DO YOU HAVE THE RIGHT TO REMAIN SILENT?:
DUTIES OF DISCLOSURE IN BUSINESS TRANSACTIONS

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I. Introduction

When does the law oblige parties to business transactions to share information with each other? Arm's-length transactions conventionally result from arm's-length negotiations in which each party, knowing what she knows, evaluates for herself the merits of the transaction and its terms. Parties negotiating at arm's length, unless they contemplate forming a partnership, are not treated as fiduciaries toward each other. Unlike a fiduciary dealing with her beneficiary, parties negotiating at arm's length are not obliged to be candid with each other, nor are they obliged to share their opinions and analyses concerning the merits of the transaction. To a considerable extent, parties who deal at arm's length are free to take a sporting view of their relationship with each other.

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1. See 2 ALAN R. BROMBERG & LARRY E. RIBSTEIN, BROMBERG AND RIBSTEIN ON PARTNERSHIP § 6.06, at 6:63 (1988) (arguing that prospective partners must deal with each other candidly). Under § 21 of the Uniform Partnership Act, partners must account as fiduciaries for profit generated by transactions "connected with the formation, conduct or liquidation of the partnership." Id. at 6:62.

2. Jurisdictions differ on whether fiduciary standards are suspended if the partners' interests become adverse. This question would arise when a partner in an ongoing partnership announces that he intends to dissolve the partnership or to sell his interest to his fellow partners if they wish to purchase it. Are the subsequent negotiations over the terms of the buyout subject to a fiduciary obligation of candor, which would oblige the prospective purchasers to disclose the maximum price they would be willing to pay for the selling partner's interest? Compare Walter v. Holiday Inns, Inc., 784 F. Supp. 1159, 1169 (D.N.J. 1992), aff'd on other grounds, 985 F.2d 1232 (3d Cir. 1993) (noting that New Jersey excepts adverse negotiations between partners that do not affect partnership's own property or business from general fiduciary standard; and further noting that certain other jurisdictions impose fiduciary standard in sale context) with MacLane Gas Co. Ltd. v. Enserch Corp., No. 10,760 (Del. Ch. Dec. 11, 1992) (holding that under Texas law, a general partner purchasing limited partnership units through tender offer owes a fiduciary duty to limited partners).
Suppose, though, that one party, prior to executing a transaction, knows something significant and also knows that the other party lacks the same information. When does a disparity in knowledge justify legal intervention to deprive someone of the fruits of superior information?

Only an author’s ingenuity limits her ability to illustrate this situation. The basic question occurs often, and in diverse settings. You sell me your farmland when I know (or strongly suspect), but you do not, that beneath its surface is a valuable deposit of minerals. I sell you my land, knowing, as you do not, that beneath its smooth surface is unstable fill. I sell you my stock in a corporation knowing, because I’m a manager, that the corporation will soon announce that, contrary to prior projections, its quarterly earnings are much lower than they were a year ago. I borrow money from you through a secured loan knowing that the value of the collateral is much less than you believe it to be. You, based on this history, would refuse to deal at all with me, but you do deal with a person who, unbeknownst to you, is my agent. Or suppose that I know, but you do not, that in your position only a fool would agree to the terms of our transaction.

My thesis is that legal doctrine does not resolve these scenarios in a symmetrical fashion. Situations that at some level of abstraction seem similar lead in actual litigation to different outcomes. Inconsistency stems in part from the diverse bodies of law that may be pertinent, including principles derived from the common law of contracts and fraud, from equity, and from restitution. Inconsistency also stems from the divergent statutory regulation of specific types of transactions, such as sales of goods and transactions in investment securities. Moreover, in many cases courts seem to apply legal doctrine in a manner that is highly fact-specific.

In pursuit of symmetry or consistency, many legal scholars have attempted to isolate a single unifying theme in these cases or to state a general doctrine that would rationalize their outcomes.³ These

scholarly efforts are doomed to fail. Common mistake scenarios implicate more than one policy objective or expression of moral intuition, all of them justifiable, many of them conflicting. In many mistake cases, the role of adjudication is to determine the content of the agreement or bargain the parties made and then hold them to its terms. That is, after all, the fundamental point of contract law. In many mistake cases, though, the content of the bargain is itself in dispute. In particular, the dispute may involve how the bargain addresses the risk of being mistaken and how the bargain allocates that risk on particular matters as between the parties. Also at issue may be the import of the obligation of good faith implied by contract law.

Separately, outcomes in some mistake cases can be explained by the policy objective of enabling people to retain the benefit of information they obtained only with difficulty or expense. This policy encourages searches for such information. An additional and sometimes competing policy objective mandates disclosure when secrecy promotes socially-disfavored behavior. That is, at times the law compels disclosure to discourage behavior that is feasible only when undertaken secretly. Analyzing the policy justifications for compelling disclosure or permitting nondisclosure inevitably implicates the justifications for prohibiting or permitting affirmative misstatements. Finally, in the most difficult cases, evident opportunism on one side of a transaction has encountered negligence on the other. Not surprisingly, no one clear pattern or template for decision emerges.

Additional complications stem from the variety of legal doctrines and remedies applicable to mistake cases. Contract law doctrines of unilateral and mutual mistake specify circumstances in which a mistake should excuse one or both parties from obligations that, but for the mistake, would otherwise bind them. Separately, mistakes in written expression may justify judicial reformation of the writing to conform it to the content of the parties' actual agreement. As it happens, some mistake situations involve breaches of express or implied warranty that enable the mistaken party to avoid the transaction and obtain restitution, or recover damages equal to the value that, but for the mistake, she would have received through the transaction.

Finally, in some circumstances, failures to disclose information constitute fraud (a tort), and may even constitute a crime. Victims of fraud generally may choose between avoiding the transaction and receiving restitution, or recovering damages in an amount sufficient to compensate for loss plus, when appropriate, punitive or exemplary
damages. Determining when nondisclosure is fraudulent is complicated by the fact that, typically, fraudulent conduct consists of an affirmative misstatement, not a failure to speak.\footnote{Fraudulent misstatement, in turn, should be differentiated from negligent misrepresentation and innocent misrepresentation. Each type of misstatement has different legal consequences. A misrepresentation is fraudulent if its maker knows it to be false, lacks confidence that he states or implies he has in the accuracy of his representation, or knows that he lacks the basis which he states or implies he has for the representation. Restatement (Second) of Torts § 526 (1977). The tort of negligent misrepresentation occurs when an actor with a pecuniary interest negligently supplies false information for the guidance of others in business transactions on which they justifiably rely. Id. § 552(1). An innocent misrepresentation as to a material fact in a sale, rental or exchange transaction, under the Restatement creates liability to one who justifiably relies on it if the statement is made to induce another to act or refrain from acting. Id. § 552C(1). In this trilogy of misstatements, only fraudulent misrepresentations evidence that the defendant had the type of motive that warrants punitive damages. See W. Page Keeton et al., Prosser and Keeton on the Law of Torts § 2, at 10-11 (1984). The Restatement limits damages for innocent misrepresentation to the difference between that with which the plaintiff parted and that which he received. Restatement (Second) of Torts § 552C(2) (1977). In an action for negligent misrepresentation, the plaintiff may, in addition, recover consequential damages. Id. § 552B. In an action for fraud the plaintiff may also recover the benefit of his bargain if damages are provable with reasonable certainty. Id. § 549(2).}

This essay explores the distinctive strengths and limits of each rationale for legal decision, in conjunction with each body of doctrine. That each rationale has its limits, of course, means only that this subject is complicated, not that the outcomes in actual cases are whimsical or inexplicable. I focus on cases that, for one reason or another, seem difficult to resolve or troubling in some other way. Most are cases in which a mistaken party either seeks to be relieved of a transaction afflicted by the mistake, or alleges that the knowledgeable party’s failure to disclose material information constituted fraud. I examine critically the hypothesis—ventured by some\footnote{A contract to which a party’s assent was induced through a misrepresentation by the other party is voidable by the victim if he justifiably relied on the misrepresentation, and the misrepresentation was either fraudulent or material. Restatement (Second) of Contracts § 164(1) (1979). If the misrepresentation was made by a third party, the contract is voidable by the victim unless the other party to the transaction in good faith and without reason to know of the misrepresentation either gave value or relied materially on the transaction. Id. § 164(2). A representation (whether or not made fraudulently) is a warranty when it promises that a matter asserted as a fact is or will be true. See 1 Arthur L. Corbin, Corbin on Contracts § 14 (1963). Warranties are either implied or express. See, e.g., U.C.C. §§ 2-313 to -315 (1990).}—that

\footnote{See, e.g., Kronman, supra note 3; Lebelle, supra note 3; Wonnell, supra note 3.}
in the interests of economic efficiency the law permits parties to exploit the value of information that they obtained as a result of a deliberate search, and that, to the extent the law does not presently do so, it should. I also examine the significance courts ascribe to a party’s carelessness in the resolution of mistake scenarios.

II. ASCERTAINING AND ENFORCING THE TERMS OF THE PARTIES’ BARGAIN

A. The Case of the Missing 000

Contract doctrine presupposes that, by entering into an enforceable contract, the parties have agreed to be bound by the terms of their agreement. This basic point is frequently helpful in resolving disputes in which a mistake of some sort accompanies the transaction. One of the most startling mistake cases in recent years, Prudential Insurance Co. of America v. S.S. American Lancer, 6 is a useful starting point even though it does not raise questions of disclosure. The dispute arose after a secured lender, Prudential Insurance, completed a refinancing of outstanding debt of United States Lines. The borrower’s outstanding indebtedness to Prudential—to be secured by an amended first mortgage—amounted to $92,885,000.7 A typist, however, omitted the final three zeroes (an omission repeated in subsequent documents), which led to instruments understating by $92,792,115 the amount of the first mortgage lender’s secured interest.8

U.S. Lines subsequently entered bankruptcy proceedings, having defaulted on the notes secured by the mortgage.9 The “missing zeroes” first came to light six months after U.S. Lines filed its bankruptcy petition, when Prudential moved to lift the automatic stay imposed by bankruptcy so it could foreclose on the mortgage.10 U.S. Lines’ bankruptcy trustee objected to Prudential’s attempt to foreclose its first mortgage interest for $92,885,000.11 Additionally, a holder of a second mortgage sought a judicial declaration that the first mortgage interest was limited to $92,885.12 The second mortgage

6. 870 F.2d 867 (2d Cir. 1989).
7. Id. at 869.
9. Id.
10. Id.
11. Prudential Ins., 870 F.2d at 870.
12. Id.
holder was unsuccessful; for one thing, the terms of its loan had been negotiated with Prudential on the assumption that Prudential had a first mortgage interest of $92,885,000. The bankruptcy trustee eventually compromised with Prudential, acknowledging the validity of the $92 million first mortgage in exchange for 17.5% of the net proceeds from the sale of the mortgaged vessels. Prudential estimated its costs attributable to the mistake at $31 million, including its payment to the bankruptcy trustee, legal fees, and delay.

