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Contract Law's Transferability Bias

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When A makes a contract with B, it comes as no surprise that she is liable to B. If B can transfer her contractual rights to C, A is now liable to C. Parties in A's position often have strong reasons to avoid being liable to suit by C. Contract law, however, seems determined to minimize and override these concerns. Under current doctrine on the assignment of contractual rights—the focus of this Article—the law often imposes its own preference for transferability on the parties. The law generally assumes that contractual rights are assignable, construes exceptions to that general rule narrowly, and renders it either impossible or extremely difficult for the parties to make rights nonassignable by agreement. After examining the range of techniques courts and legislators use to promote the transferability of contractual rights, the Article contends that these practices cannot be squared with contract law's basic principles. The law's pro-transferability policy appears to be based on an intuitive but dubious economic theory, which in turn is premised on an inaccurate vision of contracts as impersonal exchanges. The Article proposes reforms to make this aspect of contract law more faithful to the relationships it regulates and supports.

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INTRODUCTION

Should contractual rights be transferable? It depends. Rights holders generally prefer to have the option to transfer their rights, whereas those subject to duties often have reasons to prefer rights to be nontransferable. If transferability were treated as an ordinary contract issue, the law would not exhibit a preference either for or against it. Contractual rights would be transferable where the parties agreed to make them transferable; likewise, they would be nontransferable where the parties agreed to make them nontransferable, unless there was some special reason to doubt that the term was the product of genuine agreement. Where the parties had not made an express provision either way, courts would apply a default rule crafted to maximize the joint value of the contract; the content of the rule would depend, for the most part, on whether transferability or non-transferability would maximize the parties' joint value.

But that is not contemporary contract law's approach. Instead, the law of assignment—the body of doctrine mostly responsible for governing transfers of contractual rights—is biased towards transferability. Consider these examples:

(i) "Grudge Assignee": Oliver hires Andrea to replace the floors in Oliver's home. The contract says nothing about whether Andrea's rights are assignable. After Andrea does the work, Oliver gets into financial difficulty and asks for more time to pay the debt. Tatiana, Oliver's neighbor, has held a long-standing grudge against Oliver and sees the chance to drive him into bankruptcy. She pays Andrea to assign the debt to her. In return, Tatiana agrees to transfer the proceeds of any successful legal action to Andrea; Tatiana's interest in suing Oliver is purely spiteful. A court is likely to allow Tatiana's suit against Oliver to proceed: contractual rights are generally assignable in the absence of agreement to the contrary and there is no exception for malicious transferees (or "assignees").[1]

(ii) "Disputatious Developer": Ophelia Corp. is a construction company. It agrees to build an apartment block for Andrew, a property developer. Construction contracts are notoriously prone to disputes, so Ophelia Corp. wants to deal only with Andrew, with whom Ophelia has a long-term relationship. At Ophelia's insistence, the written contract contains nonassignment clauses. The contract states: "This contract is not assignable." For good measure, the contract also says that Andrew "shall not assign his rights under the contract." Later, however, Andrew suffers from a cash-flow problem, and so he purports to sell his contractual rights to Donald, a developer with a terrible reputation for litigiousness. A court is likely to recognize the assignment and to allow Donald to sue Ophelia in the event of a contractual dispute. Despite the

1. *See infra* Section II.A..

apparently plain language of the clauses, most courts will construe them to preserve rather than deny the power to assign.[2]

(iii) "Interloping Bank": Oscar's Bakery needs flour, so it enters into a year-long flour supply contract with Acme Flour Corp. Oscar wants to ensure that it is only obligated to Acme because assignment increases the risk of paying the wrong creditor due to administrative error. At the time of the contract, Acme does not see any particular reason it would want to transfer its rights to someone else, so Acme happily agrees to a contractual clause stating: "The parties hereby agree that any attempt by Acme to assign its rights under this contract is totally and absolutely invalid, void, and of no effect." Nevertheless, Acme later purports to assign its rights to payment under the contract to Terrestrial Bank as part of a refinancing transaction. Under Article 9 of the Uniform Commercial Code (U.C.C.), the nonassignment clause is void and Acme is liable to suit by Terrestrial Bank.[3]

In each of these cases, the defendant may object that she did not expect this plaintiff, a stranger to the contract, to be able to sue her. She may say that she would never have dreamed of entering into a contract with this person (as in "Grudge Assignee"). She may complain that she sought to protect herself from exactly this contingency by negotiating a clause prohibiting it (as in "Disputatious Developer" and "Interloping Bank"). In each of the examples, however, the court is likely to reject these arguments and allow the suit to proceed. Contractual rights are generally assignable, subject only to narrow exceptions (such as in "Grudge Assignee"). Attempts to make them nonassignable will often be interpreted not to have this effect (as in "Disputatious Developer") unless the parties use a special form of words. Even where the parties choose the "magic words" that would be interpreted so as to render the assignment void (as in "Interloping Bank"), a court will often be required to disregard this aspect of the parties' agreement because of Article 9's mandatory assignability rule.

These examples illustrate what courts say explicitly: "the law looks 'with favor on the free assignability of rights and frowns on restrictions that would limit or preclude assignability.'"[4] In this regard, the law treats contractual rights quite differently from contractual duties. Contractual duties may sometimes be *delegated* to, and vicariously performed by, someone else. But even then, unless the parties have expressly agreed otherwise, the original promisor remains subject to the duty she undertook and will be liable if it is not performed.[5] For obvious reasons—trustworthiness, competence, creditworthiness—the law recognizes that the identity of the person subject to a contractual duty and amenable to suit for breach is typically crucial. But the law has a general tendency to treat the identity of a contractual

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2. *See infra* Section II.C.

3. *See infra* Section II.D.

4. Easton Bus. Opportunities, Inc. v. Town Exec. Suites—E. Marketplace, L.L.C., 230 P.3d 827, 830 (Nev. 2010) (quoting 9 JOHN E. MURRAY, JR., CORBIN ON CONTRACTS § 49.9, at 214 (rev. ed. 2007)); *see also* Wykeham Rise, L.L.C. v. Federer, 52 A.3d 702, 717 (Conn. 2012) ("Assignability of rights is clearly favored with respect to contracts generally.").

5. RESTATEMENT (SECOND) OF CONTRACTS § 318(3) (AM. LAW INST. 1981) ("Unless the obligee agrees otherwise, neither delegation of performance nor a contract to assume the duty made with the obligor by the person delegated discharges any duty or liability of the delegating obligor.").

rightholder as insignificant. In this regard, contract law has come a long way since medieval common law, which held that contractual rights were, by their nature, personal to the parties and hence nontransferable.[6] A detailed examination of the law shows that contemporary contract law tends to hold that rights should be transferable, regardless of party intention.

Contract law's bias in favor of transferability, then, is not based on freedom of contract: indeed, it runs counter to contemporary contract law's general principle of party autonomy. If not freedom of contract, what explains the law's move to a pro-transferability policy? The shift to alienability appears to be a symptom of broader currents in economic thought.[7] Scholars of economic history have analyzed capitalism's "tendency to detach economic action from social context[]."[8] For Max Weber, the transferability of contractual rights is part of "that legal state of affairs which is required by advanced and completely commercial social intercourse" and "indispensable for a modern capitalistic society."[9] Echoing Weber, John R. Commons claimed that "modern capitalism begins with the assignment and negotiability of contracts."[10] The transferability of contractual rights is generally thought of as an essential component of the prevailing economic regime. In particular, permitting transferability allows the transferor to use its contractual rights as collateral and hence serves the transferor's interest by increasing its ability to access credit. According to a leading contracts treatise, if most contract rights were not assignable, our modern credit economy could not exist.[11] The policy is felt most strongly in the case of debts—that is, contractual obligations to pay agreed sums of money.[12] Contemporary market economies have long reached the stage where debt is conceptualized as a kind of asset.[13] The commodification of debt is a centuries-old process, but it has reached new heights in recent years with the intense financialization of modern economies.[14] Nor is the process limited to debts: other kinds of rights to sue for breach are also treated as marketable commodities.[15]

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6. *See* W.S. Holdsworth, *The History of the Treatment of Choses in Action by the Common Law*, 33 HARV. L. REV. 997, 1003 (1920) ("[T]he common lawyers saw as clearly as the Roman lawyers that such rights of action were personal matters between these two persons.").

7. *See, e.g.*, Sprint Commc'ns Co., L.P. v. APCC Servs., Inc., 554 U.S. 269, 276 (2008) ("[A]s English commerce and trade expanded, courts began to liberalize the rules that prevented assignments of choses in action.").

8. JÜRGEN KOCKA, CAPITALISM: A SHORT HISTORY 114 (2016).

9. 2 MAX WEBER, ECONOMY AND SOCIETY: AN OUTLINE OF INTERPRETIVE SOCIOLOGY 681–82 (Guenther Roth & Claus Wittich eds., 1978).

10. JOHN R. COMMONS, LEGAL FOUNDATIONS OF CAPITALISM 253 (1924).

11. 3 E. ALLAN FARNSWORTH, FARNSWORTH ON CONTRACTS § 11.2 (3d ed. 2004).

12. *See* 1 HENRY DUNNING MACLEOD, THE PRINCIPLES OF ECONOMICAL PHILOSOPHY 481 (2d ed. 1872) ("If it were asked—Who made the discovery which has most deeply affected the fortunes of the human race? We think, after full consideration, we might safely answer—The man who first discovered that a Debt is a Saleable Commodity.").

13. *See generally* Teemu Juutilainen, *Law-Based Commodification of Private Debt*, 22 EUR. L.J. 743 (2017).

14. *See* George M. Cohen, *The Financial Crisis and the Forgotten Law of Contracts*, 87 TUL. L. REV. 1, 10–16 (2012).

