OF FINE LINES, BLUNT INSTRUMENTS, AND HALF-TRUTHS: BUSINESS ACQUISITION AGREEMENTS AND THE RIGHT TO LIE

BY JEFFREY M. LIPSHAW

ABSTRACT

In this article, I expand upon a happy coincidence (for scholars) in reconciling the overlap between contract and fraud. Both the recent book by Ian Ayres and Gregory Klass and the opinion by the Delaware Court of Chancery in Abry Partners Acquisition V, L.P. v. F & W Acquisition, LLC addressed the matter of lies within contractual promises, whether as to the promisor's intention to perform or as to the state of the business being sold. Each treatment, however, in focusing on fraudulent affirmative representations, falls short of (1) recognizing the fundamental aspect of deceptive promising in a complex deal, namely the half-truth, (2) articulating an appropriate doctrinal principle to address it, or (3) capturing the social and linguistic context that makes the deceptive half-truth so insidious.

The archetypal facts in Abry frame the issue. When the parties to a business acquisition agreement purport to limit the buyer's reliance to those representations and warranties set forth in the agreement, just what obligations of truth-telling have the parties contractually released? We need to grapple with the interrelationship of law, language, mutual understanding, and trust. The language of the law (and the contract) is a blunt instrument by which to map the subtle fine lines of a complex agreement. I contend that there is a kind of special arrogance in the illusion onto which lawyers hold—that the uncertainties and contingencies of the world are in their power to be controlled, and to the winner of the battle of words go the spoils. The correct doctrinal result is to presume in the transactional speech acts (including the contract), as we do in everyday life, a default of truth-telling. This permits the parties to contract freely around

---

*Associate Professor, Suffolk University Law School. This article stems from a blog discussion on Conglomerate, http://www.theconglomerate.org, between Gordon Smith, Frank Snyder, and me from February 28, 2006, to March 3, 2006. I appreciate comments on the thesis from Professors Smith and Snyder, as well as from Larry Solum, Alan Palmiter, and Gregory Klass. I also appreciate comments and questions during presentations of this thesis in faculty colloquia at Suffolk Law School, Tulane Law School, Texas Wesleyan University Law School, Thomas Jefferson Law School, Marquette University Law School, and South Texas College of Law. In particular, I am indebted to Professor Arnold Rosenberg for honing the union certification hypothetical. Thanks also to Sylvia Strumpler and Matthew C. Kirkham, my research assistants at Tulane.

1891 A.2d 1032 (Del. Ch. 2006).
the rule, but it requires narrow construction of the exceptions and disclaimers.

TABLE OF CONTENTS

<table>
<thead>
<tr>
<th>I.</th>
<th>INTRODUCTION ........................................................................</th>
<th>432</th>
</tr>
</thead>
<tbody>
<tr>
<td>II.</td>
<td>THE ABRY DECISION ..................................................................</td>
<td>438</td>
</tr>
<tr>
<td>A.</td>
<td>The Context of Private Equity ........................................</td>
<td>438</td>
</tr>
<tr>
<td>B.</td>
<td>The Deal .............................................................................</td>
<td>439</td>
</tr>
<tr>
<td></td>
<td>1. The Setup .......................................................................</td>
<td>439</td>
</tr>
<tr>
<td></td>
<td>2. The Buyer and the Contract ..........................................</td>
<td>439</td>
</tr>
<tr>
<td></td>
<td>3. The Seller's Alleged Misrepresentations ..........................</td>
<td>441</td>
</tr>
<tr>
<td>C.</td>
<td>The Denouement and the Buyer's Claims ................................</td>
<td>443</td>
</tr>
<tr>
<td>III.</td>
<td>THE CRITIQUE .......................................................................</td>
<td>444</td>
</tr>
<tr>
<td>A.</td>
<td>The Doctrinal Critique ....................................................</td>
<td>444</td>
</tr>
<tr>
<td></td>
<td>1. The Source of the Problem ............................................</td>
<td>444</td>
</tr>
<tr>
<td></td>
<td>2. A Doctrinal Alternative ..............................................</td>
<td>448</td>
</tr>
<tr>
<td>B.</td>
<td>The Theoretical Critique ................................................</td>
<td>449</td>
</tr>
<tr>
<td></td>
<td>1. Restating the Problem ................................................</td>
<td>449</td>
</tr>
<tr>
<td></td>
<td>2. An Efficiency Critique ................................................</td>
<td>451</td>
</tr>
<tr>
<td></td>
<td>3. A Linguistic and Social Critique ....................................</td>
<td>455</td>
</tr>
<tr>
<td></td>
<td>a. Presumptions Based on the Use of Language and the Warranties of Speech Acts</td>
<td>458</td>
</tr>
<tr>
<td></td>
<td>1. The Illusion of Power Over Interpretation ..........................</td>
<td>458</td>
</tr>
<tr>
<td></td>
<td>2. The Implicit Warranties of Speech ..................................</td>
<td>463</td>
</tr>
<tr>
<td></td>
<td>b. Disclaimers of Truth-Telling as Social Phenomenon ............</td>
<td>467</td>
</tr>
<tr>
<td></td>
<td>1. The Lawyer's Constitutive View of Contracts ....................</td>
<td>467</td>
</tr>
<tr>
<td></td>
<td>2. Contracts and Trust ....................................................</td>
<td>469</td>
</tr>
<tr>
<td>IV.</td>
<td>CONCLUSION .........................................................................</td>
<td>474</td>
</tr>
</tbody>
</table>

I. INTRODUCTION

The parties to sophisticated business acquisitions use a number of methods to assure themselves of an appropriate allocation of risk. Sellers provide buyers an opportunity for due diligence; buyers undertake their own investigation apart from the resources made available by sellers; the parties
adjust the price to reflect risks; and the parties use the language of contracts seemingly to provide a final statement of the rights and obligations of one to the other. Yet, those methods do not wholly dispose of post agreement disputes. Whether a matter of opportunism or a matter of interpretation (or one disguised as the other), buyers still sue sellers, even where each is sophisticated and has relied on expert legal, accounting, operational, and transactional counsel.

The line in our jurisprudence between contract law and tort law becomes all the more visible where these same sophisticated parties attempt to use the language of contract to set the bounds of the seller's obligation to share information. Combined with contractual language limiting the seller's liability for breaches of covenants, warranties, and representations, there can be an intended or unintended overinclusiveness. Did the parties intend, or should they be presumed to have intended, to have those provisions limit a seller's liability for intentional misrepresentation of the state of the business?

In recent months, there have been two sophisticated treatments on the question of promissory fraud: one academic and one judicial. Ian Ayres and Gregory Klass have published *Insincere Promises: The Law of Misrepresented Intent.* The authors seek to fill the gap into which the cause of action for promissory fraud falls by arguing that promissory fraud is something beyond the scope of the contract law syllabus but something not addressed in the torts class. Their subject is the relationship between liability for the nonperformance of a promise and the liability for the nonperformance of the promise where the promisor never intended to perform from the outset. The proposed legal approach recognizes the complexity (and nonreducibility) of the world. Law ultimately is neither natural nor social science and cannot be reduced to algorithms. It is instead a social structure in which we come to agree that certain actions, even as between private parties, are worthy of sanction through the legal process. As a reflection of an "antireductionist approach to the theory of promising—which refuses to pack every aspect of the transaction into the duty to perform"—Ayres and Klass argue for the retention in the law of a doctrine by which the making of a promise without the intention to perform is separately actionable under the law of fraud.

In *Abry Partners V, L.P. v. F & W Acquisition, LLC,* Vice Chancellor Leo Strine of the Delaware Court of Chancery presided over a real-world
allegation of fraud overlapping with a promise.\textsuperscript{8} The issue was whether the fairly typical indemnity cap and exclusive remedy clause in a business acquisition agreement barred an extracontractual fraud remedy where the buyer alleged that the seller knew one of the contractual representations to be false.\textsuperscript{9} The court held that the parties intended to limit liability even for deliberate falsehood, but such limitation was not enforceable as a matter of public policy in Delaware.\textsuperscript{10}

The immediate academic reaction centered on whether one can disclaim the obligation to tell the truth, with the general consensus being: yes, it is a dog-eat-dog formalistic world out there.\textsuperscript{11} Professor Larry Ribstein criticized the opinion along those lines on his blog.\textsuperscript{12} Professor Frank Snyder suggested, in the same vein, that sophisticated parties, having agreed to this kind of disclaimer, should provide an explicit provision if they want to be protected against lying.\textsuperscript{13}

The book and the case are admirable advances in an area of the law that has previously received scant treatment.\textsuperscript{14} Each advance, however, tantalizes but falls short in different ways by truncating the inquiry, perhaps by oversimplifying the problem presented. The common focus of Ayres and Klass's book and the Abry case is the legal implication of a speech act that falsely represents something known to the speaker; in the book, that information is the speaker's undisclosed intention not to perform the promise, and in the case, it is the speaker's failure to disclose the true condition of the business. I believe Ayres and Klass have gotten closer to the essence of the problem than the Abry court by focusing on the implicit

\textsuperscript{8}Note the difference between the prototypical Ayres & Klass circumstance of promissory fraud and the facts in Abry. Ayres and Klass note that the typical type of promissory fraud occurs where "a promisor, by the very act of promising, typically communicates that she intends to perform her promise. That representation concerns an existing fact. . . . By saying something about the promisor's present intent, the act of promising creates the opportunity to lie." AYRES & KLASS, \textit{supra} note 2, at 4. Abry, on the other hand, did not involve a promisor who never intended to perform. Rather, Abry's allegations were more in the nature of fraud in the inducement, which addresses promises about the current state of the world intended to cause the buyers to enter into the transaction, even though the statements underlying the promises are false. Abry, 891 A.2d at 1051 (noting that "the complaint adequately pleads that the Seller was in a position to know of the falsity of the financial statements" used to induce Buyers to purchase the company at issue).

\textsuperscript{9}Abry, 891 A.2d at 1034-35.

\textsuperscript{10}Id. at 1064.


\textsuperscript{14}AYRES & KLASS, \textit{supra} note 2, at 6. The authors provide an extensive bibliography supporting this assertion. \textit{Id.} at 217-19 n.20.
warranties in the very use of language. But each treatment sees lying merely as a false statement, whereas the art of deception is far more nuanced.

The publication of the book and the issuance of the Abry opinion are a happy coincidence. The facts presented in Abry—the deal between the parties, the agreement, the buyer's due diligence, and the postclosing financial manipulation that provoked the postclosing lawsuit15—are an archetype. Its appeal as grist for the scholarly mill lies not in its idiosyncrasy but in its very typicality. Moreover, the very wealth and sophistication of both parties create a kind of jurisprudential laboratory to examine the intersection of fraud and contract. The case further raises fundamental theoretical issues about a subtle truth-telling understanding among those who negotiate complex deals and whether the power of language can be harnessed to reflect it. Each treatment, however, in focusing on fraudulent affirmative representations, falls short of (1) recognizing the fundamental aspect of deceptive promising in a complex deal, namely the half-truth, (2) articulating an appropriate doctrinal principle to address it, or (3) capturing the social and linguistic context that makes the deceptive half-truth so insidious.

If anything, this decision, issued by a thoughtful and scholarly judge in a universally recognized business-friendly forum, is evidence of how lawyers and judges can be seduced (or even blinded) by what they think is a lawyer's unique power over language. So, while I agree with the result, I will suggest, as a matter of doctrine, there is a rule of law that maps more precisely on the common understanding of participants in complex acquisitions, as well as the way in which all of us, including sophisticated deal negotiators, ordinarily expect language to be used. Moreover, while I think Ayres and Klass have captured the spirit of my thesis, it is necessary to expand on their thinking to address fully the issues presented in Abry.

My project here is not merely to state a better doctrine by which courts should reconcile freedom of contract and the law of fraud. As Ayres and Klass correctly observe, "Philosophers find it endlessly fascinating that by the mere act of uttering certain words one can create a duty for oneself. Legal thinkers are faced with the more pressing practical problem of whether, why, and how the law should take cognizance of such duties."16 Having criticized Vice Chancellor Strine's holding in Abry, I am obliged to state my proposed doctrinal result. And I will suggest, as a matter of efficiency-enhancing doctrine, my proposal follows wholly within the information-forcing default rule analysis proposed by Ayres and Klass.17

15 Abry, 891 A.2d at 1036-40.
16 Ayres & Klass, supra note 2, at 2.
17 Id. at 83-112; see also infra Part III.B.2 (discussing Ayres and Klass's information-forcing default rule).
But I wish to take up the philosophical inquiry left largely untouched by those scholars. This archetypal case unpeels like an artichoke, invoking, ultimately, the interrelationship of law, language, mutual understanding, and trust. The language of the law is inadequate, serving as a blunt instrument by which to map the fine lines of a complex agreement. Because of its inadequacy, the language of the law requires us to go beyond the law to the psychology and philosophy of language itself. I will contend that there is a kind of special arrogance in the illusion that lawyers hold—that the uncertainties and contingencies of the world are in their power to be controlled, and that to the winner of the battle of words go the spoils.

Vice Chancellor Strine tried admirably to reconcile the polarities of the policy of promoting freedom of contract with the law's adoption of a moral code (i.e., "don't lie") in the law of fraud. It seems to me, however, he got lost somewhere in that illusion of the power of language, resorting instead to the deus ex machina of public policy to cure what seemed to him, nevertheless, an injustice. But his solution is flawed precisely because it gives too much credit to lawyers' ability to capture the affirmative essence of the deal in the contract language and sees the contract as the embodiment, rather than a reflection, of the deal.

It is this kind of formalism, a "four corners" approach, that fails to capture the underlying texture of the promise and its context. The law of contracts, as applied here (like the Ayres and Klass analysis of misrepresented intent\(^{18}\)), only deals with affirmative misrepresentations (and reliance thereon). That law, however, does not capture that implicit context of the deal by which the parties also understand that there is some duty that has been created more akin to what in the law of fraud is half-truth or omission.\(^{19}\) And, indeed, the essence of the Abry case was not promissory fraud but half-truth and omission. The contract never addressed omissions, nor, as Vice Chancellor Strine conceded, did it ever explicitly disclaim the right of rescission on account of either intracontractual or extracontractual misrepresentation.\(^{20}\)

My doctrinal result is easy to state. Where, as in Abry, the parties have disclaimed reliance on extracontractual representations, freedom of

\(^{18}\)Ayres & Klass, supra note 2, at 46-58.