This case is both easy and troublesome. It's easy because the terms of Prudential's bargain with U.S. Lines were readily ascertainable and, indeed, were believed by all parties, including the junior lender, to be the controlling terms until the borrower's default and bankruptcy prompted the lenders and the bankruptcy trustee to inspect the instruments closely. Although the documentation appeared formidably full and final, the parol evidence rule sensibly does not bar admission of extrinsic evidence to show that a written instrument is flawed as an accurate expression of the parties' agreement. Moreover, the parties' error in expressing and transcribing their bargain did not induce detrimental reliance by any nonparties; the holder of the second mortgage did not claim that it lent more than it otherwise would in the erroneous belief that the first mortgage interest was limited to the modest amount in the first mortgage documentation.

The case is troubling because both the bankruptcy trustee and the second mortgage holder seem to have acted opportunistically and to have imposed costs on the first mortgage holder through their opportunism. That is, according to the court, both the trustee (successor to the borrower's management) and the second mortgage lender knew the terms of the actual deal between the borrower and the first mortgage lender. Neither was misled by the mistake in expression, but both seem to have been eager to seize upon the mistake in pursuit of an unbargained-for advantage over the first mortgage lender. The first mortgage lender (and the lawyers involved

13. Id. at 871.
14. Id. at 870.
17. See Kull, supra note 15, at 14 (emphasizing that diversion of value from holder of first mortgage on basis of typographical error that did not induce detrimental reliance constituted unjust enrichment).
with the transaction)\textsuperscript{18} goofed, but no one else lent more or borrowed less as a consequence. Even if the first mortgage lender, like any party, neglected at its peril to read the loan documents carefully,\textsuperscript{19} its lack of care was not culpable because other parties did not, as a result, act in reliance on the erroneous documents.

“Opportunism” is not a technical term of art for purposes of legal analysis; its evident meaning as used in judicial opinions and in academic writing is highly variable. All such meanings convey moral disapproval, however. My definition is the deliberate and successful pursuit of an unbargained-for advantage. Whether the law permits the advantage to be retained is a separate question, the answer to which varies enormously with the circumstances. In the relationships analyzed in this essay, opportunistically-obtained advantage is objectionable when it results from calculated exploitation of another party’s vulnerability, which often develops through a relationship with the opportunistic actor. Interestingly, bacteriologists define “opportunistic” infections in much the same fashion, as resulting from microbes that are incapable of breaching the host organism’s natural defenses when the host is healthy.\textsuperscript{20}

\textsuperscript{18} Prudential sued, among others, the law firm that furnished it with an opinion letter, the provision of which was a condition precedent to its obligation to close the loan. See Prudential Ins. Co. of Am. v. Dewey Ballantine, Bushby, Palmer & Wood, 605 N.E.2d 318 (N.Y. 1992). The court concluded that the opinion law firm owed Prudential a duty of care, despite the lack of contractual privity or an attorney-client relationship between them, because their relationship was sufficiently close to establish such a duty. Id. at 322. In particular, the law firm addressed and sent its opinion letter directly to Prudential; Prudential unquestionably relied on the letter, as the law firm expected it to do; and the law firm was unquestionably aware of the use Prudential would make of the letter. Id. Ultimately, though, the court held that the law firm’s motion for summary judgment had appropriately been granted because its assertions in the opinion letter did not cause Prudential’s loss. The letter made no assurance as to a specific dollar amount of security, opining only that the mortgage documents represented “‘legal, valid and binding’ obligations of U.S. Lines, which, when recorded, would be enforceable against it ‘in accordance with [their] respective terms,’ whatever those terms might be.” Id. at 323.

\textsuperscript{19} See, e.g., King v. Horizon Corp., 701 F.2d 1313, 1317-18 (10th Cir. 1983) (stating that the general principle that purchasers should read contracts, and the related principle that a purchaser may not rely on an agent’s oral representations when the seller has included a written disclaimer in contract, are inapplicable when the principal encourages or ratifies its agent’s fraud, or exercises inadequate supervision over its agent).

\textsuperscript{20} In bacteriology, an “opportunistic” is “an organism incapable of inducing disease in a healthy host, but able to produce infections in a less resistant or injured host . . . .” Blackstone’s Gould Medical Dictionary 931 (4th ed. 1979). Such organisms, that is, cannot under normal conditions breach the host’s natural de-
A further question not raised by the opinions in *Prudential Insurance* is whether the opportunistic acts of the bankruptcy trustee and second mortgage holder are themselves independently actionable. Three potential lines of attack merit exploration, but only briefly for the initial two prospects. First, did the bankruptcy trustee and second mortgage lender breach an express or implied warranty, namely, a warranty that the borrower’s actual indebtedness to Prudential corresponded to the amount stated in the instrument? Second, and relatedly, did the trustee and the junior lender defraud Prudential

fenses; infection is successfully produced only in vulnerable hosts.

This definition may correspond more closely to ordinary linguistic usage—and to case law outcomes—than do others in the literature. Professor Williamson and his co-authors define opportunism as “an effort to realize individual gains through a lack of candor or honesty in transactions.” See Oliver E. Williamson et al., *Understanding the Employment Relation: The Analysis of Idiosyncratic Exchange*, 6 *Bell. J. Econ.* 250, 258 (1975). This definition, though, does not encompass the demands of the bankruptcy trustee and second mortgage lender in *Prudential Ins.*, who withheld no information. Professor Kostrinsky, in contrast, defines opportunism in a more open-ended fashion. She treats it initially as “strategic withholding of information,” but acknowledges that in preliminary negotiations a party would act opportunistically if he “strategically avoids making a formal commitment . . . and the other party’s trust or ignorance stiffles any urge to insist on a formalized bargain before making transaction-specific investments.” Juliet P. Kostrinsky, *Bargaining with Uncertainty, Moral Hazard, and Sunk Costs: A Default Rule for Precontractual Negotiations*, 44 *Hastings L.J.* 621, 642-43 (1993). In the same context, opportunism also encompasses a putative promisor’s effort “to exploit transaction-specific investments made by the putative promisee at the promisor’s request.” *Id.* at 643. In these examples, the opportunistic party has, arguably, withheld the information that he is not trustworthy, but has not withheld information specific to the transaction.

Other treatments of opportunism emphasize the problem created by sequential performance. See, e.g., *Jordan v. Duff & Phelps, Inc.*, 815 F.2d 429 (7th Cir. 1987), *cert. dismissed*, 485 U.S. 901 (1988). In *Jordan*, Judge Easterbrook offers quintessential examples of opportunism in employment relationships: (1) an employer’s termination of an otherwise satisfactory employee one day before his pension vests, and (2) termination of a salesman one day prior to disbursement of a large commission. *Id.* at 438. Judge Posner’s textbook initially treats opportunism as resulting from the sequential performance phenomenon. See Richard A. Posner, *Economic Analysis of Law* 89-90 (4th ed. 1992). He further characterizes as “opportunistic” a borrower’s decision to increase its expected return on investments through business activity that also increases the risk that it will default on a loan. *See id.* at 396.

Professor Cohen defines the term most broadly, to encompass “any contractual conduct by one party contrary to the other party’s reasonable expectations based on the parties’ agreement, contractual norms, or conventional morality.” George M. Cohen, *The Negligence-Opportunism Tradeoff in Contract Law*, 20 * Hofstra L. Rev.* 941, 957 (1992) (footnotes omitted). This definition would treat all breaches of contract as opportunist, if we assume that one party to a contract reasonably expects that the other will perform. Such breadth, of course, vitiates the moral disapproval conventionally conveyed by the term.
through their attempts to limit Prudential’s security interest to the amount stated in the instrument? Even if the trustee and the junior lender knew that the amount stated in the instrument was mistaken, they did not use the instrument to induce Prudential to lend. In the absence of any action by Prudential that was induced by the other parties’ problematic conduct, attacks grounded in breach of warranty and fraud would fail.

A third line of attack, focused exclusively on the parties’ post-bankruptcy conduct, is more promising. Case law in some jurisdictions, most prominently California, defines as tortious certain breaches of the covenant of good faith and fair dealing, a covenant which is implied in a commercial contract. In Seaman’s Direct Buying Service, Inc. v. Standard Oil Co. of California,21 the California Supreme Court held that a party to a contract would act tortiously if it denied in bad faith the existence of a binding contract.22 In contrast, Seaman’s also held that a denial is not tortious if it reflects an honest dispute about the existence of the contract, in short, if it occurs in good faith.23 To be sure, the bankruptcy trustee and second mortgage lender in Prudential Insurance did not deny the existence of any contract between the borrower and Prudential. They only denied the enforceability of the terms of the contract they knew Prudential demonstrably made with the borrower.24 The trustee and the junior lender, like the defendant in Seaman’s, seem to have opportunistically exploited the known costs of litigation without a factual basis for disputing the content of the contract.25 Moreover, the bankruptcy

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22. Id. at 769, 686 P.2d at 1167, 206 Cal. Rptr. at 363.
23. Id.
24. Prudential Ins., 870 F.2d at 871.
25. Separately, an attorney or an unrepresented litigant in a federal civil action who interposes a pleading, motion, or other paper “for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation” has violated Rule 11 and is subject to sanctions. See Fed. R. Civ. P. 11. Harassment, unnecessary delay, and needless increases in costs are only illustrative examples, not an exhaustive listing, “of improper purposes.” Gregory P. Joseph, Sanctions: The Federal Law of Litigation Abuse § 13(B), at 183 (1989). More generally, “An improper purpose is any purpose other than one to vindicate rights (substantive or procedural) or to put claims of right to a proper test.” Id. § 13(B), at 96 (Cum. Supp. 1992). Rule 11 is also violated by the interposition of a paper that is not well-grounded in fact, or is not warranted either by existing law or a good faith argument for its extension, modification or reversal. See Fed. R. Civ. P. 11. See generally Joseph, supra (providing extensive discussion of Rule 11 sanctions).
trustee's fiduciary status does not excuse tortious behavior, even that of benefit to the bankruptcy estate. A fiduciary's loyal pursuit of its beneficiary's interest does not license theft or other wrongful conduct.

In short, the bankruptcy trustee and second mortgage lender opportunistically seized on Prudential's error; neither the borrower nor the junior lender took any prior action on the basis of the error or knew of it until after the borrower's bankruptcy. To the extent the bankruptcy trustee succeeded in extracting value from Prudential, legal institutions themselves facilitated the trustee's opportunistic pursuit.