15. *See* Sprint Commc'ns Co., L.P. v. APCC Servs., Inc., 554 U.S. 269, 302 (2008)

Although making contractual promises transferable might be regarded by some as a symptom of moral decline,[16] this Article does not seek to mount a general critique of the transferability of contractual rights. Rather, it contends that courts and legislatures have overestimated the arguments for transferability. While the economic arguments to allow parties to *opt in* to assignability are powerful, the economic arguments for *forcing* assignability upon them appear to be weak. The law's pro-assignability policy seems to be based either on circular conceptual arguments that contractual rights are a form of property and must therefore be transferable, or on simplistic instrumental arguments that predate the emergence of sophisticated economic analysis of law. Grant Gilmore, a leading supporter of the policy, admitted that his belief in it was "instinctive and irrational, not logical and reasoned."[17] This Article contends that none of the available arguments is sufficient to justify the law's pro-transferability bias. In particular, the social benefits of transferability are typically adequately factored into the initial contractual negotiation. If transferability serves social welfare, then we can expect parties to bargain for it or, at least, not to agree to a nonassignment clause.

Conversely, legal doctrine in its current form systematically underestimates the reasons for restricting transfers of contractual rights. Contractual exchange, even under capitalism, is very far from an impersonal affair. As the most sophisticated contract-law scholarship stresses, parties to contracts combine legally enforceable promises with nonlegal mechanisms based on trust, reciprocity, and social sanctions.[18] Legally enforceable contracts are typically embedded in a broader set of relations between the parties. It is not feasible, or even possible, to make precise, legally enforceable provisions for all contingencies. Parties often expect that, in a spirit of give-and-take, the terms of their exchange will be adjusted and renegotiated during performance. They fear, however, that the other party will exploit changed circumstances. They know they cannot rely on courts to protect the full extent of their interests, so they want the other party to be disposed towards cooperative behavior.

As a result, the identity of one's contractual counterparty is often crucial. Parties choose their business partners based on prior experience with that party, on that

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(Roberts, C.J., dissenting) (objecting to majority's decision that assignees for collection have standing to sue and stating that "[t]he right to sue is now the exact opposite of a personal claim—it is a marketable commodity.").

16. Conceivably, Seana Shiffrin's work on the divergence between promissory morality and contract law might provide the basis of a moral critique of the law's pro-transferability bias. *See* Seana Valentine Shiffrin, *The Divergence of Contract and Promise*, 120 HARV. L. REV. 708 (2007). Shiffrin herself has stated that "generally, a promise is not simply transferable" but says only that this *typically* the case. Seana Valentine Shiffrin, *Immoral, Conflicting, and Redundant Promises*, *in* REASONS AND RECOGNITION: ESSAYS ON THE PHILOSOPHY OF T.M. SCANLON 155, 164–65 (R. Jay Wallace, Rahul Kumar & Samuel Freeman eds., 2011).

17. *See* 1 GRANT GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY §7.6, at 212 (1965).

18. *See, e.g.*, Ronald J. Gilson, Charles F. Sabel & Robert E. Scott, *Braiding: The Interaction of Formal and Informal Contracting in Theory, Practice, and Doctrine*, 110 COLUM. L. REV. 1377, 1392–94 (2010).

party's reputation for trustworthy and reasonable behavior, and on that other party's need to maintain a good reputation in the marketplace. Assignment may render the duty holder liable to suit by someone with whom she has no experience and who has no reputation for trustworthiness and reasonableness. The transferee may also be free of reputational constraints that bound the transferor. The most extreme example is assignment to a "vulture fund," an entity with no incentive to be reasonable and with every incentive to play "hardball" to develop an aggressive and fearsome reputation. These considerations are essential to the way parties use contract law, and they cannot be brushed aside with assertions that disregarding them will make it easier for contractual right holders to obtain credit.[19]

The main purpose of this Article is to challenge contract law's pro-assignability policy. As things stand, the best explanation of the law's transferability bias is that it makes life easier for banks and other financial industry players, who have long had an outsized influence on the making of American secured-transactions law.[20] At the very least, the aim of the Article is to provoke other scholars to produce a more compelling justification for the policy than has previously been offered.[21] For, despite the topic's obvious importance, the literature on the contemporary American law of assignment is surprisingly slim. The assignability of tort and copyright claims has attracted recent scholarly attention,[22] and a few articles address assignability in particular contractual contexts.[23] But very few discuss the topic as a whole.[24] The

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19. *But cf.* Orkun Akseli, *Contractual Prohibitions on Assignment of Receivables*: *An English and UN Perspective*, 7 J. BUS. L. 650, 654 n.23 (2009) ("[S]ometimes debtors do not want to deal with new creditors who are not flexible in commercial relationships. However, for the sake of lowering the cost of credit the law should have a pro-assignee stand.").

20. *See* Robert E. Scott, *The Politics of Article 9*, 80 VA. L. REV. 1783, 1785 (1994) (detailing the influence of financial institutions on the drafting of U.C.C. Article 9).

21. In Section III.C below, I attempt to construct an argument in favor of the current law, based on Thomas Merrill and Henry Smith's argument for standardization in property law. *See* Thomas W. Merrill & Henry E. Smith, *Optimal Standardization in the Law of Property: The* Numerus Clausus *Principle*, 110 YALE L.J. 1 (2000).

22. On the assignability of tort claims see, for example, Michael Abramowicz, *On the Alienability of Legal Claims*, 114 YALE L.J. 697 (2005); Andrew S. Gold, *On Selling Civil Recourse*, 63 DEPAUL L. REV. 485, 486–87 (2014); Anthony J. Sebok, *The Inauthentic Claim*, 64 VAND. L. REV. 61 (2011). On the assignability of copyright claims, see Shyamkrishna Balganesh, *Copyright Infringement Markets*, 113 COLUM. L. REV. 2277 (2013).

23. *See, e.g.*, Neil B. Cohen & William H. Henning, *Freedom of Contract vs. Free Alienability: An Old Struggle Emerges in a New Context*, 46 GONZ. L. REV. 353 (2010) (explaining U.C.C. Article 9's mandatory assignment rule); Larry A. DiMatteo, *Depersonalization of Personal Service Contracts: The Search for a Modern Approach to Assignability*, 27 AKRON L. REV. 407 (1994) (discussing the assignability of rights and duties in personal services contracts); Alex M. Johnson, Jr., *Correctly Interpreting Long-Term Leases Pursuant to Modern Contract Law: Toward a Theory of Relational Leases*, 74 VA. L. REV. 751 (1988) (discussing the assignability of rights and duties under real property leases); *see also* Stephen M. McJohn, *Assignability of Letter of Credit Proceeds: Adapting the Code to New Commercial Practices*, 25 UCC L.J. 257 (1993) (discussing the assignability of rights under letters of credit in the related context of Article 5 of the U.C.C.).

24. For example, brief discussions can be found in Henry E. Smith, *Standardization in Property Law*, *in* RESEARCH HANDBOOK ON THE ECONOMICS OF PROPERTY LAW 151 (Kenneth Ayotte & Henry E. Smith, eds., 2011); Richard A. Epstein, *Why Restrain Alienation?*, 85

issue has attracted some attention among doctrinally oriented scholars of Anglo-Commonwealth commercial law in recent years,[25] but this important aspect of contract law rarely features in larger debates about the nature and purpose of the institution.[26] The few theoretical treatments of contract law to take notice of the assignability rules accept those rules as given. Thus, Curtis Bridgeman uses the law's attitude to the transferability of contractual rights to criticize interpretive theories that view contract law as a reflection of the moral obligation to keep one's promises.[27] "Allowing such transferability," Bridgeman points out, "is at the least not required by the moral obligation to keep one's promises, and in fact requiring the promisor to deliver performance to a stranger may go beyond what the morality of promising would even allow."[28] Bridgeman does not question the justifiability of the assignability rules; rather, he contends that this feature shows that contract law, as it currently stands, is less concerned with promissory morality and more with protecting "property-like" rights to performance.[29] Bridgeman is right to note a tension between certain conceptions of contract law and the assignability rules. Because his aim is to interpret rather than to evaluate contract law, however, he does not consider the possibility that the assignability rules might be rejected or changed.[30]

COLUM. L. REV. 970, 982–84 (1985); Merrill & Smith, *supra* note 21, at 54–55; J. E. Penner, *The "Bundle of Rights" Picture of Property*, 43 UCLA L. REV. 711, 802–03, 810–13 (1996). One of the few papers to discuss the topic at length is unpublished. Jared G. Kramer, When Should Contracts Be Assignable? An Economic Analysis (Aug. 15, 2004) (unpublished manuscript) (available on SSRN) (discussing reasons parties to contracts would want to make their contractual rights and obligations transferable and why they would wish to make them nontransferable). In addition, some articles address the law of assignability indirectly. *See* Kenneth Ayotte & Henry Hansmann, *Legal Entities as Transferable Bundles of Contracts*, 111 MICH. L. REV. 715, 716, 722–28 (2013) (proposing theory of "bundled assignability" as a function of legal entities); Randy E. Barnett, *Squaring Undisclosed Agency Law with Contract Theory*, 75 CALIF. L. REV. 1969, 1986–92 (1987) (comparing law of assignment to law of undisclosed agency); Carl S. Bjerre, *Project Finance, Securitization and Consensuality*, 12 DUKE J. COMP. & INT'L L. 411, 423–27 (2002) (discussing Article 9's effect on nonassignment clauses in the context of international project finance).

25. *E.g.*, GREG TOLHURST, THE ASSIGNMENT OF CONTRACTUAL RIGHTS 119–322 (2d ed. 2016) (providing the most detailed doctrinal treatment of the Anglo-Commonwealth law); s*ee also* Michael Bridge, *The Nature of Assignment and Non-Assignment Clauses*, 132 L.Q. REV. 47 (2016).