\(^{19}\)In fairness, the general recognition of this idea constitutes the great advancement of the book. See generally id. The book is worth the investment of time, if for nothing more than this passage:

But representations of intent are also tools that promisors use to accomplish very specific tasks. Promising is a complex joint intentional activity and involves a high degree of both coordination and trust between the parties. In most cases, it takes more than the performative force of the promissory act (the creation of an obligation to do the act promised) to secure those conditions.

Id. at 203.

\(^{20}\)Abry, 891 A.2d at 1064-65 n.85.
contract requires that the provision be given its precise effect. The disclaimer should only be effective where (1) the extracontractual representation conflicts with the contractual representation, or (2) the contract is wholly silent on the subject matter of the extracontractual representation. A disclaimer of reliance on extracontractual representations cannot and should not be deemed to impact the half-truth or omission liability that may well be the natural consequence of having made the contractual representation. Moreover, the burden should be on the party asserting the antireliance clause to show that it was intended to cover anything but liability arising wholly as a result of the falsity of extra-contractual representations.

What, I suspect, is more controversial is my reason for advocating this rule. In an effort to credit freedom of contract and efficiency, I think the court and commentators are saying that sophisticated parties must (or do) assume that everything is a lie unless affirmatively warranted in the contract. This reverses the natural import of language among human beings, lawyers, and judges alike. Our very use of language carries with it a presumption of truth-telling, and that presumption is not overcome simply because lawyers are writing contracts in their own variant of the same language. It is possible to write a contract provision that wholly and expressly disclaims any obligation of truth-telling or avoidance of half-truth deception. But that almost never happens. Instead, the law of fraud, combined with the pleading requirement of particularity, provides a truth-telling safety net. This is, in the end, a broader remedy than rational actor theorists or contract formalists might want, but one that more accurately maps on the fine line of the

---

21 There is one extensive academic treatment of contractual disclaimers of liability for fraud, which Vice Chancellor Strine cited in Abry. Id. at 1058 n.56 (citing Kevin Davis, Licensing Lies: Merger Clauses, the Parol Evidence Rule and Pre-Contractual Misrepresentations, 33 VAL. U. L. REV. 485 (1999)). In the article, Professor Davis's focus was somewhat different from mine. He too examined the impact of typical merger or integration clauses that would have the effect, if applied literally, of exculpating a party from fraudulent or grossly negligent statements made outside the bounds of the contract in pre-contract negotiations. Davis, supra, at 485. But the thrust of his analysis was the interplay of contract and agency law, and he concluded that the decision to enforce the disclaimer might turn on whether the party seeking to enforce the disclaimer was a natural person who was the perpetrator of the fraud or an enterprise seeking to protect itself from its own over-zealous agents. Id. at 533-34.

My project is different: to focus particularly on the limits of the ability to disclaim truth-telling among sophisticated parties. But Professor Davis's introductory quotation from Joel Feinberg captures my opening empirical intuition:

Not even in the business world—that one area of social life where the "battle of wits" competitive-game model is most persuasive, and people match the shrewdness of their judgments and the cleverness of their stratagems [sic] for getting the better of one another—not even here do rivals voluntarily assume the risk that the other party to an agreement is an outright liar, getting the better of one by plain deceit.

Id. at 485 (citing 3 JOEL FEINBERG, THE MORAL LIMITS OF THE CRIMINAL LAW: HARM TO SELF 285 (1986)).
understanding among lawyers and clients in the hothouse atmosphere of an intense merger or acquisition negotiation.

Part II describes the Abry opinion, primarily because it reflects an archetypal deal from which generalization is possible. Part III is a critique of the doctrinal analysis, and it proposes a doctrinal alternative. Part IV justifies the alternative through an efficiency analysis akin to that proposed by Ayres and Klass, and it also discusses a subject wholly unaddressed in the Abry opinion and not fully discussed by Ayres and Klass in Insincere Promises: The Law of Misrepresented Intent. Specifically, Part IV discusses why the language of contract cannot fully capture the complexities of the world, and why, as a result, we should continually credit the warranties of truthfulness inherent in language through a presumption that the remedy for half-truth fraud exists unless expressly and clearly disclaimed. I draw support for this position from the psychology and philosophy of language (drawing on the works of Wittgenstein and Habermas), as well as from the place the law sits in relation to everyday life (drawing on the works of Austin Sarat and Thomas Kearns).

II. THE ABRY DECISION

The facts of the case reflect the usual complexity and multiplicity of parties in private equity acquisitions, but the core allegations underlying the legal issue are relatively simple. After describing the facts, I will turn to theory. Grounding theory in these archetypal circumstances of a dispute will be helpful in bridging theory and the real world.

A. The Context of Private Equity

Private equity firms are generally in the business of buying and selling target companies, with the idea that the original cost to purchase, plus any additional investment, will be less than the proceeds upon resale of the company to a so-called strategic buyer, another private equity firm, or to the public in an initial public offering. Valuation of companies for purposes of mergers and acquisitions is an art and science. Although finance theory says the value of a company is always equal to the present value of its future cash streams, the fact that the exercise is a prediction necessitates the use of estimates and heuristics. The particular heuristic in the publishing business in Abry was that publishing companies should sell for ten times a company's free cash flow based on EBITDA, which means earnings before interest,

---

23Id. at 181-201.
taxes, depreciation, and amortization.\textsuperscript{24} EBITDA is often used as a surrogate for operating cash flow,\textsuperscript{25} and applying a multiplier to EBITDA allows a party to estimate and incorporate risk and relative profitability of an industry.\textsuperscript{26}

B. The Deal

1. The Setup

Providence Equity Partners (Seller or S) was a private equity firm.\textsuperscript{27} According to the complaint, S had purchased a company called F & W Publications, Inc. (Target), which was in the book and magazine publication and distribution business. At a certain point, S decided it wanted to sell Target and embarked on the usual merger and acquisition deal process.\textsuperscript{28} S controlled the process, but it was Target's management, who had no previous affiliation with S, that knew the company intimately.\textsuperscript{29} S announced publicly that it would sell Target through an auction conducted by Credit Suisse First Boston (CSFB), an investment banking firm, which began contacting and meeting potential buyers.\textsuperscript{30} Although the case does not say so explicitly, there can be little doubt that CSFB carried out due diligence by conducting plant tours, creating document rooms, arranging management presentations, and assembling financial records for potential buyers.

2. The Buyer and the Contract

Abry Partners (Buyer or B) was one of the suitors for Target. Like other potential buyers for companies, B conducted the usual due diligence by

\textsuperscript{24}See Abry, 891 A.2d at 1038.
\textsuperscript{27}Abry, 891 A.2d at 1036. Vice Chancellor Strine also referred to Providence, and the entities it controlled, as "the Seller" throughout his opinion. Id. at 1037.
\textsuperscript{28}The vice chancellor referred to this deal as "the usual multiplicity of related entities involved when a portfolio company of one private equity firm is sold to another private equity firm." Id. at 1036.
\textsuperscript{29}Id. at 1040-41.
\textsuperscript{30}Id. at 1038.
investigating Target.\textsuperscript{31} In parallel, it entered into contract negotiations with S. The typically lengthy acquisition agreement had six critical provisions:

(1) In the main body of the agreement, Target, and not S, made contractual representations and warranties about the condition of Target's business.\textsuperscript{32}

(2) The agreement also required S to certify the accuracy of the representations and warranties in the contract, which had the effect of making S a direct obligor on those provisions.\textsuperscript{33}

(3) As is customary, Seller warranted that the financial statements fairly represented the financial condition of Target in all material respects.\textsuperscript{34}

(4) There were two variants of relatively common provisions under which the buyer disclaimed any reliance on representations and warranties other than those set forth in the agreement.\textsuperscript{35}

\textsuperscript{31}Abry, 891 A.2d at 1038-40. After closing the sale, B alleged that it had discovered financial manipulations and book order fulfillment system manipulations that inflated Target's value improperly. \textit{Id.}

\textsuperscript{32}\textit{Id.} at 1043.

\textsuperscript{33}\textit{Id.} Vice Chancellor Strine focused on the distinction between the primary source of the representations, Target itself, and a later provision in the agreement whereby S agreed to "put its wallet behind the Company's representations and warranties to a defined extent." \textit{Id.} I think the vice chancellor's purpose was to show the closely negotiated nature of S's contractual obligation, but, for my purposes, I do not see a significant point in the way the deal was structured. S was bound to the representations and warranties as thoroughly as if it had made them in the first instance.

\textsuperscript{34}The provision addressing the company's financial position stated: The Company Financial Statements: (i) are derived from and reflect, in all material respects, the books and records of the Company and the Company Subsidiaries; (ii) fairly present in all material respects the financial condition of the Company and the Company Subsidiaries at the dates therein indicated and the results of operations for the periods therein specified; and (iii) have been prepared in accordance with GAAP applied on a basis consistent with prior periods except, with respect to the unaudited Company Financial Statements, for any absence of required footnotes and subject to the Company's customary year-end adjustments. \textit{Id.} at 1041-42.

\textsuperscript{35}Section 3.23 of the contract stated: EXCEPT AS EXPRESSLY SET FORTH IN THIS ARTICLE III, THE COMPANY MAKES NO REPRESENTATION OR WARRANTY, EXPRESS-ED OR IMPLIED, AT LAW OR IN EQUITY IN RESPECT OF THE COMPANY OR THE COMPANY SUBSIDIARIES, OR ANY OF THEIR RE-SPECTIVE ASSETS, LIABILITIES OR OPERATIONS, INCLUDING WITH RESPECT TO MERCHANTABILITY OR FITNESS FOR ANY PARTICULAR PURPOSE, AND ANY SUCH OTHER REPRESENTATIONS OR
(5) The indemnity provision provided that S would be liable for damages that "have arisen out of or . . . have resulted from, in connection with, or by virtue of the facts or circumstances (i) which constitute an inaccuracy, misrepresentation, breach of, default in, or failure to perform any of the representations, warranties or covenants given or made by the Company or the Selling Stockholder in this Agreement . . . ."\(^36\)

(6) The agreement limited Seller's obligation to indemnify to a $20 million indemnity fund that was to be "the sole and exclusive remed[y] of the Acquiror, the Acquiror Indemnified Persons, the Selling Stockholder, and the Company with respect to this Agreement and the Sale contemplated hereby."\(^37\)

Under the executed agreement, B purchased Target for $500 million,\(^38\) but S limited itself to $20 million in damages for breach of contract.

3. The Seller's Alleged Misrepresentations

As is typical in the sale of portfolio companies by private equity firms,\(^39\) not only did S's management direct the sale process, but it set the

WARRANTIES ARE HEREBY EXPRESSLY DISCLAIMED. ACQUIROR HEREBY ACKNOWLEDGES AND AGREES THAT, EXCEPT TO THE EXTENT SPECIFICALLY SET FORTH IN THIS ARTICLE III, THE ACQUIROR IS ACQUIRING THE COMPANY ON AN "AS IS, WHERE IS" BASIS. THE DISCLOSURE OF ANY MATTER OR ITEM IN ANY SCHEDULE HERETO SHALL NOT BE DEEMED TO CONSTITUTE AN ACKNOWLEDGEMENT THAT ANY SUCH MATTER IS REQUIRED TO BE DISCLOSED.

*Abry*, 891 A.2d at 1042-43. In addition, Section 7.8 provided:

Acquiror acknowledges and agrees that neither the Company nor the Selling Stockholder has made any representation or warranty, expressed or implied, as to the Company or any Company Subsidiary or as to the accuracy or completeness of any information regarding the Company or any Company Subsidiary furnished or made available to Acquiror and its representatives, except as expressly set forth in this Agreement . . . and neither the Company nor the Selling Stockholder shall have or be subject to any liability to Acquiror or any other Person resulting from the distribution to Acquiror, or Acquiror's use of or reliance on, any such information or any information, documents or material made available to Acquiror in any "data rooms," "virtual data rooms," management presentations or in any other form in expectation of, or in connection with, the transactions contemplated hereby.

*Id.* at 1041.

\(^{36}\) *Id.* at 1044.

\(^{37}\) *Id.*. The exclusive remedy provision did permit a claim for specific performance and injunctive relief if S or Target failed to comply with the contractual covenants. *Id.*

\(^{38}\) *Id.* at 1038.

\(^{39}\) *Abry*, 891 A.2d at 1036.
financial parameters and expectations for the sale.\textsuperscript{40} What is critical here is the allegation that S had already determined it wanted to derive a purchase price for Target in excess of $500 million,\textsuperscript{41} necessitating that the financial statements show EBITDA of approximately $51 million, given the industry value heuristic.\textsuperscript{42} B alleged, ultimately, that S had undertaken at least four different deceptive manipulations and nondisclosures to support the purchase price: (1) overstating its revenues through a practice known as "backstarting,"\textsuperscript{43} (2) underestimating reserves for book returns and uncollectible accounts,\textsuperscript{44} (3) "channel stuffing,"\textsuperscript{45} and (4) misrepresenting the implementation of an order entry system.\textsuperscript{46}

\textsuperscript{40}Id. at 1034.
\textsuperscript{41}Id. at 1038. Buyer alleged that S wanted to sell the company for $510 million. Id.
\textsuperscript{42}Id.
\textsuperscript{43}Revenue recognition is one of the hottest topics in accounting fraud. BARRY J. EPSTEIN, HANDBOOK OF ACCOUNTING AND AUDITING 2007-1, at C2-4 (2006). Generally, when there is an upfront fee, with a service provided over time, GAAP and the SEC require that "revenue recognition should occur over time, reflecting the provision of service." Id. at C2-17. More specially, in the magazine business, "paid subscriptions received in advance should be recorded as a liability for product or services to be provided — a liability account — and amortized to revenue as the product or services are provided to customers." Id. at D8-8.