B. The Case of the Worthless Collateral

Mistake scenarios become more complicated when one party knows that the other is about to make a serious mistake. Additionally, elements of the parties' bargain may elude straightforward analysis. Suppose that a prospective borrower has received a commitment for a secured loan and, prior to closing, learns that the designated collateral has become worthless. Is the borrower under a duty to enlighten the lender prior to closing? In Federal Deposit Insurance Corp. v. W.R. Grace & Co., the Seventh Circuit held that the borrower in a $75 million nonrecourse loan relationship committed fraud when it failed to disclose to the lender that part of the collateral was worthless. In the court's analysis, when the lender committed itself to make the loan, it bound itself to an interest rate and a principal amount with the understanding that other terms would be resolved prior to closing. The commitment, although enforceable as to the terms it contained, was incomplete because it did not address a range of risks that might materialize before the closing. The commitment fee paid in exchange by the borrower compensated the lender for agreeing to make the loan at a specified interest rate, but did not bind it to lend regardless of post-commitment events.

W.R. Grace articulates an express rationale for the borrower's duty to disclose. In general, the opinion recognizes that a seller dealing at arm's length may exploit information that it expended time or money to develop. A seller has, in contrast, a duty to

27. Id. at 618.
28. Id. at 622.
29. Id.
disclose information when it has "without substantial investment . . .
come upon material information which the buyer would find either
impossible or very costly to discover himself . . . for example, [the
seller] must disclose that the house he is trying to sell is infested
with termites." In a secured lending relationship, both the borrower
and the lender are sellers, but of different things and in different
senses. The borrower sells (and the lender buys) a security interest
through the lien that gives the lender an interest in the borrower's
property. Any lender, in a less technical sense, sells the use of its
money in exchange for the borrower's promises to repay the loan
and to pay interest. A secured lender, additionally, receives a security
interest in the borrower's property. Neither the borrower's nor the
lender's sale is precisely analogous to the homeowner's sale of his
termite-infested house. The borrower sells only a security interest
in the collateral, such that the lender's right to exercise all incidents
of property ownership is subject to many contingencies. What the
lender "sells" is the right to use an amount of a fungible medium
of exchange, i.e., its money, for a period of time on stated terms;
the borrower's commitment obviously is to repay the amount lent,
not to return particular pieces of currency.

In any event, an additional fact in W.R. Grace, not addressed
in the court's legal analysis, makes the picture more intriguing. The
collateral at issue consisted of a fifty percent interest in three natural
gas fields owned by a third party, Centex Corporation, that W.R.
Grace had agreed to buy. As the loan would be a nonrecourse
loan, it would not be repaid and the lender would have no remedy
against the borrower if the fields were nonproductive. Prior to the
loan closing, Centex told W.R. Grace that one of the fields was so
infused with water that it would never produce gas. The other

31. Id. Moreover, some sellers know that their houses are infested with termites
because they have paid for a termite inspection, but then decide to sell the house
without exterminating the termites. Have these sellers made a substantial investment,
worthy of protection, to "come upon" the information about their termites?
32. See U.C.C. § 1-201(32) (1990) (defining "purchase" to include any taking
that creates an interest in property through a voluntary transaction, including
a mortgage or lien).
33. W.R. Grace, 877 F.2d at 617.
34. Id.
35. Id. Centex also insisted that W.R. Grace perform its own contract to buy
the fields, despite Centex's discovery—revealed to Grace—that one of the fields
was worthless. Id. at 618. W.R. Grace sued Centex, alleging that Centex fraudulently
failed to disclose the water problem to Grace. The suit was settled for $13 million.
Id.
fields were productive, but natural gas prices plummeted after the loan closed. Revenues from the fields were never sufficient to repay any portion of the principal of the loan.\textsuperscript{36}

Centex did not restrict disclosure of the water problem to W.R. Grace. Centex issued a press release characterizing the waterlogged field as "non-commercial."\textsuperscript{37} The lender, Continental Bank, subscribed to a news service that carried the release, but, according to the court, "no one . . . concerned with the Grace loan noticed it."\textsuperscript{38} Continental Bank, in short, was unlike the purchaser of property infested with termites. Certain knowledge of a typical termite infestation is impossible without the owner's assistance or, perhaps, research inquiries to local pest-control experts, some of whom may have treated or inspected the property. Not only did Continental Bank have ready access to the information about the field which had been publicly released by the owner, but other departments within Continental Bank may well have had possession of the information!

Several aspects of the court's stated rationale for its decision in \textit{W.R. Grace} are problematic. One initial reservation is the asymmetric nature of the court's criterion for disclosure. Recall that the court expressly addressed the disclosure obligation of a "seller" but not that of a "buyer." In general, as explained below, buyers in many settings are able to withhold with impunity information comparable to information that a seller is obliged to disclose.

Additionally, the \textit{W.R. Grace} court applied the seller's duty to a borrower without considering the significance of the lender/buyer's access to, or possession of, the same information. Conventional statements of the requisites of fraud include reliance components: the plaintiff must in fact have relied on the defendant's misstatement, and that reliance must have been justifiable.\textsuperscript{39} Reliance questions are trickier when the defendant's conduct consists of nondisclosure. One possibility is to characterize \textit{W.R. Grace}'s conduct, not as nondis-

\textsuperscript{36} \textit{Id.}

\textsuperscript{37} \textit{W.R. Grace}, 877 F.2d at 618.

\textsuperscript{38} \textit{Id.} As it happens, under U.C.C. § 1-201(27) notice, knowledge of a notice or notification received by an organization is effective for a particular transaction when it is brought to the attention of the individual conducting that transaction and "in any event from the time when it would have been brought to his attention if the organization had exercised due diligence." U.C.C. § 1-201(27). Due diligence under this subsection requires reasonable routines, reasonably complied with, for communicating significant information. \textit{W.R. Grace} does not discuss the impact of U.C.C. § 1-201(27).

\textsuperscript{39} \textit{See Restatement (Second) of Torts} § 537 (1977).
closure, but as knowing failure to correct earlier statements of material fact about the collateral that had become false. The question then is whether Continental Bank justifiably understood W.R. Grace’s silence to constitute an assurance that nothing material had occurred to contravene the truth of earlier statements.

Separately, one might consider whether the lender justifiably, at that point in its relationship with the borrower, treated the borrower as its exclusive source of information about the collateral, rather than utilizing information to which it independently had access. The relevant question in such a case is not simply the plaintiff’s access to information and cost of acquiring information. Continental Bank was defrauded by W.R. Grace only if—wholly apart from its access to information—the lender should be able to rely on the borrower to respect the lender’s interests during their post-commitment, pre-closing relationship.

One difficulty not confronted by the W.R. Grace court is accommodating its conclusion that the borrower’s behavior in that case was fraudulent, with the general proposition that tort law does not oblige parties dealing at arm’s length to take affirmative steps to prevent loss to the other party. A lender is under no duty to disclose to a borrower information in the lender’s possession that reflects adversely on the use the borrower will make of the loan, unless the relationship between the lender and borrower can be characterized as confidential; or the lender is itself involved in the business in

40. See Keeton et al., supra note 4, § 106, at 738.
41. Cf. Restatement (Second) of Torts § 551 cmt. k (1977) (discussing the duty to disclose). The Restatement does not impose a duty to disclose on the defendant “[w]hen the facts are patent, or when the plaintiff has equal opportunity for obtaining information that he may be expected to utilize if he cares to do so, or when the defendant has no reason to think that the plaintiff is acting under a misapprehension...” Id.
42. See Keeton et al., supra note 4, § 56, at 374.
43. See Sparks v. Union Trust Co., 124 S.E.2d 365, 368 (N.C. 1962) (holding that the defendant bank was not under a legal duty to inform the plaintiff of the possible future insolvency of plaintiff’s proposed lessee).
44. See Barnett Bank of W. Fla. v. Hooper, 498 So. 2d 923, 926 (Fla. 1986) (holding that the jury reasonably could have found that the following facts constituted “special circumstances” creating a duty of disclosure on the bank to the borrower: (1) bank established confidential relationship with the borrower; (2) bank entered into transaction with borrower from which it was likely to benefit; and (3) at the time of the transaction, the bank had knowledge of material facts not otherwise available to borrower).
which it knows the borrower will invest. 45 Interestingly, in a case decided after W.R. Grace, involving a lender’s nondisclosure to a guarantor, the Seventh Circuit observed that “[b]anks’ self-interest leads them to nose out the value of collateral; if they do not, they are apt to suffer loss.” 46 Lenders, the court assumes, have a self-interest in being inquisitive about borrowers. The same capacity for self-interested inquisitiveness, applicable to guarantors, means that the lender has no obligation to a guarantor to disclose circumstances known to the lender that reduce the value of the borrower’s assets which collateralize the loan. 47 As a result, both the lender and the guarantor may incur costs in acquiring the same information.

Thus, it is not possible to explain the outcome in W.R. Grace by a simple theme of reducing transaction costs. That is, one might argue that, unless the borrower shares with the lender the information that the gas field is irreparably waterlogged, the lender will incur some cost to learn the information itself. However, the same point would apply in the guarantee case as well, assuming the lender truly knows something the guarantor does not know. The lender, though, has no obligation to disclose the information to the guarantor. In short, some information need not be disclosed even though its disclosure would save costs otherwise to be incurred by the other party in independently obtaining the information. Indeed, in commercial property transactions like that in W.R. Grace, whether the seller has acquired information without substantial investment is not an especially illuminating or even manageable criterion. The corporate seller (that is, the borrower) in W.R. Grace “knew” the gas field to be waterlogged because some of its employees acquired that information within the course of their work for the corporation, work that they presumably did not perform for free. Even if the borrower can establish that in some measurable respect it incurred costs in acquiring the information, that fact does not constitute an affirmative defense to fraud.

As it happens, the author of the W.R. Grace opinion, Judge Richard Posner, addresses fraud using much the same reasoning in

45. See Richfield Bank & Trust Co. v. Sjogren, 244 N.W.2d 648, 652 (Minn. 1976) (finding that loan officer’s heavy involvement in third party’s business created an affirmative duty of disclosure).
47. Id. Additionally, the individual guarantors in Everett were the controlling shareholders of the corporate borrower. Id. at 702.
his treatise *Economic Analysis of Law*.\textsuperscript{48} Using the termite example, Judge Posner writes:

[U]nless there is a duty of disclosure . . . the buyer will invest in a termite inspection or negotiate for a clause in the deed warranting that the house is termite-free. These costs are avoided by the imposition on the seller of a duty to disclose information that he obtained costlessly. So here is another reason for forbidding sellers to lie: to save the expense of the self-protective measures that buyers would have to take if there were no legal remedies against sales misrepresentations.\textsuperscript{49}

This rationale, however, seems over-inclusive, as it would support a lender’s general obligation to disclose to guarantors and borrowers. Additionally, tort law does not treat all affirmative misrepresentations as fraud; rather, it recognizes that some misrepresentations are negligent or innocent, and assigns legal consequences to such misrepresentations that differ from the consequences associated with fraud.\textsuperscript{50} A bit earlier in his treatise, Judge Posner suggests a somewhat different analysis of fraud. He writes: “[A] liar makes a positive investment in manufacturing and disseminating misinformation. This investment is completely wasted from a social standpoint, so naturally we do not reward him for his lie.”\textsuperscript{51} Fraud, however, also encompasses culpable nondisclosure, an activity requiring no expenditure of effort.