26. This may be because few scholars teach the material. The issue typically does appear in contract law casebooks, but it is often relegated to the last chapter. *See, e.g.*, IAN AYRES & GREGORY KLASS, STUDIES IN CONTRACT LAW 1159–77 (9th ed. 2017); CHARLES L. KNAPP, NATHAN M. CRYSTAL & HARRY G. PRINCE, PROBLEMS IN CONTRACT LAW: CASES AND MATERIALS 1057–88 (8th ed. 2016); ROBERT E. SCOTT & JODY S. KRAUS, CONTRACT LAW AND THEORY 961–1027 (5th ed., 2013).

27. Curtis Bridgeman, *Reconciling Strict Liability with Corrective Justice in Contract Law*, 75 FORDHAM L. REV. 3013, 3031–32 (2007).

28. *Id.*

29. *Id.* at 3032–33.

30. In another recent contribution to the literature of contract-law theory, Erik Encarnacion has similarly mentioned the possibility of assignment to build the case for a conception of contracts as "commodified promises." Erik Encarnacion, *Contract as Commodified Promise*, 71 VAND. L. REV. 61 (2018). He contends that "contracts involve, and

In Part I, this Article explores the reasons that parties to contracts might want to make contractual rights transferable or nontransferable. Part II explains the current law of assignability and its pro-transferability bias. Part III considers possible justifications for this bias and finds none of them persuasive. Part IV explores what the law would look like if freed from the policy in favor of transferability.

I. WHY (NOT) MAKE CONTRACTUAL RIGHTS TRANSFERABLE?

While contract law scholars have had little to say about transferability, lawyers who draft contracts have not been similarly reticent. Written contracts almost always make some provision about assignment.[31] Contracts sometimes make the rights they create expressly assignable at the option of the promisee (or "obligee"),[32] without the need for the promisor (or "obligor") to consent to the particular assignment.[33] For example, many contractual promises are made to the promisee and its assignees[34] or otherwise clearly contemplate transfer.[35] On the other hand, many contracts explicitly make rights nontransferable,[36] or they restrict the promisee's ability to

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should involve, treating promissory rights and obligations as subject to market norms, including norms permitting the purchase and sale of those rights and obligations." *Id.* at 64. For Encarnacion, commodification is not necessarily a bad thing, and it is a matter of degree. *Id.* at 70. On his account, transferability is only the most extreme form of commodification; even a nontransferable promise may be commodified if it was made in exchange for the payment of money by the promisee. *Id.* at 75–76. Encarnacion mentions some reasons to make promises nontransferable, but he does not explore the law's approach to assignability in any detail. *See id.* at 82–87.

31. Randall D. McLanahan, *Assignment, Delegation, and Choice of Law Provisions in Commercial Agreements*, 57 PRAC. LAW. 15, 15 (2011) ("[A]lmost every commercial agreement has something to say about the assignment of rights, the delegation of duties, or both.").

32. To be clear, this Article is concerned with transfers of contractual rights that empower a transferee to assert rights and bring lawsuits directly against the promisor. It does not deal with arrangements between a promisee and a third party that only transfer an entitlement to the proceeds of performance *after* the promisor has rendered performance to the promisee.

33. The law also allows for consensual transfers of rights via novation, whereby the parties to the contract agree to substitute a new party. RESTATEMENT (SECOND) OF CONTRACTS § 280 (AM. LAW INST. 1981). For the difference between assignment and novation see, for example, *216 Jamaica Ave., L.L.C. v. S & R Playhouse Realty Co.*, 540 F.3d 433, 437 (6th Cir. 2008).

34. *See, e.g.*, Cafferty v. Scotti Bros. Records, 969 F. Supp. 193, 198 (S.D.N.Y. 1997) (discussing a contract granting license to promisee, its licensees, and assignees).

35. *See, e.g.*, MacWilliams v. BP Prod. N. Am. Inc., No. Civ. 09-1844 RBK AMD, 2010 WL 4860629, at *1 (D.N.J. Nov. 23, 2010) (examining contracts providing that promisee "may assign its rights under the agreements").

36. *See, e.g.*, Riley v. Hewlett-Packard Co., 36 F. App'x 194, 194–95 (6th Cir. 2002) ("Unless otherwise agreed in writing by HP, Subcontractor shall not assign its rights or delegate its responsibilities under this Agreement. Any purported assignment or delegation by Subcontractor, including the attempted subcontracting of all or any portion of the work to [be] provided under this Agreement, shall be null and void."). For further examples of nonassignment clauses from the case law, see *infra* Section II.C.

transfer her rights to specified kinds of transferees or to particular circumstances.[37] What bears on this choice? And how should the law respond where the parties have made no explicit choice?

A. Reasons for Unilateral Transferability

The promisee will typically prefer to have the option of transferring her rights at a later time without getting the permission of the promisor (who, after the contract is concluded, might seek to hold the promisee to ransom). Some third party may value the right higher than the promisee does, creating the possibility of a transfer that is mutually beneficial for promisee and transferee. For example, a person holding a concert ticket might be unable to make it to the concert or might decide, after buying the ticket, that she no longer likes the performer. The ticket buyer would, in such circumstances, prefer to have the option of selling the ticket to someone else who values it more highly. To generalize: transfer may be beneficial because of post-contractual changes in circumstances or because of post-contractual realizations by the promisee that she has misjudged the value that the right to performance holds for her.

Much of the litigation on assignability, however, concerns rights to the payment of money. Money is valuable to all, so the value of performance is less likely to fluctuate due to a post-contractual change of circumstances or to be subjected to an erroneous assessment. Transfer of a money claim to a third party may nevertheless be advantageous for two main reasons: financing and debt collection.[38]

Financing provides a reason to transfer a right when the promisee needs money now, but the promisor is not yet obligated to pay. A transferee might be willing to provide cash now in exchange for the prospect of a later profit. To support a credit transaction, a contractual right can be transferred using various legal techniques. The right might be sold in its entirety to the transferee and enforced by her, as in the case of factoring or securitization.[39] In such cases, the risk of the promisor being unable to pay usually falls on the transferee, and the sale price will include a discount to reflect the transferee's risk that the promisor will default on the obligation.[40] Alternatively, the transfer might occur by way of security, whereby the transferee

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37. *See, e.g.*, Disk Authoring Techs. L.L.C. v. Corel Corp., 122 F. Supp. 3d 98, 102 (S.D.N.Y. 2015) (discussing a contract providing that either party could assign its rights without the other party's consent to a party acquiring substantially all of the assignor's assets, but otherwise restricting assignment without consent, such consent not to be unreasonably withheld).

38. When determining the value of the transferred promise, the transferee may wish to consider psychological research suggesting that the promisor is less likely to keep her promise after it has been transferred to a third party. *See* Tess Wilkinson-Ryan, *Breaching the Mortgage Contract: The Behavioral Economics of Strategic Default*, 64 VAND. L. REV. 1547, 1580 (2011) ("The research I have presented here suggests that the assignment of a contract, including securitization, may undermine the promisor's commitment to performance.").

39. *See* Steven L. Schwarcz, *The Alchemy of Asset Securitization*, 1 STAN. J.L. BUS. & FIN. 133, 144 (1994) (explaining factoring and securitization).

40. *Id.* at 135 ("The risk that these payments may not be made on time is an important factor in valuing the receivables.").

makes a loan to the promisee with the contractual right serving as collateral, as in the case of accounts receivable financing.[41] The transferee-lender can look to the contractual right for satisfaction if the borrower defaults on the loan. In that case, the transferee-lender aims to achieve a profit through interest payments by the promisee-borrower (at a rate that would be higher without the collateral).[42] Either way, the economic function of the transaction is the same: to provide the promisee with money now rather than later.[43]

The most extreme form of this motivation for assignment is a sale of a whole business or substantial parts of it.[44] It is sometimes possible to achieve the same result without transferring rights to another entity: functional ownership of a business can be changed through the sale of stock in a corporation.[45] But a sale of stock in the whole company is not an appropriate mechanism when only part of the promisee's business is being sold to a particular buyer. Moreover, the parties may prefer to sell the corporation's assets rather than its stock for tax reasons.[46] Thus, in many circumstances, the preferred way to sell a substantial part of a business's assets is by transferring contractual claims to a new entity.

Another major reason for assignment is the desire to pass the burdens of disputing and enforcement to someone else. Because they specialize in enforcement and benefit from economies of scale, debt-collection companies can make a profit by purchasing contractual rights at a price acceptable to the promisee, then recovering higher sums from the promisor.[47] Transferring a contractual right to debt collectors may also serve the promisee's reputational interests. Debt enforcement can have harsh consequences, including the debtor's bankruptcy, and others may judge that the promisee has acted too harshly.[48] Assignment may enable the promisee to escape

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41. *See* Dan T. Coenen, *Priorities in Accounts: The Crazy Quilt of Current Law and a Proposal for Reform*, 45 VAND. L. REV. 1061, 1068 (1992) (explaining accounts receivable financing).

42. *See* Thomas H. Jackson & Anthony T. Kronman, *Secured Financing and Priorities Among Creditors*, 88 YALE L.J. 1143, 1152–53 (1979) (borrowers offering collateral can secure lower interest rates).

43. *See* Lois R. Lupica, *Asset Securitization: The Unsecured Creditor's Perspective*, 76 TEX. L. REV. 595, 605 (1998) ("Firms securitize their assets for the same reason firms borrow money: to raise money for either special projects or working capital.").