If handled honestly, this is one of the most attractive features of a subscription-based business because the firm takes in cash before it has to perform. To over-simplify, if a subscriber pays $300 for a three-year subscription, under generally accepted accounting principles, the cash received may be counted in cash flow statements, but it may not be called revenue for income statement purposes until the company earns it by sending out a magazine. But the firm has financed its operations by what is effectively a zero-interest loan from the customer. The allegation here was that S wanted to show higher revenue, and therefore higher earnings, and thus caused Target to send back issues of the magazines upon subscription, using that as an excuse to accelerate the amortization of cash into recognized revenue. \textit{Abry}, 891 A.2d at 1038.

\textsuperscript{44}Book return reserves are a cost of the business and are reflected generally as a reduction of accounts receivable. EPSTEIN, supra note 43, at D8-25. A typical GAAP financial statement will provide something like the following in the notes:

The Company provides an estimated allowance for doubtful accounts and for future returns on sales made during the year principally based on historical experience. The allowance for doubtful accounts and returns (estimated returns net of inventory and royalty costs) is shown as a reduction of accounts receivable in the accompanying consolidated balance sheets and amounted to $[ ] million and $[ ] million at [ ], 200[ ] and 200[ ], respectively.

\textit{Id.}

Return reserves in the book publishing industry are particularly sensitive because the reduction of accounts receivable reflects a cost in the present period for an event that is anticipated to occur. Thus:

Reserve for returns, generally determined on a title-by-title basis, is perhaps the most subjective valuation made in book publishing operations. There is no "correct" method of calculating this reserve; instead, industry and internal statistics on past returns are compiled and percentages are determined by type of book. The percentage is then applied against gross sales.

\textit{Id.} at D8-21. Hence, return reserves are a fruitful avenue if a company wants to underestimate its costs deliberately and thereby show higher earnings in a particular period.

\textsuperscript{45}Abry, 891 A.2d at 1039. In this case, channel stuffing "involved the Company offering higher-than-normal discounts to book retailers and discounts to more customers than normal, which
C. The Denouement and the Buyer's Claim

After the closing, B discovered the various misrepresentations and concluded that it had paid $500 million for a business that was fairly worth $400 million.47 B claimed that S and the management of Target had together manipulated Target's financial statements to induce B to buy Target at an excessively high price.48 Accordingly, B alleged not only that the usual financial representations and warranties in the agreement were false but also that S had defrauded B by knowingly making false representations within the contract and outside of the contract in the course of B's due diligence.49

No doubt frustrated by the $20 million damage cap it negotiated on a $500 million purchase, B sought rescission of the agreement based on fraud and misrepresentation.50 S moved to dismiss for failure to state a claim, contending that (1) B had disclaimed any reliance on extracontractual representations, and (2) B had agreed its only remedy against S for misrepresentation was an arbitration claim restricted to the $20 million indemnity fund.51 B argued that the language of the agreement did not limit its remedial options and that, in any event, public policy should override any attempt to limit liability for misrepresentation.52

Vice Chancellor Strine concluded: (1) misrepresentations that are outside the contract are nonactionable because of the negotiated disclaimer of reliance;53 (2) the contract language contemplated the exclusive and capped "indemnity pool" as covering liability for fraud as well as contract misrepresentation;54 and (3) a well-pled claim (i.e., with particularity), artificially inflated revenues." Id. "Channel stuffing" may or may not be a misstatement of the financial statements themselves, although B alleged this as another way in which book returns were underestimated. Id.; see generally EPSTEIN, supra note 43, at C2.01[4][b]. Even in the absence of a contemplated sale, a company may try to increase its reported earnings in a given period by offering terms to customers that make it attractive to buy in current, rather than future, reporting periods. As an example, management may perceive that fourth quarter earnings are going to fall short and will offer discounts or extended payment terms. If the products are shipped before the end of the period, they may be counted legitimately as sales revenue. Often, however, there is an adverse impact on revenue in the subsequent quarter because customers have all of the products that they need. Where the business is being sold at the end of such a reporting period, a buyer may take the revenue numbers for the current period as indicative of annualized sales and discover, only after closing, that the practice caused earnings to be inflated. The Buyer in Abry alleged that S manipulated its financial statements in this exact manner by channel stuffing. Abry, 891 A.2d at 1039.

46Id. at 1039-40.
47Id. at 1040.
48Id. at 1038.
49Abry, 891 A.2d at 1040.
50Id.
51Id. at 1052.
52Id. at 1052-53.
53Abry, 891 A.2d at 1054-55.
54Id. at 1055.
based on fraud and on contract representations known to be false and made intentionally, may be pursued in Delaware, regardless of contract language to the contrary, as a matter of public policy.\textsuperscript{55}

III. THE CRITIQUE

A. The Doctrinal Critique

1. The Source of the Problem

In denying Buyer's fraud claims under the disclaimer language in the agreement in \textit{Abry}, Vice Chancellor Strine offered thoughtful reasons supporting a conclusion that the language of the agreement controlled.\textsuperscript{56} The opinion went awry, however, because the antireliance provision, and Vice Chancellor Strine's powerful reaction to it, blinded him to the fundamental nature of the alleged wrong.

Initially, Vice Chancellor Strine came to the conclusion, purely as a matter of contract interpretation, that the parties agreed to insulate \textit{S} from the legal consequence of outright lying because of the wording of the indemnity clause.\textsuperscript{57} \textit{S} agreed to be liable for "an inaccuracy, misrepresentation, breach of, default in, or failure to perform, any of the representations, warranties or covenants" with respect to the agreement and the contemplated sale.\textsuperscript{58} \textit{B} contended that the word "misrepresentation" as used in an acquisition agreement means \textit{innocent misrepresentations} (i.e., the type of misrepresentations that might arise if warranties and covenants turn out to be inaccurate) that appear in the agreement itself.\textsuperscript{59} Indeed, that is the point of the disclaimer of extracontractual representations in the agreement: \textit{B} was not to be permitted to substitute an extracontractual representation for one found in the agreement.\textsuperscript{60} Nevertheless, Vice Chancellor Strine concluded that the term "misrepresentation" must have meant both misrepresentations within the agreement as well as misrepresentations related to the sale outside of the agreement.\textsuperscript{61} Moreover, he concluded that the ordinary meaning of

\textsuperscript{55} \textit{Id.} at 1064.

\textsuperscript{56} See \textit{id.} at 1053-55.

\textsuperscript{57} \textit{Abry}, 891 A.2d at 1053-55 (relying on contract law and plain meaning to construe the section at issue).

\textsuperscript{58} \textit{Id.} at 1053 nn.40-41.

\textsuperscript{59} \textit{Id.} at 1053.

\textsuperscript{60} See, e.g., \textit{id.} at 1041 (noting that section 7.8 of the agreement held that the buyer acknowledged that the seller did not make "any representation or warranty, expressed or implied... except as expressly set forth in this Agreement").

\textsuperscript{61} \textit{Abry}, 891 A.2d at 1054.
"misrepresentation" included both innocent and deliberate misrepresentations. Combined with the contractual limitation on damages, he inferred that the parties intended to excuse S for outright lying to the extent the financial impact of the lies exceeded $20 million. Because it seemed that there was something amiss in this result, however, Vice Chancellor Strine resorted to public policy to hold that the fraud remedy (and rescission) would be available notwithstanding the apparent disclaimer. It is absolutely clear that Vice Chancellor Strine had no sympathy for the apparent opportunism implicit in B's resort to the fraud remedy. The vice chancellor stated:

The teaching of this court . . . is that a party cannot promise, in a clear integration clause of a negotiated agreement, that it will not rely on promises and representations outside of the agreement and then shirk its own bargain in favor of a "but we did rely on those other representations" fraudulent inducement claim.

Indeed, the judge castigates B as a liar:

To fail to enforce non-reliance clauses is not to promote a public policy against lying. Rather, it is to excuse a lie made by one contracting party in writing — the lie that it was relying only on contractual representations and that no other representations had been made — to enable it to prove that another party lied orally or in a writing outside the contract's four corners. For the plaintiff in such a situation to prove its fraudulent inducement claim, it proves itself not only a liar, but a liar in the most inexcusable of commercial circumstances: in a freely negotiated written contract. Put colloquially, this is

---

62 Id. at 1053. I have real doubts, both as an empirical and as a theoretical matter, whether this was the correct conclusion. Generally, under basic Coaseian economics, we would set a default rule of law for interpretation of a contract as the most likely hypothetical bargain and expect the parties to state explicitly if they wanted to take themselves out of the default approach. For a brief explanation of the Coase theorem, see infra note 94. My own experience as a negotiator of complex deals tells me that it is highly unlikely that parties would expect the interpretive default rule to be a free pass for promissory fraud, but I recognize that is not a rigorous empirical statement. Nevertheless, had Vice Chancellor Strine interpreted "misrepresentation" as advocated by B, the motion to dismiss would have been resolved without a need to resort to public policy. I will return to this interpretive issue later.

63 Abry, 891 A.2d at 1055.
64 Id. at 1064.
65 Id. at 1057.
necessarily a "Double Liar" scenario. To allow the buyer to prevail on its claim is to sanction its own fraudulent conduct.66

The doctrinal irony here is that the Abry case is not really about the conflicting representations, both inside and outside the contract. Nor, as is typically the case in disputes of this kind, is the case about the clear agreement of the buyer not to rely on "puffing" or even false statements made in the context of the complex process of investigation and negotiation of a business acquisition. If we consider a representation to be like a promise, then, like Ayres and Klass or Vice Chancellor Strine, we will focus on the representing party's intention to carry through on the representation or promise.67 And the natural focus of the disclaimer will be on the negation of an affirmative: the buyer did not rely on the representation or promise in going forward with the deal.68

But that is not what happened here. The vice chancellor went astray with his focus on representations as opposed to the other two ways fraud can arise: (1) omissions and (2) half-truths. If we merely focus on affirmative representations, the distinction between intracontractual and extracontractual representations is relatively easy to understand. The essence of the disclaimer is a counter-promise from the buyer to the following effect: "Whether or not I relied on the affirmative representations that were contained in the written text of the contract, I promise categorically that I did not rely on anything affirmatively presented to me outside of the written text."69

But an omission is not an affirmative misrepresentation; it is the absence of a representation. So how would a buyer disclaim an omission? Omission liability arises when there is a duty to disclose and one fails to do

66Id. at 1058.
67See Abry, 891 A.2d at 1053 (noting that parties make misrepresentations "usually with the intent to deceive"); AYRES & Klass, supra note 2, at 99.
68Other cases reach similar results. In Harsco Corp. v. Segui, 91 F.3d 337 (2d Cir. 1996), the court found that a contract provision specifically disclaiming reliance on representations made outside the contract barred an action for fraud. Id. at 339. The court distinguished an earlier holding that a contract provision could not operate as a bar to an action for fraud. Id. at 344 (distinguishing Rogen v. Ilikon Corp., 361 F.2d 260 (1st Cir. 1966)). The Harsco court observed that the parties before it were "sophisticated business entities negotiating at arm's length" and had "relative parity" in their bargaining power. Id. The court also noted that the plaintiff had been given the opportunity to conduct two weeks of due diligence and a chance to cancel the deal if it were unable to confirm the truth of the contractual representations. Id.; see also Clements Auto Co. v. Serv. Bureau Corp., 444 F.2d 169, 178 (8th Cir. 1971) (noting that "a general disclaimer clause is ineffective to negate reliance on even innocent misrepresentations"); cf. Dannan Realty Corp. v. Harris, 157 N.E.2d 597, 600 (N.Y. 1959) (holding that a plaintiff who agreed contractually that it would not rely upon extracontractual representations before a sale and who conducted due diligence could not bring a claim for fraud against the seller).
69Abry, 891 A.2d at 1057.
so.\textsuperscript{70} The contract would have to disclaim the duty of disclosure. The language would read something like: "our understanding is that this sale is 'as-is, where is, with all faults,'" or "if I said something that was a lie, you have no remedy."\textsuperscript{71} In short, that is the doctrine of caveat emptor. But we do not really find that level of disclaimer in an acquisition agreement. We do allow due diligence, and there is an expectation that the seller will not withhold data, but it seems to me the fraud remedy for extracontractual omissions is the only backstop to address the duty of disclosure.

That brings me to the half-truth liability Vice Chancellor Strine never addresses. Half-truth liability is based on the duty to disclose the whole truth if you make a half-truth representation.\textsuperscript{72} It is a hybrid of affirmative misrepresentation and omission.\textsuperscript{73} Donald Langevoort asked, "Why do we have law barring affirmative misrepresentation in the first place? Why don't we say that reasonable people should always do their own 'due diligence' investigation rather than rely on information provided by someone with an obviously conflicting interest?"\textsuperscript{74} His answer is the one we would expect: we reduce transaction costs by having the knowledgeable party disclose rather than have the uninformed party investigate.\textsuperscript{75} Langevoort observed, crucially, that (1) the same economic logic applies to half-truths,\textsuperscript{76} and that (2) it is a continuum from misrepresentation to half-truth to non-disclosure,\textsuperscript{77} noting:

\textsuperscript{70}ReSTATEMENT (SECOND) OF Torts § 551 (1977).
\textsuperscript{71}I have tried to write a provision that disclaims omission liability, and it is almost impossible to write, short of saying, "I have the right to lie to you, and you cannot do anything about it."
\textsuperscript{72}ReSTATEMENT (SECOND) OF Torts §§ 529, 551(2)(b) (1977). A half-truth occurs where the person making the representation states a partial disclosure of the material facts, but the person making the representation "knows or believes that the undisclosed facts might affect the recipient's conduct in the transaction at hand." \textit{Id.} § 529 cmts. a-b.
\textsuperscript{73}See Junius Constr. Co. v. Cohen, 178 N.E. 672, 674 (N.Y. 1931) (Cardozo, C.J.) ("We do not say that the seller was under a duty to mention the projected streets at all... What we say is merely this, that having undertaken or professed to mention them, he could not fairly stop halfway, listing those that were unimportant and keeping silent as to the other."). In \textit{Ragsdale v. Kennedy}, 209 S.E.2d 494 (N.C. 1974), the court made a similar finding:

When plaintiff undertook to describe the business as a "gold mine" and a "going concern" he incurred a concomitant duty to make a full disclosure of any extenuating financial circumstances which counteracted his positive assertions concerning the condition of the corporation. ... [E]ven though a vendor may have no duty to speak under the circumstances, nevertheless if he does assume to speak he must make a full and fair disclosure as to the matters he discusses. \textit{Id.} at 501.
\textsuperscript{75}\textit{Id.}
\textsuperscript{76}\textit{Id.} at 94-95.
\textsuperscript{77}\textit{Id.} at 96.
Almost all nondisclosure cases arise in bargaining settings where there is indeed much said between the parties. Under these circumstances, what the court is being asked to do is determine what inferences the buyer can fairly draw from the seller's statements and omissions. Here the buyer's inferences may be more extensive—there is more interpretive work going on—but the difference is only in degree.  

Even though there may be circumstances in which we may believe the informed party retains a privilege not to disclose, "the [party's] willingness to speak on the subject assuages our concern about forcing disclosure of private information, causing us to move the line toward disclosure duty even where there is some lingering ambiguity as to the extent of the implication."  

Professor Langevoort's continuum, it seems to me, subsumes the entire distinction between intracontractual and extracontractual representations that Vice Chancellor Strine tried to make. Or, to put it another way, a buyer's disclaimer of reliance on an affirmative representation does not disclaim the "omission"-style liability that ought to arise if a seller tells a half-truth. What makes these facts difficult (and interesting) is an underlying sense that courts ought not to be troubled with fraud claims between sophisticated parties (who have the ability to ask the pertinent questions), regardless of reliance or nonreliance on anything outside the contract.  

2. A Doctrinal Alternative  

At this point, I offer a doctrinal alternative to the one employed by Vice Chancellor Strine in the Abry decision. Had I decided the case, I would have reached the same result as Vice Chancellor Strine but on a wholly different basis. As a result, there would have been no need to address the public policy issue, and the holding would, I contend, be a default rule for antireliance clauses that maps far better onto the most likely hypothetical bargain of the parties than the rule in Abry. In Sections 3.23 and 7.8 of the agreement, S did everything that most sellers do to focus the attention of the buyer on the express representations of the agreement and to disclaim anything that falls outside of the agreement. But the Seller did not disclaim

---

78Langevoort, supra note 74, at 96.
79Id. at 97.
80See, e.g., Grumman Allied Indus., Inc. v. Rohr Indus., Inc., 748 F.2d 729, 737 (2d Cir. 1984) ("Where sophisticated businessmen engaged in major transactions enjoy access to critical information but fail to take advantage of that access, New York courts are particularly disinclined to entertain claims of justifiable reliance.").
81Abry Partners Acquisition V, L.P. v. F & W Acquisition, LLC, 891 A.2d 1032, 1041, 1042-43 (Del. Ch. 2006). The "as-is, where-is" clause is interesting because sellers might argue that
the duty to tell the whole truth if it told part of the truth. Rather, all S did was to say that its duty-creating affirmative statements were those in the contract and not those made outside the contract.

I would have given effect to the antireliance provisions in a more precise way. Specifically, my rule would be: the disclaimer should only be effective in the instances where either (1) the extracontractual representation conflicts with the contractual representation, or (2) the contract is wholly silent on the subject matter of the extracontractual representation. A disclaimer of reliance on extracontractual representations cannot and should not be deemed to impact the half-truth or omission liability that may well be the natural consequence of having made the contractual representation. Moreover, the burden should be on the party asserting the antireliance clause to show that it was intended to cover anything but liability arising wholly as a result of the falsity of extracontractual representations. But to justify this result, I need to turn to theory.

B. The Theoretical Critique

1. Restating the Problem

I propose to make the theoretical problem simpler by using hypothetical provisions. In Appendix A, I have proposed a series of hypothetical cases demonstrating the increasing complexity of the misrepresentations, half-truths, and omissions that the nonreliance clause could be intended or construed to cover. For purposes of the text, I will focus on three cases: cases 2, 3, and 7. In each case, the contract provides: "There are no, and Buyer disclaims any reliance on, representations or warranties, except those expressly made in the contract."

Case 2: The contract is silent on the subject of unionization of facilities. A high-ranking officer of Seller states during a management presentation that Company A does not have any unionized facilities. It turns out the company does have a unionized facility. If Buyer relied on that statement at the presentation, I would give effect to the antireliance clause. By its silence on the subject, the contract created an implicit conflict between the external and internal representations. There were no representations about unionized facilities within the contract on which Buyer could rely according to its own agreement, and the provision exculpates Seller.

---

It negates any duty of truth-telling other than that as set forth expressly in the agreement. Because my doctrinal argument is that the assertion of any representations creates the possibility of half-truth liability, however, the only really effective "as-is, where is" clause would be one in which the contract mentions no single affirmative statement about the condition of the business. And, as we know, that almost never happens!
Case 3: The contract states that the company does not have any unionized facilities. There are no other extracontractual representations, but the same high-ranking officer of Company A knows that the workers at more than one plant have approved the formation of a union. Importantly, the union election has not yet been certified by the National Labor Relations Board (NLRB), and so, technically, the company still does not have any unionized facilities.

Here, the outcome will depend on the interpretation of the word "unionized." Was it intended to include an approved but uncertified union as well as established unions? That is unclear. If it is absolutely clear to all concerned that "unionized facilities" does not include one in which the union has been approved but the election has not been certified by the NLRB, then there can be no fraud because there is no untrue statement.

But what is the relationship of scienter to the ambiguity of the original representation? The example demonstrates the possibility of a half-truth, even in what would have seemed at the outset to be a simple and clear affirmative representation. A "laissez-faire" or purely contractual approach would place the burden on the buyer to obtain the correct information by asking the correct question, or to create express liability by the prospective elimination of any possible ambiguity.

Case 7: The contract states that the company's financial statements fairly present in all material respects the financial condition of Company on the dates and for the periods presented in accordance with generally accepted accounting principles (GAAP) consistently applied. In this scenario, as in Abry, the company booked "return reserves." The standard for "return reserves" under GAAP is that the reserves must be based on a reasonable estimate of expected returns. The chief financial officer issued a memorandum to all business unit controllers indicating that it was important, for the purpose of the impending sale of the company, that the company list all return reserves in accordance with GAAP but, nevertheless, the company should err on the side of low estimates rather than high estimates. This had the effect of making the earnings appear higher to the Buyer. Moreover, the Seller deliberately did not disclose this memorandum during the Buyer's exercise of due diligence.

Presumably, the court in Abry would hold the otherwise actionable facts to be beyond the scope of the contract due to the disclaimer. In contrast to the vice chancellor in Abry, however, I would conclude that the original representation was an assurance that the Seller is not telling half-truths outside the contract. Hence, the representation itself created a duty of full disclosure, whether inside or outside the contract. And an extracontractual

---

82See supra note 44.
remedy would not be troubling. If the Seller failed to tell the whole truth within the contract, why should the Buyer be limited to the remedy inside the contract?  

2. An Efficiency Critique

I begin with an efficiency analysis, not because that is the only reason for my rule, but because the role of the law in promoting efficient business transactions was important to Vice Chancellor Strine. The notions of predictability and certainty (as hallmarks of economic efficiency) are mantras in the justification of contract law. Both are also themes in Delaware's effort to compete for the application of its law. Indeed, in Abry, Vice Chancellor Strine attempts to reconcile Delaware's pride in the efficiency of its commercial law against its abhorrence of immunizing fraud. The primary basis for justifying the contractual disclaimer of reliance on the truthfulness of assertions is that this provision, when used, is efficient, promoting predictability and certainty.

I contend that my rule of construction, which would preserve the fraud claim in all but the clearest cases that involve a broad-based disclaimer, is the most efficient result. A similar analysis of promissory fraud in *Insincere Promises: The Law of Misrepresented Intent* is instructive. As I have noted, the concerns there are somewhat different from mine. Indeed, the choice

---

83I also propose a somewhat simpler hypothetical case that I think raises the same half-truth issue as that of Case 7 of the Appendix. Seller and Buyer write a contract for the sale of a car. The sale is "as-is, where-is," except that the Seller represents and warrants that the tires were replaced at 40,000 miles. The contract contains the following clause: "There are no, and Buyer disclaims any reliance on, representations and warranties, except those expressly made in the contract." Buyer discovers after purchasing the car that seller did not replace the tires because of ordinary wear and tear but rather because the car had been in an accident that had caused the tires to be destroyed. A reasonable inspection of the car did not reveal any other indication of an accident. Buyer would not have bought the car had he known of the accident.

Does Buyer have a claim for fraud? It is undisputed that Buyer has an affirmative right to rely on the tire representation. I will also assume, for the sake of the discussion, that in the absence of the tire representation, Buyer would have no rights vis-à-vis the accident. The questions, then, are (1) did the representation about the tires create a duty to tell the whole truth about the replacement, and (2) did the disclaimer impact any such duty?

84Abry, 891 A.2d at 1059-60.

85See, e.g., id. at 1048 ("To layer the tort law of one state on the contract law of another state compounds that complexity and makes the outcome of disputes less predictable, the type of eventuality that a sound commercial law should not seek to promote.").


87Abry, 891 A.2d at 1059-60 n.67.

88Id. at 1061.

89Id. at 1059-62.

90See supra Part I.
of a default rule—one that is information-forcing rather than majoritarian91 (at least in the first instance)—ought to differ when we are talking about the difference between a descriptive use and a performative use of language.92 Ayres and Klass would be concerned about the circumstance where a buyer or seller says, "I promise to close on September 30" but has no present intention of performing on that promise.93 The issue in the archetypal Abery-style deal, in contrast, is not whether the seller intends to close. That is a given. Rather, the question is how to interpret a disclaimer of reliance in the face of a statement that x is true about the business.

It is helpful to trace through the process by which Ayres and Klass select a default rule in order to understand the Coaseian94 parameters at play and to distinguish the problem of a secret intention not to perform from the problem whereby a seller utters a half-truth about a business. J.L. Austin's insight was to identify those speech acts that are not descriptive of an independent state of reality, that are not capable of being either true or false, but are themselves the very reality (what Austin calls "performatives")).95 Examples of performatives include marriage vows, promises, bequests, and namings.96 Under this framework, Ayres and Klass focused on whether the speaker who uttered statements that appeared to be performatives intended them to be performatives. But in order to determine whether the promisor intended, at the time of the promise, to perform, it is first necessary to interpret what the promisor promised.97 Ayres and Klass lay down a set of interpretive defaults and rules for contracting around them, and those rules apply almost entirely to the disclaimer problem.98

Ayres and Klass do not advocate the elimination of the parties' ability "to choose what to say or not to say about their intentions, about the

91See AYRES & KLAFF, supra note 2, at 99-101. Ayres and Klass define a "majoritarian default" as one where the court determines what the majority of contracting parties would choose in a similar situation. Id. at 99. For more information on the information-forcing default, see id. at 83-112.

92Id. at 21 (distinguishing descriptive use from performative use of language by noting that performative use means the use of words "not to describe the world but to act in and on it").

93Id. at 99.

94The Coase theorem holds that in the absence of transaction costs, the presence of clear default rules, and freedom of contract, default rules will have no impact on welfare-enhancing transactions. RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 49-52 (6th ed. 2003). The result in practice is that "transaction costs are large and that economic actors tend to arrange their institutions with an eye to these costs." Robert C. Ellickson, The Case for Coase and Against "Coaseanism," 99 YALE L.J. 611, 612 (1989).

95See J.L. AUSTIN, HOW TO DO THINGS WITH WORDS (J.O. Urmson ed., 1965). Austin defines "performatives" as "expression[s] very commonly only used in naming the act which, in making such an utterance, I am performing." Id. at 32.

96Id. at 26-34.

97AYRES & KLAFF, supra note 2, at 86.

98Id. at 83-112.
probability of their performance, and about whether they think it in the promisee’s self-interest to rely."\textsuperscript{99} Their only mandatory rule is that "[e]very promise represents at least that the promisor does not have an intention not to perform."\textsuperscript{100} The question, then, is the appropriate default rule around which the parties may choose to negotiate. Such a default could be based primarily on what the majority of contracting parties would choose, on one hand, or "information-forcing effects," on the other (although it is entirely possible that the majoritarian default has information-forcing effects, or vice versa).\textsuperscript{101}

Ayres and Klass posit that a promise could have default interpretations across a continuum of meaning about the probability of performance (from definite to positive to opaque), as well as the promisor’s assurance to the promisee that the promisee should feel comfortable in relying on the promise (from fully warranting to semi-warranting to non-warranting).\textsuperscript{102} Their conclusion is that performatives that look like promises and that relate to the promisor’s expectation that he will perform should be subject to two default representations, which they call "positive" and "semi-warranting."\textsuperscript{103} In other words,

A’s statement "I promise to x" should be that A says both that she intends to x and that she doesn’t believe that the probability of her xing is so low that it is not in the promisee’s rational self-interest to rely [the semi-warranting representation]. In addition, the default meaning of A’s saying that she intends to x is that there is at least a 50 percent chance that she will x [the positive representation].\textsuperscript{104}

We should note that Ayres and Klass have not opted for a default rule that would force the most information.\textsuperscript{105} The promise performative can be presumed to be richer or poorer in information.\textsuperscript{106} One can presume that promises "tell the promisee that the probability of performance is at least some value (definite-probability), that the probability of performance is so great that the promisee can safely rely on it (warranting), or that the probability of performance is secured by the promisor’s intention to perform

\textsuperscript{99}Id. at 89.
\textsuperscript{100}Id. at 90.
\textsuperscript{101}AYRES & KLAS, supra note 2, at 90.
\textsuperscript{102}Id. at 83-112.
\textsuperscript{103}Id.
\textsuperscript{104}Id. at 99.
\textsuperscript{105}AYRES & KLAS, supra note 2, at 99 (arguing that "[i]nformation-forcing defaults tend to penalize one or both parties").
\textsuperscript{106}Id. at 90-91.
Whether one construes a promise to include a warranty about the promisee's level of reliance, the promise requires the promisor to gather information about the promisee. Ayres and Klass conclude that "if our only concern were to maximize information disclosure, the best interpretive default would be that a promise \textit{simpliciter} is both positive and fully warranting." By this, Ayres and Klass argue that if the promisor thought the likelihood of performance was low enough that the promisee ought not to rely on it, the promisor would be obliged to say so or be liable for promissory fraud. Because this would require the promisor to gather information about the promisee's need or desire to rely, Ayres and Klass contend that such a default "does not reflect what most promisors would choose to say with their promises."

It is important, however, to elaborate upon the proposed default rule and distinguish it as it relates to the creation of either a performative or the purely descriptive aspects of the representation. Ayres and Klass think the information costs will be too high, and therefore suboptimal, for the encouragement of value-creating promises if a promisor is presumed to have made full warranties about the promisee's ability to rely. Yet the positive default rule for the promisor's own intent is information-forcing—"[a]bsent contrary circumstances, a promise represents that the promisor intends to perform."

A performative is, however, necessarily an affirmative representation. Let us now consider the Abry issue in which we seek to set a default rule for the scope of a seller's representations in the face of the buyer's disclaimer of any reliance on extracontractual matters. The same efficiency-enhancing, information-forcing default rule that requires the promisor to disclose if she does not intend to perform supports liability, as in my hypothetical Case 3, where the promisor deceives intentionally by making representations that are only partially true:

Information-forcing defaults tend to penalize one or both parties, giving them an incentive to reveal information in order to opt out of the default. The desirability of an information-forcing default falls under the heading of informational effects and is governed by the general principle that interpretive rules

\begin{footnotes}
\item[107] Id. at 90.
\item[108] Id. at 99-101.
\item[109] \textit{AYRES \\& KLASS}, supra note 2, at 100.
\item[110] Id.
\item[111] Id.
\item[112] Id. at 100-01.
\item[113] \textit{AYRES \\& KLASS}, supra note 2, at 206.
\item[114] Id. at 2.
\end{footnotes}
should give parties an incentive to disclose the optimal amount of information.\textsuperscript{115}

For purposes of stating a default rule, we ought to be able to say, as a matter of common sense, it is cheaper for the warrantor than the warrantee to determine whether an affirmative statement has created a half-truth. It is possible that this may not be the case, but then it is incumbent upon the speaker to take some action to provide a warranty other than the one that creates the half-truth (i.e., the warrantor must contract around the default rule). To call the buyer's statement that it will not rely on extracontractual representations an avoidance of the default rule is to forsake the information-forcing nature of the acquisition agreement; the exercise becomes a word game.

Moreover, placing the burden of the default rule on the discloser makes sense intuitively if we consider the motivations of the seller (i.e., the discloser) in the sale of a business. At the closing of a deal, the seller receives typically present cash against the possibility that the buyer may make a claim at some time in the future. My casual empiricism is that sellers view a lost sale as a loss and weigh that loss far more heavily than the future prospect of liability under an indemnity clause. Hence, the natural inclination is to minimize problems, not to disclose. This is in tune with the classic prospect theory advanced by Kahneman and Tversky.\textsuperscript{116}

3. A Linguistic and Social Critique

There is something more than economic incentive at play in setting the default rule for the fine line between innocent and deliberate misrepresentation and the intracontractual and extracontractual instances of truth-telling. Ayres and Klass recall the relatively amoral Holmesian interpretation of a

\textsuperscript{115}Id. at 99.


\textit{[O]ne} of the central features of Kahneman and Tversky's prospect theory is that people evaluate outcomes based on the change they represent from an initial reference point, rather than based on the nature of the outcome itself; also, losses from the initial reference point are weighted much more heavily than gains. This aspect of prospect theory (like its other features) is based on evidence about actual choice behavior. The evaluation of outcomes in terms of gains and losses from an initial reference point, coupled with the special aversion to losses, means that it matters a great deal whether something is presented as a gain or a loss relative to the status quo; a perceived threat of a loss relative to the status quo weighs more heavily than a perceived threat of foregoing a gain.

\textit{Id.} at 1535-36.
contract: a contractual promise means that the party will either perform or pay damages for nonperformance.\textsuperscript{117} What comes through Ayres and Klass's work, notwithstanding the law's primary concern in commercial matters for consequences, is a distaste for the efficient breach,\textsuperscript{118} at least when it was preceded by an intention never to perform.

By all accounts (legal, economic, and moral), we start with a presumption of truth-telling. Vice Chancellor Strine makes it clear that extracontractual statements carry with them a presumption of truth-telling upon which fraud could be based if the parties "do not clearly state that [they] disclaim reliance upon extra-contractual statements . . . . If parties fail to include unambiguous anti-reliance language, they will not be able to escape responsibility for their own fraudulent representations made outside of the agreement's four corners."\textsuperscript{119} But if it is a moral concern, the presumption of truth-telling is grounded not in a duty for truth-telling but in a concern for commercial consequences if lying is permitted.\textsuperscript{120} The court's rejection of a disclaimer of fraud is primarily based on efficiency grounds: "there is little support for the notion that it is efficient to exculpate parties when they lie about the material facts on which a contract is premised."\textsuperscript{121} Indeed, the supporting footnote for the preceding sentence is to Judge Posner's seminal text, in which he declares, "The lie is different. The liar makes a positive investment in manufacturing and disseminating misinformation. This investment is completely wasted from a social standpoint."\textsuperscript{122}

And yet, it is not wholly a consequential matter. As Vice Chancellor Strine states:

I use the plain word "lie" intentionally because there is a moral difference between a lie and an unintentional misrepresentation of fact. This moral difference also explains many of the cases in the \textit{fraus omnia corrumpit} strain, which arose when the concept of fraud was more typically construed as involving lying, and thus it is understandable that courts would find it distasteful to enforce contracts excusing liars for responsibility

\textsuperscript{117}AYRES & Klass\textsuperscript{, supra note 2, at 4-6; see also Oliver Wendell Holmes, The Path of the Law, 10 Harv. L. Rev. 457, 462 (1897), reprinted in 110 Harv. L. Rev. 991, 995 (1997) ("The duty to keep a contract at common law means a prediction that you must pay damages if you do not keep it, and nothing else.").

\textsuperscript{118}For a discussion of the efficient breach, see POSNER, supra note 94, at 120.

\textsuperscript{119}Abry Partners Acquisition V, L.P. v. F & W Acquisition, LLC, 891 A.2d 1032, 1058-59 (Del. Ch. 2006).

\textsuperscript{120}Vice Chancellor Strine referred explicitly to lying as a moral matter. \textit{Id.} at 1062.

\textsuperscript{121}\textit{Id.} at 1062.

\textsuperscript{122}\textit{Id.} at 1062 n.78 (quoting POSNER, supra note 94, at § 4.6).
for the harm their lies caused.\textsuperscript{123}

I believe there is a reason for this confusion. I am not sure, were Judge Posner to consider it more deeply, that he would conclude some lies, particularly of the "white lie" variety, might well be efficient.\textsuperscript{124}

The issue, then, becomes how broadly one should interpret a disclaimer of truth-telling when it appears in a contract. Like Vice Chancellor Strine, I have no particular compunction against a buyer freely agreeing that it imposes no duties whatsoever upon the seller to say anything at all, truthful or not, about the business. It is certainly possible to write a provision in an agreement that says:

Buyer is simply buying the business. It acknowledges the possibility that nothing the Seller has said in the contract is wholly true, particularly in view of facts or circumstances Seller may have intentionally or unintentionally failed to disclose, and Buyer hereby absolves Seller of any duty to clarify what in hindsight may be deemed to have been a half-truth.

As a result, the question does not turn on what the law of Delaware might endorse as a matter of moral philosophy—whether utilitarian efficiency, on one hand, or deontological revulsion against the telling of lies, on the other. Either might be the basis for law, but neither really captures the complex context of a heavily negotiated business acquisition agreement.

The counterthesis to this is that the negotiations and closing of complex business deals constitute a "linguistic jungle," full of outright lies, nondisclosures, and half-truths, and the only protection is what one's lawyer is able to capture in the four corners of the documents. This counterthesis is consistent with the reemergence in modern contract of the theory of formalism,\textsuperscript{125} particularly in complex transactions, on the presumption that

\textsuperscript{123}Abry, 891 A.2d at 1062.

\textsuperscript{124}See POSNER, supra note 94, at § 4.6 (discussing different types of lies and their legal impact on fraud claims). Indeed, one of the objections to Kant's own categorical views on lying to save a friend is that the result is, nevertheless, offensive to our moral intuition. See, e.g., THOMAS E. HILL, HUMAN WELFARE AND MORAL WORTH 23 (2002). At the risk of political incorrectness, there is also the Talmudic injunction that it is not morally wrong to tell a bride the white lie that she is beautiful even when she is not. See Jonathan Sacks, The White Lie, in COVENANT AND CONVERSATION: THOUGHTS ON THE WEEKLY PARSHA FROM THE CHIEF RABBI (Dec. 25, 2004), available at http://www.chiefrabbi.org/thoughts/vayechi5765.pdf. Presumably, from the standpoint of the parents of the bride, this particular investment in deception was not completely wasteful from a social perspective.

sophisticated business people would prefer a formalistic approach. I suggest instead that the bases for the presumption of truth-telling (and the concomitant narrow construction of disclaimers of truth-telling) are the more fundamental properties of speech acts and our everyday expectations of each other.

In the remainder of this article, I want to suggest that language and social theory serve as an alternative basis for having courts presume that the parties (1) did not adopt the doctrine of caveat emptor, and (2) did undertake the agreement with some consciousness of the law of fraud. Accordingly, any contract language purporting to allow, expressly or implicitly, the right to lie should be construed narrowly. A model, or inspiration, for this theory may be Dennis Patterson's introductory comments to his attempt to articulate a general theory of good faith under Article 9 of the Uniform Commercial Code (UCC). The problem is interesting because, as Professor Patterson observed of the UCC, it is a concrete problem where alternative theoretical approaches might, nevertheless, illuminate the issue.

a. Presumptions Based on the Use of Language and the Warranties of Speech Acts

1. The Illusion of Power Over Interpretation

When we rely on the blunt instrument of language to describe the fine lines on which statements parties relied and did not rely, absolute predictability and certainty collapse, and rightly so. Insights from philosophy of language raise questions about the parties' ability to capture fully the agreement in words to a scientific certainty. The first problem is in the inter-


127 Dennis M. Patterson, Wittgenstein and the Code: A Theory of Good Faith Performance and Enforcement under Article Nine, 137 U. PA. L. REV. 335, 336-41 (1988). Professor Patterson quotes a call for research that seems even more apropos some twenty years after it was made: We need more legal studies that aren't narrowly internalist renditions of doctrine, but that don't try to reduce doctrine to an epiphenomenal reflex of economics or anything else. We need more legal studies that aren't obsessed with the drama of appellate review. Instead we need richly theoretical ways to explore the interaction of law and other institutions.

Id. at 339 n.13 (quoting Don Herzog, As Many as Six Impossible Things Before Breakfast, 75 CAL. L. REV. 609, 630 (1987)). I do not presume any success in offering this study, but it is an aspiration for this piece.

128 Id. at 338-42.
pretation of the word "misrepresentation." P.S. Atiyah, citing Wittgenstein's "family resemblance" argument, commented on this situation:

Too often, the problems which have beset the contract arise precisely because the parties did not foresee the events which have occurred, and they did not, therefore, have any relevant intentions at all. It is true, of course, that a person may use language intended to cover (or exclude) a general class of things without necessarily adverting to each item in the class individually. Wittgenstein gives a well-known example: "Someone says to me: 'shew the children a game'. I teach them gaming with a dice, and the other says, 'I didn't mean that sort of game'."

Hence, the issue is not the assiduousness, preparedness, or foresight of lawyers. The issue is that language and the law are blunt instruments that are often incapable of drawing the fine line of the implicit understanding.

The exercise is foremost one of interpretation. "We interpret an utterance when we choose between different ways of understanding it. Legal interpretation is the activity of deciding which of several ways of understanding a given provision is the correct or preferable way of understanding." For the purposes of this interpretive exercise, the main focus is the utterance in a contract by which the parties agree to rely only on those representations and warranties made in the agreement. We need to parse the language of the antireliance clause as a linguistic sign. To understand what the parties mean when they recite that the buyer relies only upon the representations and warranties contained in the agreement, we must assess it "against the background of public, intersubjective practices." We are projecting several concepts—reliance, representations, and warranty—onto the reality of a relationship between the seller and the buyer. The words are part of the "language game"; as Wittgenstein describes, "the whole, consisting of language and the actions into which it is woven."

For example, Patterson quotes Stanley Cavell's explanation of the grammar of a chair. Under our conception, a chair is not merely something on which we sit. It is not even something on which we sit that serves all the functions of a chair (for example, a rock pushed up against a wall may

130 Dennis M. Patterson, Interpretation in Law, 42 SAN DIEGO L. REV. 685, 687 n.2 (2005).
131 Patterson, supra note 127, at 356.
133 Patterson, supra note 127, at 362 (quoting STANLEY CAVELL, THE CLAIM OF REASON: WITTGENSTEIN, SKEPTICISM, MORALITY AND TRAGEDY 71 (1979)).
serve as a chair, but it is not a chair). "What can serve as a chair is not a chair, and nothing would (be said to) serve as a chair if there were no (were nothing we called) (orthodox) chairs." Thus, to sweep representations into half-truths or omissions and to ignore their differences is to ignore the grammar of the "reliance." An omission or half-truth is no more a representation that something that serves as a chair is a chair. It is somehow related, but it is not the same. We cannot rely on an omission, and to suggest that by disclaiming reliance on a representation we have somehow impacted omissions is to ignore, or at least to gloss over, an important distinction.

This is the trap into which Vice Chancellor Strine fell in his interpretation of the indemnity clause. If the word "misrepresentation" in the indemnity clause did not include an intentional misrepresentation but only the innocent circumstance under which the facts did not match up to the contractual representation, there would have been no issue as to whether Delaware would recognize the right to lie. The problem arose because Vice Chancellor Strine took the contractual provision to anticipate outright lying, and, a fortiori, more subtle forms of deception, like half-truths and palliatives. Here, there is a question whether we are even talking the same language; the court turns to the legal lexicon to define misrepresentation, citing Black's Law Dictionary, and not to what the words signify as linguistic signs in the deal context. To paraphrase Atiyah, someone says to me: shew the buyer an indemnity clause protecting him against misrepresentation. I include a contractual indemnity against fraud, and the other says, "I didn't mean that kind of misrepresentation."

The benefit of contractual representations is that they are a form of strict liability; all we need to determine is if they are untrue (or perhaps materially untrue). It is something altogether different to indemnify the party that relied upon the misrepresentation, not only because the misrepresentation was untrue, but also because of the state of mind of the speaker at the time the representation was made. The antireliance disclaimer makes perfect sense when applied against strict liability assertions of the state of the business. But it becomes nonsensical when the purpose of the assertion was the deception by a half-truth, and the essence of the wrong is in what was not said and could never have been the subject of reliance.

It is a particular conceit of lawyers (and many lawyer-scholars), however, that they can obtain control over the world with a unique ability to map language on reality. Yet I would contend that this is not the case, even for lawyers. That there may be a gap between language and reality is the

---

134 Id.
136 Id. at 1053 (citing BLACK'S LAW DICTIONARY 419 (pocket ed. 1996)).
upshot of thinking in the philosophy of language in recent years. Benjamin Zipursky has observed:

[W]e now realize that the idea that language represents reality is a myth. In fact, the languages of various communities are simply tools we use to get around, to interact, to impose norms on one another, and to carve the world up as we wish at any point in time. Any particular community at any particular time is roughly limited by its language and its conceptual scheme to seeing the world a certain way, but the connection between language and world is ultimately ineffable. Moreover, even with respect to individual speakers, the task of interpretation is daunting, and fundamentally indeterminate.\textsuperscript{137}

The most articulate response to my thesis—that the contractual disclaimer has to be construed narrowly—is that contract negotiations among sophisticated parties are a stylized, ritualized business, and the ordinary use of language defers to the particular language of lawyers (and, I suppose, business people) in that particular setting. As articulated nicely at a workshop on this paper, the reason is that the writing serves to speak to a judge someday if necessary; hence, this lends even more support to the notion that the only words with meaning were those expressly set forth, at least in the face of a disclaimer.\textsuperscript{138}

My thesis is controversial because it tends to undercut the lawyer's self-image of value creation, something on which it is difficult to have a balanced perspective if one has always been a lawyer and has looked at the world through a lawyer's eyes. As someone who has spent a good portion of his life in the exercise of "wordsmithing," even I am troubled by its implication. If making the language clear and precise is what we do as lawyers, why do we bother if it is all for naught? "Not to worry," say my colleagues (implicitly), "we operate in a special community of language technicians in which the relative cost-avoiding positions of the receiver of the statement and the maker of the statement are up for grabs."\textsuperscript{139}

Yet even these language specialists react in ordinary ways when they are the victims of the close parsing of language. Let us consider a thought experiment in which every relevant participant is a lawyer and, hence, an


\textsuperscript{138}I am indebted to Professor Dru Stevenson at the South Texas College of Law for the cogent articulation of this objection.

\textsuperscript{139}See, e.g., Peter Tiersma, \textit{Some Myths About Legal Language}, 2 LAW, CULTURE & HUMANITIES 29, 42 (2006) (noting that legal language can be as precise or imprecise as the author chooses).
equally proficient parser of language. A lawyer related the story of a witness at an evidentiary hearing on whether to lift a temporary restraining order (TRO) which had been issued in a trademark infringement case. The issue was laches, i.e., whether the plaintiff had known about the infringement but nevertheless sat on its rights. The TRO had been issued, in part, on the basis of an affidavit of one of the plaintiff's officers that stated that the officer first became aware of the issue in August. The cross-examining lawyer learned that the officer had really heard about the infringement in February or April, but somehow his affidavit (drafted by his lawyer) ended up with the far more favorable, from a laches perspective, unequivocally false statement that he first heard about the problem much later. Assume that the witness (call him Smith) told his lawyer (call her Ms. Jones) he heard about the infringement in April, forgot about it, but then recalled that he learned of the infringement in August so that his affidavit said, "I became aware in August." This statement is literally true, but it is a half-truth, because what is left out is that Smith also became aware of infringement in April. Assuming the plaintiff is chargeable (for laches purposes) with Smith's earlier knowledge of the infringement, the plaintiff's misrepresentation is a significant half-truth.

In this case, Ms. Jones has deliberately misrepresented the truth. In the adversarial setting, is it fair game for one party to misrepresent the truth and then force the opponent (call her Ms. Johnson) to ferret out the full truth? Presumably, Ms. Jones and Ms. Johnson are equally capable of discerning impreciseness in the language that gives rise to the ambiguity suggesting the half-truth (i.e., does "became aware" imply "first became aware"?). And, assuming Ms. Johnson misses the half-truth, the judge is also a lawyer and is also, presumably, as capable as either lawyer of discerning that kind of trick. So why is everybody so angry (particularly the judge) when it turns out that Ms. Jones has outwitted both Ms. Johnson and the judge?

My thesis is that even sophisticated lawyers presume the truth of the words in their communicative action according to a community standard that is far less precise than lawyers (or economists) would generally like to think. We have an intuitive reaction, even as sophisticated lawyers, that we have been wronged in this instance. If we credit my general thesis about default interpretations as applied to half-truths, we can muster a coherent explanation of the source of the dilemma. But if, in my thought experiment,

---

141 Id.
142 Id.
I make all the lawyers and judges fully rational actors in their use of language, there is no accounting for the sense that something has gone terribly amiss.  

2. The Implicit Warranties of Speech

The issue, however, is not merely interpretation; there are implicit and preconscious warranties in language. That is, we begin with the proposition that what we say or what we seem to be saying ought to be taken at face value. As noted earlier, the contractual representations and warranties are merely descriptive and not performative. It seems to me that those descriptive utterances have linguistic truth warranties to them that precede any legal warranties. To put it another way, if the thesis is that every statement in a negotiation is a potential lie and can only be given some truth by virtue of the contract, it is only the contract, and not our ordinary language, that serves to communicate. In short, we have reversed the intuitive use of language.

We can unpack this by reference to Habermas's distinction between discourse and communicative action. Habermas focuses on language as the sole manner by which people have intersubjective communicative action. Taking a Kantian approach, he intuits an access to universal norms that go beyond mere empiricism. To Habermas, it is simply counter-intuitive to believe the positive science of the physical world is all there is. Nevertheless, he is unwilling to posit a completely subjective access to truth, and this insight is derived from the development in philosophy he refers to as the "linguistic turn." Following on Wittgenstein, language is how we intermediate between ourselves and our world. Wittgenstein demonstrated (similar to Kant's deduction that there is an objective world as to which each subject is an observer) that there are no private languages. That is, if our minds conceive of ideas in a wholly private language, it is as though those

---

143 For more anecdotal evidence of the ordinary human reaction judges have to the deceptive use of language, see "On Further Review": Need More Serious Reaction to Too-Clever Lawyering, Posting of Alan Childress to Legal Profession Blog (Dec. 17, 2006), available at http://lawprofessors.typepad.com/legal_profession/2006/12/needed_serious_.html.

144 See AUSTIN, supra note 95; see also supra Part III.B.2.

145 JÜRGEN HABERMAS, ON THE PRAGMATICS OF SOCIAL INTERACTION 89-93 (Barbara Fultner trans., 2001).


147 Id. at 18-20.

148 Id. at 18-22.

149 HABERMAS, supra note 145, at vii; HABERMAS, supra note 146, at 8-13.

150 HABERMAS, supra note 145, at 61-65.

151 Id. at 51 (explaining Wittgenstein's recognition that "language systems are public in character and always require the interaction of at least two subjects").
ideas did not exist because they cannot be communicated to anyone. Indeed, language is itself a social structure, and we are assuming too much about our own individuality if we assume that we are so alone as to have developed the very medium by which we express our ideas.

So what is our agreement? When we begin to discuss our individual goals and the possibility of the attainment of value through mutual understanding and a bargain, we do so through language, the only means by which such discussion is possible. For example, one might say, "Let's agree that the price escalates by increases in the cost of living." When we have a handshake agreement or a preliminary understanding like this, it is still an exercise in intersubjective understanding by the intermediation of language. But our lawyers show us the ways in which that communication might break down: "Did you mean to measure that increase by the consumer price index? Or by the wholesale price index? For which goods and services? And in which geographic areas?"

This provides the lawyer's analog to Habermas's discourse ethics. When a speaker asserts a proposition, and the listener purports to understand it, there are implicitly four "background" claims being made with respect to the proposition. These are not, in the ordinary course, at the top of the speaker's and listener's minds; they only become so when there is (what Habermas calls) a breakdown in communicative action. They are, however, \textit{a priori} aspects of the way we process other's speech (akin to Kant's categories of the understanding in ordering the data of the outside world):

- The proposition is \textit{intelligible}—the speaker and the listener each understand something from the proposition. It is correct syntactically and follows the accepted "internal relation between symbolic expressions and the relevant system of rules, according to which we can produce these expressions." Thus, "[a]n utterance is intelligible if it is grammatically and pragmatically well formed, so that everyone who has mastered the appropriate rule systems is able to generate the same utterance." Consider Bertrand Russell's famous example: "[T]he present King of France is Bald." The sentence is nonsensical, but, nevertheless, we understand it syntactically.

\hspace{1cm} 152 Id. at 89-90.
\hspace{1cm} 153 Id. at 91.
\hspace{1cm} 154 HABERMAS, supra note 145, at 91.
\hspace{1cm} 155 Bertrand Russell, \textit{On Denoting}, 14 \textit{Mind} 479, 485, 490 (1905). The problem, under Russell's treatment, is that we recognize the phrase "the present King of France" as one that denotes, even though there is no real king to which the phrase refers. \textit{Id.} at 485-93.
• As to statements making truth claims, each party recognizes the truth of the proposition. 156 "Truth is a relation between sentences and the reality about which we make statements." 157

• As to statements making normative claims, each party acknowledges the normative rightness of the norm that the statement may be fulfilling. 158 This is distinct from truth: the implicit claim is "that it is right to recognize a prevailing norm and that this norm 'ought' to have validity." 159

• Neither party casts doubt on the sincerity of the other. 160 "A speaker is sincere if she deceives neither herself nor others. Just as 'truth' refers to the sense in which I can put forth a proposition, 'sincerity' refers to the sense in which I disclose or manifest in front of others a subjective experience to which I have privileged access." 161

Most of the time we communicate without any consciousness of the underlying validity claims of our speech. But it is certainly possible to contest either the truth or the normative rightness of an assertion. Truth involves grounding an assertion in experience (or, at least, not being subject to a showing of contradictory experience). 162 Normative rightness, on the other hand, makes no claim against experience, but claims of normative rightness can be considered universal only if all involved in rational discussion would agree to their rightness "under ideal conditions." 163

---

156HABERMAS, supra note 145, at 90-91.
157Id. at 91.
158Id. at 90.
159Id. at 92.
160HABERMAS, supra note 145, at 90.
161Id. at 91.
162Id. at 88.
163Id. at xx; JÜRGEN HABERMAS, TRUTH AND JUSTIFICATION 36-40 (Barbara Fultner ed. & trans., 2003). Ideal conditions of discourse are: "(a) [a] public debate and complete inclusion of all affected; (b) [ ] equal distribution of the right to communicate; (c) [ ] a nonviolent context in which only the unforced force of the better argument holds sway; and (d) [ ] the sincerity of how all those affected express themselves." Id. at 37. In his earlier work, Habermas maintained that truth assertions had to be redeemed through argumentation in "ideal conditions." Id. at 34-35. With his publication of Truth and Justification in 2003, Habermas appears to have come to the conclusion that requiring "ideal conditions" is not necessary to the acceptance of truth claims, because it would preclude the possibility of even a universally accepted claim being disproved later. Id. at 38. Nevertheless, he continues to acknowledge the regulative aspect of reason in the assertion of scientific claims, and so discourse and argumentation are necessary:

Despite this revision, the concept of rational discourse retains its status as a privileged form of communication that forces those participating in it to continue decentering their cognitive perspectives. The normatively exacting and unavoidable communicative presumptions of the practice of argumentation now as
Normative rightness goes beyond mere empiricism—it "idealizes" a universal norm.\(^\text{164}\)

Moreover, to Habermas, the linguistic turn in philosophy makes pragmatic what had been Kant's attempt to distinguish the "noumenal" or "transcendental" from the "phenomenal" or "empirical":

The idea of the redeemability of criticizable validity claims requires idealizations that, as adopted by the communicating actors themselves, are thereby brought down from transcendental heaven to the earth of the lifeworld. The theory of communicative action \textit{detranscendentalizes} the noumenal realm only to have the idealizing force of context-transcending anticipations settle in the unavoidable pragmatic presuppositions of speech acts, and hence in the heart of ordinary, everyday communicative practice.\(^\text{165}\)

In other words, when you make a statement about what ought to be, even in the most mundane circumstances, you are claiming one kind of validity or another in what you say. The test of validity of normative statements is not correspondence with facts in the world but with reasons that justify the universality of the claim, even if you have not stated them.\(^\text{166}\) The process of argumentation and attainment of rational consensus around either truth or normative rightness—the redemption of the validity claim—is what Habermas calls discourse.\(^\text{167}\)

---

then imply that impartial judgment formation is structurally necessary. Argumentation remains the only \textit{available} medium of ascertaining truth since truth claims that have been problematized cannot be tested in any other way. There is no unmediated, discursively unfiltered access to the truth conditions of empirical beliefs. After all, only the truth of unsettled beliefs is subject to question—beliefs that have been roused from the unquestioned mode of functioning practical certainties.

\textit{Id.}\(^\text{164}\) \textit{HABERMAS, supra} note 145, at 92.
\textit{Id.}\(^\text{165}\) \textit{HABERMAS, supra} note 146, at 18-19.
\textit{Id.}\(^\text{166}\) at 19.
\textit{Id.}\(^\text{167}\) \textit{HABERMAS, supra} note 163, at 36-42. There is a natural segue from discourse ethics to the process of adjudication, but in the end, Habermas concludes it is problematic to equate them. \textit{Id.} at 198-99. Habermas proposes an alternative theory of legal discourse that responds to the positivist-naturalist debates over certainty and legitimacy in law. This is a theory of argumentation, much like Patterson's: there are many norms that may be applied in a particular case, and the argument, more often than not, turns on the selection or interpretation of the norm: [L]egal hermeneutics has the merit of having revived the Aristotelian insight that no rule is able to regulate its own application. If we consider a case to be a state of affairs falling under a rule, then such a case is constituted only by being described in terms of the norm applied to it. At the same time, the norm acquires a more concrete meaning precisely in virtue of its application to a corresponding state of
The kind of rational discourse in which a lawyer might parse language to the extent that one expressly, rather than implicitly, warrants the truth ought not to be the presumed default state. We communicate as normal human beings; lawyers engage in discourse, whether it is in the ex ante attempt to make communication precise, or in the ex post exercise of figuring out what a communication meant. The lawyer's exercise is to predict the inevitable breakdowns in the "unavoidable pragmatic presuppositions of speech acts."\(^{168}\)

The half-truth is the most pernicious kind of lie, under this reasoning, because it violates both the warranty of truth and the warranty of sincerity. The subjective experience to which the speaker has access is the whole truth, though it remains unspoken. Discourse is not even possible in this case because the speaker and the listener do not have a shared speech act that allows them to perceive jointly the possibilities in which the proposition fails to mirror reality. Even in communicative action, we must undertake to explain its breakdown, cure it by discourse, and presume sincerity. As Ayres and Klass observed about the complexity of a speech act: "In most cases, a promisor's representation that she intends to perform does not require a separate utterance—This casserole is sine cera'—but is understood to be part of the meaning of the very act of promising."\(^{169}\) It would be linguistically impossible to operate, even in the most sophisticated, arm's-length setting, on the presumption that every speech act, except the one embodied in the language of the contract, is potentially insincere.

Accordingly, the proper presumption for disclaimers of sincerity is that they only apply to the extent they are patently and expressly clear and only apply in the narrowest possible way.

b. **Disclaimers of Truth-Telling as Social Phenomenon**

1. **The Lawyer's Constitutive View of Contracts**

There is a particular worldview of lawyers and judges in the position that buyers should expect all representations, other than those warranted, to be lies, and should simply decline to go forward with the deal if the parties

\(^{168}\) HABERMAS, supra note 145, at 18-19.

\(^{169}\) AYRES & KLASS, supra note 2, at 202.
cannot obtain satisfactory warranties and acceptable contractual remedies.\textsuperscript{170} It suggests a sharp divide between the world of the legal and the world of the everyday that lawyers and legal scholars perceive, but which seems to me self-deceptive (or worse). The mistake is to assume that there is some kind of guild-like code, some special language, to which lawyers apply special magic to create a precise rendition of the parties' complete agreement apart from any common sense notions.\textsuperscript{171} Even more fundamentally, lawyers bring to the table an "inflated 'rights consciousness' that disrupts more flexible and consensual extralegal relationships."\textsuperscript{172}

The presumption of the divide between the everyday and the legal seems to be particularly lawyer-centric and consistent with the way in which lawyers maintain that they are "different" through licensing, language, and culture.\textsuperscript{173} Austin Sarat and Thomas Kearns have explored the everyday relationship to law and compared it to the way in which scholars analyze law.\textsuperscript{174} They criticize both instrumentalism—a sharp distinction between legal standards, on one hand, and nonlegal human activity, on the other—and the constitutive view—a view holding that law shapes (and reflects) society by providing the categories and classification that make society seem coherent.\textsuperscript{175} In the deal context, legal instrumentalism would be the idea that the documents are the means (and, one suspects, the sole means) by which the deal gets done. In contrast, legal constitutivism would see the documents as the deal. Vice Chancellor Strine reflects a not uncommon lawyer's constitutive view about the relationship of the contract language to reality itself: the purpose of the antireliance provision is to "define those representations of fact that formed the reality upon which the parties premised their decision to bargain."\textsuperscript{176}

\textsuperscript{170}See Ribstein Posting, \textit{supra} note 12; Snyder Posting, \textit{supra} note 13.


\textsuperscript{172}Mark C. Suchman \& Mia L. Cahill, \textit{The Hired Gun as Facilitator: Lawyers and the Suppression of Business Disputes in Silicon Valley}, 21 \textsc{Law \& Soc. Inquiry} 679, 680 (1996). Suchman and Cahill theorize that Silicon Valley lawyers are effective because they have managed to discard this attitude. See \textit{id}.

\textsuperscript{173}This is hardly rigorous, but one of the ways that I could always be sure to grate on my non-lawyer colleagues in the corporation was to suggest that lawyers were different: that they needed to stick together in groups, rather than reside with the businesses, that their evaluation and compensation needed to be different, and that their goals and objectives were different.

\textsuperscript{174}Austin Sarat \& Thomas R. Kearns, \textit{Beyond the Great Divide: Forms of Legal Scholarship and Everyday Life}, in \textsc{Law in Everyday Life} 21-61 (Austin Sarat \& Thomas R. Kearns eds., 1993).

\textsuperscript{175}\textit{Id.} at 21-22.

\textsuperscript{176}Abry Partners Acquisition V, L.P. \textit{v.} F \& W Acquisition, LLC, 891 A.2d 1032, 1058 (Del. Ch. 2006).
This is the epistemological center of the constitutive legal view: if you do not like a provision of the contract, you are entirely free to walk away. In castigating the Abry buyer for its attempt to circumvent the antireliance clause, Vice Chancellor Strine said, "The enforcement of non-reliance clauses recognizes that parties with free will should say no rather than lie in a contract."177 While this might appeal to the Kantian, and might well be true in highly simplified models of contracting, it sells short the complex social structure that is a business acquisition. As Ayres and Klass recognize, even simple promises, much less large-scale deals, are complex communications.178 It is a conceit to believe either that lawyers are (or should be) capable of manipulating the parties' myriad of understandings through language trickery or that what they are doing in the drafting session constitutes the whole of the speech act that is the transaction. In a typical transaction, CEOs speak to CEOs; transition teams plan the integration of the businesses; pension experts value assets and projected liabilities; labor negotiators deal with unions and works councils; accountants and auditors work to create a pro forma set of financial statements for the business; environmental experts do sampling and estimate remediation costs; and sales and marketing personnel plot the way in which customers will be contacted. The reality (and not necessarily the contract-negotiating lawyer's perception) is that there is much of the everyday going on, and everyday activity is no doubt just as critical to the required information exchange in the transaction as the lawyer-created contract language.

2. Contracts and Trust

Rather than adopting the lawyer's perspective, Sarat and Kearns propose instead a far more nuanced relationship between the law and everyday life. It is one where attention to the law is neither wholly explicit nor wholly ignored—a kind of legal shadow in the background influencing the way parties conduct themselves.179 I suggest that there is such a shadow influencing conduct in the law's incorporation of the everyday notion that we do not lie to each other, even in contractual situations, and we do not deceive each other by parsing meanings so finely as to create half-truths. The law of fraud forms a kind of base condition—a safety net—that makes this moral notion concrete (even if it is rarely used).180

177Id.
178See AYRES & KLASS, supra note 2, at 203.
179Sarat & Kearns, supra note 174, at 45.
180See AYRES & KLASS, supra note 2, at 202 ("[T]here is often a level of mistrust going into the transaction that makes it in the parties' mutual interest to have the representation backed up by a legal guarantee.").
If we proceed from a "state of nature" model, why would a presumption of lying ever be the default state? Lawrence Friedman uses the example of Tristan de Cunha, a tiny and isolated island in the mid-Atlantic, as an organic society in which implicit norms of behavior never had to develop into explicit rules of law.\(^{181}\) Friedman suggests that while we continue to operate in our own small environs of Tristan de Cunha-like nonlegal normativity, a dispersed and complex society develops law.\(^{182}\) In other words, even while modern society imposes organization and structures, our day-to-day interaction consists of interpersonal ties and informal norms. To suggest that the presumption of lying, a modern and complex view, trumps the presumption of truth-telling, inverts the very process by which societies modernize.

The law has had a long struggle with reconciling the tort and contract actions for misrepresentation; Vice Chancellor Strine recognized as much.\(^{183}\) Even at the height of the freedom of contract doctrine, there were still significant restrictions on caveat emptor, and the law of fraud as a separate action, even in a commercial context, never disappeared.\(^{184}\) Moreover, Anglo-American law bespeaks a rational and litigious culture in which consensus is less important than being correct, so we try to reach the "right" answer instead of working it out like the Europeans do.\(^{185}\) Lawyers are generally more rational and formalistic than their clients, which is why there is never truly a caveat emptor business acquisition agreement.\(^{186}\)

---

182. Id.
183. Abry Partners Acquisition V., L.P. v. F & W Acquisition, LLC, 891 A.2d 1032, 1054-55 (Del. Ch. 2006). The nature of that recognition is ironic, however. It comes in the context of construing whether the parties intended the word "misrepresentation" in the indemnity clause to include intentional, as well as innocent, misrepresentations. Id. Vice Chancellor Strine concluded that they did, observing:

It is difficult to fathom why rational contracting parties would attempt to cut, by contract, a clear division that American jurisprudence has never been able to achieve: a division between the role of contract and tort law in addressing the consequences of false representations inducing the making and closing of contracts.

Id. at 1054.
185. In German practice, the parties appear to be less opportunistic, not because they have managed to achieve a higher level of draftsmanship, but because the norm is simply to "stop sooner" in the process of customizing agreements. Claire A. Hill & Christopher King, How Do German Contracts Do as Much with Fewer Words?, 79 CHI.-KENT L. REV. 889, 903 (2004). German parties adopt "good enough" provisions, apparently recognizing that agreeing on a tightly drafted provision is not a reliable way of getting exactly what one wants in litigation anyway. Id. at 920-21.
186. Suggesting a Gemeinschaft to Gesellschaft progression is beyond my scope here, but such a progression also seems plausible to me. In his 1887 Gemeinschaft und Gesellschaft [Community and Society], Ferdinand Tönnies, the German sociologist and colleague of Max Weber, developed the concepts of Gemeinschaft and Gesellschaft by elaborate analyses of their empirical prototypes: kinship, neighborhood, town, and spiritual community
In a simple case, like the sale of wheat in a first year contracts class hypothetical, the contract may well constitute the reality of the deal (or model it so closely that it is essentially the same thing). In a business acquisition, however, the contract sits within (and, indeed, perhaps at the center of) a far more complex web of a trust and distrust relationship. It is simply disingenuous to think that the essence of the deal is being captured solely by lawyers with no other intersubjective relationships. Recent work in the area of trust and the law is instructive. Francis Fukuyama has proposed a matrix on which to plot the way norms (including trust relationships) form—hierarchical versus spontaneous on one axis, and rational versus a-rational on the other.\textsuperscript{187} For example, economics itself is the discipline by which we study rational, but spontaneously generated, norms.\textsuperscript{188} Yet Fukuyama is skeptical of a wholly rational approach to trust norms, and there is no reason to believe deal makers are wholly rational actors.\textsuperscript{189}

The contract may reflect the deal, but it is not itself the deal. In their study of trusting and trustworthiness, Professors Ben-Ner and Putterman observed:

are prototypes of the former; contractual relationships, collectives based on common interests, and special purpose associations are prototypes of the latter. . . . He saw the transition from a predominantly Gemeinschaft-like to a predominantly Gesellschaft-like social order primarily as a consequence of increasing commercialization together with the rise of the modern state and the progress of science.


\textsuperscript{188} Fukuyama, supra note 187, at 487.

\textsuperscript{189} Fukuyama concludes:

Today there is relatively little exchange and even less consensus across disciplinary lines concerning the question of norm genesis and trust. Those who believe that the social sciences can achieve a unified approach to the study of this aspect of behavior tend to come out of an economics tradition. For the reasons outlined above, I am very skeptical that this kind of unity will ever be achieved. The social capital and trust relationships we see in the real world are highly complex outcomes that exhibit both emergent properties and path dependencies that were the products of long-forgotten initial conditions. A game-theoretic approach yields many important insights into the circumstances in which norms and trust arise, and for that reason is highly useful to policy. But in other circumstances, we have to content ourselves not with analysis that is not "scientific," but rather ethnographic and descriptive in nature.

Id. at 493-94 (citations omitted).
Especially when companies engage in business dealings with one another, there are typically small numbers of distinct individuals involved in the process, including managers who work out the terms, lawyers consulted on various details, and top executives who have to ratify any major transactions. Individuals place not only their company's, but their personal reputations for toughness, honesty, and so forth, on the line as they deal with one another on behalf of their companies. Telephone conversations, face-to-face meetings, and handshakes occur between flesh-and-blood individuals, and the usual cues of reliability—reliability, that is, of the individuals concerned—are evaluated to form estimates of whether the trading partner can be counted upon.190

Business people know intuitively that the contract will be incomplete, and resolving the many issues that arise once a deal is closed will depend on some modicum of mutual good faith.191 Whether one approaches the concept of trust from an economic perspective (i.e., that it serves to enhance efficiency by reducing the transaction costs of the creation and enforcement of contracts),192 or from, what is for me, a far more satisfying psychological, philosophical and ethical perspective,193 there seems to be no real debate that trust is, in the words of Professor Bainbridge, a "lubricant to reduce social friction" in the deal context as much as any other.194

Claire Hill and Erin O'Hara posit that the role of the law should be not necessarily to encourage or discourage trust, but to optimize it.195 Their

191 While I would never suggest that a major acquisition could be done on a mere handshake, when I was in practice, I would pose the question to clients to complete a deal with this question: "If you could, would you do this deal on a handshake?" The question is a reflection of a shared understanding that neither the contract nor resort to the legal system is likely to be an effective way of resolving most post-closing issues.
193 Lawrence E. Mitchell, The Importance of Being Trusted, 81 B.U. L. REV. 591, 599 (2001). Professor Mitchell's essay is worth a full read in its own right, apart from its helpfulness as a citation here. He taps into the mystery of trust that transcends rational calculation, largely in response to Oliver Williamson's attempt to demonstrate that trust only exists in narrow areas of human life outside of the economic realm. Id. at 596 (citing Oliver Williamson, Calculativeness, Trust and Economic Organiza-tion, 36 J.L. & ECON. 453 (1993)). Mitchell's thesis is that for trust to have the instrumental value given to it in economic models, the capacity for trust must be deeply internalized in a way that economic modeling cannot explain. Id. at 597. Trust in some respects is a matter of epistemology: "To trust is . . . to organize our world." Id. at 599.
thesis is that legal scholars assume trust to be wholly good or wholly bad without recognizing or acknowledging that trust and distrust can coexist in the same relationship.\(^{196}\) Accordingly, the law should create incentives to trust where more trust is beneficial and discourage it where it is not.\(^{197}\) An example of concurrent trust and distrust in a relationship is that of corporate board to corporate management.\(^{198}\) Hill and O'Hara observe (correctly, I believe) that the relationship of board to management is not wholly one of monitoring (implying distrust), leadership, or management (implying trust), and the regulatory incentives need to be fine-tuned so as not to suboptimize either aspect.\(^{199}\)

Both the process and the substance of making deals reflect this concurrent trust/distrust polarity. Parties regularly go forward with significant expenditures on nonbinding letters of intent. Lawyers cede drafting responsibilities, act as informal escrow agents with respect to in-process documents, or accept each other's promises on their face. Indeed, as Ayres and Klass note, contract damages are notoriously undercompensating.\(^{200}\) Making a deal means inherently trusting the other party to some extent because the legal remedies embodied in the contract will almost never equal the expectation value of the agreement.\(^{201}\) Or as Professor Seligman observed, "[T]here is of course the connection between trust and risk."\(^{202}\) Precisely because there is no viable legal remedy, trust mediates "the risk that is incurred when we cannot expect a return or reciprocal action on alter's part (which of course we could, at least within certain boundaries, when

\(^{196}\)Id. Perhaps one of the most notable popular renditions of this theme was President Reagan's use of the Russian maxim "trust but verify" to characterize his attitude toward negotiating with Mikhail Gorbachev. Ronald Reagan, Farewell Address to the Nation (Jan. 11, 1989), available at http://www. reaganfoundation.org/reagan/speeches/farewell.asp.

\(^{197}\)Hill & O'Hara, supra note 195, at *5.

\(^{198}\)Id. at *48-61.

\(^{199}\)Id. at *56-61.

\(^{200}\)AYRES & KLASS, supra note 2, at 71.

\(^{201}\)William Sahlman, the dean of entrepreneurship scholars, has made the following observation about the relationship of contract language to deal-making:

Often, deal makers get very creative, crafting all sorts of payoff and option schemes. That usually backfires. My experience has proven again and again that sensible deals have the following six characteristics:

- They are simple.
- They are fair.
- They emphasize trust rather than legal ties.
- They do not blow apart if actual differs slightly from plan.
- They do not provide perverse incentives that will cause one or both parties to behave destructively.
- They are written on a pile of papers no greater than one-quarter inch thick.


\(^{202}\)Seligman, supra note 186, at 623.
interaction is defined solely by the reciprocally defined nature of role obligations and commitments).” Trust is the completion of the incomplete contract. 204

What then is the optimum default rule with respect to the construction of antireliance clauses? We can connect this exegesis on trust by returning to Professor Langevoort’s discussion of half-truths. He proposes a sliding scale for half-truth liability.205 Where there is little or no trust between the parties, he concludes, it is difficult to justify the half-truth doctrine at all.206 But he leaves open how far the doctrine should operate in negotiations marked by a higher degree of trust. 207 It seems clear that the volume of communication in the complex deal setting entails some significant level of trust, with, as Professor Langevoort puts it, “a broad half-truth doctrine, one with little privilege to conceal once a matter is addressed at all.” 208 It seems to me, then, barely a leap to my doctrinal result: any disclaimer that flies in the face of this trust must be narrowly construed.

IV. CONCLUSION

The idea that the law governing business transactions should be wholly predictable and certain adopts a scientific world view that does not map onto basic notions of either fairness or morality in everyday life. What makes us moral is making choices and not knowing the outcome to a certainty (a Kantian view). The law does a pretty good job of letting that happen by building uncertainty into the system of resolution itself. Because the ultimate determination of whether we made the right choice will be backward looking and casuistic in every instance, determinations of good faith, fiduciary duty, and fair dealing can never be algorithmic. The principles are predictable and welfare enhancing to the extent society has

203 Id.
204 Professor Seligman concludes:
Risk, as an aspect of social relations (no less than metaphysical doubt or mathematical probability) has emerged as a constitutive aspect of life in modern society and trust as a solution to this form of risk has, similarly, been its defining component.

Risk, I have endeavored to argue, became inherent to role-expectations when, with the transformation of social roles and the development of role-segmentation, there developed an in-built limit to systemically based expectations (what we have termed confidence) of role behavior.

Id. at 633.
205 Langevoort, supra note 74, at 96.
206 Id. at 98.
207 Id.
208 Id.
adopted some rule of law, but they are not predictable in the algorithmic resolution of any individual case.\textsuperscript{209}

Vice Chancellor Strine made a valiant attempt, but ultimately failed, to draw the fine line in Abry (something he recognized in a footnote with "intellectual candor").\textsuperscript{210} Courts do not need to be concerned that the world of commerce will collapse if the threat of a fraud claim hangs over deal participants because the existence of some fraud remedy, even if the impact goes beyond the contractual representations, reflects the way the parties do and should act. Accordingly, courts should give effect to disclaimers of truth-telling but should presume that they are exceptions to the default state, and, hence, they must be construed as narrowly as possible.

\textsuperscript{209}See F.A. Hayek, The Road to Serfdom 80-96 (1944). I think it is this very subtle distinction that is at the heart of the Sarat and Kearns thesis about law as a shadow to everyday life, as well as Chancellor Allen's point about the ability of the Delaware corporate bench and bar to have "created the tools, the attitudes and the very rich information that permit the moderate productive management of a system with great formal ambiguity." Sarat & Kearns, supra note 174, at 44; Allen, supra note 86, at 73.

\textsuperscript{210}Abry Partners Acquisition V, L.P. v. F & W Acquisition, LLC, 891 A.2d 1032, 1064 n.85 (Del. Ch. 2006).
In this appendix, I propose a series of seven hypothetical cases that demonstrate the increasing complexity of misrepresentations, half-truths, and omissions that might be made during business negotiations and that a nonreliance clause could be intended or construed to cover. I discuss more thoroughly cases 2, 3, and 7 in the text. See Part III.B.1.

<table>
<thead>
<tr>
<th>Contract Provisions</th>
<th>Fact Situation</th>
<th>Contract Outcome</th>
<th>Fraud Outcome Under Abry</th>
<th>Comment</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>1</strong></td>
<td>&quot;Company A does not have any unionized facilities.&quot;&lt;br&gt;&quot;There are no, and Buyer disclaims any reliance on, representations or warranties, except those expressly made in the contract.&quot;</td>
<td>A Company A official said, during a Buyer's exercise of due diligence, that Company A did have a unionized facility. The company does have a unionized facility.</td>
<td>Buyer wins. The non-reliance provision is not relevant. Seller wins only if the law or contract imposes a rule under which Buyer's knowledge of the falsity of the representation from other sources negates reliance.</td>
<td>Unclear. Presumably, the knowing misrepresentation element of fraud would be met, but the noncontractual disclosure should negate reliance for purposes of fraud.</td>
</tr>
<tr>
<td><strong>2</strong></td>
<td>Contract is silent on the subject of unionization of facilities. &quot;There are no, and Buyer disclaims any reliance on, representations or warranties, except those expressly made in the contract.&quot;</td>
<td>A Company A official, during a management presentation, says that Company A does not have any unionized facilities. The company does have a unionized facility.</td>
<td>Seller wins.</td>
<td>This seems to be a fair case to allow the operation of the nonreliance clause.</td>
</tr>
<tr>
<td>Contract Provisions</td>
<td>Fact Situation</td>
<td>Contract Outcome</td>
<td>Fraud Outcome Under Abry</td>
<td>Comment</td>
</tr>
<tr>
<td>-------------------------------------------------------------------------------------</td>
<td>--------------------------------------------------------------------------------</td>
<td>------------------</td>
<td>--------------------------</td>
<td>--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>3 &quot;Company A does not have any unionized facilities.&quot;</td>
<td>There are no other noncontractual representations, but a senior official of Company A knows that the workers at more than one plant have approved the formation of a union. The union election has not yet been certified, however, so, technically, the company still does not have any unionized facilities.</td>
<td>The outcome will depend on the interpretation of the word &quot;unionized.&quot; Was it intended to include an approved but uncertified union as well as established unions?</td>
<td>Unclear. If it is absolutely clear to all concerned that &quot;unionized facilities&quot; does not include one in which the union has been approved but the election has not been certified by the NLRB, then there can be no fraud because there is no untrue statement. What is the relationship of scienter to the ambiguity of the original representation?</td>
<td>The example demonstrates the possibility of a half-truth, even in what would have seemed at the outset to be a simple and clear affirmative representation. A <em>laissez-faire</em> approach would place the burden on the buyer to obtain the correct information by asking the correct question or to create express liability by requiring the correct and complete representation.</td>
</tr>
<tr>
<td>4 Contract is silent on the subject of unionization of facilities.</td>
<td>There are no other noncontractual representations, but a senior official of Company A knows that the workers at more than one plant have approved the formation of a union. At the same time, the union election has not yet been certified, and so, technically, the company still does not have any unionized facilities.</td>
<td>Seller wins.</td>
<td>Seller wins.</td>
<td>If an outright lie is disclaimed in Case 2, then a half-truth, one supposes, is also disclaimed.</td>
</tr>
<tr>
<td>Contract Provisions</td>
<td>Fact Situation</td>
<td>Contract Outcome</td>
<td>Fraud Outcome Under Abry</td>
<td>Comment</td>
</tr>
<tr>
<td>-----------------------------------------------------------------------------------</td>
<td>----------------------------------------------------------------------------------</td>
<td>----------------------------------------------------------------------------------</td>
<td>------------------------------------------------------------------------------------------</td>
<td>--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------</td>
</tr>
<tr>
<td>5 &quot;Company A's financial statements fairly present in all material respects the financial condition of Company on the dates and for the periods presented in accordance with generally accepted accounting principles consistently applied.&quot;</td>
<td>Company A violated GAAP by recognizing revenue out of cash received from pre-paid subscriptions.</td>
<td>Buyer wins. The nonreliance provision is not relevant.</td>
<td>Buyer wins. Presumably, one only misstates one's revenue knowingly.</td>
<td>What if Buyer has full access to the financial records during its exercise of due diligence but there is no &quot;antisandbag&quot; clause? This is the same issue as in Case 1.</td>
</tr>
<tr>
<td></td>
<td>&quot;There are no, and Buyer disclaims any reliance on, representations or warranties, except those expressly made in the contract.&quot;</td>
<td></td>
<td></td>
<td>The point here is to show a representation that is far more a standard than a rule (in contradistinction to the representation on unionization).</td>
</tr>
<tr>
<td>6 &quot;Company A's financial statements fairly present in all material respects the financial condition of Company on the dates and for the periods presented in accordance with generally accepted accounting principles consistently applied.&quot;</td>
<td>Company A engaged in &quot;channel stuffing.&quot; This means that it caused its customers to buy during Quarter 1, even though the clear expectation was that customers would not likely buy during Quarter 2, after the sale of the company. This practice does not violate GAAP, and the sales were in fact all made and properly booked.</td>
<td>Unclear. How does one interpret the GAAP standard? For the periods in question, the financial statements do present the financial condition accurately. Thus, a strict constructionist (or Seller) will argue that this is literally true. The unstated fact is that, to the extent Buyer is relying on one quarter to look like the next (even accounting for normal seasonal variation), Seller knows it is creating a mistaken impression.</td>
<td>Presumably, Seller wins because, under a literalist construction of the contract, all other representations are extracontractual.</td>
<td>Here, the issue between intracontractual and extracontractual representations and reliance is not nearly as clear. Does the original GAAP representation create a partial disclosure, the effect of which is to create a duty of candor in the due diligence? Does the burden of disingenuousness fall on Buyer or Seller?</td>
</tr>
</tbody>
</table>


<table>
<thead>
<tr>
<th>Contract Provisions</th>
<th>Fact Situation</th>
<th>Contract Outcome</th>
<th>Fraud Outcome Under Abry</th>
<th>Comment</th>
</tr>
</thead>
</table>
| "Company A's financial statements fairly present in all material respects the financial condition of Company on the dates and for the periods presented in accordance with generally accepted accounting principles consistently applied."

"There are no, and Buyer disclaims any reliance on, representations or warranties, except those expressly made in the contract." | Company A booked "re-turn reserves." Under GAAP, re-turn reserves must be based on a reasonable estimate of expected returns. *See supra* note 44. The Chief Financial Officer issued a memorandum indicating that it was important, for the purpose of the impending sale of the Company, that all return reserves be in accordance with GAAP, but that the controllers should, nevertheless, err on the side of low estimates rather than high estimates. This had the effect of making the earnings look higher. Company A did not disclose this memorandum in due diligence deliberately. | Seller wins. | A strange outcome, but presumably Seller wins, despite the original questionable practice of using low estimates under the broad strictures of GAAP and the ensuing cover-up during due diligence. | The original representation serves as an assurance that Seller is not telling half-truths outside the contract. If that is the case, why should Buyer be limited to the remedy inside the contract by the nonreliance provision? |