Would it be preferable to analyze the events in *W.R. Grace* as a breach of warranty by the borrower rather than fraud? The principal consequence is that the defendant, not having committed a tort by breaching the warranty, would not be subject to punitive damages. Even though the borrower in *W.R. Grace* did not expressly warrant the value of the collateral at closing, it can reasonably be understood to have impliedly warranted that any prior express representations about the collateral had not been undone by subsequent events. The borrower would breach the implied warranty even if it did not know about the subsequent events;\textsuperscript{52} the borrower’s knowing nondisclosure,

\textsuperscript{48} Posner, supra note 20.

\textsuperscript{49} Id. at 110.

\textsuperscript{50} See supra note 4.

\textsuperscript{51} Posner, supra note 20, at 109-10. See also id. at 208 (providing a comparable analysis of theft).

in contrast, is fraudulent.\textsuperscript{53} In both situations the lender's basic assumptions about the loan have become unfounded, and it has lent on terms it would not have, had it been fully informed at the time of closing. From the lender's standpoint, in both situations it has mispriced the loan transaction; to protect itself against the risk of mispricing requires additional investment in obtaining and analyzing information.

In short, the distinction between fact situations creating claims of breach of warranty and those creating claims of fraud is not readily explained either by the likely costs to the victim in protecting herself, or by the extent to which the transaction is mispriced. Such bases for distinction, moreover, do not explain the distinctive extra-compensatory remedies (including punitive damages and, in some circumstances, criminal sanctions) associated with fraud. These remedies typify conduct that society, acting through the legal system, deems worthy of deterrence and vengeance. One who commits fraud takes her victims' property without their consent, conduct that if left unsanctioned could deter future transactions by those particular victims and by others who reasonably fear becoming victims. Being cheated, that is, is different from being mistaken. Additionally, in contexts like \textit{W.R. Grace}, treating nondisclosure as fraudulent acknowledges the value of protecting reliance (even that of the moderately foolish) on the integrity of another when the parties' relationship has progressed to the point that cooperative behavior could fairly be expected.

In general, the pre-closing relationship between lender and borrower imposes on the parties a duty of good faith that inhibits a party's ability to evade or escape the obligation she has undertaken, so long as the lender's loan commitment accepted by the borrower creates definite and certain duties to perform.\textsuperscript{54} In this context, the duty of good faith encompasses negotiation over terms not contained in the commitment that are requisite to the final loan documentation.\textsuperscript{55} The visibly incomplete nature of a loan commitment, and the

\textsuperscript{53} See \textit{Restatement (Second) of Torts} § 551 (1977).


\textsuperscript{55} The loan commitment is a useful example of parties' ability to create enforceable contractual obligations with an instrument that they mutually understand to be incomplete. Loan commitments conventionally condition the lender's obligation to close on the satisfaction of express conditions by some stated date. See, \textit{e.g.}, \textit{Penthouse Int'l, Ltd. v. Dominion Fed. Sav. \& Loan Ass'n}, 855 F.2d 963 (2d Cir. 1988), \textit{cert. denied}, 490 U.S. 1005 (1989).
separation in time between the commitment and loan closing, invite evasion unless the parties are subject to a robust duty of good faith. In contrast, once the loan closes, the final loan documentation surely appears to be intended by the parties as a full and final statement of their agreement. Courts resist a robust reading of the duty of good faith to supplement or vary the explicit terms of such a full and final statement of an agreement. The pre-closing environment, in short, conduces to a relaxation of the lender’s inquisitiveness because the duty to negotiate in good faith toward closing presupposes something other than an arm’s-length relationship. Such a relationship, in turn, nurtures expectations that relevant information will be shared, not withheld.

Finally, the lender in W.R. Grace was mistaken in two material respects. As noted, it mistakenly believed that all of the property collateralizing the loan could produce natural gas. Additionally, the lender mistakenly assumed that gas produced by the fields would sell at sufficiently high prices to generate revenues to repay the loan. If the lender had recognized this mistake, it certainly would not have lent on a nonrecourse basis. This latter type of mistake, though, is not conventionally treated as a basis for relief. Contract doctrine recognizes that parties may assume the risk of being mistaken even when, as in W.R. Grace, the mistake results in disparate exchanges of value. Nor is it unconscionable to hold a party to a bargain.

56. See, e.g., Metropolitan Life Ins. Co. v. RJR Nabisco, Inc., 716 F. Supp. 1504 (S.D.N.Y. 1989). That such a statement is intended to be final as of the time of its execution does not exclude the prospect of subsequent attempts to modify its terms. The import of good faith as a limit on proposals to modify is beyond the scope of this essay. See generally Victor Brudney, Corporate Bondholders and Debtor Opportunism: In Bad Times and Good, 105 HARV. L. REV. 1821, 1843-49 (1992) (discussing how the good faith requirement limits the modification of the long-term, contractual relationship between stockholders and bondholders).

57. Mistaken predictions or assumptions about future events do not count as “mistakes” for purposes of contemporary contract law, which restricts the concept of mistake to facts believed to be existent at the time the contract is made. RESTATMENT (SECOND) OF CONTRACTS § 151 cmt. a (1981). As to such facts, in the absence of an allocation of the risk in the parties’ agreement, a party bears the risk of a mistake when “he is aware at the time the contract is made, that he has only limited knowledge with respect to the facts to which the mistake relates but treats his limited knowledge as sufficient,” or when the court allocates the risk to him on the basis that doing so is reasonable under the circumstances. Id. § 154. Contemporary contract law does not treat most mistaken predictions about future events as occasions to excuse performance on the basis of its impracticability unless reasonable efforts are used to overcome the insurmountable obstacles. See id. § 261 cmt. d.
that results in a disparate exchange of values, when the party has assumed the risk of such an outcome.\textsuperscript{58} Indeed, one might wonder whether Continental Bank suffered any loss caused by the borrower’s nondisclosure, since the drop in natural gas prices meant that the producing fields did not yield revenues sufficient to repay the loan. Perhaps Continental could have established that, had it known that one of the fields would never have been productive, it would not have closed the loan with W.R. Grace and would have lent all or some of the money elsewhere.\textsuperscript{59}

Both \textit{Prudential Insurance} (the ship mortgage case) and \textit{W.R. Grace} illustrate that courts limit parties’ efforts to take advantage of others’ careless errors. In \textit{Prudential Insurance}, the bankruptcy trustee and the junior lender attempted, with minimal success, to use the first mortgage lender’s careless failure to accurately proofread as a basis for reducing the amount of the security interest. Likewise, the borrower’s failure in \textit{W.R. Grace} to disclose the reduction in collateral value seems opportunistic, especially given the evolution in the legal character of the parties’ relationship, from arm’s-length negotiations prior to the loan commitment, to mutual commitment in good faith to achieve the full agreement requisite to closing. W.R. Grace had no basis for believing that Continental Bank, in issuing a loan commitment, knowingly assumed the risk of all developments prior to closing that would reduce the value of the collateral.\textsuperscript{60} Continental Bank’s careless failure to review publicly available information should

\textsuperscript{58} See generally \textit{id.} \textsuperscript{\textsc{208}} (discussing unconscionable contracts and terms therein). Comment \textsc{c} observes that “[i]nadequacy of consideration does not of itself invalidate a bargain, but gross disparity in the values exchanged may be an important factor in a determination that a contract is unconscionable and may be a sufficient ground, without more, for denying specific performance.” \textit{id.} \textsuperscript{\textsc{261}} cmnt. \textsc{c}.

\textsuperscript{59} In \textit{W.R. Grace}, the Seventh Circuit remanded for a new trial solely on the issue of damages. \textit{W.R. Grace}, \textsc{877 F.2d} at \textsc{624}. The jury awarded $25 million in compensatory damages and $75 million in punitive damages. The trial court reduced the award of punitive to $25 million. \textit{id.} at \textsc{617}. The Seventh Circuit held that, at trial, the parties presented insufficient evidence on compensatory damages, particularly with regard to the present value of the loan to the borrower at the time of trial, the interest Continental received on the loan and the principal, and interest Continental would have obtained from an alternate loan. \textit{id.} at \textsc{623}.

\textsuperscript{60} In the same spirit, some courts disapprove of the pretextual use of trivial violations of contract terms to take advantage of the other party’s prior investment. \textit{See} \textit{Original Great Am. Chocolate Chip Cookie Co. v. River Valley Cookies, Ltd.}, \textsc{970 F.2d 273}, \textsc{280} (7th Cir. 1992) (discussing the cancellation of a franchise on the pretext of trivial violations in order to take advantage of a franchisee’s success by the franchisor).
not enable the borrower to add a significant unbargained-for risk to the lender’s commitment.

III. Protecting Investments in Information

A. Mistakes About Cows, Jewels, Tobacco and Mineral-Laden Farmland

Outcomes in mistake cases also elude simple explanation when one focuses on cases from an earlier era in the history of contract doctrine. To illustrate the difficulty, consider the variation in outcomes in three well-remembered cases in general contract law. All three cases involved owners of property who, unaware of a characteristic of the property or a circumstance otherwise affecting its value, sold it to a buyer at a price the seller would not have found acceptable, had the seller known of the characteristic or circumstance. In Sherwood v. Walker, the buyer was unsuccessful in his suit to replevy Rose, a cow, sold by an owner who erroneously believed Rose to be infertile. The court held for the seller on the basis that both parties shared the erroneous belief and priced Rose’s sale on that basis. In contrast, in Wood v. Boynton the seller was unsuccessful in an action for restitution following her sale to a jeweler of a small stone for a small amount of money. The stone turned out to be an uncut diamond worth $700. The court’s opinion states that restitution might be warranted had the jeweler known the stone to be a diamond. The third case illustrates that a buyer’s knowledge of the seller’s error does not invariably support rescission. In Laidlaw v. Organ, the buyer knew at the time of contracting to buy tobacco that, unbeknownst to the seller, a peace treaty had been signed that would end the War of 1812 and the British blockade of New Orleans.

61. Professor Kull, who sees greater promise in the historically-based approach, notes that the traditional view of unilateral mistake did not afford relief when the mistake concerned the value of the subject matter. See Kull, supra note 3, at 65. “Value,” however, is not a concept that defines itself. Was the lender’s mistake in W.R. Grace one simply about the value of the collateral? Or does it suggest that the lender “in some fundamental sense does not know what [it] is doing...” Id. (emphasis added).

62. 33 N.W. 919 (Mich. 1887).
63. 25 N.W. 42 (Wis. 1885).
64. Id. at 45 (“It cannot... be said that there was a suppression of knowledge on the part of the defendant as to the value of the stone which a court of equity might seize upon to avoid the sale.”).
66. Id. at 182-84.
This news was significant, as the war and the blockade had depressed the price of tobacco in New Orleans.\textsuperscript{67} Although the United States Supreme Court reversed a directed verdict for the buyer, the Court observed in dictum that a buyer was under no duty to disclose a change in extrinsic circumstances known to him exclusively, "where the means of intelligence are equally accessible to both parties."\textsuperscript{68}

The outcomes in this trilogy are, upon reflection, difficult to reconcile. \textit{Sherwood} might be treated as a case of mutual mistake, a rare phenomenon that prevents contract formation if the mistake concerns a basic aspect of the subject matter of the parties’ bargain. Otherwise, the benefits and detriments generated by the exchange would in some major respect not be those for which the parties bargained. In \textit{Wood}, the court’s suggestion that rescission would be justified when a unilateral mistake is known to the other party erodes any special significance to be ascribed to mutual mistake. Not all courts deny the benefit of a transaction to a party who knows the other to be mistaken. The dictum in \textit{Laidlaw} suggests an outcome in the tobacco transaction inconsistent with the dictum in \textit{Wood}, as the tobacco buyer surely knew that his seller was ignorant. To distinguish \textit{Laidlaw} requires separate treatment of mistakes about incidents of the contract’s subject matter itself, in contrast to mistakes about external circumstances. This seems artificial, given the significant impact on value that external matters may have.\textsuperscript{69}

Moreover, as the dissent argued in \textit{Sherwood}, perhaps the parties were not mutually mistaken about Rose. The seller, to be sure,

\textsuperscript{67} See \textit{id.} at 183. The Court held that the jury, not the trial judge, should determine whether the buyer practiced any imposition on the seller. \textit{id.} at 195.

\textsuperscript{68} \textit{id.} at 195. The dictum permitting nondisclosure concludes with the caveat that "each party must take care not to say or do anything tending to impose upon the other." \textit{id.} In \textit{Laidlaw}, the seller asked the buyer whether there was any news that would affect the price of tobacco. \textit{id.} at 183. The trial court found the buyer did nothing to impose upon or mislead the seller, which suggests that the buyer did not respond to the seller’s question. \textit{id.}

\textsuperscript{69} In any event this distinction, which some opinions articulate, seems to have been discarded. The \textit{Restatement (Second) of Contracts} provides that a mutual mistake makes a contract voidable when it concerns "a basic assumption on which the contract was made [which] has a material effect on the agreed exchange of performances . . . ." \textit{Restatement (Second) of Contracts} § 152 (1981). Almost a century after its opinion in \textit{Sherwood}, the Michigan Supreme Court limited the case to its facts, stating that the distinction drawn in \textit{Sherwood} between mistakes affecting value and those affecting the substance of consideration served only as "an impediment to a clear and helpful analysis for the equitable resolution of cases in which mistake is alleged and proven." Lenawee County Bd. of Health v. Messerly, 331 N.W.2d 205, 209 (Mich. 1982).
mistakenly believed that Rose was barren, but the buyer (well-known as a cattle breeder) was optimistic. Additionally, both parties knew the limits of nineteenth-century veterinary science and realized that Rose’s fecundity would be knowable only with time. In this light, each party in Sherwood, like the parties in Wood, knowingly assumed the risk of their own ignorance about the subject matter of the transaction. The difference between the cases is that neither party in Sherwood could have known Rose’s full potential at the time of the transaction. Transactions differ in the degree of certainty the parties may attain in their knowledge of the subject matter. One can become entirely certain whether any given stone is a diamond; appropriate testing can unmask even the most skillful fakes. In contrast, transactions in purported antiques and works of fine art raise questions of authentication and identification that sometimes are matters of expert opinion and are not susceptible to resolution with the certainty of diamond testing. Sellers may more easily be found to have assumed the risk of mistake in these cases when the buyer’s superior knowledge is ultimately a matter of educated connoisseurship not ultimately susceptible to scientific verification.

These cases also illustrate that contract doctrine does not unequivocally protect parties’ ability to exploit information that they have obtained with effort. The dictum in Wood, like the outcome in Sherwood, works to deny expert buyers the full benefit of insights made possible by a lifetime of specialized dealing. Why would a jeweler, recognizing a stone to be a diamond, not be as free to exploit that recognition as the tobacco buyer in Laidlaw was to exploit

70. To assume the risk of a mistake has been held to require conscious awareness of the possibility of error. See Beachcomber Coins, Inc. v. Bosket, 409 A.2d 78 (N.J. Super. Ct. App. Div. 1979) (granting rescission of sale of coin that, unbeknownst to either party at time of sale, was a counterfeit; at time of sale, both parties were certain coin was genuine).

71. Even some attributions of Old Masters that passed muster with Bernard Berenson—himself a scholar and connoisseur who detected many erroneous attributions—have subsequently been challenged. See Ernest Samuels, Bernard Berenson: The Making of a Connoisseur 287 (1979).

72. Focusing specifically on Laidlaw v. Organ, Professor Coleman argues that in some cases “any authoritative rule ” provided by the court will solve the parties’ problem. Jules L. Coleman, Risks and Wrongs 161 (1992). Professor Coleman characterizes the problem as one of coordination, that is, a need for basic ground rules that enable parties to determine whether they will gain through negotiating a transaction. Id. With such a rule, the parties can negotiate more easily. Coleman additionally notes that in Laidlaw, both buyer and seller were repeat players in a highly competitive market. Id.
information about the end of the blockade? If anything, the jeweler is likely to have invested more of his time and intellectual energy in learning how to identify unprepossessing gemstones than the tobacco dealer has invested in learning how to react to market-sensitive information.

To be sure, divergent outcomes in some mistake scenarios can be explained more easily. A purchaser of real estate has no duty to inform the seller that the purchaser has an excellent reason to believe that the land is worth much more than its purchase price. Thus, a mining company, Texas Gulf Sulphur (Texas Gulf), was free to buy mineral rights on land adjoining a site on which it conducted exploratory drilling that yielded promising results, without telling the sellers that comparable mineralization probably lay beneath their land as well.73 However, executives and directors of Texas Gulf who knew about the exploratory results and bought stock prior to the company’s announcement of its ore strike committed federal securities fraud.74 Their duty, according to the court, was to disclose the information or abstain from trading.

Why the divergence? Why may Texas Gulf do to adjacent landowners what its insiders may not do to shareholders? For one thing, Texas Gulf’s insiders seemed to be exploiting the company’s information, not their own. Moreover, if they were free to exploit the information by buying stock, they may well have been tempted to delay its release or to understate its impact when they did release it publicly.75

Mandated disclosure, in short, sometimes operates as a preventive measure when the party obliged to disclose might be strongly tempted to engage in socially disfavored conduct. Texas Gulf’s executives must disclose the information or abstain from trading because, if free to exploit it in the securities market, their decisions in handling the information on behalf of the company are likely to be biased.76

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73. See Kronman, supra note 3, at 20 (providing a more detailed account of the facts). In SEC v. Texas Gulf Sulphur Co., 401 F.2d 833, 834 (2d Cir. 1968) (en banc), cert. denied, 394 U.S. 976 (1969), the court noted that Texas Gulf, for business reasons (i.e., the purchase of mining rights on adjacent land) delayed disclosing the fact of the ore strike.
74. Texas Gulf, 401 F.2d at 852.
76. In particular, they may delay disclosure of negative information, to fa-
In contrast, Texas Gulf's own secrecy in real estate transactions does not seem as vulnerable to abuse. Obvious forms of abuse by Texas Gulf would be inhibited because they would be treated as fraud. Thus, if Texas Gulf affirmatively took steps to dissuade the adjacent landowners from learning about the mineralization on their property, its failure to disclose the information it possessed would constitute fraud. If an adjacent landowner asked Texas Gulf whether it were aware of any new information about mineralization in the vicinity, and Texas Gulf lied in response, its false affirmative response would also constitute fraud.

This conclusion troubles Professor Levmore, who has written that economic efficiency is defeated by permitting the seller to free ride on the buyer's research. Levmore advocates a policy of "optimal dishonesty" that would privilege the buyer's false denial. He argues that a policy of optimal dishonesty would produce misinformation (here, the false denial) that would cause the misled party to behave as he would have without the information. This line of reasoning is unpersuasive. The lied-to seller might be dissuaded—knowing of Texas Gulf's superior resources—from undertaking his own investigation, which he would have undertaken had Texas Gulf refused to answer his question or responded "no comment." Indeed, the jeweler in Wood, if free to exploit an ignorant seller's known

cilitate their own exodus from stock ownership. How positive information may be handled is harder to predict. Insiders may also delay its disclosure to facilitate their own purchases and purchases by persons they tip. But if an insider’s compensation is structured to reward him for increases in stock price that occur sooner rather than later, she may accelerate disclosure. In Professor Trebilcock’s terminology, such a situation illustrates a “classic agency cost problem,” which is appropriately resolved by a stringent disclosure rule. See Michael J. Trebilcock, The Limits of Freedom of Contract 115 (1993).

77. See Levmore, supra note 3, at 139. Professor Barnett would permit the buyer to lie in this situation on the basis that the seller’s question is inappropriate “and, therefore, he simply is not entitled to a truthful answer.” Randy E. Barnett, Rational Bargaining Theory and Contract: Default Rules, Hypothetical Consent, the Duty to Disclose, and Fraud, 15 Harv. J.L. & Pub. Pol’y 783, 799 (1992). Professor Barnett’s analysis does not distinguish between failing to answer the seller’s question and answering it falsely. It seems also to counter common-sensical instincts toward self-protection, chief among them the American folk aphorism that “it never hurts to ask.”

78. Levmore, supra note 3, at 140.

79. Id.

80. See generally Basic Inc. v. Levinson, 485 U.S. 224, 239 n.17 (1988) (characterizing “no comment” responses as the functional equivalent of silence). In a similar scenario, Texas Gulf could purchase the land as an undisclosed principal by employing an agent. See infra text accompanying notes 100-05.
mistake, may be tempted to dissuade her from trying to discover the stone's value before selling it to him. The ease with which the knowledgeable party may divert or prevent the other's discovery of the truth, in short, explains some outcomes that otherwise seem hopelessly divergent. Like the significance properly ascribed to a party's carelessness, this factor seems to guide judicial decisions in a highly fact and context-specific manner.

Even when one party does nothing to dissuade the other from discovering the truth, the nondisclosure of certain types of information in some relationships is not privileged. Agents, as fiduciaries, may not profit secretly from transactions connected to matters undertaken on behalf of the principal.81 However, the "secret profit" rule may also operate in some relationships that are not characterized as fiduciary.

To illustrate this point, consider the relationship between franchisor and franchisee. Suppose a franchise agreement requires the franchisee to purchase supplies from vendors designated by the franchisor, and further suppose that the vendors pay the franchisor for the designation. Case law that disapproves of the franchisor's secret profit at its franchisees' expense82 implicitly recognizes that vendors are likely to recoup commissions paid to the franchisor through higher prices charged to franchisees. Franchisees who are ignorant of the vendor payments may, in turn, unwittingly overpay for the franchise itself.

Prospective franchisees, to be sure, are free to inquire about the franchisor's relationships with designated vendors. Whether the "secret profit" rule should protect prospective franchisees who fail to inquire, or who buy a franchise from a franchisor who declines to answer the question, requires an assumption about the relative level of sophistication or credulity common among prospective franchisees. That many franchisors refuse to negotiate the terms of the

81. See Restatement (Second) of Agency § 388 (1958) (creating a duty to pass profits to the principal that were received from transactions conducted by the agent on the principal's behalf). But see Restatement (Third) of the Law Governing Lawyers § 111(1) & cmt. c (Tentative Draft No. 3, 1990) (permitting a lawyer to use confidential client information in market transaction for lawyer's own enrichment, unless prejudice to client is reasonably likely to occur, or client forbids such usage).

82. See Bain v. Champlin Petroleum Co., 692 F.2d 43, 47 (8th Cir. 1982) (finding for the franchisor due, in part, to franchisees' awareness of franchisor's pricing policy).
franchise contract and seem to "prefer to enroll a franchisee with no experience." Illustrates the wisdom of a firm mandate that the franchisor disclose payments received from designated vendors. Moreover, the franchise contract contemplates an ongoing relationship of advantage to both franchisor and franchisee. Looking ahead to the relationship, and once in it, the franchisee may well expect at least to be told when the franchisor derives a benefit through its contractual control over the franchisee's business, a benefit derived through transactions likely to result in additional costs passed through to the franchisee.

B. Mistakes Involving Goods and Property Undermined by Termites or Fill Dirt

Sellers systematically appear obliged to disclose information that, in the obverse situation, a buyer would be free to withhold. Consider the general distinctions drawn by U.C.C. Article Two, applicable to sales of goods. If a seller who is a merchant in certain types of goods knows that particular goods are not merchantable, the seller breaches an implied warranty by selling them, unless the sale occurs on terms—like an "as is" sale—that unequivocally warn the buyer to investigate or bear the risk of nonmerchantability. Many remedies, usually including rescission, become available to the buyer as a consequence of the seller's breach of warranty. Indeed, an unknowing seller of goods that are not merchantable would breach the implied warranty as well.

In contrast, Article Two does not place warranty obligations on buyers. A prospective buyer need not share with the seller information

83. See Gillian K. Hadfield, Problematic Relations: Franchising and the Law of Incomplete Contracts, 42 Stan. L. Rev. 927, 951 (1990) (describing franchisor's refusal to negotiate as a "hallmark of the relationship that the franchisee is purchasing").
84. Id. at 962 (quoting Senate Select Comm. on Business, 92d Cong., 1st Sess. 125, Report Prepared for the Small Business Administration: The Economic Effects of Franchising (Comm. Print 1971) (written by Urban B. Ozame & Shelby D. Hunt)).
86. Id. § 2-316(3)(a).
87. Id. § 2-711. Once the buyer accepts the goods, unless the buyer justifiably revokes acceptance under § 2-608, the buyer's principal remedy will be damages for breach of warranty. See id. § 2-714.
that enhances the value of the goods involved in the transaction.\(^8\) Why this systematic divergence? Article Two, like many common law cases, may reflect a generally-shared aversion to a particular type of loss: the discovery, after the deal is closed, that we have bought a house infested with termites or a car lacking an engine. This type of loss, in turn, may be perceived as less palatable than a lost opportunity for gain or profit. We would regret, that is, selling

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88. In a transaction governed by U.C.C. Article Two, would the dictum in Wood be applicable? That is, would a merchant buyer be free to buy from a nonmerchant seller, knowing the seller to be mistaken? Section 1-103 makes applicable "the principles of law and equity" unless particular provisions in the Code displace them. U.C.C. § 1-103 (1990). Within Article Two’s own framework, § 2-302 authorizes the court to grant relief when it finds a contract or any clause in the contract to have been unconscionable at the time it was made. Id. § 2-302. The underlying principle is "one of the prevention of oppression and unfair surprise . . . and not of disturbance of allocation of risks because of superior bargaining power." Id. § 2-302 cmt. 1. If the nonmerchant seller fails to persuade the court that the transaction was unconscionable, general contract law—as embodied in the Restatement (Second) of Contracts—would enable the seller to avoid the transaction if the buyer knew or had reason to know of an error going to a basic assumption on which the contract was made. Restatement (Second) of Contracts § 153 (1981).

Professor Palmer's comprehensive treatise, however, identifies a number of cases in which courts have granted rescission when one party knew of the other's error, and the party seeking relief seemed incapable of establishing unconscionability. See 2 Palmer, supra note 16, § 12.3. See, e.g., Ruffner v. Ridley, 81 Ky. 165 (1883) (involving plaintiff's belief that land sold by defendant included 626 acres; in fact, as defendant knew, land included 100 fewer acres). For Palmer's discussion of Ruffner, see 2 Palmer, supra note 16, § 12.3, at 554 n.12. In such cases, Professor Palmer observes, the defendant's conduct "stands condemned as unfair dealing." 2 id. at 553.

As it happens, the U.C.C. provides that every contract or duty within its ambit "imposes an obligation of good faith in its performance or enforcement." U.C.C. § 1-203 (1990). Within Article Two, a merchant's "good faith" is defined by § 2-103 to mean "honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade." Id. § 2-103. Does a merchant's obligation of "fair dealing" extend back in time to conduct associated with contract formation? Or is it limited as the treatment of good faith in § 1-203 suggests, to post-formation conduct involving questions of performance and enforcement under the contract? One might argue that a merchant's obligation of fair dealing is contravened by attempts to enforce—or to resist the rescission of—a contract with a nonmerchant whom the merchant knows or should know to be seriously mistaken. One major qualification to this argument stems from the reference in § 2-103 to "standards of fair dealing in the trade." Id. (emphasis added). Merchant buyers in some trades, like antiques and fine art, who buy from nonmerchant sellers, are not conventionally believed to be under a duty to share their better-informed assessment of the object. Perhaps, in such markets—unlike markets in standardized commodities—all attributions and assessments are understood to be potentially vulnerable to disproof. See supra text accompanying note 71.
grandpa’s violin only to learn later that the buyer recognized it to be a Stradivarius, or selling the farm to learn later of the minerals beneath its surface; but, dollar for dollar of loss, our resentment would be less than in the termite scenario. 89

In sales of real property, though, the seller’s obligation of disclosure is less categorical than it is sometimes stated to be. Suppose that the seller knows that beneath the land’s surface is fill dirt (“disturbed earth” appears to be a trade euphemism) that will, in time, cause severe settling in structures built on the surface above it. The opinion in W.R. Grace strongly suggests that this type of material information must be disclosed because the information has likely been acquired by the seller without substantial investment—indeed with no additional investment if the seller placed the fill in the process of developing the property—while the buyer would, at best, find the information only after incurring costs.

A nicely-matched brace of fill dirt cases from North Carolina, however, illustrate that courts in fact consider a more complex set of factors in evaluating the seller’s failure to disclose. In Brooks v. Ervin Construction Co., 90 the North Carolina Supreme Court held that the vendor committed fraud when it failed to disclose to the purchasers of a house constructed by the vendor the fact that fill dirt lurked beneath the surface. 91 Precisely the opposite outcome was reached by the court of appeals in C.F.R. Foods, Inc. v. Randolph Development

89. This systematic divergence invades the sphere of public matters as well. Writing extrajudicially, Judge Friendly observed that there is “a distinction between cases in which government is seeking to take action against the citizen from those in which it is simply denying a citizen’s request... And whatever the mathematics, there is a human difference between losing what one has and not getting what one wants.” Henry J. Friendly, Some Kind of Hearing, 123 U. Pa. L. Rev. 1267, 1295-96 (1975). In Goldberg v. Kelly, 397 U.S. 254 (1970), the Court held that the due process clause of the Constitution entitled recipients of public assistance to a hearing when termination of their benefits is threatened. Cf. Walters v. National Ass’n of Radiation Survivors, 473 U.S. 305, 320 n.8 (1985) (noting that the Court has never held that applicants for benefits have hearing rights mandated by procedural due process).

90. 116 S.E.2d 454 (N.C. 1960).

91. Note that the buyer’s remedy does not turn on whether, or to what extent, the contract has been performed. In Brooks, the buyers sued almost four years after purchasing their house, which in the interim experienced substantial settling. Id. at 456-57. But cf. Andrew Kull, Mistake, Frustration, and the Windfall Principle of Contract Remedies, 43 Hastings L.J. 1, 12-17 (1991) (noting that under the traditional common law approach, courts generally would not permit rescission in mutual mistake cases if there had been partial performance of the contract).
in which the vendor, who was also the property’s developer, sold a commercial plot without disclosing the existence of subsurface fill to the purchaser, who constructed a restaurant on the property.93

Why was the vendor’s failure to disclose fraudulent in one case but not the other? In C.F.R. Foods, the court’s opinion emphasizes the commercial nature of the transaction. Even more emphatically, C.F.R. Foods analyzes whether the buyer’s reliance on the seller’s nondisclosure was reasonable, a question not addressed in Brooks. The seller in C.F.R. Foods provided the buyer, on request, with a topographical map specifically indicating some use of fill. The buyer, rather than investigating further, “chose to rely upon the mere appearance of the land, which it alleges appeared ‘ready-to-build.’”94 Brooks, in contrast, explains that the seller must disclose to the buyer “material facts . . . accessible to the vendor only, [if] he knows them not to be within the reach of the diligent attention, observation and judgment of the purchaser . . . .”95 The sad fact of the fill dirt is not, strictly speaking, knowable only to the seller; for one thing, the purchaser could always ask.

Diligence and reasonableness, of course, may well demand more from purchasers of commercial property than they do from purchasers of residences. A purchaser of commercial property typically anticipates an economic benefit to be achieved either by operating a business out of the property, or by leasing the property to tenants. If we anticipate that such purchasers analyze the prospect of economic benefit before making the purchase, we may well expect the analysis to encompass characteristics of the property. Purchasers of residences, in contrast, anticipate personal consumption value and, sometimes, potential resale value. We may believe that their decisions are systematically more apt to be driven by idiosyncrasy and impulse than by research, analysis and reflection. Additionally, C.F.R. Foods illustrates that the purchaser who has a clue to investigate further is not always entitled to the vendor’s explicit disclosure.

The prospect that the purchaser could always ask the vendor leads inexorably to the prospect that the vendor could always lie in

94. Id. at 389.
95. Brooks, 116 S.E.2d at 457.
response. As it happens, a third fill dirt case from North Carolina, *Libby Hill Seafood Restaurants, Inc. v. Owens*,
features this scenario. In *Libby Hill*, the vendor represented that the property was a fit location for a restaurant. The court held that even if those representations embraced facts beyond the vendor’s mere opinions, the purchaser failed to show reasonable reliance. If the purchaser is “on an equal footing with the vendor and has equal means of knowing the truth,” the purchaser is contributorily negligent if he relies on the vendor’s statement about the property’s physical condition. In short, at least in North Carolina, the vendor’s failure to disclose is not culpable when a commercial purchaser is careless (as in *C.F.R. Foods*) or gullible (as in *Libby Hill*).
Indeed, even if the seller’s misrepresentation is made unknowingly and not negligently, if the buyer seeks to rescind, the buyer must show that he justifiably relied on the representation in deciding to make the contract.

C. Mistakes About Identity

Parties to business transactions sometimes wish their identity to be unknown to the other party; such a party would typically deal through an agent as the agent’s undisclosed principal. Only rarely


97. *Id.* at 569.

98. *Id.* In contrast, the Restatement (Second) of Torts explicitly rejects the proposition that a victim’s contributory negligence should bar recovery by one who justifiably relies upon a fraudulent misrepresentation. RESTATEMENT (SECOND) OF TORTS § 545A (1977). The “justifiable reliance” standard is specific to the particular plaintiff. *Id.* § 545A cmt. b. A leading commentator treats it as more exacting than the “reasonable reliance” standard. See Robert G. Byrd, *Misrepresentation in North Carolina*, 70 N.C. L. Rev. 323, 332-33 (1992).

99. In contrast, the defense of contributory negligence is inapplicable to actions brought under the state statute prohibiting unfair and deceptive trade practices. See Winston Realty Co. v. C.H.G. Inc., 331 S.E.2d 677, 681 (N.C. 1985) (interpreting N.C. Gen. Stat. § 75-1.1 (1988)). If the defendant knows the adverse information regarding the property’s condition and actively engages in efforts to prevent the purchaser from learning the information, the defendant’s conduct on its face is unfair or deceptive within the statutory meaning, even if the purchaser’s failure to inspect constituted contributory negligence. See Robertson v. Boyd, 363 S.E.2d 672, 676 (N.C. Ct. App. 1988) (holding that although plaintiff was aware of indicia of termite damage due to a written termite report furnished by defendant, the report, while it recommended further inspection, understated the extent of termite damage). See Byrd, supra note 98 (providing a careful and comprehensive study of misrepresentation cases).

100. See Norton v. Poplos, 443 A.2d 1, 6 (Del. 1982).
is the undisclosed principal’s identity so significant that its subsequent revelation would enable the other party to assert a claim of fraud or avoid the transaction. Even if the agent, upon inquiry, lies about the undisclosed principal’s involvement, the principal’s identity may not always be material. This confluence of agency principles with contract law seems curious or anomalous to some observers. A contract, as a basis for imposing legal obligations, is often said to be the product of voluntary agreement, of assent to be bound. The presence of the undisclosed principal seems to impose a legally consequential relationship without assent to having such a relationship with the particular person who is the principal. Indeed, agency law tends to presuppose that most people don’t care; they bargain over price and performance terms but rarely ask if someone represents another person in the transaction.

Purchasers most often conceal their identities when they fear that, if the seller knew the would-be buyer’s identity, the seller would demand a higher price, a phenomenon well-known in real estate transactions. Some buyers may be known to be so wealthy or so desperate that a rational seller will raise her price. Texas Gulf Sulphur, for example, would have been acting prudently to buy the farmland adjacent to a visible drilling site through an agent as an undisclosed principal. In such cases, the buyer and its agent know information (the buyer’s identity) that is clearly price-sensitive and that the seller may have difficulty discovering independently. On the other hand, it will be difficult for the seller to credibly establish after the fact just how much more she would have demanded had she known the buyer’s identity at the time of the transaction. Even if the seller can establish that she would have demanded a higher price had she known the buyer’s identity, the seller seems merely to be

101. See, e.g., Kelly Asphalt Block Co. v. Barber Asphalt Paving Co., 105 N.E. 88, 90 (N.Y. 1914) (stating that court would consider the materiality of the agent’s misrepresentation prior to granting rescission).


103. Id. at 1990-91. Even if the seller has previously refused to deal with the particular buyer on any terms, if the seller fails to ask the agent whether he is buying on behalf of anyone else, has the buyer assumed the risk that the agent is in fact acting for the previously rebuffed buyer? Professor Barnett argues that if the seller’s contract with the agent makes the contract freely assignable to anyone, the assignment provision is a basis for concluding that the seller assumed the risk of selling through an agent acting for the disfavored buyer. See id. at 1991.
in the same position as any seller who regrets, after selling property, her ignorance of its resale potential.\textsuperscript{104}

The analysis is more complicated if the parties are reversed. Suppose that a buyer can establish that she would never, on any terms, deal with a particular seller, an intransigence grounded perhaps in prior unhappy dealings. If the seller nonetheless, acting as an undisclosed principal through an agent, obtains an agreement to sell to the buyer, what consequences should follow if the seller performs? If the transaction can be unwound, as a practical matter it seems easy to permit the buyer to avoid the transaction, subject to returning the goods or property to the seller. However, the buyer may decline to do so and take the position that the seller has behaved so officiously that the buyer should be able to retain the benefit of the seller's performance without paying for it.\textsuperscript{105} The buyer could concede that she has been enriched through the seller's performance; indeed, perhaps the buyer received goods that conformed perfectly to the terms of the sales agreement. Nevertheless, the buyer might argue that the enrichment was not unjust because the seller's devious conduct compelled the buyer to deal with someone with whom she demonstrably desired not to deal at all. According to Professor Palmer, the resolution "is by no means certain under present law."\textsuperscript{106} One practical answer that vitiates the impact of this theoretical impasse is heightened judicial skepticism to claims of mistake that, if believed, would lead to unbargained-for enrichment of the party claiming to have been mistaken.

The impasse, however infrequently it may occur, is serious. Although the buyer has been tricked into dealing with an unacceptable seller, the buyer is also seeking an unbargained-for benefit. In short, the opportunistic buyer has met the officious seller.\textsuperscript{107} If the court

\textsuperscript{104} See \textit{id.} at 1992.

\textsuperscript{105} See \textit{Restatement of Restitution} § 2 (1937). The accompanying comment defines "officiousness" as "interference in the affairs of others not justified by the circumstances under which the interference takes place." \textit{Id.} § 2 cmt. a.

\textsuperscript{106} 2 Palmer, \textit{supra} note 16, § 12.9, at 611.

\textsuperscript{107} Cases exist, of course, in which the opportunistic seller has met the opportunistic buyer, each supposing the other to be subject to a different mistake. In Taylor v. Johnson, 151 C.L.R. 422 (Austl. 1983), a leading Australian case, the seller of real estate believed that the buyer was mistaken about the property's zoning. The buyer purchased in the belief that the seller was mistaken about the purchase price. Specifically, the buyer believed the seller thought the contract stated a price per acre, but in fact the contract stated a price \textit{in toto} for the parcel. The buyer, but not the seller, correctly believed the other party to be mistaken. The
requires the buyer to pay for the goods, it enforces terms of a contract otherwise demonstrably acceptable to the buyer. The buyer who truly cares intensely about the seller's identity could easily confirm it. Perhaps we should systematically be skeptical of claims of mistaken identity asserted by parties who failed to inquire.

IV. ILL-ADVISED TRANSACTIONS

Some transactions are mistaken because, from the very start, their terms are highly disadvantageous to one party and comparably advantageous to the other. Statutory regulation aside, parties are generally free to take advantage of others' foolishness. This freedom is not unbounded, as two very different Delaware cases illustrate.

The doctrine of unconscionability, as applied in 1992 by the court of chancery in Ryan v. Weiner, limits a party's ability to exploit another's evident foolishness. In Ryan, Mr. Ryan sought cancellation of a deed to his house that he gave in 1984 to Mr. Weiner. Prior to the transaction, Mr. Ryan had fallen $1,000 into arrears in making mortgage payments on his house. At the time, the house had a fair market value of $19,800, less $8,000 that remained owing on the mortgage. The mortgage lender foreclosed and obtained a default judgment for the amount still owing.

Enter Mr. Weiner, a licensed real estate broker theretofore unknown to Ryan. Indeed, literally enter Weiner, who arrived at Ryan's house unannounced about a month before the sheriff's sale was scheduled for the house. Thereafter, Ryan and Weiner agreed to a transaction, the terms of which were disputed at trial. Ryan claimed Weiner offered to lend him cash to make up the mortgage arrears, the loan to be secured by a deed on the property. Weiner claimed he offered to buy the house and rent it to Ryan. The

court permitted the seller to rescind the sale on the basis that the buyer deliberately took steps to ensure that the seller would not learn of her error. In particular, the buyer hastened the seller's execution of the transaction. Id. at 427-28. Oddly enough, each party's belief that the other was mistaken gave both parties incentives to move the transaction rapidly to closure.

109. Id. at 1378.
110. Id.
111. Id.
112. Ryan, 610 A.2d at 1378.
113. Id.
114. Id. at 1378-79.
115. Id. at 1379.
documents supported Weiner's claim. The next day, Weiner drove Ryan to the office of a lawyer who regularly represented Weiner, and Ryan signed several documents without reading them. The lawyer did not speak to Ryan or explain the documents to him.

At trial, Ryan claimed he trusted Weiner's statements that the documents were loan documents. They were not. Ryan signed a deed transferring ownership of the house to Weiner and a settlement sheet. Ryan received no cash from Weiner, who made payments to the mortgagee to bring the loan current. Ryan, however, remained liable to pay off the balance of the mortgage loan. He continued to live in the house and to make monthly payments to Weiner. Ryan, over seven years, paid Weiner $21,480, while Weiner paid $12,149.27 for the mortgage, taxes, insurance, water, and sewer charges. By May 1991, Ryan reached the conclusion that his payments to Weiner exceeded the balance of the mortgage loan. He stopped making payments. Weiner, in turn, attempted to evict Ryan, a proceeding stayed by the court of chancery.

To an unusual degree, judicial opinions in cases like Ryan v. Weiner personalize the parties. We learn things about the parties and their relationship beyond the simple fact of the transaction and its formal terms. Mr. Ryan, a widower, had a ninth grade education and was an active alcoholic at the time he deeded his house to Weiner. Ryan was retired from the work force at the time, having worked as a laborer. Although Ryan and Weiner were, prior to the transaction, strangers, the court's opinion does not address whether Weiner, in fact, knew any of Ryan's circumstances.

One element in the court's analysis of Ryan's predicament is the unconscionability of his transaction with Weiner. The court's opinion quotes Justice Story's early exposition of the doctrine of

116. Ryan, 610 A.2d at 1379.
117. Id.
118. Id.
119. Id.
120. Ryan, 610 A.2d at 1379.
121. Id.
122. Id.
123. Id. at 1379-80.
124. Ryan, 610 A.2d at 1380.
125. Id.
126. Id.
127. Id. at 1378.
128. Ryan, 610 A.2d at 1378.
unconscionability in the United States. Story wrote that there exist some

bargains of such an unconscionable nature, and of such
gross inequality, as naturally lead to the presumption of
fraud, imposition, or undue influence. . . . [T]here may be
such unconscionableness or inadequacy in a bargain, as to
demonstrate some gross imposition or undue influence; and
in such cases, Courts of Equity ought to interfere, upon
the satisfactory ground of fraud. But then such unconscio-
bleness or such inadequacy should be made out, as would,
to use an expressive phrase, shock the conscience, and
amount in itself to conclusive and decisive evidence of fraud.
And where there are other ingredients in the case of a
suspicious nature, or peculiar relations between the parties,
gross inadequacy of price must necessarily furnish the most
vehement presumption of fraud.¹²⁹

In Ryan, the court found that, in financial effect, the transaction
resembled a gift,¹³⁰ surely satisfying Justice Story’s criterion of gross
inadequacy. The court made no express finding that Weiner affirma-
tively deceived Ryan, or that he indeed knew of the circumstances
that made Ryan vulnerable.¹³¹ In Ryan v. Weiner, far from having a
“peculiar relation” (to quote Justice Story’s terminology), the parties
had no relationship at all prior to the transaction.

The court permitted Ryan to avoid the transaction by canceling
the deed to Weiner and awarding Ryan the amount of money he
paid Weiner over the years, minus Weiner’s payments to the mort-
gagee and other parties on account of the house, plus interest.¹³²
Ryan, the court held, deeded his house to Weiner as the consequence
of a unilateral mistake about the nature of the transaction.¹³³ Such
a mistake, according to the court, justifies rescission (1) when it
results in a transaction with “shockingly unconscionable financial
terms,”¹³⁴ (2) when the court is able to restore the status quo ante.

¹²⁹. Id. at 1381-82 (quoting Joseph Story, Commentaries on Equity Juris-
prudence §§ 244-46 (1835)).
¹³⁰. Id. at 1385.
¹³¹. Id. at 1386.
¹³². Ryan, 610 A.2d at 1386.
¹³³. Id.
¹³⁴. Id. at 1387.
and (3) when the party seeking relief was not culpable. This third element permits, in turn, a "comparative assessment of fault" as between the unilaterally mistaken party and the party who benefitted from the transaction. Ryan, in the court's analysis, was careless but innocently mistaken. In contrast, Weiner, a "manipulative and skillful predator," sought out Ryan, initiated the transaction, and rushed Ryan into it. Weiner should have known and taken into account the circumstances that made Ryan vulnerable. At a minimum, having initiated the transaction, a party of "substantially greater knowledge, experience, and resources" who "seeks out the powerless to deal with them directly on matters of vital importance" has "some responsibility to assure, to the extent circumstances per-

135. Professors Arthur Corbin and Samuel Williston, authors of the leading treatises on contract law, differ in their treatment of this point, as they do on much else. Williston treats unilateral mistake as a basis for rescission only when the mistake occurred regardless of the mistaken party's exercise of ordinary care, and apparently even when the other party knew of the mistake. See 13 SAMUEL WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 1573, at 488-89 (Walter H. E. Jaeger ed., 3d ed. 1970). Williston's treatment of the relationship between these two ideas is not explicit. Although one "classic element" requisite to rescission is said to be the exercise of ordinary care, see id. at 489, four pages earlier a basis for rescission is said to be the other party's knowledge of the error. See id. at 486. Corbin, in contrast, envisioned contracting as a more gentlemanly pursuit. His treatise states that a unilateral mistake justifies rescission when the other party to the transaction was aware of the victim's error, even when the victim failed to exercise ordinary care that would have revealed the mistake. ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 610 (1960). The Restatement (Second) of Contracts, also in contrast to Williston's formulation, permits rescission when one party is mistaken as to a basic assumption, in two circumstances: (1) when the effect of the mistake is such that enforcement would be unconscionable, or (2) when the other party caused the mistake or had reason to know of it. See RESTATEMENT (SECOND) OF CONTRACTS § 153 (1981). The mistaken party will not be entitled to rescission, however, if he bears the risk of the mistake. Id. A party bears the risk of a mistake when the parties' agreement allocates it to him, when he is aware of his limited knowledge but treats it as sufficient when entering into the contract, or when the court so allocates the risk because it is reasonable to do so. Id. § 154. Thus, rescission is possible even when one party did not, in fact, know of the other's unilateral mistake but simply had reason to know of it. Id. § 153 cmt. e. Like the court in Ryan, the Restatement (Second) of Contracts formulation suggests that some transactions in themselves suffice to give notice either that the other party is probably mistaken, or that his circumstances are such as to make a mistake very likely. The Restatement (First) of Contracts limits relief for one party's unilateral mistake known to the other party to situations in which the mistake concerned a matter so basic that, were the mistake mutual, rescission would be warranted. See RESTATEMENT (FIRST) OF CONTRACTS § 472 cmt. b (1932).

136. Ryan, 610 A.2d at 1386.
137. Id.
mit, that they do understand the nature of the transaction proposed.\textsuperscript{138}

Several aspects of the opinion and the outcome in Ryan invite reflection. First, is the remedial posture of the case significant? Ryan sought restitution in the form of cancellation of his deed to Weiner and monetary restitution. Would the facts, and the court's analysis of Ryan's mistake, support an action for fraud? Ryan might argue that, like the lender in \textit{W.R. Grace}, he would not have proceeded with the transaction had he realized his error. Like the borrower in \textit{W.R. Grace}, Weiner took knowing advantage of the other party's error. Moreover, Ryan's failure to use ordinary care—the failure of an alcoholic individual—seems less compelling as a defense to fraud than the commercial lender's failure in \textit{W.R. Grace} to consult publically-available information likely reposing elsewhere in the same bank. The lender in \textit{W.R. Grace}, that is, made mistakes with its investors' and depositors' money; Ryan's mistake injured only his own interests. Indeed, the court's opinion may somewhat overemphasize the significance of the fact that Ryan, a sad individual, was involved in a highly personal transaction with Weiner. Continental Bank, however hapless, does not resemble Ryan.

Second, prior to contacting Ryan, Weiner presumably invested effort researching foreclosure sales. Relatively indulgent doctrines of excuse, like that applied in Ryan, may reflect the view that people ought not to be encouraged to sniff out information about others' vulnerabilities in order to exploit them. Not all information, and not all searches to gather information, have equal social value.

Finally, recall that the lender in \textit{W.R. Grace} was willing to make a nonrecourse loan for $75 million. In retrospect, this seems not to have been a clever lending decision, given the subsequent drop in natural gas prices.\textsuperscript{139} Wholly apart from the borrower's failure to disclose the destruction of collateral value, was the borrower obliged to warn the lender that the nonrecourse nature of the loan created a significant risk of nonrepaayment? Like Weiner, was W.R. Grace at least under a duty to refrain from exploiting Continental Bank's lack of acumen and prudence?

\footnotesize{\textsuperscript{138} Id. \hfill \textsuperscript{139} It is of interest that the plaintiff in \textit{W.R. Grace} was the FDIC, which substituted itself for Continental Bank after it bailed out the failed lender. \textit{W.R. Grace}, 877 F.2d at 617. See generally \textsc{Mark Singer}, \textit{Funny Money} (1985) (describing lending practices, including those of Continental Bank, in oil and gas transactions).}
A very different Delaware case, Smith v. Van Gorkom, although famous for other reasons, also illustrates legally-imposed limits on a party’s ability to take advantage of another’s evident foolishness. In Van Gorkom, the Delaware Supreme Court held that the directors of Trans Union Corporation breached their fiduciary duty of care to Trans Union’s shareholders by approving the terms of a cash-out merger in a grossly negligent manner. Of immediate interest is the fact that the individuals who owned the corporate purchaser of Trans Union remained defendants in the shareholders’ class action through completion of the trial. Although they were dismissed with prejudice as defendants pending the trial court’s decision, they later paid over half the settlement amount. One basis for the purchasers’ contribution to the settlement would be their knowledge (or suspicion) that Trans Union’s directors were proceeding with such acquiescence in the buyer’s demands for speed, or with such an evident lack of concern over the deal’s price or terms, that the directors’ conduct fell short of their fiduciary duty of care. If the purchasers knew of the directors’ breach of duty, and benefitted to the extent the purchase price was below Trans Union’s fair value, the purchasers received a benefit knowing its origins were tainted. Although Trans Union and its purchasers dealt at arm’s length, if the purchasers knew that Trans Union’s directors were not fulfilling their fiduciary duties toward their shareholders, the purchasers were not entirely free to take advantage of their superior ability to shape a deal.

Like Mr. Weiner, the purchasers of Trans Union may have recognized that they were dealing with unusually compliant sellers, or, more precisely, unusually compliant representatives of a corporate seller. The compliant representatives’ folly, unlike Mr. Ryan’s, injured interests beyond their own; namely, the interests of Trans Union’s shareholders. Such purchasers know that the bargained-for advantage they receive has resulted from a seriously flawed bargaining process. Are such purchasers, like Mr. Weiner, under a duty to

140. 488 A.2d 858 (Del. 1985).
141. Id. at 864 n.2.
143. See Restatement of Restitution § 138(2) (1937) (stating that a third person who colludes with fiduciary in committing breach of duty and who benefits thereby must make restitution to beneficiary); Restatement (Second) of Torts § 874 cmt. c (1979) (stating that a person who assists fiduciary in committing breach of trust is subject to tort liability for harm caused).
assure, to the extent circumstances permit, that the seller’s directors realize the extent of their own folly? Such advice may go unheeded by truly headstrong and foolish directors. Moreover, the advice is not likely to reach the seller’s shareholders. If the purchasers proceed with the transaction, they do so possessing knowledge that warrants disgorgement of a benefit obtained under unjust circumstances. Otherwise, in the absence of a duty to disgorge a benefit obtained under such circumstances, prospective purchasers might have an incentive to formulate search strategies to emphasize the detection of prospectively negligent directors, over the detection of undervalued assets.

V. Conclusion

Difficult cases involving claims of mistake, claims that a failure to disclose information was wrongful, invite close judicial scrutiny of the factual context in which the mistake occurred. Many inquiries may be relevant. To what extent is the knowledgeable party’s gain the product of opportunism that results in an unbargained-for benefit at the expense of the other party? To what extent is the gain the product of the ignorant party’s knowing assumption of the risk of error? Less generally, the knowledgeable party’s failure to disclose is more likely to be wrongful if secrecy seems conducive to socially disfavored behavior, and if the knowledge seems a matter of factual certainty rather than a matter ultimately of expert opinion. The significance to be given to carelessness or gullibility on the part of the ignorant party seems to vary greatly with the context. Difficult mistake cases, all things considered, are not well served by sharp-edged doctrine and theory. Looser-fitting doctrine, which facilitates judicial sensitivity to context, to the flavor of the transaction and the parties’ relationship, is much preferable.