44. Additional reasons for assignment include the desire to move assets from one member of a corporate group to another, either for tax avoidance or for corporate-efficiency reasons. Thus, for example, it is common for international joint venture agreements to be transferable to a subsidiary of an original party or to some other party controlled by the transferor. *See* RONALD CHARLES WOLF, THE COMPLETE GUIDE TO INTERNATIONAL JOINT VENTURES WITH SAMPLE CLAUSES AND CONTRACTS 164–65 (3d ed. 2011).

45. *See* Ayotte & Hansmann, *supra* note 24, at 723–24.

46. *Id.* at 743 n.53 (noting that stock sales and asset sales have different tax consequences).

47. *See* Kramer, *supra* note 24, at 2 (stating that businesses can often sell receivables to debt collection firms, "who because of their specialization extract more value per cost of servicing their accounts").

48. *See* Arthur Allen Leff, *Injury, Ignorance and Spite—The Dynamics of Coercive Collection*, 80 YALE L.J. 1, 35–36 (1970) (discussing the different reputational concerns of original creditors and debt collectors).

this kind of reputational cost while effectively reaping the benefit of aggressive and misleading conduct by the debt collector[49]—even though the promisee might have transferred the right to a debt collector with full knowledge that the debt collector would act in this way.[50]

B. Reasons Against Unilateral Transferability

On the other hand, the promisor would, other things being equal, typically prefer that rights against her are not transferable without her consent. The reasons are various.[51] Some stem from sheer administrative convenience. A nonassignment clause, if it is enforceable, leaves the promisor in no doubt to whom she owes her contractual obligations. Promisors who pay an assignor after having received notice of an assignment are at risk of having to pay the same debt twice.[52] While the requirement that the promisor receives notice of the assignment will generally prevent this kind of error, mistakes are inevitable.[53] In response to the possibility of assignment, promisors may need to maintain a costly bureaucratic infrastructure to keep track of whom it owes its debts to.[54] Further, the validity of a purported assignment, particularly when the assignment is governed by foreign law, may be difficult for the debtor to discern.[55] And when there are multiple assignments, the debtor may have to figure out which takes priority.[56] For these reasons, the risk of payment to the wrong party is described by one commentator—perhaps with some exaggeration—as the "main reason" for contractual provisions barring transfers of contractual rights.[57]

More generally, the identity of one's contractual counterparty may be an essential element of the deal. The point is more obvious when it comes to contractual duties,

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49. The prevalence of aggressive and misleading debt-collection practices in the industry prompted the passage of the Fair Debt Collection Practices Act, 15 U.S.C. §§ 1692–1692p (2012).

50. *See* Barb. Tr. Co. v. Bank of Zam., [2007] EWCA (Civ) 148 (Eng.) (explaining that Bank of America was apparently unwilling to sue the central bank of a developing country because of the reputational losses it would suffer in the context of widespread arguments in favor of debt forgiveness. Instead, the bank transferred its claim to a vulture fund immune from such reputational pressures); *see also supra* text accompanying notes 194–196.

51. *See* Roy Goode, *Contractual Prohibitions Against Assignment*, 2009 LLOYD'S MAR. & COM. L.Q. 300, 303–04; Gerard McCormack, *Debts and Nonassignment Clauses*, 2000 J. BUS. L. 422, 424–26.

52. *See* RESTATEMENT (SECOND) OF CONTRACTS § 338(1) (AM. LAW INST. 1981) ("[T]he assignor retains his power to discharge or modify the duty of the obligor to the extent that the obligor performs or otherwise gives value until but not after the obligor receives notification that the right has been assigned and that performance is to be rendered to the assignee.").

53. *See* Hugh Beale, Louise Gullifer & Sarah Paterson, *A Case for Interfering with Freedom of Contract? An Empirically-Informed Study of Bans on Assignment*, 2016 J. BUS. L. 203, 220.

54. *See* Kramer, *supra* note 24, at 4–5.

55. 1 GILMORE, *supra* note 17, at § 7.7.

56. *Id.*

57. LARRY A. DIMATTEO, INTERNATIONAL CONTRACTING: LAW & PRACTICE 79 (4th ed. 2016).

a matter dealt with not by the law of assignment but by the legally distinct topic of "delegation."[58] It obviously matters who owes duties under a contract.[59] What may be less obvious is that the identity of a right holder may be similarly essential.[60] Most clearly, the content of the legal obligation sometimes changes with the identity of the right holder. For example, the terms of an insurance policy typically depend on the particular characteristics of the policy holder.[61] An insurer will decide which risks it is willing to cover and how much to charge as a premium, based partly on what it knows about the policy holder and the likelihood of a claim.[62] Similarly, the content of a supplier's duty to meet a right holder's requirements could be changed radically by the substitution of a different buyer with different requirements.[63] Hence, requirements contracts often prohibit assignment, though they may make an exception for assignments whereby the transferee acquires the promisee's entire business.[64]

Promisors may also seek to make rights against them nontransferable so that they can engage in price discrimination.[65] A supplier of a good or service may wish to charge different prices for the same product, for example, because some customers

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58. RESTATEMENT (SECOND) OF CONTRACTS § 316 (AM. LAW INST. 1981) ("In this Chapter rights are said to be 'assigned'; duties are said to be 'delegated.'").

59. The original party subject to duties under the contract—say, a supplier of services—is usually selected for its various qualities, most obviously an expected level of performance. Likewise, a supplier extending credit will do so only to a creditworthy customer, or it may charge a higher price to compensate for a greater risk of default. Transferring a duty away to a less competent or less creditworthy duty holder might completely change the value of the right. For this reason, unless the parties agree otherwise, it is not possible for a contracting party to unilaterally absolve herself of a duty by transferring it to a third party. *Id.* § 318(3). It is typically permissible, however, for a promisor to satisfy her own performance obligation by nominating someone else to discharge it, *id.* § 318(1), unless the promisee has a substantial interest in performance by the promisor herself, as in the case of an author's obligation to write a book, *id.* § 318(2).

60. Though this Article claims that the law does not sufficiently recognize the significance of a right holder's identity, it does not aim to show that a right holder's identity is of such pervasive importance as the identity of a duty holder. *Cf.* Kramer, *supra* note 24, at 15 (claiming that assignments of rights and delegations of obligations are "largely symmetrical").

61. *Id.* at 54–56.

62. *Id.*

63. For an example from the case law, see *Crane Ice Cream Co. v. Terminal Freezing & Heating Co.*, 128 A. 280, 283 (Md. 1925) (smaller ice-cream manufacturer attempting to assign requirements contract to larger ice-cream manufacturer).

64. *See*, *e.g.*, Supply Agreement Number: 99xxxx, for Purchase of Production Parts and Non-Production Goods And Services Between A123 Systems, Inc. (Supplier) and Think Global AS (Think), cl. 18 (2007), https://contracts.onecle.com/a123/think-global-supply-2007-11-28.shtml [https://perma.cc/22WP-4KB8] (barring assignment of rights under a requirements contract except in connection with a merger, consolidation, reorganization or sale of all or substantially all assets).

65. Kramer, *supra* note 24, at 4; *see also* Larry E. Ribstein & Bruce H. Kobayashi, *State Regulation of Electronic Commerce*, 51 EMORY L.J. 1, 17 (2002) ("By preventing resales by original buyers [of computer software], [nonassignment] terms allow licensors to price discriminate between low-value and high-value users.").

may be willing to pay more than others.[66] If a low-paying customer can assign its rights to a high-paying customer, the assignment will serve as form of arbitrage that undermines the purpose of the price-discrimination scheme.[67] Relatedly, promisors may wish to limit a secondary market in contractual rights for moral reasons. One prominent example is the market for concert tickets.[68] These tickets are often sold at lower than market value to permit access to committed fans who could not afford the market price, and they are either nontransferable or saleable only at face value. Free assignability frustrates the promisor's purpose.

Additionally, contractual rights and duties may be effectively intertwined. Thus, if the promisee has transferred her rights to a transferee, the promisee's own incentive to perform her side of the bargain may be reduced.[69] The promisor may also wish to prevent transfer because it may have a continuing course of dealing with the promisee—in such circumstances the promisor may wish to set off cross-claims that it has against the promisee and thereby reduce or extinguish its indebtedness to the promisee. If the promisee transfers the right and the promisor is notified of the transfer, the promisor is limited in its ability to set off its cross-claims against the promisee that accrue after notification.[70] This may be crucial in the event of the promisor's insolvency. For example, the International Swaps and Derivative Association's (ISDA) 2002 Master Agreement, which governs over-the-counter derivative transactions, generally prohibits the transfer of rights arising under it prior to default.[71]

More generally, the identity of a right holder under a contract matters because contracts do not enforce themselves. As civil recourse theorists have stressed, private law confers *powers* to bring lawsuits to redress wrongdoings.[72] Contract law leaves choices about whether and when to start proceedings in the hands of the victims of alleged wrongdoings or, sometimes, in those of their transferees.[73] The person holding the power to sue can choose to exercise it at the first opportunity, or to be more lenient and attempt to reach an agreed solution in the event of an arguable breach by the duty holder. As noted above, one major reason to transfer a right is that

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66. Kramer, *supra* note 24, at 4.

67. *Id.*

68. Gregory M. Stein, *Will Ticket Scalpers Meet the Same Fate As Spinal Tap Drummers? The Sale and Resale of Concert and Sports Tickets*, 42 PEPP. L. REV. 1, 7 (2014) ("Some performers may be reluctant to be the first to raise ticket prices dramatically and thus depart from the prevalent pricing model, perhaps out of fear of being perceived as greedy.").

69. McCormack, *supra* note 51, at 425.

70. U.C.C. § 9-404 (AM. LAW INST. & UNIF. LAW COMM'N 2017).

71. Goode, *supra* note 51, at 302.

72. Nathan B. Oman, *Why There Is No Duty to Pay Damages: Powers, Duties, and Private Law*, 39 FLA. ST. U. L. REV. 137, 139 (2011) (law of contract and tort "gives plaintiffs the power to extract wealth from defendants but does not impose duties on defendants to compensate those that they have wronged"); Benjamin C. Zipursky, *Civil Recourse, Not Corrective Justice*, 91 GEO. L.J. 695, 721 (2003) ("In torts, the liability of a defendant to a plaintiff is correlative to a power of the plaintiff against the defendant.").

73. *See* Nathan B. Oman, *Consent to Retaliation: A Civil Recourse Theory of Contractual Liability*, 96 IOWA L. REV. 529 (2011).

the transferee may be more willing, or in a better position, to pursue the promisor through litigation or arbitration.[74]

On a simplistic view of the role of law in contracting, the expectation that the right holder will not rush to court at the first opportunity is just that: a factual expectation rather than a consideration relevant to legal analysis.[75] This argument, however, does not survive a collision with reality. As countless scholars of contract law have shown, it is impossible to provide at the outset for every eventuality that might arise.[76] When circumstances change or transpire differently from how the parties envisaged, the possibility of opportunism raises its head. Contract law has some tools for combating such opportunism, but it does not attempt to enforce a generalized norm of fair cooperation[77]—nor will the parties often wish for an adjudicator to try to enforce such a norm.[78] Courts and arbitrators face formidable difficulties in discerning whether a contested action is opportunistic or, instead, is reasonably self-interested.[79] Parties may thus prefer predictable and cheaper forms of adjudication, even at the cost of losing out on attempts by the adjudicator to reach the "correct" result.[80]

In such circumstances, promisors are often fully aware that a promisee might have a legally enforceable right that is not perfectly calibrated with considerations of fairness or efficiency. For these reasons, and also because conducting litigation or arbitration is expensive, parties to legally enforceable contracts will also rely on alternative nonlegal mechanisms to induce cooperative behavior. [81] When, as so often, it is not possible to use formal enforcement methods, contracting parties rely on social sanctions to avoid opportunistic exploitation of changed circumstances.[82] Most notably for present purposes, they use reputational mechanisms or informal leverage to induce reasonable behavior.[83]

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74. *See supra* text accompanying note 47.

75. *E.g.*, Bridge, *supra* note 25, at 65 ("The obligor's expectation of counting upon a supine obligee is but a mere factual expectation unprotected by the law of contract."). The obligor may be counting less on a supine obligee than on a reasonable obligee, or one who will exercise her discretion to enforce her obligations in accordance with good faith.

76. *See, e.g.*, Robert E. Scott, *A Theory of Self-Enforcing Indefinite Agreements*, 103 COLUM. L. REV. 1641, 1641 (2003) ("All contracts are incomplete. There are infinite states of the world and the capacities of contracting parties to condition their future performance on each possible state are finite.").

77. *See* Paul MacMahon, *Good Faith and Fair Dealing as an Underenforced Legal Norm*, 99 MINN. L. REV. 2051, 2052–54 (2015).

78. *Id.* at 2093–95.

79. *See* David Charny, *Nonlegal Sanctions in Commercial Relationships*, 104 HARV. L. REV. 373, 392–93 (1990).

80. *See, e.g.,* Robert E. Scott, *In (Partial) Defense of Strict Liability in Contract*, 107 MICH. L. REV. 1381, 1392 (2009) ("[P]arties may prefer contracts that only crudely encourage efficient behavior but significantly reduce the contracting costs of enforcement").

81. Robert E. Scott, *The Case for Formalism in Relational Contract*, 94 NW. U. L. REV. 847, 861 (2000).

82. *Id.*

83. Epstein, *supra* note 24, at 982 ("The promisee is a known quantity chosen and selected by the promisor. Even if the legal system gives the promisor the same rights against the promisee's assignee, the value of those rights still may be reduced by the assignment [in part because] [t]he promisor may not have any informal leverage against the assignee . . . .").

Knowing that the right holder's identity matters, promisors select their partners with care. These points are well summed up in a manual on construction contracts, explaining the basis for including prohibitions on assignments: "[O]wners and contractors choose whom to contract with on the basis of mutual expectations of good performance and a co-operative attitude in the event of difficulties."[84] Or, as one court has put it, "[b]uilding contracts are pregnant with disputes: some employers are much more reasonable than others in dealing with such disputes."[85] As a result of their complexity and the near inevitability of unforeseen circumstances, construction contracts are sometimes thought of as paradigmatically "relational" contracts.[86] And the insight that formal contracts are complemented by nonlegal methods is commonly and rightly attributed to relational contract theory. As Robert Gordon famously noted, "[i]n the 'relational' view of Macaulay and Macneil, parties treat their contracts more like marriages than like one-night stands."[87] Parties to marriages are not indifferent to the identity of their spouses.

The attribution of these insights to relational contract theory might lead one to underestimate their general acceptance among contracts scholars across the ideological spectrum. While scholars may disagree about the right way to respond to the facts, they generally agree that the picture painted by relational contract theory is descriptively accurate.[88] Further, the identity of a right holder is not significant only in paradigmatically relational contracts like construction contracts.[89] To a greater or lesser extent, "all or virtually all contracts are relational."[90] The significance of the

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84. ISSAKA NDEKUGRI & MICHAEL RYCROFT, THE JCT 05 STANDARD BUILDING CONTRACT: LAW AND ADMINISTRATION 235 (2d ed. 2009).

85. Linden Gardens Tr. Ltd. v. Lenesta Sludge Disposals Ltd., [1993] 1 AC 85 (HL) 105 (appeal taken from Eng.).

86. Robert G. Eccles, *The Quasifirm in the Construction Industry*, 2 J. ECON. BEHAV. & ORG. 335 (1981); Ian R. Macneil, *The Many Futures of Contracts*, 47 S. CAL. L. REV. 691, 760 (1974) (citing standardized construction contracts as examples of relational agreements); Walter W. Powell, *Neither Market Nor Hierarchy: Network Forms of Organization*, 12 RES. ORGANIZATIONAL BEHAV. 295, 306–07 (1990) (citing construction contracts as an example of network forms of organization).

87. Robert W. Gordon, *Macaulay, Macneil, and the Discovery of Solidarity and Power in Contract Law*, 1985 WIS. L. REV. 565, 569.

88. *See* Randy E. Barnett, *Conflicting Visions: A Critique of Ian Macneil's Relational Theory of Contract*, 78 VA. L. REV. 1175, 1200 (1992) ("To a significant degree, we are all 'relationalists' now."); Scott, *supra* note 81, at 852 ("We are all relationalists now. In that sense Macneil and Macaulay have swept the field.").

89. *See, e.g.*, P.G. Turner, *Legal Assignment of Rights of Restricted Assignability*, 2008 LLOYD'S MAR. & COM. L.Q. 306, 313 ("Grantors of contractual options to buy commercial leases find it necessary to ensure that rivals and ill-reputed businesses do not become entitled to exercise the options granted. Syndicates of banks (the viability of which may affect national economies) find it important to have exclusive access to valuable long-term income streams.").

90. Melvin A. Eisenberg, *Why There is No Law of Relational Contracts*, 94 NW. U. L. REV. 805, 821 (2000); *see also* Scott, *supra* note 81, at 852 ("All contracts are relational, complex and subjective."); Symposium, *Relational Contracting in a Digital Age*, 11 TEX. WESLEYAN L. REV. 675, 679 (2005) ("I start from the proposition that all contracts of every kind, are relational, and they all occur *in* relations. Even the most truncated ones you can think of occur within relations.") (quoting Ian R. Macneil at a panel discussion).

right holder's identity differs from contract to contract and will tend to vary depending on the kind of contract under consideration. But a world where promisees are generally indifferent to the identity of the persons who hold rights against them is purely imaginary.

C. Party Choice Concerning Transferability

Promisors generally prefer non-transferability, while promisees prefer transferability. Economic theory suggests that, in the absence of transaction costs, parties to contracts will bargain to the position that maximizes joint value.[91] Where unilateral transferability benefits the promisee more than it harms the promisor, the parties will agree on assignability—whereas if it harms the promisor more than it benefits the promisee, the parties will agree on non-assignability.[92] Through the mechanism of bargaining, the benefit to one party of a chosen arrangement can be shared with the other party; hence, a lender's ability to transfer the benefit of the contract to a third party should, in principle, result in a lower interest rate for the borrower. Conversely, where a right holder agrees to non-transferability, she should be able to bargain for a higher level of contractual performance than she would otherwise be able to obtain. There is no general reason to think that transferability or non-transferability is better: as in the case of so many other contractual terms, it depends on the circumstances.

Having weighed the costs and benefits of assignability, the parties might prefer various intermediate positions between full transferability and total non-transferability.[93] They might agree to permit assignment to a certain class of assignees but otherwise prohibit it.[94] They might specify that assignment only to a particular class of transferees is permitted. For example, they might want to prohibit assignment except where the transferee is a member of the promisee's corporate group.[95] In such cases, any harm to the promisor resulting from the assignment will usually be minimal.[96] As another example, a developing country borrowing money from a bank might be happy to permit assignment to another bank but unhappy with assignment to a vulture fund. [97]

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91. Kramer, *supra* note 24, at 2.

92. *Id.*

93. *Id.* at 17–22.

94. *Id.*

95. *See*, *e.g.*, Stock Purchase Agreement by and among Yahoo! Inc. and Verizon Communications Inc, § 8.02, (July 23, 2016), https://contracts.onecle.com/yahoo/verizon-spa-2016-07-23.shtml [https://perma.cc/GP6T-ATDA] ("Neither this Agreement nor any of the rights, interests or obligations hereunder shall be assigned, in whole or in part, by operation of Law or otherwise, by Seller or Purchaser without the prior written consent of the other party hereto; provided, however, that Purchaser may assign, at any time prior to the Closing, in its sole discretion, any of or all its rights, interests and obligations under this Agreement to any wholly owned U.S. Subsidiary of Purchaser . . . .").

96. *See* Ayotte & Hansmann, *supra* note 24, at 723–24.

97. Barb. Tr. Co. v. Bank of Zam., [2007] EWCA (Civ) 148, [2007] 1 C.L.C. 434 (Eng.); *see also supra* text accompanying notes 194–196.

The parties might agree instead to allow assignment by consent of the promisor but provide that the consent cannot be unreasonably or arbitrarily withheld.[98] This kind of provision allows a more fact-specific approach to assignability, because assignability depends on the circumstances at the time of assignment, the identity of the assignee, and so on. Allowing assignability to turn on reasonableness, a matter that might have to be determined by a third party, is likely to create controversy and unpredictability.[99] But if the parties have chosen such a provision, we can generally assume that they have weighed the costs of uncertainty against the benefits of a more sensitive approach and have decided that the benefits of the provision exceed its costs.

II. TRANSFERABILITY RULES AND THE LAW OF ASSIGNMENT

Though parties to contracts usually have their own ideas, the current legal regime generally sides with transferability. There is now a strong presumption in favor of the free assignment of contract rights.[100] The current position is the product of centuries of evolution. Medieval common law did not generally recognize assignments of choses in action, including contractual rights; such rights were considered inherently personal to the original parties.[101] At a later stage, the law's reluctance to allow assignments was attributed to the legal prohibitions on champerty and maintenance.[102] Allowing assignments of contractual rights would, according to Lord Coke, "be the occasion of multiplying . . . contentions and suits."[103] One plausible explanation for the law's extreme hostility to the transferability of contractual claims is that it coexisted with the possibility of imprisonment for unpaid debt: when the right holder has the ability to put the debtor in prison, the identity of the right holder is of overwhelming importance.[104]

The common law's initial hostility to transferability came under pressure from business practice.[105] First, to allow the transfer of obligations to pay money, mercantile courts developed the institution of negotiable instruments.[106] A negotiable instrument is an unconditional promise, embodied in a document, to pay to the bearer or to order a fixed sum of money either on demand or at a fixed time.[107] The right to

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98. Webb Interactive Services Master Software License Agreement, § 15.0, https://contracts.onecle.com/webb/vetconnect.lic.shtml [https://perma.cc/499R-LS2H] ("Webb may not assign . . . its rights . . . under this Agreement, either in whole or in part, without the prior written consent of Client, which shall not be unreasonably withheld . . . .").

99. Kramer, *supra* note 24, at 21–22.

100. Khan v. Douglas Mach. & Tool Co., 661 F. Supp. 2d 437, 446 (S.D.N.Y. 2009).

101. Holdsworth, *supra* note 6, at 1003.

102. *See id.* at 1016–27.

103. Lampet's Case, [1613] 77 Eng. Rep. 994, 997 (KB), 10 Co. Rep. 46 a, 48 a (Eng.).

104. Stanley J. Bailey, *Assignments of Debts in England from the Twelfth to the Twentieth Century (Part III)*, 48 L.Q. REV. 547, 549 (1932).

105. Holdsworth, *supra* note 6, at 1021–22.

106. *See* J. MILNES HOLDEN, THE HISTORY OF NEGOTIABLE INSTRUMENTS IN ENGLISH LAW (1955). On the contemporary law of negotiable instruments, see 2 JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE chs. 16–21 (5th ed. 2000).

107. U.C.C. § 3-104(a) (AM. LAW INST. & UNIF. LAW COMM'N 2017).

payment under a bill of exchange, promissory note, or check is transferred via a process known as "negotiation" rather than assignment.[108] Once courts accepted freedom of contract as a general principle, the case for recognizing the transferability of negotiable instruments was strong. The promisor or issuer of a negotiable instrument is on fair notice that she is opting in to a scheme of rules for the transfer of rights to subsequent holders.[109] The common law recognized the transferability of negotiable instruments, but only after commercial interests struggled to convince judges influenced by a "precommercial" mindset.[110]

Leaving negotiable instruments to one side, the law's policy moved from prohibiting the assignment of contractual rights to allowing it through a series of steps in the seventeenth, eighteenth, and nineteenth centuries. At least from the late seventeenth century,[111] courts of equity would give effect to a purported assignment, particularly where the right in question was a debt claim.[112] Where the assigned right was enforceable in the common-law courts, as in the case of a debt, a court of equity would grant an injunction, requiring the assignor to lend his claim in the common-law courts on the assignee's behalf, and would restrain the assignor from recovering payment of legal debts on his own behalf.[113] Common-law courts then acquiesced in the reform by permitting assignees to conduct litigation in the assignor's name.[114] Finally, as part of reforms to pleading practice in the nineteenth century, American legislatures allowed the assignee to sue in its own name without having to join the assignor as a party.[115]

Contemporary law, however, does not just allow assignability—it favors it. Part II of the Article explains the current law on assignability, showing that (a) there is a general default rule of assignability, (b) exceptions to the general default rule have been narrowly curtailed, (c) attempts by parties to displace the general rule of

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108. *Id.* § 1-201(b)(21) (definition of "negotiation"); *see* 2 WHITE & SUMMERS, *supra* note 106, at 72 ("One policy [behind Article 3's narrow concept of negotiability] is to put persons who deal with negotiable instruments on notice of their negotiability. Many business people and some consumers appreciate the unique legal liabilities associated with negotiable instruments and conduct their affairs accordingly.").

109. The position of the transferee of a negotiable instrument is often significantly stronger than the position of the original promisee: in particular, the holder in due course of a negotiable instrument generally takes free from defenses and claims that could have been asserted against a previous holder. *See* 2 WHITE & SUMMERS, *supra* note 106, at 168–69. Unlike the simple fact of transferability, the holder in due course doctrine is less obvious to signatories, and the rule has been abrogated for many consumer debts so as to preserve the rights of consumers. 16 C.F.R. § 433.2 (2019).

110. For an account of the nineteenth-century American history of negotiability, see MORTON J. HORWITZ, THE TRANSFORMATION OF AMERICAN LAW, 1780–1860, at 253–66 (1979) (arguing that the rise of negotiability in nineteenth-century American law reflected the triumph of commercial interests over a "precommercial" mindset).

111. *See* Walter Wheeler Cook, *The Alienability of Choses in Action*, 29 HARV. L. REV. 816, 821 (1916).

112. Holdsworth, *supra* note 6, at 1020–21.

113. TOLHURST, *supra* note 25.

114. *Id.*

115. 3 FARNSWORTH, *supra* note 11, § 11.2; Garrard Glenn, *The Assignment of Choses in Action; Rights of Bona Fide Purchaser*, 20 VA. L. REV. 621, 623 (1934).

assignability are often deprived of that effect by narrow judicial construction, and (d) many rights are mandatorily assignable regardless of what the parties agree.

A. General Default Rule of Assignability

Courts considering assignability issues often start by saying that "[i]n general, all contracts are assignable."[116] The Restatement (Second) of Contracts likewise begins with a presumption of assignability: "A contractual right can be assigned" unless some exception to this general rule applies.[117] Contractual rights, then, are usually transferable even without any express agreement to that effect. Though the identity of a person entitled to assert rights might be considered one of the most basic terms of a contract, the general rule of assignability is seemingly not conceived of as an implied term.[118] Rather, it is a rule of law that the parties may try—and, as we will see below, often fail—to dispense with by agreement.

There is, moreover, no exception for bad faith or malicious assignees. As an illustration, consider *C.H. Little Co. v. Caldwell Transit Co.*,[119] where the promisee under a contract of carriage assigned its contractual rights to the promisor's direct competitor. The promisor offered to prove to the court that the whole purpose of the assignment was for the competitor to drive the promisor out of business.[120] The court, however, considered this allegation irrelevant.[121] Another particularly egregious example is *Fitzroy v. Cave*,[122] a nineteenth-century English case still cited in all three leading American treatises on contracts.[123] Fitzroy and Cave were two company directors who disagreed over how the corporation should be run. Fitzroy, having learned that Cave owed money to some tradesmen in Ireland, persuaded the tradesmen to assign their rights against Cave to Fitzroy. Fitzroy frankly confessed that he had no financial interest in the suit: indeed, by agreeing to turn over the proceeds of any suit to the tradesmen, he was acting as a free debt-collection agency. He flatly admitted to the court that his motivation in suing Cave was to force Cave to declare bankruptcy, which would disqualify him from serving as a director of the

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116. Vinson & Elkins v. Moran, 946 S.W.2d 381, 394 n.7 (Tex. App. 1997); *see also, e.g.*, Elliott Assocs.. L.P. v. Republic of Peru, 948 F. Supp. 1203, 1211 (S.D.N.Y. 1996) ("contracts are freely assignable in the absence of 'clear language expressly prohibiting assignment'").

117. RESTATEMENT (SECOND) OF CONTRACTS § 317(2) (AM. LAW INST. 1981); *see also* U.C.C. § 2-201(2) (AM. LAW INST. & UNIF. LAW COMM'N 2017) ("Unless otherwise agreed all rights of either seller or buyer can be assigned except where the assignment would materially change the duty of the other party, or increase materially the burden or risk imposed on him by his contract, or impair materially his chance of obtaining return performance.").

118. *Cf.* Bridge, *supra* note 25, at 54 (contending that assignability must be conceived of as a term of the contract).

119. 163 N.W. 952 (Mich. 1917).

120. *Id.* at 953.

121. *Id.* at 954.

122. [1905] 2 KB (CA) 364 (Eng.). For near-contemporary criticism of *Fitzroy v Cave*, see Percy H. Winfield, *Assignment of Choses in Action in Relation to Maintenance and Champerty*, 35 L.Q. REV. 143, 150–51 (1919).

123. 3 FARNSWORTH, *supra* note 11, § 11.4 n.10; 17 RICHARD A. LORD, WILLISTON ON CONTRACTS § 74:55 (4th ed. 2003) [hereinafter WILLISTON ON CONTRACTS]; 9 MURRAY, *supra* note 4 § 49.

corporation. The assignee's motive, however, was considered irrelevant, and the suit was allowed to proceed.

Like many other decisions to be discussed in this Part, *Little* and *Fitzroy* are hard to square with a party-focused approach to assignability. In neither case did the parties make any explicit provision allowing assignability. But had the parties to the original contracts discussed the matter, the promisors would never have agreed to allow the promisees to assign their rights to an enemy.[124] The courts, however, having embraced the general idea of assignability, seemed unable to countenance an exception despite the assignees' obvious bad faith.[125]

B. Truncating Exceptions to the Assignability Default

The general rule of assignability is not completely without exception, even where the parties do not seek to prohibit assignment. In addition to nonassignment clauses, considered below, some assignments are ineffective because they are contrary to public policy; others are ineffective because they would materially change the promisor's duty. These exceptions, however, are severely limited.

1. Public Policy

The *Restatement (Second) of Contracts* ("*Restatement (Second)*") notes that a contractual right may be unassignable where "assignment is forbidden by statute or is otherwise inoperative on grounds of public policy."[126] For example, claims against the federal government are generally unassignable.[127] Almost all states have statutory restrictions on the assignment of future wages as a paternalistic measure to protect workers.[128] Future social security payments are also unassignable[129] for the same reason. Assignments of unearned entitlements to salaries by public officials are often prohibited by statute; such rules are sometimes justified on the ground that assignment would undermine the public official's incentive to discharge his or her duties.[130] Claims for personal injury and death are generally unassignable, so a right

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124. Contracts do sometimes explicitly prohibit the assignment of rights to the promisor's direct competitors. *See, e.g.*, Exhibit 4.21 Loan & Security Agreement, 36–37, 2018 WL 01710385 (Apr. 10, 2018).

125. *Fitzroy* was decided just ten years after *Bradford Corp. v. Pickles*, [1895] AC 587 (HL) (appeal taken from Eng.), the case generally regarded as establishing that an otherwise lawful exercise of legal rights could not be considered unlawful because of bad motive. *Id.* at 601 ("If the act, apart from motive, gives rise merely to damage without legal injury, the motive, however reprehensible it may be, will not supply that element."). One of the judges in *Fitzroy v. Cave*, Cozens-Hardy LJ, was losing counsel in *Bradford Corp. v. Pickles*.

126. RESTATEMENT (SECOND) OF CONTRACTS § 317(2)(b) (AM. LAW INST. 1981).

127. 31 U.S.C. § 3727 (2012) (providing that assignments of claims against the federal government "may be made only after a claim is allowed, the amount of the claim is decided, and a warrant for payment of the claim has been issued," with the exception of assignments to "financing institutions" of claims worth at least $1,000).

128. RESTATEMENT (SECOND) OF CONTRACTS ch. 15, statutory note (AM. LAW INST. 1981) ("Virtually every state has statutory restrictions on the assignment of wages.").

129. 42 U.S.C. § 407(a) (2012).

130. Fox v. Miller, 121 S.W.2d 527, 529 (Tenn. 1938); *see also* Swenk v. Wyckoff, 20 A.

to sue for medical malpractice may be unassignable even if it can be framed as a breach-of-contract claim.[131]

These public-policy limitations are relatively narrow, particularly in comparison to historical limitations based on the prohibitions on maintenance (interfering in another's dispute) and champerty (interfering in another's dispute for profit). These prohibitions were once considered sufficiently strong to justify barring almost all assignments. But the idea that it is wrong to interfere in another's dispute is anachronistic: much of what the modern legal profession does would be covered, to say nothing of litigation funding.[132] In the United States, this limitation on assignment was severely curtailed at an early stage.[133] Occasionally, defendants seek to invoke similar ideas in contemporary litigation. In the late 1990s, for example, the Peruvian government sought to resist an action by a "vulture fund" that had acquired some of Peru's sovereign bonds.[134] The Peruvian government invoked a nineteenth-century statutory provision of New York law stating that "[n]o person . . . engaged directly or indirectly in the . . . collection and adjustment of claims . . . shall solicit, buy or take an assignment of . . . any claim or demand, with the intent and for the purpose of bringing an action or proceeding thereon."[135] Read literally, this provision would bar all assignments where the assignee contemplated having to bring legal action to enforce the debt. This statute, however, had been interpreted by the New York Court of Appeals in 1882 to permit assignments for the purpose of debt

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259, 260 (N.J. 1890) ("If the officer should be deprived of this support, there would arise a hazard of his being driven to an inappropriate meanness of living, of his being harassed by the worry of straightened circumstances, and tempted to engage in unofficial labor, and of the likelihood of his falling off in that official interest and vigilance which the expectation of pay keeps alive.").

131. RESTATEMENT (SECOND) OF CONTRACTS ch. 15, statutory note (AM. LAW INST. 1981).

132. *See* Sebok, *supra* note 22. While this Article contends that the law is, in some respects, too willing to allow assignability, it does not support a revival of maintenance and champerty as limitations on assignment. While these doctrines would limit assignment, they would do so in the wrong way. In particular, they would prevent assignment even if the parties had explicitly opted in to assignability. As the Second Circuit pointed out in *Elliott Associates, L.P., v. Banco de la Nacion*, interpreting section 489 to bar all assignments made in contemplation of debt collection would have harmed developing countries by removing the option of consenting in advance to suit by assignees in these circumstances, thereby reducing their ability to access debt financing. 194 F.3d 363, 380 (2d. Cir. 1999).

133. Max Radin, *Maintenance by Champerty*, 24 CALIF. L. REV. 48, 68 (1935). Elsewhere in the common law world, this exception to assignability survives, though, like many aspects of the law of assignability, its scope is unclear. In England, where champerty and maintenance still present an exception to assignability, an assignment of a "bare cause of action" is invalid, but the rule has no application where the assignee has a "genuine commercial interest" in receiving the assignment. Trendtex Trading Corp. v. Credit Suisse [1982] AC 679 (HL) (appeal taken from Eng.). The scope of the exception to assignability has, moreover, been narrowly curtailed by rulings holding that the exception does not affect the assignment of debt claims. Camdex Int'l Ltd v. Bank of Zam. (No. 1) [1996] QB 22 (AC) (appeal taken from Eng.).

134. Elliott Assocs., L.P. v. Banco de la Nacion, 194 F.3d 363 (2d Cir. 1999).

135. N.Y. JUD. LAW § 489 (McKinney 2004).

collection.[136] Reaffirming that holding and rejecting the Peruvian government's argument, the Second Circuit cited "New York's interests as a global financial center" in support of a narrow construction of Section 489.[137] Section 489 has recently been held to bar assignments where the purpose is simply for the assignee to bring a lawsuit as a proxy for the assignor,[138] but even in such cases, the statute does not apply to assignments where the purchase price is $500,000 or more.[139]

2. Material Change of Promisor's Duty

The main exception to the default rule of assignability is the idea that some assignments would harm the promisor by making a significant difference to her duty under the contract.[140] The *Restatement (Second)* provides that assignment is not permissible where the assignment would "would materially change the duty of the obligor, or materially increase the burden or risk imposed on him by his contract, or materially impair his chance of obtaining return performance, or materially reduce its value to him."[141] Sometimes, this limitation is expressed by saying that the right is "personal" to the original promisee.[142] On this basis, courts have sometimes found the buyer's right under a requirements contract to be unassignable: a promise by A to supply B with its requirements for a particular good is not generally understood as a promise to supply C's requirements.[143] Likewise, courts have generally found the employer's rights under a personal services contract to be nonassignable: "the law is clear that an employee cannot be compelled to work for another company."[144] Employers wishing to preserve this right must expressly provide for it—for example, with a clause permitting assignment on the sale of an entire business.[145]

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136. Moses v. McDivitt, 88 N.Y. 62, 65 (1882).

137. *Elliott*, 194 F.3d at 379.

138. *See* Justinian Capital SPC v. WestLB AG, 65 N.E.3d 1253, 1256 (N.Y. 2016).

139. N.Y. JUD. LAW § 489.

140. This exception to assignability is presumably itself a default rule that can be overridden by contrary agreement that a right is assignable; the *Restatement (Second)* provides that a clause providing for assignability is valid. *See* RESTATEMENT (SECOND) OF CONTRACTS § 323(1) (AM. LAW INST. 1981). Cohen, however, appears to treat it as a mandatory rule, suggesting that it might be applied even in cases where the parties have provided for express assignability. *See* Cohen, *supra* note 14, at 28–29.

141. RESTATEMENT (SECOND) OF CONTRACTS § 317(2)(a) (AM. LAW. INST. 1981); *see also* U.C.C. § 2-210 (AM. LAW INST. & UNIF. LAW COMM'N 2017) (similar wording); Hess v. Gebhard & Co., 808 A.2d 912, 922 (Pa. 2002) ("[A]n assignment of a right will not be effective if it purports to make a material change in the duties or responsibilities of the obligor.").

142. *See* Crane Ice Cream Co. v. Terminal Freezing & Heating Co., 128 A. 280, 283 (Md. 1925) (explaining the contractual promise to supply buyer's requirements for ice is not assignable from a smaller ice-cream manufacturer to a larger ice-cream manufacturer).

143. *Id.*

144. *E.g.*, Logical Networks, Inc. v. Murdock, No. 239779, 2002 WL 31187877, at *2 (Mich. Ct. App. Oct. 1, 2002).

145. Kramer, *supra* note 24, at 28–32. Even without an express assignability clause, a court might recognize an implied exception to the default rule that an employer's rights are nonassignable in cases of sales of whole businesses. *See* Roeder v. Ferrell-Duncan Clinic, Inc., No. 103CC0497, 2003 WL 21976388, at *4 n.1 (Mo. Cir. Ct. Aug. 11, 2003) ("[A]nother

Crucially, however, the material-variation exception does not apply where the promisor's objection is simply that the transferee is likely to wield the power to sue more aggressively than the promisee would. In particular, "[w]hen the obligor's duty is to pay money, a change in the person to whom the payment is to be made is ordinarily not material."[146] Courts seem to universally reject arguments that a change in the creditor's identity materially increases the burden on the promisor[147]—even though, in reality, the creditor's identity may be all-important.[148] As explained above, where the original promisee might have been willing to renegotiate the extent of payment or provide extra time in response to changed circumstances, the transferee may be unwilling to do so.[149] This idea was similarly rejected when gas station franchisees objected that assignment of the franchisor's rights would create an increased risk that the transferee would exercise discretion under the contract to enlarge the franchisees' obligations. [150] The Seventh Circuit ruled that the change in the right holder's identity was irrelevant because the original franchisor would have had the legal right to do exactly the same thing.[151] The *Restatement (Second)* provides that "if the duty is to depend on the personal discretion of one person, substitution of the personal discretion of another is likely to be a material change."[152] But it does not accept that, in reality, the decision to enforce a contractual right always depends on the right holder's discretion.[153]

C. "Strict Construction" of Nonassignment Clauses

In theory, aside from the mandatory rules considered in Section II.D below, courts respect the parties' freedom of contract on the issue of assignability.[154] But in fact,

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exception to the general rule against assignability of professional services contracts is when an employment contract is assigned in conjunction with the sale of a business and assets: such an assignment is deemed incident to the property conveyed.").

146. RESTATEMENT (SECOND) § 317 cmt. d (AM. LAW. INST. 1981).

147. *See, e.g.*, Craft Works Const., Inc. v. Nest, No. Civ. A. RE-03-012, 2003 WL 22765942, *2 (Me. Super. Ct. Nov. 14, 2003) (explaining the right to payment under construction contract could be assigned despite absence of assignment clause because identity of payee is not material to the promisor's obligation); *In re* FH Partners, L.L.C., 335 S.W.3d 752, 764 (Tex. Ct. App. 2011) ("There is simply no Texas authority holding that a creditor's right to receive payment on a debt is the sort of contractual right that Texas law regards as being predicated on a debtor's 'personal trust . . . or credit' in a creditor, such that the creditor cannot freely assign that right."); Easton Bus. Opp. v. Town Exec. Suites, 230 P.3d 827, 830 (Nev. 2010) ("When the obligor's duty is to pay money, a change in the person to whom the payment is to be made is not ordinarily material and there is nothing extraordinary about the assignment of commission rights here.") (internal quotation marks and citation omitted).

148. *See* Cohen, *supra* note 14, at 25–30 (making a similar point with respect to the assignability of mortgage contracts).

149. *See supra* Section I.B.

150. Beachler v. Amoco Oil Co., 112 F.3d 902, 908 (7th Cir. 1997).

151. *Id.*

152. RESTATEMENT (SECOND) § 317 cmt. d (AM. LAW. INST. 1981).

153. *See supra* Section I.B.

154. Contractual freedom to restrict assignability was recognized in the eighteenth-century case of *Lynch v. Dalzell*, in which the court gave effect to a restriction in an insurance policy

freedom of contract bends decidedly in one direction. The *Restatement (Second)* provides that the parties may make rights expressly assignable.[155] Conversely, although the *Restatement (Second)* states that assignment may be "validly precluded by contract"[156] and concedes that "the parties to a contract have power to limit the rights created by their agreement,"[157] the *Restatement's* provision on contractual prohibitions on assignment is largely devoted to providing ways for courts *not* to apply nonassignment clauses.[158] The *Restatement* took its cue from the U.C.C.,[159] which in turn followed the case law—in the 1960s, Grant Gilmore noted that "[i]n case after case where a commercial debtor has sought to prohibit assignment, the courts have regularly managed to construe the heart out of the clause before them."[160] While courts "recit[ed] by dictum that a no assignment clause is good, [they would] hold that in this case no intent to forbid the assignment appears."[161]

The *Restatement (Second)* justifies the pro-transferability interpretive approach by reference to "the policy which limits the validity of restraints on alienation."[162] Even aside from Article 9's mandatory provisions, the rule that contract rights are assignable is a "sticky default," or perhaps better, a "quasi-mandatory rule."[163] This policy inspires a series of what public law scholars would call "normative canons."[164] The upshot is that the plain language of a nonassignment clause is a poor predictor of its legal effect.[165]

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that restricted rights to the original policyholder. (1729) 2 Eng. Rep. 292; 4 Bro. P.C. 431.

155. RESTATEMENT (SECOND) OF CONTRACTS § 323(1) (AM. LAW. INST. 1981) ("A term of a contract manifesting an obligor's assent to the future assignment of a right or an obligee's assent to the future delegation of the performance of a duty or condition is effective despite any subsequent objection.").

156. *Id.* § 317(2).

157. *Id.* § 322 cmt. a.

158. The provision is entitled "Contractual Prohibition of Assignment," but lists four different default rules that restrict the scope of contractual prohibitions. *Id.* § 322.

159. *See id.* § 322 reporter's note (noting that section 322(*1*) was "based on" a similar provision in U.C.C. Article 2).

160. Grant Gilmore, *The Commercial Doctrine of Good Faith Purchase*, 63 YALE L.J. 1057, 1118 (1954).

161. *Id.* Gilmore, an opponent of restrictions on assignment, thought the courts' treatment of nonassignment clauses illustrated the idea "that a rule, universally conceded to be 'the law,' is almost never applied suggests that courts must instinctively feel that it is a bad rule, from which avenues of escape must be discovered and maintained." 1 GILMORE, *supra* note 17, at 210–14.

162. RESTATEMENT (SECOND) OF CONTRACTS § 322 cmt. a (AM. LAW. INST. 1981).

163. On "sticky defaults" or "quasi-mandatory rules," see generally Ian Ayres, *Regulating Opt-Out: An Economic Theory of Altering Rules*, 121 YALE L.J. 2032, 2084–96 (2012).

164. *See* Kenneth A. Bamberger, *Normative Canons in the Review of Administrative Policymaking*, 118 YALE L.J. 64 (2008).

165. *See*, *e.g.*, Caleb Trotter, *Be Wary of Over-Reliance on AIA Form Contracts*, MOD. CONTRACTOR SOLUTIONS, Aug. 2016, at 36, 37 (warning construction contractors that they may be liable to suit by a party whom "[they] never worked for or knew," despite a seemingly clear antiassignment clause in the American Institute of Architects (AIA) standard form contract).

1. Requiring "Magic Words" to Remove the Power to Assign

Intuitively, one might expect that a nonassignment clause would prevent assignment from occurring. Under the "modern approach," however, courts generally construe nonassignment clauses to impose a duty on the promisee not to assign the contract, but will not deprive the promisee of the power to do so.[166] Section 322(2) of the *Restatement (Second)* provides that "[a] contract term prohibiting assignment of rights under the contract, unless a different intention is manifested . . . (b) gives the obligor a right to damages for breach of the terms forbidding assignment but does not render the assignment ineffective."[167] This means that even if the contract explicitly states, for example, that the promisee "shall not assign" its rights, many courts would find that an assignment is nevertheless effective to transfer the right to sue to the assignee unless the word "void" or "invalid" appears.[168] Some courts have taken this interpretive canon to extreme lengths.[169] For example, in *Rumbin v. Utica Mutual Insurance Company*, the Supreme Court of Connecticut construed a clause that stated "[n]o payment under this annuity contract may be . . . assigned" so as to preserve the power to assign.[170]

Construing a nonassignment clause to preserve the power to assign essentially renders the clause ineffective.[171] True, the promisor can still sue the promisee for damages for breach of contract, but it will almost always be impossible to prove the extent of a promisor's loss resulting from the transfer.[172] Moreover, the remedy of damages will generally be useless in the event of the promisee's bankruptcy.[173] A

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166. Rumbin v. Utica Mut. Ins. Co., 757 A.2d 526, 533 (Conn. 2000).

167. RESTATEMENT (SECOND) OF CONTRACTS § 322(2)(b) (Am. Law. Inst. 1981).

168. Pravin Banker Assocs., Ltd. v. Banco Popular Del Peru, 109 F.3d 850, 856 (2d Cir. 1997) ("[T]o reveal the intent necessary to preclude the power to assign, or cause an assignment violative of contractual provisions to be wholly void, [a contractual] clause must contain express provisions that any assignment shall be void or invalid if not made in a certain specified way." (alteration in original) (quoting Univ. Mews Assocs. v. Jeanmarie, 471 N.Y.S. 2d 457, 462 (N.Y. Sup. Ct. 1983))).

169. Not all courts require "magic words"; the Supreme Court of Minnesota, for example, has rejected this approach and interpreted a clause stating that "the rights . . . of [the parties] shall not be assignable" as removing the power to assign. Travertine Corp. v. Lexington-Silverwood, 683 N.W.2d 267, 272, 274 (Minn. 2004) (emphasis omitted). The decision in *Travertine* has been criticized on the ground that it "den[ies] Minnesota citizens the benefits of the modern majority rule requiring strict construction of non-assignment clauses." Joy Anderson, Case Note, *Contracts—Looking for "Something": