oral) agreements matches the preferences of most contracting parties, judged from an *ex ante* perspective. This is both because most parties intend for later agreements to supersede earlier ones concerning the same subject matter²⁶ and because judicial resolution of cases will be more predictable if courts are attempting to interpret written words rather than prior discussions.²⁷

Given the parol evidence rule, parties who subjectively understand that a subsequent writing is inconsistent with prior agreements or understandings and are not willing to allow the writing to trump will withhold assent. Where the *Borat* problem arises, the problem is that the non-drafting party asserts that he did not actually assent to the terms in the writing. Under prevailing principles of contract law, however, assent under the law is usually determined by objective indicia, not subjective desire or knowledge. Thus, applying the parol evidence rule requires courts to determine what constitutes an objective manifestation of assent on the part of the non-drafting party.

Typically, courts will not enforce the terms of a written contract against a non-drafting party unless that party would reasonably recognize that he was entering into a contract. An early 20th century example of this rule is that a passenger who leaves a bag at a railroad station claim-check is not bound by the terms printed on the back of the claim-check ticket if she is not alerted to those terms by the clerk.²⁸ Because the passenger would reasonably expect that the purpose of the ticket is to demonstrate ownership of a particular item when she returns rather than communicate terms and conditions of the transaction, she is not bound by those terms. A late 20th century analog is what has been called a "browse wrap" agreement.²⁹ A software user is not bound by the terms printed

²⁶ See, e.g., Nicholas R. Weiskopf, Supplementing Written Agreements: Restating the Parol Evidence Rule in Terms of Credibility and Relative Fault, 34 *Emory L.J.* 93, 94 (1985) (concept underlying the parol evidence rule is negotiators "typically intend" for written, integrative agreements to discharge terms "proposed, discussed, or tentatively assented to in the dickering process").

²⁷ Cf. Patton, 841 F.2d at 745 (citing Farnsworth on Contracts for the proposition that the parol evidence rule "satisfies the parties' desire" to simplify contract administration and dispute resolution excluding matters from prior negotiations even if they were agreed upon).

²⁸ See, e.g. Healy v. New York Central & Hudson River R.R. Co., 138 N.Y. 287 (1912).

²⁹ See Hines v. Overstock.com, Inc., 668 F.Supp.2d 362, 366 (E.D.N.Y 2009) (defining browsewrap as "where website terms and conditions of use are posted on the website typically as a hyperlink at the bottom of the screen.").

(or linked to) at the bottom of a web site if she can purchase the software from the site without seeing that the site contains contractual language, because she could reasonably believe the purpose of the text on the web site is to describe the software's functionality rather than terms and conditions of the transaction.³⁰

As long as the non-drafting party has generalized notice that a set of terms exists, however, the law usually finds what Karl Llewellyn called "blanket assent"³¹ to the terms, even without evidence that the non-drafter has specifically assented to the content of those terms.³² That is, a party who signs the signature line of a written contract or clicks an online box that says "I agree to the terms and conditions" is considered to have assented to the stated terms, even in the absence of subjective knowledge of the import, or even the existence, of the included terms.

A corollary to the assumption of blanket assent is the oft-stated principle that contracting parties have a "duty to read" documents that they sign. Parties may choose to disregard this duty completely, or to fulfill it with only modest attention (i.e., negligently), but by doing so they assume the risk that they will be surprised later by the embodied terms.³³ As the U.S. Supreme Court stated in the 19th century, "[a] contractor must stand by the words of his contract; and if he will not read what he signs, he alone is responsible for his omission."³⁴

The objective theory of contract, the principle of blanket assent, and the duty to read, combine to produce the result that a non-drafting party's signature constitutes legal assent to the terms specified in an integrated writing. When these presumptions are combined with the parol evidence rule, the result is that, when a signed writing contradicts or disclaims prior representations, those prior representations lack legal relevance.

³⁰ *Specht v. Netscape Communications Corp.*, 306 F.3d 17 (2d. Cir. 2002)

³¹ Karl Llewellyn, *The Common Law Tradition: Deciding Appeals* 370-71.

³² See, e.g., Hillman & Rachlinski, *supra* note __, at 461 ("Despite criticism, Llewellyn's notion of 'blanket assent' dominates contemporary judicial treatment of standard form provisions.")

³³ See, e.g., *Torres v. State Farm Fire & Cas. Co.*, 483 So.2d 757 (Ala., 1983) (finding that, when insurance agent told plaintiffs she would obtain flood insurance but such coverage was not reflected in insurance policy, the subsequent "loss was attributable to the plaintiffs' carelessness and neglect rather than to misrepresentation" by the agent).

³⁴ *Upton v. Tribilcock*, 91 U.S. 45, 50 (1875).

2. The Tort Approach: Fraud

Notwithstanding the prior analysis, black letter law does not completely bar non-drafters from challenging the enforceability of signed writings when they are inconsistent with prior representations or promises.³⁵ Although the default assumption is that a signature provides blanket assent to all the terms within the writing, challenges to enforceability of the entire writing can be sustained by demonstrating that a party's assent was compromised by duress, mistake, or – most pertinent to the *Borat* problem – fraud.³⁶ I will refer to this as “the fraud rule.”³⁷

There are efficiency justifications for prohibiting false representations in negotiations, of course, in addition to moral ones. With correct knowledge concerning the subject matter of an agreement and the commitments being made by the counterparty, a negotiator will only enter into an agreement that makes him better off than he otherwise would be, and contracts will satisfy the Pareto efficiency criteria: at least one party is made better off by the agreement, and no party is made worse off.³⁸ If false information causes the negotiator to overestimate the value of his counterparty's commitments, however, it is possible that the misled party will be left worse off as a result of the agreement.³⁹ This would not only violate the Pareto criteria, it would call into question whether the agreement actually increased net social welfare.

Assume, for example, that Michael Psenicska was willing to provide a driving lesson in an Eastern European documentary film for \$400, but that he would have demanded a minimum of \$20,000 to appear in *Borat* had he had

³⁵ Restatement (Second) of Contracts § 214(d).

³⁶ Restatement (Second) of Contracts § 214 cmt. c; Corbin on Contracts § 28.21.

³⁷ The fraud rule is sometimes referred to as an “exception” to the parol evidence rule, see, e.g., *Union Bank v. Swenson*, 707 P.2d 663, 665 (Utah 1985), *Pancakes of Hawaii, Inc., v. Pomare Props. Corp.*, 944 P.2d 97, 107 (Haw. Ct. App. 1997), but the doctrinally correct explanation is that the parol evidence rule applies only to disputes over the proper interpretation of a contract, not disputes over whether the alleged contract (including the term in question) is enforceable. See, e.g., Scott J. Burnham, *The Parol Evidence Rule: Don't Be Afraid of the Dark*, 55 *Mont. L. Rev.* 93, 133 (1994).

³⁸ See Richard A. Posner, *Economic Analysis of Law* 14-15 (5th Ed. 1998).

³⁹ Cf. Russell Korobkin, *Negotiation Theory and Strategy* 32 (2d ed. 2009) (calling reaching an agreement when he would have been better off with an impasse one of the two “fundamental bargaining mistakes”).

known the true facts about the movie, its star, and its target audience. Given this assumption, enforcement of the signed writing left Psenicska worse off as a result of participating in the film shoot than he would have been if he had refused. If his participation was not worth more than \$20,000 to Twentieth Century Fox, the transaction also reduced total social welfare.

3. Doctrinal Indeterminacy

The parol evidence rule's purpose of choosing which set of representations or promises to enforce contrasted with the fraud rule's concern with false representations appears to suggest a reasoned distinction between circumstances that should be governed by two rules,⁴⁰ but the distinction turns out to be ephemeral where the *Borat* problem arises.

A drafting party's statement concerning the qualities of the consideration it will provide as part of an agreement can almost always be interpreted as a promise to provide consideration of that quality. When the drafter then provides non-conforming consideration, the aggrieved non-drafter can plausibly allege that the drafter breached his contractual obligation or, alternatively, that he misrepresented the quality of what he would provide.⁴¹ Thus, when a non-drafting party believes that he was promised something other than or additional to what is described in the signed writing, he can allege breach of contract or, alternatively, promissory fraud (a promise made without a present intent to perform⁴²). In either case, the choice of doctrinal category is logically indeterminate. If we assume the signed writing describes the contractual consideration, the inconsistent prior statements (if made) would be misrepresentations. But this prejudices the question of what constitutes the content of the agreement, which the parol evidence rule is supposedly necessary to determine. If we assume that there is a question concerning the drafting party's contractual obligations (which the parol evidence rule is needed to help sort out), then both of the competing representations concerning the drafter's

⁴⁰ See 3 Corbin on Contracts § 578 (contending that the parol evidence rule applies to agreements but not to false statements of fact).

⁴¹ Cf. Alfred Hill, *Breach of Contract as Tort*, 74 Colum. L. Rev. 40, 41-42 (1973) (arguing that when a statement of fact inducing a sale turns out to be false, the proper ground for complaint is that there has been a breach of promise).

⁴² Ian Ayres & Gregory Klass, *Insincere Promises: The Law of Misrepresented Intent* 4 (2005). Not all jurisdictions recognize the promissory fraud as a cause of action but, according to Ayres and Klass, the doctrine is "unequivocally recognized" in at least 44 states. *Id.* at 6.

obligations are potential descriptions of the consideration that must be provided, and thus neither can be considered a misrepresentation.

As an example of a dispute over a factual representation, consider the case of *Davis v. G.N. Mortgage Corp.*⁴³ Thomas and Cathy Davis alleged that G.N. Mortgage represented that the Davis's home loan would require a prepayment penalty only if the Davis's were to repay the balance within two years.⁴⁴ The written documents, in contrast, which the Davis's signed at closing, specified a five-year prepayment penalty period.⁴⁵ On one view, in the entire course of the interaction G.N. represented two sets of terms (i.e., one including a two-year penalty period and the other a five-year penalty period). Either set of terms could possibly describe the parties' contractual obligation, but it is nonsensical to describe either as being "false." On another view, G.N. misrepresented the content of a five-year prepayment term contract. That is, the resulting litigation can alternatively be described as a dispute over whether the parties contracted for a short or long prepayment penalty period or whether the mortgage company misrepresented the prepayment penalty term it was offering to provide to the Davis's.

When a plaintiff alleges promissory fraud -- such as that the *Borat* producers promised to use the film footage of Psenicska and the other plaintiffs for an Eastern European documentary, all the while intending to produce a documentary-style comedy for an American audience -- there is a similar indeterminacy concerning the nature of the dispute. The issue can be described, on one hand, as whether the parties contracted for the plaintiffs to appear in an actual documentary or, alternatively, a documentary-style film. On the other hand, the issue can be described as whether the producers misrepresented the nature of a contract for a documentary-style film. If we presume the contract is for a documentary-style film, Twentieth Century Fox's representation that it was making an actual documentary is (if it was indeed made) false. But if Twentieth Century Fox committed itself to use the plaintiffs' performances in an actual documentary, there is no misrepresentation at all, but rather a contractual obligation to use the footage only in such a production (in which case Twentieth Century Fox then breached the contracts by using the footage in another type of film).

It is only in a relatively unusual third type of situation -- in which the statement allegedly made by the drafting party is unrelated to the consideration

⁴³ 396 F.3d 869 (7th Cir. 2005).

⁴⁴ *Id.* at 874.

⁴⁵ *Id.* at 874-75.

that the drafter will provide as part of a deal -- that a claim of misrepresentation is logically distinct from a dispute over the terms of the agreement itself. In *Williams Ford, Inc. v. The Hartford Courant Co.*,⁴⁶ for example, a group of Connecticut automobile dealers alleged that they were induced to enter bulk-rate advertising contracts with Hartford's primary newspaper by false statements made by *Courant* salespeople that the deal in question was the most cost-effective of the newspaper's various purchasing plans.⁴⁷ In this situation, there was no arguable dispute over the parties' contractual obligations -- it was undisputed that they had agreed to a particular (high-cost) advertisement package -- so misrepresentation is the only possible claim. Note, however, that precisely because the allegedly false statement concerned a matter of only tangential relevance to the parties' contract, the materiality of that falsehood (a doctrinal requirement of fraud/misrepresentation claims⁴⁸) is questionable.

B. Inconsistent Solutions

American courts have responded to the doctrinal conundrum created by the *Borat* problem in various, and inconsistent, ways. What the variety of approaches have in common is that courts rarely, if ever, directly consider whether their choice of doctrinal categories promotes contractual efficiency or any other normative value that the law might wish to encourage.

1. Follow the Complaint

The most frequent approach is to rely on the basic principle that plaintiffs are entitled to remedies for whatever claims that they can prove and thus defer to the doctrinal category that plaintiffs invoke in their pleadings.⁴⁹

The Eighth Circuit's decision in the case of *Pinken v. Frank*⁵⁰ exemplifies this approach. Frank, an executive of Permaneer Corporation, purchased stock

⁴⁶ 657 A.2d 212 (Conn. 1995).

⁴⁷ *Id.* at 216.

⁴⁸ Restatement (Second) of Torts § 538 (1977).

⁴⁹ See *Applications Inc. v. Hewlett Packard Co.*, 501 F.Supp. 129 (S.D.N.Y. 1980) ("fraud is a magic word...by casting this complaint in tort, i.e., fraud, plaintiff has avoided the perils of the parol evidence rule"); see also *Vigortone AG Prods.*, 316 F.3d 641, 644 (7th Cir. 2002); *Pinken v. Frank*, 704 F.2d 1019, 1023 (8th Cir. 1983); *Downs v. Wallace*, 622 So.2d 337, 340 (Ala. 1993).

⁵⁰ 704 F.2d 1019 (8th Cir. 1983).

in the corporation from the three principal shareholders, including Pinken, under a stock purchase agreement that called for Frank to pay \$6.50 per share in cash plus provide promissory notes for an additional \$240,000.⁵¹ When Pinken tried to collect on the notes, Frank claimed that he was fraudulently induced to enter into the agreement by Pinken's oral representation that he would enforce the notes only if the share price rose subsequent to the sale and Frank was able to sell his shares at a profit, which had not happened.⁵² Pinken attempted to invoke the parol evidence rule to prevent Frank's testimony but the court, applying Missouri law, sided with Frank on the ground that Frank's evidence was being "offered to invalidate or defeat, not to vary or reform, the written contract."⁵³ There is nothing to back up the court's assertion, however, other than Frank's framing of the case.

Frank might have argued that the contract between he and Pinken made the enforceability of the promissory notes contingent on the appreciation of Frank's stock, and thus that Pinken had no contractual right to call the notes. Pleading fraud or negligent misrepresentation, however, usually allows plaintiffs to avail themselves of tort damages (including the possibility of punitive damages)⁵⁴ and it provides a way around the usual preference of the parol evidence rule for signed writings. For both reasons, it is unsurprising that plaintiffs in *Borat*-type cases usually concede that the signed writing constitutes the "contract" and allege that they were induced by fraud to sign it, rather than arguing that the signed writing does not accurately reflect the actual agreement.

If the court credits the plaintiff's labeling of his claim as fraud, the plaintiff still must prove he was "justified" or "reasonable" in relying on the false statement.⁵⁵ Logically, the reasonableness of the reliance might be

⁵¹ Id. at 1021.

⁵² Id.

⁵³ Id. at 1023.

⁵⁴ Restatement (Second) of Torts § 908.

⁵⁵ Restatement (Second) of Torts §§ 537-45, 547 (1979). According to one review of the law of all 50 states, three quarters require that reliance be justified or reasonable. Debra Pogrud Stark & Jessica M. Choplin, A License to Deceive: Enforcing Contractual Myths Despite Consumer Psychological Realities, 5 N.Y.U. J. L. & Bus. 617, 621 (2009). The Second Restatement of Contracts allows a party to void a contract when he is "justified" in relying on a fraudulent or material misrepresentation. Rest. (2d) Contracts § 164. Although there is arguably a difference between the "justified" and "reasonable" standards, courts appear to treat them as synonyms in this context. See Mark Gergen, Contracting Out of Liability for Deceit, Inadvertent

undermined by the fact that the allegedly false claim has been disclaimed by the language contained within the signed writing, but this should depend on the particular circumstances of the interaction. In *Shah v. Racetrac Petroleum Co.*,⁵⁶ the plaintiffs were interested in purchasing a gas station/convenience store business but were concerned that their investment would be at risk if the lease of the property could be terminated. The plaintiffs allegedly received a series of promises from the defendant and its agents that the lease would not be terminated⁵⁷ before signing a written agreement that, on its face, permitted termination upon 30 days notice, and included a merger clause stating that the written document “constitutes the entire understanding between the parties...with respect to the facilities covered.”⁵⁸ When the defendant sold the property and attempted to exercise the termination provision in the signed writing,⁵⁹ the plaintiffs alleged promissory fraud and the defendant argued that the merger clause rendered it *per se* unreasonable to rely on any prior representations. The court responded that there was no “*per se* rule,” noted that the plaintiffs alleged six separate misrepresentations, and held that the plaintiffs had “raised a genuine issue of material fact.”⁶⁰

2. The Back Door Parol Evidence Rule

It is easy to see how permitting *Borat*-type plaintiffs to label their claims as fraud or misrepresentations threatens to swallow the parol evidence rule whole,⁶¹ or at least reduce it to a mere drafting obstacle in many situations. Some courts, including those that ruled on the *Borat* plaintiffs’ claims, have responded to this by purporting to follow the fraud rule while actually applying the parol evidence rule surreptitiously.

Misrepresentation and Negligent Misstatement in Exploring Contract Law 237 (Jason W. Neyers et. al eds., 2009).

⁵⁶ 338 F.3d 557 (6th Cir. 2003).

⁵⁷ *Shah*, 338 F.3d at 561, 563-66.

⁵⁸ *Id.* at 561-63.

⁵⁹ *Id.* at 565.

⁶⁰ *Id.* at 568.

⁶¹ See, e.g. Eric A. Posner, The Parol Evidence Rule, the Plain Meaning Rule, and the Principles of Contractual Interpretation, 146 U. Pa. L. Rev. 533, 536 (1998); *Extra Equipamentos e Exportacao, Ltda. V. Case Corp.*, 541 F.3d 719, 724 (7th Cir. 2008).

Both the federal District Court for the Southern District of New York,⁶² which heard the consolidated cases brought by Psenicska, Martin, and Streit, and the Second Circuit, which disposed of the case on appeal with a Summary Order,⁶³ found that the fraud rule applied to the plaintiffs' claims, and thus that the parol evidence rule was inapplicable.⁶⁴ This turned out, however, to be a pyrrhic victory for the plaintiffs. Both courts held that the plaintiffs' reliance on the alleged oral misrepresentations of the producer was not reasonable, as a matter of law, because the no-reliance clause in the signed writing stipulates that the plaintiffs did not rely on any prior statements about the "nature of the film" or the "identity of any other Participants."⁶⁵

The *Borat* decisions do not reveal whether, in the absence of the no-reliance clause, the courts would have ruled that reliance on the producer's false statements could not have been justified because of the conflict between the oral statement that the filmmakers were making a foreign documentary and the written statement that the undertaking's purpose was to produce an "entertaining...documentary-style" film. That is, neither the Southern District of New York nor the Second Circuit revealed how they might have ruled if Twentieth Century Fox had used only the first of the four distinct drafting approaches that lead to the *Borat* problem (i.e., substantive inconsistency between the text of the signed writing and prior representations that drafting parties commonly employ in these types of written documents).⁶⁶

⁶² Psenicska v. Twentieth Century Fox Film Corp. 2008 WL 4185752 (S.D.N.Y. 2008) [hereafter, "Psenicska, S.D.N.Y."].

⁶³ Psenicska v. Twentieth Century Fox Film Corp., 2009 U.S.App. LEXIS 25170 (2d Cir. 2009) (Summary Order).

⁶⁴ The claims of the John Doe fraternity members were brought in California Superior Court and handled somewhat differently. The court ruled that, under California's anti-SLAPP (Strategic Lawsuit Against Public Participation) statute, Cal. Civ. Proc. Code 425.16, the producers were entitled to dismissal unless the plaintiffs could demonstrate a probability of prevailing on the merits because the film constituted an exercise of free speech in connection with a public issue. The court then determined that plaintiffs could show no such probability of success on their various claims. Unfortunately, the court's analysis of the claims relevant to this article -- those labeled as claims for "fraud" and for "rescission" -- constituted only conclusory statements that the plaintiffs had offered no evidence of damages for fraud and that the rescission claim was a thinly veiled request for an injunction. *John Doe 1 v. One American Productions, Inc.*, No. SC091723 at 6 (Cal. Super. Ct., Feb. 15, 2007). The decision was not appealed.

⁶⁵ 2008 WL 4185752 at *7; Summary Order at 5.

⁶⁶ See text accompanying note ___, supra.

The New York Court of Appeals has held, however, that reliance on oral statements cannot be reasonable if the oral statement is contradicted by the written document, even in the absence of a no-reliance clause. In *Citibank v. Plapinger*,⁶⁷ that court upheld a grant of summary judgment in favor of Citibank against the officers and directors of a company who had signed personal guarantees of the company's debts.⁶⁸ When Citibank sought to enforce those guarantees, the guarantors claimed they had been induced to provide the guarantees by the bank's false representation that it would provide the company an additional line of credit, which never did materialize.⁶⁹ The court found that the alleged statement was indeed fraudulent but ruled for the bank on the theory that the guarantors' reliance was unreasonable in light of the statement in the guarantee documents that the guarantors' obligations were "absolute and unconditional."⁷⁰

Other courts have followed the same line of reasoning. In *Barnes v. Burger King Corp.*,⁷¹ for example, a federal court in the Southern District of Florida granted summary judgment for Burger King when a franchisee alleged he had been fraudulently induced to purchase a Los Angeles hamburger franchise by the company's claim that it had a "good faith policy" of not granting new franchises within two miles of existing franchises, only to find Burger King approved another franchise five blocks away less than a year later.⁷² The court held Barnes' reliance unreasonable as a matter of law because the "good faith policy" was contradicted by the subsequently signed franchise agreement, which provides that the agreement "does not in any way grant or imply any area, market or territorial rights proprietary to the Franchisee."⁷³

Where the *Borat* problem exists, this approach renders the court's antecedent determination that the parol evidence rule does not apply to fraud claims hollowly formalistic. The ultimate resolution of the dispute is the same as if the parol evidence rule were invoked directly and strictly: the terms recorded in the signed writing are rendered enforceable and prior inconsistent

⁶⁷ 66 N.Y. 2d, 90 (NY. 1985).

⁶⁸ Id. at 93-94.

⁶⁹ Id. at 93.

⁷⁰ Id. at 93-95.

⁷¹ 932 F.Supp. 1420 (S.D. Fla., 1996).

⁷² Id. at 1423-24.

⁷³ Id. at 1428.

representations are stripped of any legal import, both as a matter of law.⁷⁴ Like the direct application of the parol evidence rule, this back-door application of the parol evidence rule is premised – sometimes explicitly, often implicitly -- on contracting parties having a duty to read the contents of written agreements to which they give general assent, even when drafted by the other party or presented as a contract of adhesion (that is, presented on a take-it-or-leave-it basis). Thus, for example, the Alabama Supreme Court has explained that summary judgment for the defendant is appropriate when the party claiming fraud was “fully capable of reading and understanding their documents, but nonetheless made a deliberate decision to ignore written contract terms.”⁷⁵

In a few cases, courts have also turned the concern for fraud on its head, justifying deference to the signed writing as necessary to counter frauds that *non-drafting* parties attempt to perpetrate.⁷⁶ In *Danann Realty Corp. v. Harris*, the New York Court of Appeals' leading decision in the field (as well as the primary precedent relied upon by Second Circuit in the *Borat* litigation itself), the court dismissed a commercial real estate purchaser's complaint that the seller had provided false oral information about the property.⁷⁷ As justification, the court majority noted that, in light of a provision in the seller-drafted written agreement that “neither party [was] relying on any statement or representation” made by the other, the buyer's allegations that it relied on a prior oral statement demonstrated that “it is guilty of deliberately misrepresenting to the seller its true intention.”⁷⁸ In other words, it is the party who represents that he is not relying on any prior statements of his counterpart and then claims to have done

⁷⁴ This is occasionally recognized by more candid courts. In one case, Judge Posner called bring a fraud suit in the context of the *Borat* problem “a device for trying to get around the limitations [of] the parol evidence rule” and held that no-reliance clauses “serve a legitimate purpose of closing a loophole in contract law.” *Extra Equipamentos e Exportacao, Ltda. v. Case Corp.*, 541 F.3d 719, 724 (7th Cir. 2008).

⁷⁵ *Foremost Ins. Co. v. Parham*, 693 So.2d 409 (Ala. 1997); see also *Andrus v. Ellis*, 887 So.2d 175 (Miss. 2004) (a party “may not complain of an oral misrepresentation the error of which would have been disclosed by reading the contract”). As Mark Gergen has pointed out, this position is at odds with the competing rule that contributory negligence is not a defense to fraud. Gergen, *supra* note __, at 245; see also Restatement (Second) of Torts § 545A.

⁷⁶ This is sometimes called the “double liar” problem. See *Abry Partners V, L.P., v. F&W Acquisition LLC*, 891 A.2d 1032, 1058 (Del. Ch. 2006).

⁷⁷ *Danann Realty Corp. v. Harris*, 5 N.Y.2d 317 (1959).

⁷⁸ *Id.* at 323.

just that who is guilty of fraud, not the party who makes false oral statements and attempts to disclaim them in the subsequent written documents.

3. Fraud in the Inducement vs. Fraud in the Execution

In an attempt to prevent the fraud rule from swallowing the parol evidence rule and vice versa, other courts faced with the *Borat* problem have attempted to draw a line between claims of “fraud in the inducement” (trumped by the parol evidence rule) and “fraud in the execution” (permitted).⁷⁹ According to this distinction, non-drafting parties may not challenge the enforcement of a signed writing on the grounds that prior misrepresentations disclaimed in the writing induced them to sign. However, they may invoke the fraud rule if the drafter represented that the writing itself contained representations that are different from those it actually included.⁸⁰ In short, the parol evidence rule precludes a claim of “he told me X,” but it does not preclude a claim of “he told me the document says X.” Arthur Corbin favored this position, based on the reasoning that the signed writing supersedes any obligations or representations in the first case, and thus the prior statements cannot be considered fraudulent.⁸¹

A pair of Pennsylvania Supreme Court cases illustrates just how thin the distinction between fraud in the inducement and fraud in the execution can be in practice.⁸² In *Yocca v. Pittsburgh Steelers Sports, Inc.*, plaintiff football fans claimed that the Steelers franchise promised that the season ticket seat licenses the fans were purchasing would guarantee them seats in a choice location (which they did not ultimately receive), whereas the subsequent signed writing made a much looser promise concerning location and included a merger clause.⁸³ The court determined that the signed writing constituted “the parties’

⁷⁹ Eric Posner calls these “hard” parol evidence rule jurisdictions, as opposed to “soft” parol evidence rule jurisdictions. Posner, Parol Evidence Rule, *supra* note __, at 536.

⁸⁰ See, e.g., *Hamade v. Sunoco, Inc.* 721 N.W. 2d 233 (Mich.App. 2006) (evidence of alleged oral promise by franchisor not to permit another franchise to operate close to franchisee inadmissible absent claim that franchisor fraudulently convinced franchisee that the promise was actually contained in the writing when it was not); See also *Apolito v. Johnson*, 3 Ariz.App. 358, 359-60 (1966) (alleged oral misrepresentation of buyer's liability inadmissible under parol evidence rule where contradicted by the written document).

⁸¹ Corbin, *supra* note __, at 620-21.

⁸² See *Yocca v. Pittsburgh Steelers Sports, Inc.* 854 A.2d 425, 437 n.26 (Pa. 2004).

⁸³ *Yocca v. Pittsburgh Steelers Sports, Inc.* 854 A.2d 425 (Pa. 2004).

entire contract with respect to the sale of [seat licenses],” and thus that the parol evidence rule prevented the admission of any evidence to vary those terms.⁸⁴

Just three years later in *Toy v. Metropolitan Life Ins. Co.*, the same court confronted an insurance purchaser’s challenge to a signed writing that clearly specified the substantive terms of a permanent life insurance policy and included a no-representations clause.⁸⁵ The buyer alleged that the seller falsely led her to believe she was investing in a savings plan.⁸⁶ Here the court held the fraud rule applicable and the parol evidence rule inapplicable because the trial court determined that the plaintiff alleged that the defendants had represented that the savings plan features of the financial instrument “would be included in the parties’ agreement.” Thus, the plaintiff’s claim was one of “fraud in the execution of a contract” and therefore subject to “a far different analysis than that applied to the fraud claim alleged by the plaintiffs in *Yocca*.”⁸⁷

This approach to the *Borat* problem implicitly rests on the notion that a signature should indicate blanket assent to the terms of a writing in the former case but not the latter, but the normative basis for this distinction is unclear. If a non-drafter has a duty to read a writing before signing to ensure that the drafter did not slip in text inconsistent with prior representations, why does the duty to read disappear just because the drafter affirmatively states that the documentation reflects prior representations? Whatever the basis for the distinction (perhaps that it is more reasonable to assume that a counterparty will not directly lie about what is in a document than to assume he will not attempt to trick you into signing a document that disclaims his prior promises), it seems that it is easily avoided by careful drafting of a plaintiff’s complaint. In most cases, a non-drafting party who could honestly claim that the drafting party made a prior representation that was inconsistent with the text of the signed writing could also honestly claim that the drafting party represented – implicitly through conduct if not explicitly – that the representation on which the non-drafting party relied would be reflected in the signed writing.

4. Scier-Based Classification

A fourth approach to the *Borat* problem is to base the doctrinal categorization of disputes on the scier of the drafting party. Specifically,

⁸⁴ *Yocca*, 854 A.2d at 438.

⁸⁵ *Toy v. Metropolitan Life Ins. Co.*, 928 A.2d 186 (Pa. 2007).

⁸⁶ *Id.* at 189.

⁸⁷ *Id.* at 206.

plaintiffs may challenge the terms in a signed writing only if prior false representations were made with an intent to mislead concerning the quality or extent of consideration. Otherwise, following the principle of the parol evidence rule, evidence of prior inconsistent representations would be inadmissible.

Several courts have relied on this distinction, allowing parties to introduce prior oral evidence to prove “fraud,” which requires intentionality (or recklessness), but not to prove merely “negligent misrepresentation,” which does not require intent to mislead.⁸⁸ Implicitly, this approach assumes that, per the parol evidence rule, the signed writing constitutes the contract between the parties, but that public policy considerations preclude enforcement of contract terms that disclaim liability for intentionally-caused harm. The public policy limitation does not apply, however, to disclaimers of negligently-caused harm.

The Wyoming Supreme Court’s decision in *Snyder v. Lovercheck*⁸⁹ provides an example. Snyder entered into a contract to purchase Lovercheck’s wheat farm, which, according to Snyder, turned out to have a substantial rye infestation over 1800 acres.⁹⁰ Snyder alleged that Lovercheck had told him that the problem was limited to only 100 acres, but the undisputed evidence showed that Snyder subsequently signed a written real estate form contract that included a broad no-reliance term along with merger clause.⁹¹ Snyder subsequently sued, alleging both fraud and negligent misrepresentation.

With a nod to the “age-old proposition that fraud vitiates all contracts,” the court dismissed the “sanctity of the right to contract” in general as well as the Second Circuit’s holding in *Danann Realty* in particular, and found that Snyder was not precluded from bringing a fraud claim.⁹² Then, mere paragraphs later, the court provided an impassioned defense of the “vitality of contract” and the

⁸⁸ See, e.g., *Isler v. Texas Oil & Gas Corp.*, 749 F.2d 22 (10th Cir. 1994); *United States Welding Inc. v. Burroughs Corp.*, 640 F.Supp. 350 (D. Colo. 1985); *Snyder v. Lovercheck*, 992 P.2d 1079 (Wyo. 1999); *Rio Grande Jewelers Supply, Inc. v. Data General Corp.*, 101 N.M. 798 (N.M. 1984); *Wilkinson v. Carpenter*, 554 P.2d 512, 514-17 (Or. 1976); *Sound Techniques, Inc. v. Hoffman*, 737 N.E.2d 920 (Mass. Ct. App. 2000). “A negligent misrepresentation claim ...is in essence a fraud claim with a reduced state of mind requirement.” *Corp. Prop. Assocs. 14 Inc. v. CHR Holding Corp.*, 2008 WL 963048, at *8 (Del. Ch. 2008).

⁸⁹ 992 P.2d 1079 (Wyo. 1999).

⁹⁰ *Id.* at 1083.

⁹¹ *Id.*

⁹² *Id.* at 1084-86.

duty to read against the attempted encroachment of tort law and concluded that Snyder's negligent misrepresentation claim must be dismissed as an impermissible attempt to rewrite the contract.⁹³ The court acknowledged that "there is practically no difference in the harm that can result from either fraud or negligence" but asserted that only fraud is "sufficiently egregious to warrant the intermingling of tort and contract principles."⁹⁴

II. THE NORMATIVE TENSION: BILATERAL OPPORTUNISM

Contract law generally attempts to encourage parties to enter into mutually beneficial (and thus social-welfare enhancing) contracts by minimizing their joint costs of avoiding opportunistic exploitation by their negotiation counterparts.⁹⁵ But where the *Borat* problem arises, a legal rule protective of the interests of drafting parties -- what I will call a "pure duty-to-read rule" -- will subject non-drafting parties to the possibility of opportunistic exploitation and, conversely, a rule protective of drafting parties -- what I will call a "no-exploitation rule" -- will subject non-drafting parties to the risk of drafter opportunism. Either polar position that the law might take will undoubtedly cause some combination of three problems that reduce the ability of the parties to contract efficiently, and thus reduce social welfare: (1) the enforcement of agreements that reduce rather than increase one party's utility, (2) the expenditure of transaction costs by one of the parties to reduce the risk of such exploitation, and (3) a decrease in the number of mutually beneficial contracts produced because a party wishes to avoid both the risk of exploitation and protective transaction costs.

The first step toward addressing the *Borat* problem, which this Part attempts to accomplish, is to carefully identify the costs of a pure duty-to-read rule and the costs of a no-exploitation rule. Part III then proposes a doctrinal approach designed to minimize the joint costs of the bilateral risk of exploitation.

⁹³ Id. at 1087-89.

⁹⁴ Id. at 1088.

⁹⁵ See, e.g., Frank B. Cross, Law and Trust, 93 Geo. L. J. 1457, 1485 (2005); Timothy J. Muris, Opportunistic Behavioral and the Law of Contracts, 65 Minn. L. Rev. 521 (1981).

A. Risks to Drafting Parties

A no-exploitation rule has no direct social cost of its own. Truth-telling is certainly no more difficult than deception, and often it is significantly easier and cheaper. Such a rule, of course, also has the virtue of being consistent with the common moral intuition that deception is wrong and the law should discourage it, or at the very least not encourage it. Extending the prohibition to unintentional exploitation would create some positive cost, as drafting parties would have to invest to avoid making unknowing statements that are inconsistent with their signed writings. The cost of identifying and avoiding discrepancies between prior representations and signed writings usually will be lower for drafters than non-drafters, however. This intuition underlies the rulings of courts that allow plaintiffs in *Borat*-type cases to maintain fraud claims and misrepresentation claims.

Providing such legal protection to non-drafting parties, however, exposes drafting parties to the risk of three types of post-contractual exploitation, discussed below. Drafting parties could respond to this risk by accepting occasional exploitation as a cost of doing business, expending transaction costs to try to protect themselves against exploitation, choosing not to engage in what could be mutually beneficial transactions, or – most likely – some combination of these three strategies. Any of these choices will reduce the net social value of contracting compared to its potential.

1. Knowingly False Claims

In a legal regime in which non-drafting parties may challenge the validity of written terms based on testimony concerning prior statements, non-drafting parties who become unhappy with a contract in hindsight might attempt to opportunistically exploit the drafting party by falsely alleging that the drafting party made prior oral representations that were inconsistent with the subsequent written terms.⁹⁶ If courts could always identify such claims as false when they in fact are, and do so early in the litigation process, threats to bring false claims would have little credibility. Defendants would know they would always

⁹⁶ See, e.g., *Rissman v. Rissman*, 213 F.3d 381, 384 (7th Cir. 2000) (no-reliance clauses "ensure[] that both the transaction and any subsequent litigation proceed on the basis of the parties' writings, which are less subject to the vagaries of memory and the risks of fabrication"); Stewart Macaulay, *Private Legislation and the Duty to Read – Business Run by IBM Machine, the Law of Contracts, and Credit Cards*, 19 *Vand. L. Rev.* 1051, 1065 (1966) ("when a court announces a sweeping duty to read...one senses that the court is concerned with the likelihood of perjury and difficulties of adjudicating facts").

prevail in litigation, ensuring that plaintiffs bringing such claims would receive negative payoffs. With this knowledge, few plaintiffs would bring such cases, and plaintiffs' lawyers working on a contingent-fee basis would put forth significant effort to avoid them.

In reality, judges and juries will have difficulty distinguishing true allegations from false ones, and a consequence of this is that potential plaintiffs will have an incentive to make false claims in some cases.⁹⁷ Even if juries could evaluate the veracity of such allegations with perfect accuracy, judges usually will not be able to identify false claims based on pleadings or even party affidavits.⁹⁸ Thus, even assuming drafting parties would ultimately prevail in litigation based on false allegations, they would incur the substantial litigation costs of taking a lawsuit all the way to trial in order to do so. Worse, the judges and juries sometimes ultimately will accept false allegations as true, with the result being that a rule protecting non-drafting parties from opportunistic exploitation will enable them to opportunistically exploit drafting parties. To the extent that juries might be unduly sympathetic to non-drafting parties, who are more likely to be the economic underdogs in such disputes, such errors could occur more often than would be dictated by random chance.⁹⁹

The risk of an adverse verdict, in addition to the transaction costs of taking a case all the way to trial, will force the non-drafting party to settle lawsuits based on false allegations for more than their expected litigation costs, or to renegotiate terms of the contract to avoid litigation.¹⁰⁰ This fact, in turn, gives non-drafting parties who are not deterred by legal (i.e., perjury) or reputational

⁹⁷ Cf. Posner, *The Parol Evidence Rule*, supra note __, at 562 (observing that the prospect of judicial error is what encourages opportunism that the parol evidence rule is designed to prevent).

⁹⁸ See Glenn D. West & W. Benton Lewis Jr., *Contracting to Avoid Extra-Contractual Liability – Can Your Contractual Deal Ever Really Be the “Entire” Deal?*, 64 *Bus. Law.* 999, 1034 (fraud and negligent misrepresentation claims are “hard to dismiss on a threshold, pre-discovery motion [and] difficult to disprove without expensive, lengthy litigation”).

⁹⁹ Charles McCormick, *The Parol Evidence Rule as a Procedural Device for Controlling the Jury*, 41 *Yale L.J.* 365, 366 (1932) (“The average jury will, other things being equal, lean strongly in favor of the side which is threatened with possible injustice and certain hardship by the enforcement of the writing.”); Cf. Corbin, supra note __, at 608 (1944) (describing the fear of jury sympathy for the underdog as one reason for the parol evidence rule).

¹⁰⁰ See Allen Blair, *A Matter of Trust: Should No-Reliance Clauses Bar Claims for Fraudulent Inducement of Contract*, 92 *Marquette L. Rev.* 423, 468-69 (2009).

risks or personal integrity, an incentive to fraudulently allege that the drafting party made earlier oral statements or promises that are inconsistent with the subsequent set of written terms. It also reduces the incentive of contingent-fee lawyers to vigorously screen out false claims, even assuming that they would not knowingly suborn perjury. In the face of this incentive, drafting parties who choose to contract will bear some combination of the costs of losing, settling and/or defending against non-meritorious claims. Whether drafting parties bear these costs or avoid them by declining to contract, the incentive for non-drafting parties to bring such claims will create social costs and thus reduce the value of contracting compared to a world in which the incentive is eliminated by a legal rule that bars the introduction of evidence of representations that are inconsistent with what is included in the text of a signed writing.

2. Unconscious Opportunism

Even in a world of scrupulously honest non-drafting parties, costs associated with false claims of pre-contractual representations would still exist. Research demonstrates that memory retrieval is not like rewinding and playing a video tape. It is, instead, a constructive process that draws in part on the expectations, biases and world views the individual attempting to remember.¹⁰¹ As a consequence, memories are often imprecise and sometimes entirely inconsistent with the events that actually occurred, although intensely believed.¹⁰² Simply put, recollections of what exactly was said or not said over the course of a negotiation can be mistaken.

The risk of false claims concerning contradictory oral statements or promises is exacerbated by the problem of self-serving bias; that is, “the common human tendency to interpret the world to make it square more comfortably with one’s own interests and beliefs.”¹⁰³ In a seminal study dating to the 1950s, experimenters showed students at Dartmouth and Princeton the film of a particularly contentious football game between the two schools, and

¹⁰¹ Daniel J. Simons & Christopher F. Chabris, What People Believe about How Memory Works: A Representative Survey of the U.S. Population, *PLoS ONE*, 6(8): e22757. doi:10.1371/journal.pone.0022757.

¹⁰² See, e.g. Craig E.L. Stark et al., Imaging the Reconstruction of True and False Memories Using Sensory Reactivation and the Misinformation Paradigms, 17 *Learning & Memory* 485, 485 (2010).

¹⁰³ Ward Farnsworth, The Legal Regulation of Self-Serving Bias, 37 *U.C. Davis L. Rev.* 567, 570 (2003).

asked the students to identify the fouls committed by the teams.¹⁰⁴ Perceptions of which team was guilty of the most infractions differed markedly by the allegiance of the subjects -- Princeton students were more likely to identify violations by Dartmouth than by Princeton, and vice versa.¹⁰⁵ As a result of the self-serving bias, the consequences of faulty memories are likely to be systematically biased rather than randomly distributed. That is, non-drafting parties who misrecall the exact nature of the bargaining interaction that preceded written documentation are differentially likely to recollect those statements as being to their advantage.¹⁰⁶

Not only does evidence of the self-serving bias imply that non-drafting parties are likely to disproportionately interpret hazy recollections to their benefit, it also suggests that they will believe that they are more likely to prevail in litigation than the facts warrant. A wealth of research demonstrates both that people are overconfident in their predictions of the likelihood of desirable outcomes occurring.¹⁰⁷ Research also demonstrates that individuals strongly believe that unbiased others (like judges and jurors) are more likely to view the world as they (the individuals) do than is actually the case.¹⁰⁸ Studies of students playing the role of lawyers in hypothetical lawsuits¹⁰⁹ and of real lawyers predicting the resolutions of actual cases¹¹⁰ have both found self-serving and unjustifiably optimistic predictions of outcomes, on average.

¹⁰⁴ Albert H. Hastorf & Hadley Cantril, *They Saw a Game: A Case Study*, 49 *J. Abnormal & Soc. Psychol.* 129 (1954).

¹⁰⁵ *Id.* at 130-32.

¹⁰⁶ See, e.g., Rissman, *supra* note __ at 384 ("Acting in the best of faith, people may "remember" things that never occurred but now serve their interests.")

¹⁰⁷ One literature review calls this "one of the most robust findings in the psychology of prediction." David A. Armour & Shelley E. Taylor, *When Predictions Fail: The Dilemma of Unrealistic Optimism*, in *Heuristics and Biases: The Psychology of Intuitive Judgment* 334, 334 (Thomas Gilovich et al. eds., 2002).

¹⁰⁸ In a particularly telling example of this, one study found that 87 percent of magistrate judges believed that they are reversed on appeal less often than at least half of their colleagues. Chris Guthrie et al., *Inside the Judicial Mind*, 86 *Cornell L. Rev.* 814 (2001).

¹⁰⁹ George Loewenstein et al., *Self-Serving Assessments of Fairness and Pretrial Bargaining*, 22 *J. Legal Stud.* 135 (1993).

¹¹⁰ Jane Goodman-Delahunty et al., *Insightful or Wishful: Lawyers' Ability to Predict Case Outcomes*, 16 *Psychol., Public Pol. & Law* 133 (2010).

The prediction that follows is this: if non-drafters are permitted to introduce evidence of inconsistent prior representations, the non-drafters will bring more lawsuits than would perfectly calibrated, unbiased non-drafting parties. This, in turn, will increase the costs of such claims for drafting parties. A pure duty-to-read rule could protect drafting parties against imprecise or confused memories about what representations were made, qualified, or taken back during the course of negotiations, thus reducing the costs of contracting for drafting parties and increasing social value.¹¹¹

3. Rogue Agents

In addition to the costs associated with false claims that result from the twin realities of judicial error and self-serving bias, a no-exploitation rule also subjects drafting parties to risk of opportunistic exploitation by their own negotiating agents.

Business entities are often represented in negotiations by agents whose interests are not in complete alignment with the entity itself. One consequence of this is that an agent in the field who is compensated on a commission basis might stand to profit from convincing a counterparty to enter into an agreement, even if the agreement proves to be unenforceable at a distant date.¹¹² When incentives diverge, agents might be tempted to make representations or promises in the course of negotiations that suggest a proposed deal is more desirable to the non-drafting party than is indicated in the written terms, which are likely to be prepared by the entity's lawyers and more closely controlled by the entity's top officers, or at least employees whose personal financial and reputational issues are more closely aligned with those of the entity as a whole. As long as the agent's statements are within his apparent realm of authority, they are legally attributable to the principal.¹¹³

The problem extends beyond the faithless agent to the merely negligent one. An agent who does not intentionally attempt to present the counterparty with a set of more favorable provisions than are embodied in the written terms might do just this as a result of being insufficiently aware of what representations and limitations are actually embodied within the written terms.

¹¹¹ See also Blair, *supra* note __, at 436.

¹¹² See generally Stewart Macaulay, *Private Legislation and the Duty to Read – Business Run by IBM Machine, the Law of Contracts, and Credit Cards*, 19 *Vand. L. Rev.* 1051, 1059 (1966) (observing businesses use standard forms to control agents).

¹¹³ See, *Restatement (Second) of Agency* §§ 257-259A.

A no-exploitation rule requires drafting parties to, in some combination, bear the risk of exploitation (intentional or not) by rogue agents, expend resources to control the behavior of their agents through better training, monitoring, or incentivizing, or choose not to contract in order to avoid both of these primary costs. This can be inefficient when the cheapest of these alternatives is still more costly than it would be for a non-drafter to read and understand terms in the signed writing that limit the agent's authority, effectively deputizing the non-drafter to monitor the drafter's agent.

4. Legal Protection

A no-exploitation rule would impose risks on drafting parties. Drafters could respond to these risks by bearing them, expending transaction costs to mitigate them, or declining to enter into contracts to avoid them altogether. Whatever combination of these three strategies drafters were to choose, however, the legal rule would act as an implicit tax on contracting, reducing the gains in trade that can be created.

Importantly, these costs would reduce the benefits available from contracting for non-drafters as well as drafters. Depending on the slope of the supply and demand curves applicable to particular transactions, at least some of the social costs created by the risk of exploitation of drafting parties would be passed on to non-drafting parties in the price and quality of goods and services. And when the costs are high enough that marginal drafting parties decide not to contract at all, non-drafters would also lose out the share of the cooperative surplus they would have enjoyed if deals that are never consummated had in fact been made.

This implicit tax on contracting can be substantially reduced, if not eliminated entirely, by instituting a pure duty-to-read rule.

B. Risks to Non-Drafting Parties

Although a pure duty-to-read rule would greatly reduce the risk of exploitation of drafting parties and the attendant social costs, it would increase the risk that opportunistic drafting parties would exploit non-drafters by inducing the latter to enter agreements based on oral promises and factual representations and then disclaiming the statements in the signed writing. This is, of course, exactly what the *Borat* plaintiffs allege that Twentieth Century Fox did.

As is true for drafters, non-drafting parties could respond to the risks of exploitation created by an unfavorable legal rule using one or a combination of

three strategies: accepting the risk of occasional exploitation as a cost of doing business, expending resources to reduce or eliminate the risk, or refusing to engage in transactions that have the potential to increase social welfare. Having to employ any of these strategies reduces the expected value of contracting for non-drafters, and thus reduces the cooperative surplus of contracting that ultimately is divided between the parties.

While drafting parties must invest heavily in litigation in order to minimize exploitation (and even then the risk of exploitation remains due to the potential for judicial error), drafters need only read the written document before signing it. Descriptions of the duty-to-read rule sometimes describe the failure to read as an act of negligence,¹¹⁴ thus implying that the costs of reading are relatively low, at least compared to its benefits. Sometimes, the assumption that reading is an inexpensive self-help measure is stated explicitly, such as when the Wisconsin Supreme Court scolded a plaintiff raising the *Borat* problem for “asking the court to protect him against the wrong of another merely because he failed to take the few moments of time that would have enabled him to protect himself.”¹¹⁵

The remainder of this section contends that the intuition that “reading” is cheap is wrong, at least in the context of the *Borat* problem. That is, at least when the drafting party has already described the salient elements of the proposed deal, reading is not a low-cost way to avoid the risk of opportunist exploitation of non-drafting parties. This realization, in turn, suggests that a pure duty-to-read rule is not necessarily the most efficient solution to the *Borat* problem.

1. Direct Costs of Reading: Complexity and the Confirmation Bias

It has never been a secret that extremely few non-drafting parties read contracts, especially those that are prepared on a standard form and/or

¹¹⁴ See, e.g., *Godfrey, Bassett & Kuykendall Architects Ltd. v. Huntington Lumber & Supply Co., Inc.*, 584 So.2d 1254, 1259 (Miss. 1991) (“parties to an arms length transaction are charged with a duty to read what they sign; failure to do so constitutes negligence”); *Bostwick v. Duncan, Johnston & Co.*, 60 Ga. 383(1878) (refusing to “relieve [the defendant] from [his] gross negligence in making their contracts” when he failed to read and instead relied on the assurances of an agent); *Williston on Contracts* 70:113 (4th ed., 2011) (calling harms suffered from failing to read the consequences of the non-reader’s “own negligence”).

¹¹⁵ *Knight & Bostwick v. Moore*, 234 N.W. 902, 903 (Wis. 1931).

presented on a take-it-or-leave-it basis.¹¹⁶ Recent empirical research has underscored just how uncommon reading actually is. In one study of more than 45,000 households, researchers found that less than 0.2% of customers who purchased retail software over the internet even accessed the terms of the licensing agreement before indicating their agreement to those terms, and most of the members of this select group had the agreement itself opened for too short a period of time to have read very much.¹¹⁷

The evidence of non-reading, notwithstanding the obvious risk of exploitation, strongly suggests that the cost of reading contract terms is far from *de minimis*. The duty-to-read rule came to prominence in a different era, when most written agreements were shorter than they typically are today and standard form contracts were rare.¹¹⁸ In the more complex and standardized environment of 21st century commerce, the time and effort required to read and understand standard form contracts can be substantial, even for sophisticated and educated parties. Further, since standard form contracts are usually drafted by lawyers, the language is often inaccessible to lay people.¹¹⁹ When this is the case, the task of “reading” the standard form actually requires paying a lawyer to review it, a process that is costly even if the contract itself is not long.

When a drafting party makes prior representations about the nature of a transaction, as is the case when the *Borat* problem arises, the common heuristic known as “confirmation bias” can make it difficult for even sophisticated laypeople to identify and understand the significance of contradictions or disclaimers. People tend to search for information in a way that confirms rather

¹¹⁶ See, e.g., Omri Ben-Shahar, The Myth of the ‘Opportunity to Read’ in Contract Law, Univ. of Chicago John M. Olin Law & Economics Working Paper No. 415 at 1 (2008) (“Real people don’t read standard form contracts.”); Russell Korobkin, Bounded Rationality, Standard Form Contracts, and Unconscionability, 70 U. Chi. L. Rev. 1203, 1217 (2003); Todd D. Rakoff, Contracts of Adhesion: An Essay in Reconstruction, 96 Harv. L. Rev. 1174, 1179 (1983); W. David Slawson, Standard Form Contracts and Democratic Control of Lawmaking Power, 84 Harv. L. Rev. 529, 530-31 (1971).

¹¹⁷ Yannis Bakos et al., Does Anyone Read the Fine Print? Testing a Law and Economics Approach to Standard Form Contracts (available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1443256).

¹¹⁸ See, e.g., Corbin on Contracts sec. 29.12 (2010) (noting that the duty-to-read rule is rooted in “bargaining practices of the past, when the self-reliance ethic was strong and standardized agreements were rare.”)

¹¹⁹ See, e.g., Robert A. Hillman & Jeffrey J. Rachlinski, Standard Form Contracting in the Electronic Age, 77 NYU L. Rev. 429, 446 (2002).

than contradicts their prior beliefs about the world.¹²⁰ Perhaps more importantly, when people have in mind only a single hypothesis about some fact in the world, they tend to interpret ambiguous information as supportive of rather than inconsistent with that hypothesis and pay more attention to supportive than counterindicative information.¹²¹ Thus, although it often seems obvious in hindsight that the terms embodied in the signed, written document are inconsistent with a drafting party's prior representations, the inconsistency may be difficult for the non-drafting party to recognize at the time, even when they read the written documents.¹²² This effect is likely to be magnified when the drafting party wishes to mislead the non-drafting party and attempts to leave the smallest possible distance between its oral representations and the later-provided written terms.

The *Borat* case itself illustrates this problem. Twentieth Century Fox agents allegedly told the plaintiffs that the studio was making a documentary film for an Eastern European audience. The written disclaimer then specified that it would use the footage for a "documentary-style film."¹²³ To the district court, able to interpret the written language entirely divorced from the context provided by the surrounding events that the plaintiffs experienced (and already alerted to the dispute that ultimately arose), this language seemed a truthful description of the feature film. *Borat* was not a documentary, of course, but it was presented in the style of a documentary. Thus, the court held that, as a matter of law, "the term 'documentary-style film' is not ambiguous,"¹²⁴ and chastised the plaintiffs for their "unwilling[ness] to recognize that the operative word in the phrase 'documentary-style film' is 'style' and not 'documentary.'"¹²⁵

¹²⁰ See generally Margit E. Oswald & Stefan Grosjean, Confirmation Bias, in *Cognitive Illusions: A Handbook on Fallacies and Biases in Thinking, Judgement and Memory* 79 (Rudiger F. Pohl, ed., 2004); Martin Jones & Robert Sugden, Positive Confirmation Bias in the Acquisition of Information, 50 *Theory & Decision* 59 (2001) (demonstrating the bias when subjects have to pay for information).

¹²¹ See Raymond S. Nickerson, Confirmation Bias: A Ubiquitous Phenomenon in Many Guises, 2 *Rev. of General Psychol.* 175, 177-78 (1998).

¹²² See, e.g., *O'Neil v. Int'l Harvester Co.*, 575 P.2d 862 (1978) (plaintiff interpreted "as is" clause in contract to mean "as the defendant had verbally represented" the truck for sale to be, rather than as it actually was).

¹²³ *Borat Release*, supra note ___, at ¶ 1.

¹²⁴ *Psenicka S.D.N.Y.*, supra note ___, at 14.

¹²⁵ *Id.* at 15.

The problem with such a sterile interpretation of the language is that a person who had been told by an agent of the producer that the project was an actual documentary and had no reason to believe otherwise would be inclined to interpret the text as consistent with that expectation. The natural result would be for a reader to place greater attention on the word "documentary" than the word "style." It does not seem like a stretch to hypothesize that this was exactly the result the studio's lawyers hoped for when they drafted the language.¹²⁶

This does not mean, of course, that it would have been impossible for a very careful reader (or a lawyer with a working hypothesis that the drafting party is seeking to exploit his client) to have recognized the subtle distinction between the term "documentary" and "documentary-like film" and suspected that trickery might be afoot. It is possible, even likely, that other would-be stooges besides the *Borat* plaintiffs did just this and decided not to sign the form and play their assigned roles in front of the cameras. But to have unearthed the deception would have required the *Borat* plaintiffs to make a conscious and determined effort to overcome the heuristics on which the human mind typically relies. This increases the cost of avoiding exploitation, which in turn increases the incentive for drafting parties to attempt to exploit non-drafters.

2. Indirect Costs: Undermining Trust

Many of the terms provided in the boilerplate of standard form contracts deal with unlikely contingencies or are otherwise tangential to the primary purpose of the agreement. Because cognitive limitations on the ability of human beings to process information causes individuals to narrow their focus when making contracting decisions to a relatively small number of "salient" decision attributes, individuals often -- and reasonably -- choose to ignore the content of remaining, "non-salient" attributes, including terms nestled deep within standard form contracts.¹²⁷

Neither the cost of thoroughly reading and understanding standard forms nor the lack of salience of many terms commonly included in boilerplate satisfactorily explains, however, why non-drafters often appear unwilling even

¹²⁶ Cf. Jon D. Hansen & Douglas A. Kysar, Taking Behavioralism Seriously: The Problem of Market Manipulation, 74 N.Y.U. L. Rev. 630, 747 (1999) (arguing that marketers can and will exploit nonrational yet predictable cognitive phenomena).

¹²⁷ Korobkin, Bounded Rationality, *supra* note __, at 1225-34; see also Ronald J. Mann, "Contracting" for Credit, 104 Mich. L. Rev. 899, 911 (2006).

to skim standard form contracts to make sure that they do not contradict or disclaim prior representations that have been made by the drafting party concerning central or salient terms – such as, for example, the nature of the film in which the *Borat* plaintiffs would be appearing. A more promising explanation of the almost resolute determination exhibited by many non-drafting parties to not even quickly peruse written agreements prior to signing is the consequence that reading can have on the bonds of trust between the parties – defined as a willingness to rely on the good faith of another when doing so risks exploitation.

Research in behavioral economics on what is often called the “trust game”¹²⁸ provides some potential insights. In a basic, a-contextual version of the game, one player (the “Trustor”) is provided with a fixed amount of money (the “endowment”) and has the choice of keeping it all or transferring some or all of it to the second player (the “Trustee”). If the Trustor keeps the entire endowment, the game ends. If she transfers some or all of the endowment to the Trustee, the experimenter multiplies the amount transferred by some factor (often by 3). The Trustee then has the choice of keeping the multiplied amount or returning some or all of it to the Trustor, at which point the game ends.¹²⁹

If the Trustor demonstrates trust by taking the risk of transferring part or all of the endowment and the Trustee proves to be trustworthy by returning at least as much as the Trustor risked, the two players create value through their transaction and both can end up better off than if there had been no trust. Notwithstanding this happy possibility, the prediction of game theory is that the players will fail to create this value (at least if the game is a one-shot interaction).¹³⁰ The Trustee will maximize his income by keeping any portion of the endowment he receives from the Trustor – he has nothing to gain by making a return transfer. Realizing this, a rational Trustor will not transfer any of the initial endowment. Consequently, the unique Nash equilibrium of the trust game is for the Trustor to decline to transfer any of the endowment.

In stark contrast to game theoretic predictions, laboratory experiments demonstrate that a large percentage of Trustors do exhibit trust and a large percentage of Trustees reward that trust by returning at least the amount

¹²⁸ The game is also sometimes called the “investment game.” See, e.g., Joyce Berg et al., Trust, Reciprocity, and Social History, 10 *Games & Econ. Beh.* 122 (1995).

¹²⁹ See, e.g., Ernst Fehr & Simon Gächter, Fairness & Retaliation: The Economics of Reciprocity, 14 *J. Econ. Persp.* 159, 162 (2000); Berg et al, *supra* note __, at 123.

¹³⁰ Berg et al, *supra* note __, at 123.

transferred to them, even in one-shot interactions,¹³¹ and even when the stakes are very high relative to the income of subjects.¹³² The propensity to trust increases substantially when players are permitted to exchange verbal communications with one another.¹³³ Presumably this is because Trustees use communication to send signals that they are trustworthy.¹³⁴ In addition, and importantly, exhibiting trust seems to have a positive causal effect on the trustworthiness of Trustees, a relationship sometimes called “trust responsiveness.”¹³⁵ That is, the more trust exhibited by the Trustor, the more that Trustees reward that trust, even though doing so is contrary to their selfish interest.¹³⁶

Other laboratory experiments, modeled on principal-agent relationships, have generated similar findings. In one type of game, “Agents” choose between investments that benefit the “Principal,” whom they represent, and themselves. Principals can allow their Agents complete freedom of action concerning the investment choice or, at a cost, they can choose to “monitor” the Agent’s behavior, which limits the extent to which the Agent can exploit them

¹³¹ See, e.g., Michael Bacharach et al., *The Self-Fulfilling Property of Trust: An Experimental Study*, 63 *Theory & Decision* 349, 353-54 (concluding from a review of the experimental literature that more than half of Trustors demonstrate trust in one-shot games); Catherine C. Eckel & Rick K. Wilson, *Is Trust a Risky Decision?*, 55 *J. Econ. Beh. & Org.* 447, 451 (“previous results from variations on this game indicate that a large fraction of subjects trust by sending some positive amount, and trust is just reciprocated on average”). Results reported in one oft-cited, double-blind study are typical: 30 of 32 Trustors transferred part or all of the endowment, and 16 of 28 Trustees who received at least \$1 returned money, with Trustors who trusted ending the game with slightly more than their initial endowment, on average. Berg et al., *supra* note __, at 131.

¹³² See Fehr & Gächter, *supra* note __, at 162 (experimental income equal to 10 weeks salary).

¹³³ Cf. Daniel Balliet, *Communication and Cooperation in Social Dilemmas: A Meta-Analytic Review*, 54 *J. Conflict Res.* 39, 46-47 (2010) (finding a substantial positive correlation between the ability to communicate and the cooperation in a range of social dilemma games (of which the trust game is one variety), with face-to-face communication have a greater affect than written communication).

¹³⁴ Cf. Eckel & Wilson, *supra* note __, at 461 (finding trusting behavior is positively correlated with the return Trustors expect to receive from Trustees).

¹³⁵ Vittorio Pelligra, *Trust Responsiveness: On the Dynamics of Fiduciary Interactions*, 39 *J. Socio-Economics* 653 (2010); Bacharach et al., *supra* note __, at 355-56;

¹³⁶ See Bacharach et al., *supra* note __, at 371-72, 380.

by selecting investments that disproportionately benefit the Agent. Studies have found that Agent subjects are more likely to make investment choices that benefit the Principal -- at real cost to themselves -- when the Principal subject has placed his payoff at risk by choosing not to monitor the Agent's behavior.¹³⁷

When a Trustor keeps the initial endowment rather than transferring, or when a Principal engages in costly monitoring, he sends a signal that he does not trust his counterpart to refrain from exploitation and instead engage in cooperative, social welfare-enhancing behavior. In contrast, when a Trustor transfers part or all of his endowment, or a Principal allows her Agent free rein, this signals a high degree of trust, which can create a "virtuous circle"¹³⁸ of behavior. The mechanism by which trust affects the extent of cooperative, other-regarding behavior is not entirely clear: it could be that the reciprocity norm encourages similarly-sized transfers,¹³⁹ or that recipients of trust desire to live up to the high expectations (and the implicit compliment) bestowed upon them.¹⁴⁰ Whatever the precise mechanism, the widespread willingness of actors to extend trust in these situations suggests an implicit (and perceptive) calculation that signaling distrust will be more costly than risking

¹³⁷ Armin Falk & Michael Kosfeld, *The Hidden Costs of Control* 96 *Am. Econ. Rev.* 1611, 1617 (2006). These findings support are consistent with the assertions of relational contract theorists that formal contracts can undermine profitable relationships. See, e.g., David Charny, *Nonlegal Sanctions in Commercial Relationships*, 104 *Harv. L. Rev.* 373, 426-30 (1990); Stewart Macaulay, *Non-Contractual Relations in Business: A Preliminary Study*, 28 *Am. Soc. Rev.* 55, 64 (1963).

¹³⁸ Jonathan Baron, *Trust: Beliefs and Morality*, in *Economics, Values and Organisation* 408, 411 (Ben-Ner & Petterman eds., 1998).

¹³⁹ See Berg, *supra* note __, at 132. Cf. Fehr & Gächter, *supra* note __ at 169 (summarizing experimental games in which "workers" expend more costly effort for "employers" who offer higher pay than is necessary to attract them to the job).

¹⁴⁰ Pelligra, *supra* note __, at 655, 657; Falk & Kosfeld, *supra* note __, at 1623 (finding a positive correlation between an Agent's perception of the Principal's expectations and the Agent's actual performance).

exploitation.¹⁴¹ One group of researchers has called this negative consequence of engaging in self-protection “the hidden cost of control.”¹⁴²

When drafting parties make oral representations to non-drafters and then present a standard form contract for signature, the non-drafter is arguably placed in an analogous position to that of Trustors or Principals. By signing the form without reading, the non-drafter signals his trust that the drafter will not exploit him. By reading the document carefully, the non-drafter signals something less than complete trust in his counterpart.¹⁴³ Asking for an extended amount of time to consider the document or seek legal counsel likely increases the negative effect of the signal.

The choice of signals might be particularly important to the future behavior of the parties in the context of contracting between relative strangers. Most people, it turns out, use social cues as a focal point around which to coordinate behavior, exhibiting prosocial behavior when the context seems clearly to call for it and selfish, individualistic behavior when the social context seems to call for it.¹⁴⁴ Arms-length contracting is arguably an ambiguous context¹⁴⁵: a contractual partner is alternately someone with whom you work with to create mutually-beneficial cooperative surplus and someone with whom you compete to appropriate that surplus.¹⁴⁶ Thus, signals of trust or distrust

¹⁴¹ Florian Herold, Contractual Incompleteness as a Signal of Trust, 68 *Games & Econ. Behav.* 180, 187 (2010); Cf. Bacharach *supra* note __, at 370 (explaining that trusting behavior can be explained as Trustors who are students of game theory playing based on the assumption that Trustees are likely not students of game theory).

¹⁴² Falk & Kosfeld, *supra* note __, at 1630.

¹⁴³ Although he did not have the modern social science literature on trust available, Professor Macaulay intuitively recognized 45 years ago the relationship between reading standard forms and discouraging trust, observing that “part of decent social and business conduct is trust,” and that “in many negotiation situations all of the pressures push for friendly gestures rather than a suspicious line-by-line analysis of the writing.” Macaulay, *supra* note __, at 1061.

¹⁴⁴ Lynn Stout, *Cultivating Conscience: How Good Laws Make Good People* 106-110 (2011).

¹⁴⁵ *Id.* at 190-91 (identifying contracting as a context with ambiguous cues concerning whether prosocial or selfish behavior is appropriate).

¹⁴⁶ The tension between the benefits of behaving cooperatively and benefits of behaving competitively in contracting situations is referred to by negotiation theorists as “the negotiator’s dilemma.” See David A. Lax & James K. Sebenius, *The Manager as Negotiator* 29-45 (1986).

conveyed in this context are likely to have a larger-than-usual impact on their counterpart's mental determination of whether the situation calls for prosocial or selfish behavior.

Unlike the situation in the Trust Game or the Principal-Agent Game, in the case of the *Borat* problem, the non-drafter's trust signal cannot affect the drafter's immediate choice of whether or not to exploit. In the *Borat* case itself, for example, the fraudulent statements about the nature of the film and the interviewer had already (allegedly) been made at the time the plaintiffs affixed their signatures to the producer's standard form. But few contracts involve one-time, spot transactions. Most agreements require one or both parties to expend post-contractual effort, and many require joint efforts, in order to satisfy the goals of the agreement. In these circumstances, bonds of trust are likely to increase the chances that parties will engage in cooperative behavior that both maximizes the value of the deal and builds a basis for profitable cooperation in the future.¹⁴⁷

Although contractual completeness reduces uncertainty and the risk of misunderstandings,¹⁴⁸ some empirical research has found that it can also lead to lower levels of trust between contracting parties.¹⁴⁹ As one group of researchers concludes, suggestions by a contracting party that more detail or more clauses be added to a contract can convey he is more concerned about his own risks than about the relationship, which can "crowd out rapport and undermine

¹⁴⁷ See generally G. Richard Shell, *Opportunism and Trust in the Negotiation of Commercial Contracts*, 44 *Vand. L. Rev.* 221, 226 (1991) (identifying trust as the key to successful commercial dealings); Kenneth Arrow, *Gifts and Exchanges*, 1 *Philosophy & Public Aff.* 343, 357 (1972) ("Virtually Every commercial transaction has within itself an element of trust, certainly any transaction conducted over a period of time").

¹⁴⁸ See Cross, *supra* note ___, at 1501-02 (describing this virtue of contracting).

¹⁴⁹ See Deepak Malhotra & Fabrice Lumineau, *Trust and Collaboration in the Aftermath of Conflict: The Effects of Contract Structure*, -- *Acad. Mgmt. J.* -- (201x) (draft at 24) (finding more indications of "goodwill-based trust" between real contracting parties involved in a dispute when their contracts contained fewer "control provisions" that specify legal constraints on the relationship); Eileen Y. Chou et al., *The Relational Costs of Complete Contracts*, draft at 15 (finding lower levels of trust in experimental context when a contracting partner proposed more rather than less specific contract terms). It is likely that the affect on trust on contractual completeness is highly dependent on context. Other studies have concluded that contractual completeness can enhance trust. See, e.g., Laura Poppo & Todd Zenger, *Substitutes or Complements: Exploring the Relationship Between Formal Contracts and Relational Governance*, 23 *Strat. Mgmt. J.* 707 (2002).

trust.”¹⁵⁰ This, in turn, can lead to lower levels of cooperative behavior in subsequent interactions. One experiment found that when a contracting partner proposed a more, rather than less, specific set of contract terms, his counterparts chose less cooperative strategies on average in a game the two subjects subsequently played with each other in which cooperation could increase joint rewards but risked exploitation.¹⁵¹ Similarly, the decision to read the text of a standard form contract in the face of a prior description of the deal’s salient terms risks undermining the trust between the parties by privileging legal over relational constraints on behavior, threatening the potential for future cooperation. Such a reduction in the expected long-term social welfare of the contractual relationship makes the indirect cost of reading potentially very high.

In addition, unlike the direct costs of reading, the indirect costs associated with distrust are not inversely related to the value of the deal or the brevity of the signed writing. From a transaction cost perspective, although it might be reasonable for a non-drafting party to choose not to read (or not to hire a lawyer to review) a long standard form agreement concerning the purchase of a trinket, a pure duty-to-read rule seems more justified when an individual is purchasing a house or a business is completing a merger, or if a drafter provides a one page rather than a 100 page term sheet for even a relatively less important transaction. (Recall that the standard consent form proffered to the *Borat* plaintiffs was only one page long.) The signal of distrust sent by reading the form to verify the veracity of prior oral representations, however, increases in costliness as the potential value of the deal or the relationship increases, because the distrust places a potentially more valuable opportunity at risk.

The literature on economic development suggests a strongly positive correlation between a society’s level of generalized social trust (belief that other citizens will act honestly and nonexploitatively)¹⁵² and economic growth,¹⁵³ as

¹⁵⁰ Eileen Y. Chou et al., *The Relational Costs of Complete Contracts*, draft at 4; see also Malhotra & Lumineau, *supra* note __, draft at 27; Malhotra & Murnighan (2002); Cf. S.B. Sitkin & A. L. Roth, *Explaining the Limited Effectiveness of Legalistic “Remedies” for Trust/Distrust*, 4 *Org. Sci.* 367, 376 (1993) (“legalistic remedies can erode the interpersonal foundations of a relationship...because they replace reliance on an individual’s good will with objective, formal requirements”).

¹⁵¹ Chou et al., *supra* note __, draft at 19-20 (study 3).

¹⁵² Christian Bjornskov, *Determinants of Generalized Trust: A Cross Country Comparison*, 130 *Public Choice* 1 (2007).

¹⁵³ Stephen Knack & Philip Keefer, *Does social Capital Have an Economic Payoff: A Cross-Country Investigation*, 112 *Q. J. Econ.* 1251 (1997) Knack & Keefer, 112 *QJE* 1251, 1260 (1997); Paul J. Zak & Stephen Knack, *Trust and Growth*, 111 *Econ. J.* 295,

trust reduces both the risks of being exploited and the cost of monitoring one's contracting partners.¹⁵⁴ The usual lesson derived from this relationship is that dependability of the rule of law is necessary for economic efficiency: few will trust the promises of strangers, for example, in the absence of a legal system that enforces contracts.¹⁵⁵ When parties can count on enforcement of their contracts, this reduces the risk of exploitation by potential non-performers, and makes trusting safer. Similarly, if a no-exploitation rule protects non-drafting parties from opportunistic drafters tempted to say one thing and write down another, it becomes less risky for non-drafters to extend – and thus build -- trust by passing up the opportunity to carefully compare the signed writing to prior representations.¹⁵⁶ This, in turn, should help to increase social trust and thus the efficiency of contractual relationships.

3. Costs of “Bait and Switch”: The Status Quo Bias

A different reason that non-drafting parties often cannot avoid actual exploitation at low cost merely by “reading” standard forms is that false representations can increase the costs of later declining to sign the written document.

One of the best known findings of research in behavioral decisionmaking is that individuals usually display a preference for the status quo state of the world, all other things being equal, as opposed to alternative states of the world.

307-09 (2001). Troublingly, social trust appears to have been in steep decline in the United States for the last half century. Robert Putnam, *Bowling Alone: The Collapse and Revival of American Community* 140-44 (2002) (tracing the decline in trust since 1962).

¹⁵⁴ Zak & Knack, *supra* note __, at 305.

¹⁵⁵ See, e.g., Martin Leschke, *Constitutional Choice and Prosperity: A Factor Analysis*, 11 *Const. Pol. Econ.* 265, 277 (2000); Ismail Serageldin & Christiaan Grootaert, *Defining Social Capital: An Integrating View*, in *Social Capital: a Multifaceted Perspective* at 40, 50 (attributing Chili's superior economic performance to Brazil in part on the more reliable enforcement of contracts in the former); See generally Douglass North, *Institutions, Institutional Change, and Economic Performance* 54 (1990) (attributing Third World economic stagnation to the failure to develop institutions for the low-cost enforcement of contracts).

¹⁵⁶ Cf. Frank B. Cross, *Law and Trust*, 93 *Geo. L. J.* 1457, 1466 (2005) (“by giving legal assurances of remedies for breaches of trust, the law makes parties more likely to be both trusting...and trustworthy...”).

Known as the "status quo bias,"¹⁵⁷ or often as the "endowment effect,"¹⁵⁸ this behavioral finding is in turn a consequence of "loss aversion" – people usually experience more pain from losing something than they experience pleasure from gaining something of equivalent value.¹⁵⁹ Numerous laboratory and real-world experiments¹⁶⁰ have demonstrated findings such as the following: people demand more money to sell a small consumer item that is given to them than they would pay to buy that same item with money that is given to them¹⁶¹; drivers are unlikely to choose no-fault insurance if fault-based insurance is the default option but they are also unlikely to choose fault-based insurance if no-fault is the default option¹⁶²; most employees fail to opt-in to their employer's 401K plan, but most employees do not opt-out if enrollment is automatic; parties considering a contract demand more to agree to change a form contract from a more desirable to a less desirable term than they are willing to pay to change from the less desirable term to the more desirable one.¹⁶³

By making representations that are favorable to the non-drafting party early in negotiations and then contradicting or disclaiming them in the final written document, drafting parties can use the status quo bias to increase the likelihood that non-drafting parties will agree to the written terms, even if they understand that the original representations are being disclaimed. Again, the *Borat* case provides a useful illustration. When originally contacted by Twentieth Century Fox, the *Borat* plaintiffs had no expectation of either the income or the non-financial utility that they could obtain by sharing their

¹⁵⁷ William Samuelson & Richard Zeckhauser, Status Quo Bias in Decision Making, 1 J. Risk & Uncertainty 7 (1988).

¹⁵⁸ Richard Thaler, Toward a Positive Theory of Consumer Choice, 1 J. Econ. Behav. & Org. 39, 44 (1980).

¹⁵⁹ Amos Tversky & Daniel Kahneman, Loss Aversion in Riskless Choice: A Reference-Dependent Model, 106 Q. J. Econ. 1039 (1991).

¹⁶⁰ For a survey of the literature and an application to a range of legal issues, see Russell Korobkin, The Endowment Effect and Legal Analysis, 97 Nw. U. L. Rev. 1227 (2003).

¹⁶¹ Daniel Kahneman et al., Experimental Tests of the Endowment Effect and the Coase Theorem, 98 J. Pol. Econ. 1325 (1990).

¹⁶² David Cohen & Jack L. Knetsch, Judicial Choice and the Disparities Between Measures of Economic Values, 30 Osgood Hall L.J. 737, 747 (1992).

¹⁶³ Russell Korobkin, The Status Quo Bias and Contract Default Rules, 83 Cornell L. Rev. 608, 611 (1998).

respective expertise on camera. There is little doubt that, at this time, they viewed the producer's proposition as a potential "gain" vis-à-vis the status quo. At the time that the studio's agents presented them with the standard form to sign -- long after reaching an oral agreement concerning the terms of the encounter, scheduling the film shoot, and planning for it -- it is probable that the plaintiffs viewed the opportunity as part of their endowment. Although it was possible for the plaintiffs to refuse to sign the waiver and simply walk away, doing so would have meant accepting a loss from the presumed status quo position, making it psychologically more costly to decline to participate at this point than it would have been at the time of first contact.

Just as the principle of loss aversion causes most people to place a higher value on protecting their endowment from a loss than adding to it with a gain, it causes people to assume risks to avoid losses that they would not be willing to accept for the possibility of obtaining an equivalent gain. This empirical finding suggests that even if the *Borat* plaintiffs realized that the inconsistencies and disclaimers in the written release suggested that *Borat* and his project might not be precisely as they had been represented previously, they would be more likely to accept these risks at the time of filming than had they been asked to sign the same document at the time of the original contact, before internalizing the *Borat* opportunity as part of their endowment.

4. Legal Protection

The preceding analysis can be understood as demonstrating that "reading" makes it possible for non-drafting parties to avoid exploitation, but the direct and indirect costs of reading standard form contracts -- especially in the face of prior representations concerning the salient elements of the proposed deal -- can be substantial. This, in turn, increases the likelihood that reasonable non-drafters will decline to read standard forms at all, a result consistent with widespread anecdotal observation and some rigorous scholarship. But this result, of course, means that non-drafters will usually either sign forms without reading (creating an incentive for drafters to exploit them) or simply decline to consider potentially profitable deals that carry a perceived risk of exploitation (creating a dead-weight loss).

III. ADDRESSING THE *BORAT* PROBLEM

In the context of the *Borat* problem, a pure duty-to-read rule encourages the exploitation of non-drafting parties, and a no-exploitation rule encourages

exploitation of drafting parties. Either rule reduces the expected social value of contracting.

Conceptually, the optimal way to confront the *Borat* problem is to structure the law such that it minimizes the joint costs of opportunistic exploitation and protecting against such opportunistic exploitation. Non-drafting parties should be permitted to introduce evidence of prior inconsistent representations when the risk that judges and jurors will err in determining that such representations were actually made is low relative to the cost that non-drafting parties would have had to expend to avoid relying on the misrepresentations. Drafting parties, in turn, should be able to exclude such evidence in favor of the final written terms when it would be difficult for them to protect themselves against exploitation compared to the risk that the judicial process would errantly find false representations when none were actually made.

A. Costs of Contracting vs. Costs of Judicial Error

Most attempts by courts and scholars to wrestle with the *Borat* problem are flawed because they privilege the risks of exploitation on one side of the equation while downplaying or ignoring the countervailing risks. Two Seventh Circuit cases, authored by Judges Richard Posner and Frank Easterbrook, provide examples of analyses that seem to be concerned only the risks to drafting parties. In *Carr v. CIGNA Securities, Inc.*,¹⁶⁴ the plaintiff alleged that he relied on the defendant's agent's representation that an investment was safe and did not read the form disclosures that warned the investment was risky.¹⁶⁵ In dismissing the plaintiff's claim, Judge Posner held that the written document must govern or "sellers would have no protection against plausible liars and gullible jurors."¹⁶⁶ In *Rissman v. Rissman*, the plaintiff challenged his agreement to sell his stock in a family-owned company to his brother when the brother's prior representation proved to be false.¹⁶⁷ In enforcing the written agreement, which disclaimed the existence of any external statements or

¹⁶⁴ 95 F.3d 544 (7th Cir. 1996).

¹⁶⁵ *Id.* at 545.

¹⁶⁶ *Id.* at 547. This is notwithstanding Judge Posner's recognition in other contexts that the cost of avoiding exploitation can be high: "[n]ot all persons are capable of being careful readers." *Emery v. Am. Gen. Finance, Inc.*, 71 F.3d 1343, 1346 (7th Cir. 1995).

¹⁶⁷ 213 F.3d 381 (7th Cir. 2000).

inducements, Judge Easterbrook pointed out that writings are "less subject to the vagaries of memory and the risks of fabrication."¹⁶⁸

Analyses that favor non-drafting parties, in contrast, tend to see the risks faced by non-drafter clearly but ignore the very real risks faced by drafters.¹⁶⁹ Professors Deborah Stark and Jessica Choplin, for example, oppose the enforcement of no-reliance clauses against claims that the agreement was induced by false oral representations on the grounds that such a rule "grant[s] a license to deceive to unscrupulous companies."¹⁷⁰ Professor Robert Prentice argues, in the specific context of securities transactions, that waivers of liability for fraud and no-reliance clauses should be unenforceable because they encourage false oral representations.¹⁷¹

When attempts are made to address both sides of the opportunism coin simultaneously, the most commonly proposed solution is to draw a bright line between fully-negotiated contracts between "sophisticated" parties (perhaps only when represented by counsel) and standard forms presented as contracts of adhesion to consumers or other "unsophisticated" parties.¹⁷² In the former class of cases, the terms of the signed writing would be enforced scrupulously against any claims of prior inconsistent or misleading statements. In the latter class of cases, non-drafting parties would be permitted to recover damages by using parol evidence to prove to a jury that the drafting party made inconsistent prior statements or promises.

The Delaware courts have attempted to draw precisely this line. In a detailed and wide-ranging decision, Chancellor Strine invoked the "American tradition of freedom of contract, ... especially strong in our State, which prides itself on having commercial laws that are efficient," in defense of a line of cases

¹⁶⁸ *Id.* at 384.

¹⁶⁹ *Downs v. Wallace* 622 So. 2d 337, 341 (Ala. 1993); *Gloucester Holding Corp. v. U.S Tapes*, 832 A.2d 116, 124-25 (Del. 2003).]

¹⁷⁰ Stark & Choplin, *supra* note __.

¹⁷¹ Robert Prentice, *Contract-Based Defenses in Securities Litigation: A Behavioral Analysis*, 2003 U. Ill. L. Rev. 337, 419.

¹⁷² See, e.g., West & Lewis, *supra* note __, at 1033-34 ("Contracts made between sophisticated parties, represented by counsel...are fundamentally different from the adhesion contracts made by consumers who buy cars, rent jet skis, or sign consents allowing their children to participate in rafting excursions"); Stark & Choplin, *supra* note __, at 624 (arguing against enforcement of written no-reliance and waiver clauses except when terms are negotiated by attorneys representing "sophisticated" parties in "commercial transactions.");

that enforces no-reliance and no-representation clauses against fraud claims when the contracts are "between sophisticated parties with equal bargaining strength."¹⁷³ Strine distinguished apparently conflicting precedent that refused to permit "[a] perpetrator of fraud...to close the lips of his innocent victim by getting him blindly to agree in advance not to complain about it"¹⁷⁴ as "involv[ing] the protection of a relatively unsophisticated party or a party lacking bargaining clout who signs a contract with a boilerplate merger clause."¹⁷⁵

Arguably, the New York courts have attempted to draw the same line. In *Cirillo v. Slomin's Inc.*, the New York Court of Appeals refused to enforce a no-representation clause appearing in the signed writing to block an alarm system customer's claim that the defendant's salesman made false statements about the system's capabilities.¹⁷⁶ In doing so, it distinguished *Danann Realty* by observing that that case involved "sophisticated business people."¹⁷⁷ (Notably, neither the Southern District of New York nor the Second Circuit discussed this potential distinction, which would have cut in favor of the plaintiffs, when issuing unpublished opinions and orders in favor of the defendant in the *Borat* case.)

This approach is attractive because it takes seriously both the efficiency benefits of allowing informed parties to structure their transactions as they see fit and the dubious nature of the assent provided by non-drafting parties to written terms in many cases. It also captures the reasonable intuition that the direct costs associated with reading written agreements are relatively lower for sophisticated parties with legal counsel (who can interpret them better and faster), and the indirect harm caused to the relationship is likely to be less when the reader can blame what might look like distrustful behavior on his lawyer or business custom.

The strict divide is problematic, however, because, like most bright-line rules, the categories it seeks to define are over- and underinclusive in relation to the distinction that it implicitly seeks to recognize.¹⁷⁸ Many contracts are not

¹⁷³ *Abry Partners V, L.P. v. F & W Acquis. LLC*, 891 A.2d 1032, 1059-60 (2006).

¹⁷⁴ *Id.* at 1061 (quoting *Webster v. Palm Beach Ocean Realty Co.*, 139 A. 457, 460 (Del.Ch. 1927).

¹⁷⁵ *Id.*

¹⁷⁶ 768 N.Y.S. 2d 759 (2003)

¹⁷⁷ *Id.* at 767.

¹⁷⁸ Russell Korobkin, *Behavioral Analysis and Legal Form: Rules v. Standards Revisited*, 79 *Or. L. Rev.* 23, 36-37 (2000).

fully negotiated or fully boilerplate, and it is possible that even sophisticated parties can be surprised by written terms that are inconsistent with prior representations. On the other hand, even relatively unsophisticated, non-drafting parties (often consumers) would find it in their interest, in some circumstances, to be able to consent to disclaimers of prior representations.

In the remainder of this Part, I contend that the legal system can better respond to the challenge of minimizing the two-sided opportunism made possible by the *Borat* problem with a more nuanced approach than the sophisticated/unsophisticated dichotomy allows.

B. Protecting Non-Drafting Parties: Specific Assent

All parties, whether sophisticated or unsophisticated, businesses or consumers, should have the ability to agree to a contract in which representations or promises made in the final written document override some or all prior statements, as long as both parties determine that such a contract serves their interests. As described above, there are several reasons that such agreements can minimize the joint costs of contracting and preventing opportunism, and thus can maximize the welfare of both drafting and non-drafting parties.

The concern with a preference for the signed writing over prior representations -- and what makes the opportunism allegedly practiced by Twentieth Century Fox in *Borat* possible -- is that non-drafting parties often do not determine that the terms included in the signed writing are in their best interest. The problem lies in the disconnect between the degree to which non-drafting parties subjectively assent to contract terms and the assent that the law, based on objective indicia, usually presumes. This disconnect can be repaired by requiring a higher level of assent to form contract terms that contradict or disclaim prior representations.

It is no doubt impractical to impose a heightened standard of assent for all terms found in standard form contracts. Most terms buried in fine print are relevant only to unlikely contingencies and are of little interest to non-drafting parties, making it rational for them to avoid spending the time reading and understanding them.¹⁷⁹ Many are also adhesive, so understanding them would provide no benefit to inframarginal parties who would agree to the contract almost completely regardless of their content. Forcing non-drafting parties to bear the transaction costs of reading and understanding boilerplate is inefficient

¹⁷⁹ See, e.g., Ben-Shahar, *supra* note ___, at 18.

when those parties would prefer to remain uninformed.¹⁸⁰ In addition, a significant deadweight loss would result from any rule that attempted to force the rationally ignorant to bear these costs, as many non-drafting parties would choose to walk away from potentially Pareto efficient transactions rather than tangle with the boilerplate. For these reasons, although a case can be made for replacing boilerplate with law-provided, gap-filling terms,¹⁸¹ there is at the very least a plausible argument for giving effect to standard form terms that are not otherwise addressed by the parties based on the principle of blanket assent.

The case for enforcement based on the principle of blanket assent is much less convincing, however, when the written terms are inconsistent with prior representations made by the drafting party. When a term appearing in a signed writing conflicts with or disclaims a prior representation, that resulting difference is highly likely to be material to the allegedly misled party. If the content of a particular representation were not material, at least to many non-drafting parties, why would drafters have gone to the trouble to make the representation? It follows that written terms that are inconsistent with or completely disclaim earlier representations or promises are also likely to be material. Unlike boilerplate that concerns arcane issues or remote contingencies, when material terms are at issue, the transaction costs associated with non-drafting parties reading and understanding the terms will usually be justified.

The problem is that, short of reading and understanding the entire standard form contract, which is both costly¹⁸² and can signal distrust,¹⁸³ non-drafting parties will not know which terms they should target with their limited attention. The solution is to incentivize drafting parties to call the attention of non-drafting parties to such terms, reducing the direct cost of reading and avoiding the signal of distrust. This can be done by requiring drafters to obtain

¹⁸⁰ Cf. W. David Slawson, Standard Form Contracts and Democratic Control of Lawmaking Power, 84 Harv. L. Rev. 529, 552 (1971) (“Under what conceivable calculus of social value...would it be worthwhile to raise the price of a ten-cent consumer product enough to cover the cost of individually negotiating the warranty of each one sold?”).

¹⁸¹ Such terms could be provided ex ante, in the form of default terms that cannot be superseded unless terms are individually dickered, or ex post, in the form of courts selecting gap-fillers that maximize social welfare when disputes arise. See generally Korobkin, supra note __, at 1247-55.

¹⁸² See Part II.B.1, supra.

¹⁸³ See Part II.B.2, supra.

the objective manifestation of specific assent on the part of non-drafters to the terms in question.

1. Clear Statement

To satisfy the specific assent standard, drafting parties should be able to enforce terms in a signed writing that are inconsistent with prior oral or written statements only if they can satisfy two requirements. First, the text of the written document must clearly indicate that it takes precedent over specific prior representations or, at least, a specifically-defined category of prior statements. I refer to this as the "clear statement" requirement.

Some courts already require something enforce something akin to a clear statement requirement before they will enforce no-reliance or no-representation clauses against claims of fraudulent inducement. In *Danann Realty*, for example, the New York Court of Appeals dismissed the plaintiff's allegation that the defendant made false oral representations concerning the building's operating expenses and profitability because the signed writing included a disclaimer of any representations "as to the physical condition, rents, leases, expenses, [and] operations" of the building. A general merger clause, the court opined, would not have been sufficient to trump the plaintiff's claim of prior false statements about the building's existing income and expenses.¹⁸⁴ Other courts, however, do not demand a clear statement as to exactly what type of representations are being disclaimed or superseded, allowing very broad no-representation or no-reliance clauses to trump the implications of any prior representations.¹⁸⁵

2. Realistic Notice

Second, there must be evidence that the non-drafter was presented with information that place a reasonable party on notice of the written term, taking into account the reality that virtually no one attends to the entire collection of boilerplate in standard form contracts. I call this the "realistic notice" requirement. The requirement would be satisfied if the term in question that contradicts or disclaims prior representations were actively negotiated, rather

¹⁸⁴ *Danann Realty*, 147 N.E.2d at 598-600; see also *Envtl. Sys., Inc. v. Rexham Corp.*, 624 So.2d 1379, 1384 (Ala. 1993); *LaFazia v. Howe*, 575 A.2d 182, 185-86 (R.I. 1990).

¹⁸⁵ See, e.g., *MBIA Ins. Corp. v. Royal Indem. Co.*, 426 F.3d 204, 216, 218 (3d Cir. 2006) (enforcing a "broad" waiver of reliance after specifically finding that "specificity" is not legally required under Delaware law).

than adhesive.¹⁸⁶ Thus, this requirement is consistent with the view of courts that have held that no-reliance clauses are enforceable only in the context of sophisticated parties and negotiated contracts. But parties should be able to satisfy the the requirement by other means as well; there is no good reason that non-drafting parties should be categorically precluded from consenting to such terms just because they happen to be written on a standard form, even if the form is adhesive.¹⁸⁷

One way for the drafting party to provide realistic notice in such a situation might be to obtain a separate signature from the non-drafting party acknowledging the content of that particular term. Separate signature (or separate initialization) requirements, are sometimes used as tools by consumer protection statutes to ensure the specific assent by non-drafting parties to terms considered to be particularly likely to be unanticipated or surprising, while still ultimately allowing for freedom of contract.¹⁸⁸ Because it is generally reasonable for non-drafting parties to rely on prior representations made by drafting parties, the rescission or disclaimer of such representations is exactly the type of term that has potential to be surprising, as well as material.

Obtaining a separate signature should be understood only as one potential means of satisfying the realistic notice standard, not a bright-line safe harbor. When a separate signature is obtained for one or two paragraphs of boilerplate, it is reasonable to conclude the non-drafter knows what is in those paragraphs. One recent study found that a large majority of student subjects admit that they will not read standard form contracts of various types in their entirety, but most claim a willingness to read or skim at least a portion of such contracts.¹⁸⁹ If a

¹⁸⁶ See *Forest Oil Corp. v. McAllen*, 268 S.W.3d 51, 60 (Tex. 2008) (identifying the fact that the waiver term appearing in the writing was actually negotiated as favoring its enforcement against a fraud claim)

¹⁸⁷ Cf. *Schlumberger Technology Corp. v. Swanson*, 959 S.W.2d 171, 179-81 (Tex. 1997) (holding that several factors – including but not limited to party sophistication and whether the term was negotiated – should be taken into account in determining whether a disclaimer of reliance is binding).

¹⁸⁸ See, e.g., Cal.Civ.Code sec. 1677 (requiring liquidated damages provisions in real property transactions to be separately signed or initialed). The failure to obtain the separate assent renders the term voidable. *Guthman v. Moss*, 150 Cal.App.3d 501, 512 (Cal.App. 1984).

¹⁸⁹ Shmuel I. Becher & Esther Unger-Aviram, *The Law of Standard Form Contracts: Misguided Intuitions and Suggestions for Reconstruction*, 8 DePaul Bus. & Com. L. J. 199, 213 (2010) (between 8 and 25% of subjects said they would read a car rental, bank

drafting party asks the non-drafter to hastily initial every paragraph in a long document, however, there is little reason to believe a reasonable non-drafter would recognize the presence and understand the consequence of no-reliance, no-representation, or waiver clauses. For the realistic notice requirement to serve its purpose, courts need to ensure drafters cannot satisfy it by requiring ministerial acts that increase the transaction costs of contracting without actually increasing the non-drafter's understanding of terms that are highly likely to be material to the transaction.

3. The *Borat* Litigation

Under the specific assent standard, as outlined above, Twentieth Century Fox arguably would satisfy the requirement in two instances but not in a third.

The statement in the Standard Consent Form that non-drafting party will not bring future claims of "fraud (such as any alleged *deception or surprise about the Film* or this consent agreement)"¹⁹⁰ provides a clear statement that the studio was not standing behind prior statements about the nature of the film. Similarly, the no-reliance clause arguably provides a clear statement when it specifies that the "Participant is not relying upon any promises or statements made by anyone *about the nature of the Film or the identity of any other Participants or persons involved* in the film," although this language would more certainly satisfy the clear statement requirement if it referred "to the identity of the reporter" rather than the "identity of any other Participant or persons." The statement that the studio was filming a "documentary-style...motion picture" using "entertaining content and formats" would not satisfy the clear statement requirement, however, because this language does not make clear that this description overrides any prior statements about the nature and intended audience of the film. Without presenting such a contrast, it is likely that signatories would interpret this clause as being consistent with the prior oral claims about the nature of the movie.

Regardless of whether the clear statement standard was met, Twentieth Century Fox would have failed to satisfy the realistic notice requirement, because it could provide no objective evidence that the plaintiffs assented to these specific terms. Although a jury could determine, based on the testimony of all parties and the circumstances surrounding the agreement, that the best interpretation of the agreement is one in which the plaintiffs agreed to appear in

account, or laundry contract thoroughly, while half or more said they would skim or read parts of the contract).

¹⁹⁰ Borat Release, *supra* note ___, at ¶ 4.

any "documentary-style film" the studio might produce, Twentieth Century Fox should not be entitled to judgment on the pleadings or at the summary judgment stage.

C. Consistency with Established Doctrine

The specific assent approach not only promotes efficiency by guarding against the exploitation of non-drafting parties at a reasonable transaction cost, it enables courts to resolve the *Borat* problem with fidelity to basic doctrinal principles of contract law concerning both interpretation and enforceability of contracts.

1. Contract Interpretation.

A foundational principle of contract interpretation, as established in Section 201 of the Restatement (Second) of Contracts, is that when contracting parties attach different meanings to an agreement or term therein, the meaning attached by one party governs where that party had no reason to know that the counterpart attached a different meaning but the counterpart had reason to know of the meaning attached by the party.¹⁹¹ To be sure, this principle is most often invoked when the parties agree that certain contractual language governs their respective rights and responsibilities but disagree over the meaning that should be attributed to that language.¹⁹² The principle is just as applicable, however, when the disagreement concerns which language should govern: the language of prior oral representations or subsequent written provisions. When a drafting party makes an oral representation that it then contradicts or disclaims in the written documentation, in the absence of specific assent to the disclaimer, the drafter has reason to know that its interpretation of the contract is not shared by the non-drafting party, whereas the non-drafting party would have no reason to be aware of the dissociation.

This general principle is reflected in the more specific doctrine of "reasonable expectations," which provides that the court's interpretation of a contract should be consistent with the reasonable expectations of non-drafting

¹⁹¹ Restatement (Second) Contracts 201(2)(b).

¹⁹² See, e.g., *Johnston v. Comm'n of Internal Revenue*, 461 F.3d 1162, 1165 (9th Cir. 2006); *Centron DPL Co., Inc. v. Tilden Financial Corp.*, 965 F.3d 673, 675 (1992); *Foundation Int'l v. E.T. IGE Construction, Inc.* 78 P.3d 23, 33-34 (Ha. 2003);

parties, even when this is at odds with the boilerplate, if carefully studied.¹⁹³ A staple of insurance contract interpretation, the reasonable expectations doctrine has not been widely adopted in other contexts, largely because of the difficulties both with identifying the circumstances in which a non-drafting party might reasonably expect a different bargain than what is recorded in the signed writing and with determining what the terms of that different bargain might reasonably be understood to be.

Because many types of insurance contracts are ubiquitous, the reasonable expectations of a purchaser in that context can be evaluated on the basis of commercial standards. That is, absent specific assent to some different set of terms, the purchaser of a general liability insurance policy might reasonably expect that his policy will protect him against hazards commonly insured by similar policies. At the same time, knowing that insurance customers usually lack actual knowledge as to the content of complicated provisions, insurance sellers are on notice that their buyers understand the transaction to protect them against the standard hazards. When specific oral representations or promises are made to a non-drafting party, the content of those statements also provides an objective basis for determining what expectations the non-drafting party might reasonably possess that are inconsistent with the subsequent written document (i.e., expectations that were created by the oral representations and not contradicted or retracted with specific notice).

2. Defenses to Enforcement

In most jurisdictions, a finding that a term appearing in a signed writing is unconscionable, and therefore unenforceable, requires both a finding of imperfections in the bargaining process, known as “procedural unconscionability,” and an unfairly one-sided term, known as “substantive unconscionability.”¹⁹⁴ One indicia of procedural unconscionability¹⁹⁵ is that a

¹⁹³ See Robert Keeton, *Insurance Law Rights at Variance with Policy Provisions*, 83 *Harv. L. Rev.* 961, 966-67 (1970).

¹⁹⁴ See, e.g., *Harris v. Green Tree Financial Corp.*, 183 F.3d 173, 181 (3d Cir. 1999); *Williams v. Walker-Thomas, Furniture Co.*, 350 F.2d 445, 449 (D.C. Cir. 1965); *Armendariz v. Foundation Health Psychcare Services, Inc.*, 24 Cal.4th 83 (2000); see also Arthur Allen Leff, *Unconscionability and the Code – The Emperor’s New Clause*, 115 *U. Pa. L. Rev.* 485, 497 (1967) (coining the terms).

¹⁹⁵ The other indicia of procedural unconscionability is that the complaining party had “no real choice” but to assent to an unfavorable term. See, e.g., *Williams*, 350 F.2d at 449.

non-drafting party is “unfairly surprised” by the content of the term in a form that he signed.¹⁹⁶ Courts are most likely to find the “unfair surprise” requirement is met when it is physically arduous for the complaining party to learn the content of a written term – such as when the font size is small,¹⁹⁷ the term is buried in long list of terms that the party has limited time to read,¹⁹⁸ or when the term is written in confusing language or “legalese.”¹⁹⁹ Courts also have invoked the unfair surprise safeguard, however, when non-drafting parties are given insufficient notice that a document contains the type of term in question. For example, one federal district court found unfair surprise, and thus procedural unconscionability, when the letter in which a telephone company’s modified terms appeared began by stating “please be assured that your AT&T service or billing will not change...there’s nothing you need to do.”²⁰⁰

An unqualified and unretracted oral representation or promise, like a written statement assuring that service will not change, implies that its recipient need not fear a subsequent written document will modify prior agreements or representations. The recipient might be wise to read and understand the document, when he can do so at reasonable cost, in order to learn how the contract will deal with issues not previously discussed, but language that contradicts or disclaims prior representations easily fits within the rubric of unfair surprise.

A successful claim of unconscionability also requires a judicial finding of “substantive unconscionability,” however. This standard, which courts have uniformly resisted defining with a list of clear triggering facts, requires that the term or terms at issue be not merely unfavorable to the complaining party but generate a high degree of opprobrium in the mind of a neutral reader. Courts have variously described the requirement as that the term be “overly harsh” or “one-sided,”²⁰¹ “unreasonably favor[able] to one party,”²⁰² “shock[ing to] the

¹⁹⁶ See, e.g., *Ting v. AT&T*, 182 F.Supp. 902, 929 (N.D. Cal. 2002) (finding evidence of surprise satisfies the procedural unconscionability requirement.)

¹⁹⁷ See, e.g., *John Deere Leasing Co. v. Blubaugh*, 636 F.Supp. 1569, 1574 (D. Kan. 1986); *East Ford, Inc. v. Taylor*, 826 S.2d 709, 716-17 (Miss. 2002); *Philadelphia Indemnity Ins. Co. v. Barerra*, 21 P.3d 395, 402 (Az. 2000).

¹⁹⁸ See, e.g., *Villa Milano Homeowners Assoc. v. Il. Davorge*, 102 Cal. Rptr. 2d 1, 7 (2001); *Kinney v. United Healthcare Services, Inc.*, 83 Cal. Rptr. 2d 348, 353 (1999).

¹⁹⁹ See, e.g., *Blubaugh*, 636 F.Supp. at 1574; *Bank of Indiana NA v. Holyfield*, 476 F.Supp. 104, 111 (S.D. Miss. 1979); *Kinney*, 83 Cal. Rptr. 2d at 553.

²⁰⁰ *Ting*, 182 F.Supp.2d at 913.

²⁰¹ See, e.g., *Armendariz v. Foundation Health Psychcare*, 6 P.3d 669, 690 (Ca. 2000)

conscience,”²⁰³ or “so oppressive that no reasonable person would make them”²⁰⁴

Absent content, there is nothing obviously objectionable about purchasing a party’s performance in a “documentary-style film” (even one that is not, in fact, a documentary), nor would a waiver of legal claims or even a no-reliance clause “shock the conscience.” But unconscionability determinations are fact specific, and courts routinely determine whether a term is substantively unconscionable given in the very context in which the case arises. It would be quite consistent with the established doctrine for courts to determine a written term is substantively unconscionable because it is materially different from an oral representation, even if the term would not be substantively unconscionable in the absence of the prior representation. For example, even assuming that it would not be substantively unconscionable for Twentieth Century Fox to contract to pay Michael Psenicska \$500 to appear in a documentary-style film, it might well be substantively unconscionable to contract to pay him \$500 to appear in a documentary-style film after having represented that the film would be a documentary. And even assuming that a no-reliance clause is not substantively unconscionable as a general matter, it might well be in the context in which the studio’s agents intentionally made a false representation in an effort to obtain Psenicska’s assent to the agreement.

Related to unconscionability, the Restatement (Second) of Contracts provides that a lack of actual knowledge of terms within a standard form contract can evidence a lack of assent to the contract and thus defeat its enforcement if the knowing buyer would have refused to sign the contract.²⁰⁵ This provision demonstrates that established contract law recognizes the possibility that reasonable non-drafting parties might not have actual knowledge of terms appearing in a standard form contract, and that courts may decline to enforce such contracts when they are Pareto inferior to the status quo. The *Borat* signed writings would appear to fit this description.

²⁰² See, e.g., *Alexander v. Anthony Int’l, L.P.*, 341 F.3d 256, 265 (3d Cir. 2003)

²⁰³ See, .g., *Zuver v. Airtouch Communications, Inc.* 103 P.3d 753, 759 (Wash. 2004)

²⁰⁴ See, e.g., *Brenner v. Little Red School House, Ltd.*, 274 S.E. 2d 206, 210 (N.C. 1981)

²⁰⁵ Restatement (Second) of Contracts 211(3).

D. Protecting Drafting Parties: A Heightened Evidentiary Requirement

The specific assent standard provides protection to non-drafting parties from opportunistic exploitation by drafting parties. The cost is that it threatens to place drafting parties who do not disclaim prior representations and obtain the non-drafter's specific assent at risk of opportunistic exploitation by non-drafting parties who might claim falsely, whether fraudulently or unintentionally, that prior representations inconsistent with the written document were made. To provide drafting parties with increased protection from such exploitation, courts should require that claims that the drafting party made prior inconsistent or deceptive representations be supported by proof that satisfies a heightened evidentiary standard before the claim can proceed to a jury.

1. A Strong Clear and convincing Standard

Typically, fraud must be pled with particularity, and many jurisdictions require that fraud be proven by clear and convincing evidence (although most states have consumer protection statutes that allow fraud to be proven by only a preponderance of the evidence²⁰⁶). For several reasons, however, what at first appear to be rules that protect drafting parties from exploitation²⁰⁷ turn out to often provide insufficient protection from the risks associated with the *Borat* problem.

Particularity requirements, such as Rule 9 of the Federal Rules of Civil Procedure,²⁰⁸ are designed to provide notice to the defendant of the specific conduct that underlies the fraud claim.²⁰⁹ Such requirements allow a defendant to win dismissal if the plaintiff has only a vague suspicion of a fraudulent act

²⁰⁶ Stark & Choplin, *supra* note ___, at 629 n.38.

²⁰⁷ See Gergen, *supra* note ___, at 248 (claiming that these rules “discourage unfounded fraud claims and avoid unjust fraud verdicts”).

²⁰⁸ In contrast to the general pleading standing in federal court that requires only “a short and plain statement of the claim showing that the pleader is entitled to relief,” Fed. R.Civ. P. 8(a)(2), Rule 9 requires that, when “alleging fraud or mistake,” a plaintiff “must state with particularity the circumstances constituting fraud or mistake.” Fed. R. Civ. P. 9(b).

²⁰⁹ See, e.g., *U.S. Ex Rel. Marlar v. BWXT Y-12, LLC*, 525 F.3d 439, 445 (6th Cir. 2008).

but cannot allege particular acts or circumstances²¹⁰ -- the “who, what, when, where, and how” that justify relief.²¹¹ As long as a plaintiff identifies a particular statement that, if made, would constitute fraud, the defendant will fail in a motion to dismiss the claim, even if the vast weight of the evidence suggests that the statement was not in fact made.²¹²

The requirement of clear and convincing evidence is more complicated. Typically, courts state that where the law requires clear and convincing evidence of fraud, this standard applies to all of the elements of the fraud claim. In practice, however, the heightened requirement of proof is often invoked to provide summary judgment for the defendant only when it is scienter (i.e., the drafter’s intent) that is in doubt. When the issue is whether the drafter actually made the (allegedly false) statement in question, courts often find that the trier of fact may determine that the issue has been proved by clear and convincing evidence even when the only evidence is the plaintiff’s recollection.

Consider, for example, the Mississippi case of *McMullen v. Geosouthern Energy Corp.*²¹³ Paul and Mary George McMullen, along with others, had previously prevailed in a securities fraud lawsuit against the defendant. In post-verdict settlement negotiations, the McMullens agreed to release their claims against the defendant in return for a discounted payment of the verdict amount.²¹⁴ When the defendant paid a larger settlement payment to another plaintiff, the McMullens alleged promissory fraud on the grounds that the defendant had orally agreed to increase the McMullens payment if it paid any other plaintiff a larger pro-rata portion of the verdict and subsequently failed to

²¹⁰ See, e.g., *Kearns v. Ford Motor Co.*, 567 F.3d 1120, 1126 (9th Cir. 2009) (affirming dismissal when the plaintiff failed to specify what the allegedly fraudulent advertisements and sales materials stated); *Marlar*, supra note __, at (affirming dismissal when “fail[ed] to allege concrete facts, rather than inferences based ‘[o]n information and belief’ that defendant submitted false claims to the government”).

²¹¹ *Vess v. Ciba-Geigy Corp.*, 317 F.3d 1097, 1106 (9th Cir. 2003).

²¹² Cf. *Ackerman v. Northwestern Mutual Life Ins. Co.*, 172 F.3d 467, 469-70 (7th Cir. 1999) (observing that heightened pleading and heightened proof requirements both attempt to protect defendants against irresponsible and defamatory claims, but that they “do not move in lockstep with each other”).

²¹³ 556 So.2d 1033 (1990).

²¹⁴ *Id.* at 1034.

do so. The defendant implicitly denied making the promise²¹⁵ (which was not recorded in the written settlement agreement). The trial court granted summary judgment for the defendant, but the Mississippi Supreme Court reversed, holding that the “clear and convincing standard required of the evidence to sustain a claim of fraud is certainly met in a summary judgment posture when one witness specifically claims a representation was in fact made.”²¹⁶ This holding is consistent with cases from other jurisdictions establishing that whether fraud allegations satisfy even a heightened evidentiary standard is ordinarily a jury question, even when the allegations are supported only by the testimony of a single witness who is contradicted by others.²¹⁷

When the heightened evidentiary requirement for fraud claims is enforced this weakly, defendants are insufficiently protected from plaintiff opportunism for two reasons. First, notwithstanding that the judge will instruct the jury to require clear and convincing evidence, juries may well determine that an alleged statement inconsistent with the final written document was made when in fact was not. The general assumption that juries can distinguish truthful from untruthful testimony with a high degree of accuracy²¹⁸ has long since been undermined by social science research.²¹⁹ And the precariousness of human memory combined with the self-serving bias demonstrate that non-drafting parties who falsely claim that drafting parties made statements inconsistent with the written documents will often do so in good faith.²²⁰ If the law permits the jury to decide that a single plaintiff’s testimony, standing alone, constitutes clear and convincing evidence that the defendant made an alleged statement, there is little doubt that juries will sometimes find that the plaintiff has satisfied this burden even when the statement was, in fact, never made. Second, even if juries use the clear and convincing requirement to screen out false allegations, the law, as applied, does not protect innocent drafting parties from suffering the expense of defending false allegations all the way to trial.

²¹⁵ The defendant’s affidavit “only conceded” that it had told the McMullens that it “had no intention” of paying the other plaintiff in question a greater percentage of the judgment. *Id.* at 1035.

²¹⁶ *Id.* at 1037.

²¹⁷ See, e.g., *City of Pittsburgh v. Ihrig*, 256 Pa. 410, 415 (Pa. 1917).

²¹⁸ George Fisher, *The Jury’s Rise as Lie Detector*, 107 *Yale L. J.* 575, 577 (1997) (“We say that lie detecting is what our juries do best.”).

²¹⁹ See generally Olin Guy Wellborn III, *Demeanor*, 76 *Cornell L. Rev.* 1075 (1991) (reviewing research).

²²⁰ See Part II.A.2, *supra*.

For both of these reasons, a weak clear and convincing standard gives drafting parties insufficient protection against false claims of fraud. This, in turn, enhances the credibility of a non-drafting party's threat to challenge an agreement for which there is a signed writing, and encourages drafting parties to renegotiate in light of such a threat. Since this will increase the cost of doing business, parties on both sides of the agreement are likely to be rendered worse off *ex ante*.

To provide balanced protection to drafters as well as non-drafters, courts should enforce a strong clear and convincing evidence requirement for fraud or misrepresentation claims that conflict with a signed writing. Specifically, defendants should be entitled to summary judgment unless plaintiffs can proffer evidence that is more substantial than the testimony of one plaintiff when that testimony is disputed by the defendant or the defendant's agent. Plaintiffs should be able to avoid summary judgment and reach a jury only when they can provide testimony by at least one third party that the defendant made representations or promises contradictory to terms embodied in the final written document, produce recorded evidence of such statements, or demonstrate a pattern of similar conduct in other negotiations as that alleged by the plaintiff.

2. The *Borat* Case

Even under a strong clear and convincing evidentiary standard, Twentieth Century Fox should not have been entitled to dismissal or summary judgment because several unrelated parties alleged that the defendants made nearly identical false statements and fraudulent promises. It is, in fact, this very consistency in the plaintiffs' allegations that provokes the strong intuition that the studio actually did exploit the plaintiffs in this case, as opposed to itself being the victim of exploitation by plaintiffs who agreed to appear in a movie for a small fee and came to regret their decision later, perhaps as a result of learning the extent of the movie's profitability.

E. Limitations

Because protecting non-drafting parties necessarily increases the likelihood that they might exploit drafting parties and vice versa, any attempt to balance protections to maximize social welfare *ex ante* will provide incomplete protection to both sides. The proposal advanced here certainly has flaws in this respect.

In order to protect the freedom of contract that can increase joint welfare, the regime would permit drafting parties to make representations that they

ultimately disclaim in the signed writing, as long as they then obtain the indicia of specific assent. Most obviously, actions that satisfy the specific assent requirement will not guarantee that the non-drafting party subjectively comprehends the import of a term in question. The indicia of specific assent might not override the confirmation bias, for example.²²¹ So even had the *Borat* plaintiffs received a clear statement that the standard release disclaimed all prior representations about the nature of movie, they might still have assumed that the studio was filming a documentary. Even if the plaintiffs had determined from the notice that the nature of the film-shoot might not be what they had anticipated, if the lapse of time between the scheduling of the shoot and their appearance caused them to view their star-turn in front of the camera as part of their endowment, they might have chosen to proceed forward anyway to avoid a “loss,” even if they would have declined the offer had the disclaimers been provided at an earlier time.²²² In other words, dishonesty might still pay in particular cases, even though the specific assent rule will reduce its expected value. And, of course, even when the specific assent rule succeeds in preventing exploitation, it does create a small transaction cost for both drafter and non-drafter that can be viewed as a tax on contracting.

In addition, a strong clear and convincing evidentiary standard will leave non-drafting parties exposed to some exploitation risk. Drafters can still exploit non-drafters if they make their false representations beyond the observation of third parties and avoid creating a record, although the possibility that non-drafters could produce pattern-of-behavior evidence should provide a check on the worst abuses. At the same time, this heightened evidentiary standard will not provide a foolproof guarantee against intentionally fraudulent or unintentionally self-serving recollections of non-drafting parties. For example, in order to demonstrate a pattern of representations, several similarly-situated non-drafting parties might collude in creating such “recollections,” or an overzealous plaintiffs’ attorney might off-handedly inform potential litigants of the experience of others, along with the hint that corroboration will be necessary for any plaintiffs to prevail in court.

These points conceded, the legal regime for responding to the *Borat* problem must be compared to plausible alternatives, not theoretical perfection.

²²¹ See Part II.B.1, *supra*.

²²² See Part II.B.3, *supra*.

CONCLUSION

There is no perfect solution to the *Borat* problem. Legal rules that protect non-drafting parties from exploitation make it easier for them to exploit drafting parties, and vice versa. But it is possible for courts to provide significant protection to both sides, at relatively low cost to the other, and in so doing reduce the social costs of contracting compared to the polar regimes of strictly enforcing signed writings or permitting all parol evidence. Requiring drafters to obtain specific assent (clear statement plus realistic notice) to form terms that contradict or disclaim prior representations protects non-drafters by reducing the cost of comprehension. Requiring non-drafters to satisfy a strong clear and convincing evidence requirement protects drafting parties by reducing the risk of judicial error. The proposed approach also has the distinct benefit of being consistent with basic principles of the law of contract and fraud, thus making implementation by the judiciary feasible.

I have used the *Borat* litigation as the primary example of a far more general problem because it starkly illuminates the costs of following either polar legal regime, and thus helps make the case for a more nuanced approach that takes seriously both sides of the coin of bilateral opportunism. The representativeness of the *Borat* illustration might be questioned, however, on the ground that, unlike more garden-variety transactions in which the *Borat* problem arises, the making of a movie of its type *requires* subterfuge. If the unwitting stars of the movie had known that the journalist “Borat” was actually comedian Sacha Baron Cohen, the studio could not have obtained the unknowing, confused reactions central to the film’s brand of humor.

While this is true, it is worth noting that, per the Coase Theorem,²²³ it does not follow that this type of movie can only be made under a pure duty-to-read legal regime. Had the courts employed the approach proposed in this article, it is quite possible (although far from certain) that the plaintiffs would have satisfied the clear and convincing evidentiary standard for proving inconsistent prior statements and that the defendants would have failed to prove specific assent to the contradictions and disclaimers contained in the signed writing. But Twentieth Century Fox could have simply approached the plaintiffs after the completion of the filming and negotiated for the rights to use their performances in the movie the studio actually intended to make.

²²³ Private parties will reallocate legal rights efficiently when transaction costs are zero (or low). See, e.g., A. Mitchell Polinsky, *An Introduction to Law and Economics* 11-14 (1983). The “Theorem” is derived from R.H. Coase, *The Problem of Social Cost*, 3 *J. L. & Econ.* 1 (1960).

Some plaintiffs might have refused any offer within the movie's budget, forcing the studio to find and film new stooges, but many likely would have agreed to appear in *Borat*, albeit perhaps at somewhat higher rates of compensation. The movie cost \$18 million to produce²²⁴ and ultimately earned more than \$323 million in revenue.²²⁵ Even assuming that *Borat*'s financial success far exceeded the studio's pre-release expectations, it seems likely that there would have been a substantial bargaining zone in post-filming negotiations over use rights between Twentieth Century Fox and the stooges who turned in the most entertaining "performances" in reaction to Baron Cohen's antics. Almost certainly, the comedic story of the faux-Kazakhstani journalist interacting with befuddled Americans as he makes his way across the "U, S, and A" still would have graced the silver screen. And if it turned out that no ordinary Americans could be found who were willing to knowingly license their amusing performances for this endeavor at a price the studio was willing to pay, the implication would have been that that movie's social costs exceeded the value of its expected profits and, therefore, under an efficiency analysis, should not have been produced.

²²⁴ Box Office and Business for *Borat: Cultural Learnings of America for Make Benefit Glorious Nation of Kazakhstan* (<http://www.imdb.com/title/tt0443453/business>.)

²²⁵ See note __, *supra*.