PERSPECTIVES on CONTRACT LAW

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WHY NOMINAL CONSIDERATION SHOULD BE BINDING*

Joseph Siprut

Suppose a wealthy uncle wishes to convey a portion of his real estate holdings to his nephew. Although very pleased to hear the good news, the nephew asks whether his uncle might put the promise in writing. To satisfy his nephew's skepticism, the uncle drafts a document stating that "for valuable consideration of $1, receipt of which is hereby acknowledged," he promises to pledge "Blackacre" to the nephew. The purported consideration of $1 is never paid. The uncle signs and notarizes the document, affixes his own personal seal to it (handily ordered off of the internet for $99), and writes in block letters at the top of the document: "THIS PROMISE IS A LEGALLY ENFORCEABLE OBLIGATION." The nephew promptly takes the document to an attorney and asks if the promise is indeed binding.... Should a gratuitous promise be binding if the promisor so desires? And if so, through what mechanism?...

SELF-INTERESTED ALTRUISM

Although it is commonly presumed that gratuitous promisors are motivated by altruism, some evidence suggests otherwise.... Readers may well ask themselves whether the last time they stopped to give change to someone on the street they felt good about themselves afterward. They might then wonder about the degree to which that feeling of self-righteousness motivated the act of giving itself.... Today, however, most significant gifts are made either to someone in one's circle of friends or family, or to a charity. Those who make them are not motivated solely or even primarily by altruism.

Farnsworth... cite[s] professional fundraisers who argue that the merits of donor behavior models favor exchange over pure altruism: "To say that one asks for nothing in return is not to say that one expects

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*From Joseph Siprut, The Peppercorn Reconsidered: Why a Promise to Sell Blackacre for Nominal Consideration Is Not Binding, But Should Be, 97 Nw. U. L. Rev. 1809 (2003).

nothing in return."[1] There are certainly other (self-interested) reasons why a donor might make a gift.

> [A]n expectation of an enhanced reputation is only one of many reasons for making a gift. In the case of a gift to charity, one might expect to gain tax advantages. In the case of a gift to a relative or friend . . . one might hope for love and affection or, if death seems near, better treatment in the hereafter. A decision to give often results from a complex mixture of these and other motives that sometimes are difficult to identify. Although one may get something in return for one's gift, one does not get it as the result of a swap. Despite the exchange, there is no bargain.[2]

The foregoing suggests there is something amiss in the law of consideration. The Restatement (Second) majority rule that would have courts police exchanges for a bargain "in fact" neglects that many exchanges, which are not regarded as bargains by the Restatement (Second) and most courts, still satisfy the reciprocity element of Restatement (Second) §71. . . .

LON FULLER'S LEGACY AND GRATUITOUS BEHAVIOR BENEATH THE SURFACE

Commentators generally agree as a basic rule that society should foster exchange, though the justifications commonly offered differ somewhat. Most would concur, however, that if economic actors behave as rational agents, then no one enters into an exchange unless it makes them better off. A "regime of enforceable promises" is therefore justified because it increases the likelihood of beneficial exchange.

However, making more than nominal consideration a necessary condition for enforcement of a promise—*i.e.*, policing for a bargain in fact—implies that only bargain promises play a role in increasing utility through exchange. This assumption is unjustified, yet finds itself enshrined in common contractual knowledge.

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1. [E. Allan Farnsworth, Promises and Paternalism, 41 Wm. & Mary L. Rev. 385, 387-388 (2000).]

2. *Id.* at 388-389 (internal citations omitted) (emphasis added). . . .

For the past fifty years, Lon Fuller's *Consideration and Form* has represented the standard account of the presumed nonenforceability of gratuitous promises (absent reliance). Fuller offered a functional defense of the consideration doctrine and argued that consideration was not merely a historical relic of English common law. His view posits that a promise should be enforced only if it satisfied the "evidentiary," "cautionary," and "channeling" functions of a formality such as the seal. Accordingly, "the bargain context . . . provided an 'informal satisfaction' of the 'desiderata' of the formal requirements (the evidentiary, cautionary, and channeling functions) after the formalities themselves were no longer available."[3]

Fuller goes further, however, and surmises that "[w]hile an exchange of goods is a transaction which conduces to the production of wealth and the division of labor, a gift is, in Bufnori's words, a 'sterile transaction.' " Thus, the legacy of Fuller's seminal piece is that the consideration doctrine serves the purpose of determining whether the interaction between parties is productive, and therefore worthy of the judicial effort of enforcement. Of course, because only bargain promises are upheld under the consideration doctrine, the implication is that gratuitous promises are not "productive."

In fact, however, the conclusion that a gratuitous transfer produces less utility than an otherwise comparable, but bargained-for, transaction lacks support. As explained in the previous section, unless a voluntary gratuitous transaction is beneficial to both parties, it will not take place. Moreover, no doubt based on this reasoning, the American legal system does not otherwise discriminate against gratuitous transfers once executed (*i.e.*, once the gift is delivered).

Wherever the law provides a facility for private ordering — the possibility of making an enforceable promise; of transferring property by sale, gift, lease, or will; of creating a trust, appointing an agent, or forming a corporation — as a general rule, it will permit and uphold any lawful undertaking on the same terms, without inquiring into its importance or wisdom.

What is more, if a contractual system that enforces bargain promises is justified because it increases the likelihood of beneficial exchange, then the same argument accordingly applies with equal force to gratuitous

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3. Andrew Kull, Reconsidering Gratuitous Promises, 21 J. Leg. Stud. 39, 46 (1989).

promises: gifts have a wealth redistribution effect (*i.e.*, wealth is redistributed to persons who have more utility for the goods or the money than do the donors).

The argument that gratuitous promises do not merit enforcement, therefore, cannot depend merely on the belief that the gratuitous transfer is itself of insufficient social importance. And if the apparent prejudice against gratuitous transfers is actually focused on the absence of a "channeling" or "evidentiary" function, that would merely be an argument in favor of using formalities in the context of gratuitous transfers, but not for removing gratuitous transfers from the scope of enforceability altogether.

We have thus far seen that donors are often motivated to make gratuitous promises, not by the force of purely altruistic motives, but by the same self-interested purposes that underlie bargain promises. Moreover, contrary to the central tenet of Fuller's *Consideration and Form*, if the consideration doctrine serves the purpose of determining whether the interaction between parties is productive, and therefore worthy of judicial enforcement, then consideration satisfies what should be a sufficient, but not necessary, condition to enforceability. The presence of consideration might signal a productive promise and may evidence deliberation (thus satisfying Fuller's conception of the functional role of consideration), but the *absence* of consideration does not necessarily mean the promise is any *less* productive or that the promisor deliberated any less carefully than he might have with consideration present.

Accordingly, economic-based arguments that the non-enforceability of gratuitous promises is justified because enforcement would be an overly costly use of judicial resources misses the mark. Surely there are gratuitous promises whose enforcement would be cost-prohibitive—e.g., "a case where a man promised to take a woman to dinner but later reneged." But suppose the same woman promised to give the man a dance lesson in exchange for dinner, and that he ultimately reneged. Such a bargain would satisfy the classical consideration requirement, and yet suing to enforce the agreement would be an absurdity every bit as much as suing to enforce the gratuitous promise (if it were enforceable) would be. Likewise, the case of the wealthy uncle promising to give his nephew Blackacre involves a very significant monetary sum: "Why should we suppose that the cost/benefit comparison is necessarily unfavorable to enforcement?"

With this theoretical underpinning in place, this Comment now discusses more explicitly why having some means available by which to bind an otherwise gratuitous promise literally raises the value of the promise to both parties.

WHY GRATUITOUS PROMISES SHOULD BE ENFORCED

A gratuitous promisor may have a self-interested preference in making the promise to give a gift binding. In the case of any gratuitous promise to make a gift (but in which, for whatever reason, the promisor chooses to defer delivery), the promisor might wish to alleviate the promisee's potential uncertainty about its conveyance. The promisor, in other words, might wish to counteract the promisee's fears of non-completion. In so doing, the promisor enhances the value of the prospect of his gift by committing himself.

This point is more powerfully illustrated by way of example. Suppose an academic think-tank has organized a series of academic lectures throughout the country. The extent of the tour (*i.e.*, the number of cities visited, the number of lectures per city, and the length of the tour) is contingent on funding. It happens that this particular organization, and most others like it, survives primarily on donations and pledges.

Now suppose that the business manager of this organization is informed that a donor has promised to give $10,000 to help fund the lecture series. Clearly, the business manager cannot open up the accounting books and record a $10,000 deposit immediately thereafter. In other words, the organization cannot plan $10,000 worth of lectures because there is no guarantee that the donor will actually make the payment. Therefore, the standard practice of any business in like circumstances is to plan future events based only on the pledge amount multiplied by the probability that the pledge will actually be executed. If past history suggests that comparable pledges are fulfilled only half the time, the organization will accordingly plan only $5,000 worth of events.

By contrast, if the organization knew the promise was legally binding, then the promise would be worth more than the amount the think-tank could otherwise record in the books. It might cost $1,000 to enforce a $10,000 promise, and there might be a risk of insolvency. But even so,

the resulting entry will likely be higher than the alternative $5,000. Thus, the value of the promise to the promisee is literally increased the moment that the promise becomes binding. Perhaps less obviously, but of great importance here, because the promise actually equates to more dollars on the organization's books, the promisor will himself benefit in like manner. That is, if a promisor derives satisfaction from the degree of happiness experienced by the promisee because of the promise, it stands to reason that, if the promisee derived a greater degree of happiness from the promise (because the promise is enforceable), so too would the promisor derive greater satisfaction. . . .

Skeptics may still find unsatisfactory a legal rule that would enforce a gratuitous promise for a promisee who has "neither incurred a detriment nor conferred a benefit" and who would therefore "receive a morally undeserved windfall" from enforcement of the promise. Two responses may be offered to this criticism. First, as we have already seen, it is simply not the case that enforcement of a gratuitous promise — or the prospect of enforcement — would demure benefits to the promisee and not the promisor. Promisors may have a self-interest in making, and will enjoy the benefits that flow from, a binding gratuitous promise. Second, if preventing a "windfall" is a concern, it should be noted that the promisor stands in equal stead with the promisee in this regard. "Having made a promise in order to capture a benefit for himself, the [promisor] cannot fairly be allowed to enrich himself by breaching the promise. In other words, a strong element of potential unjust enrichment is present."[4]

MENDING THE BRIDGE: FROM NOMINAL CONSIDERATION TO GRATUITOUS PROMISES

Although this Comment has demonstrated that a promisor may have a self-interest in making a binding gratuitous promise yet lack the means to do so, "[m]any of us indeed would shudder at the idea of being bound by every promise, no matter how foolish, without any chance of letting increased wisdom undo past foolishness. Certainly, some freedom to

4. Melvin A. Eisenberg, The World of Contract and the World of Gift, 85 Cal. L. Rev. 821, 848 (1997).

change one's mind is necessary for free intercourse between those who lack omniscience."[5] Fortunately, this Comment has not proposed that all promises should be binding, but rather, that if a promisor seeks to make a binding gratuitous promise, he ought to be able to do so.[6] The only task remaining, therefore, is to choose a formality by which to signal this intention.

Although use of a formality is necessary for purely evidentiary reasons, formalities . . . serve many of the additional ends that consideration serves. Legal formalities, such as a formal promise under seal, "facilitate in varying degrees at least seven functions: ceremonial, evidentiary security, cautionary, deterrent, channeling or earmarking, clarification and certainty, and economic efficiency."[7] Therefore, even if one remains committed to paternalism — *i.e.*, if gratuitous promises are unenforceable for the "promisor's own good" — it is not clear why consideration rather than an appropriate formality would suffice to make the promise binding.

Carving out a doctrinal role for formalities quickly leads to the question of which formality should be adopted for the purpose of binding gratuitous promises. The seal, it may be said, had its day in the sun but failed to survive the test of time. The Model Written Obligations Act was a nearly uniform disaster, at least if acceptance by legislatures is the standard for measuring success.

Nominal consideration, however, could effectively fill this formality role in the context of enforcing gratuitous promises. This is so for several reasons.

Ultimately, the doctrine of consideration is one part of a larger system of rules and principles. Indeed, "jettisoning the doctrine of consideration from the common-law system of contracts might create enormous and unpredictable strains elsewhere in the system."[8] Adopting nominal

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5. Morris R. Cohen, The Basis of Contract, 46 Harv. L. Rev. 553, 573 (1933). It is also unclear why a yearning for "letting increased wisdom undo past foolishness" should reflect poorly on enforcing gratuitous promises. As noted, many enforceable bargains have also led some unfortunate contracting parties, reflecting in the wisdom experience brings, to lament their foolishness.

6. Opponents of the theory that a gratuitous promise should be binding if the promisor so desires, therefore, attack a straw man with assertions that enforcing all promises will have undesirable consequences. . . .

7. [Eric Mills Holmes, Stature and Status of a Promise Under Seal as a Legal Formality, 29 Willamette L. Rev. 617, 626 (1993).]

8. [Mark B. Wessman, Retaining the Gatekeeper: Further Reflections on the Doctrine of Consideration, 29 Loy. L.A. L. Rev. 713, 840 (1996).]

consideration to enforce gratuitous promises, therefore, would not disrupt the "seamless web" of contract law, and consideration law specifically. In fact, using nominal consideration in this regard would make consideration doctrine more internally consistent. Although courts would have the world believe that they "will not inquire as to the adequacy of consideration," . . . this is not true. Courts do inquire into the adequacy of consideration when they police for bargains that are "mere pretense." Attempting to determine whether consideration was "genuinely bargained for" is nothing less than inquiring into the adequacy of consideration, irrespective of whether courts disguise the essence of this endeavor with different language. Thus, to that extent, adopting nominal consideration to enforce promises would be a move toward greater doctrinal consistency.

Second, . . . nominal consideration already functions as a formality in contexts other than gratuitous promises, as demonstrated by the second Restatement's explicit acknowledgment of nominal consideration's role as a formality in guaranty and option contracts. Thus, the path to nominal consideration serving as a formality in the context of gratuitous promises has already been paved.

Third, many courts and commentators (and practitioners) apparently believe that the doctrine of nominal consideration already does function as a formality in the context of gratuitous promises — or even that it always has. Thus, introduction of the "peppercorn doctrine" into contracts law — in the context of gratuitous promises — would presumably be more seamless than introducing an entirely new legal apparatus.

Fourth, modern English law does accept nominal consideration as a formality in the context of gratuitous promises. Therefore, the common law of England, particularly the case law of the last fifty years, provides an empirical analysis of how using nominal consideration for this very purpose would work in practice.

Fifth, nominal consideration "represents a partially successful *judicial* effort to create a formality."[9] Courts at the highest state level are presumably empowered to accept the doctrine of nominal consideration as legally binding whenever they wish. Thus, the fate of nominal

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9. [1 Samuel Williston & Richard A. Lord, A Treatise on the Law of Contracts 983 (4th ed. 1990).]

consideration need not turn on approval by state legislatures, as it might, for example, for the seal.

CONCLUSION

That the legal adage "a peppercorn is sufficient consideration" has achieved cocktail-party popularity belies its true power as a legal formality. Nominal consideration is an operative formality only in the context of options and guaranty contracts. What is more, . . . nominal consideration has never been used as a formality to bind gratuitous promises. . . . Hence, the time has come to rethink the rigid delivery requirement of gift law. If a formality is to be adopted to enforce a gratuitous promise, nominal consideration is not only well-suited for the job but it would also shore up the somewhat embarrassing doctrinal wrinkle in contract law caused by the current rules pertaining to adequacy of consideration questions and the general bar against enforcing gratuitous promises.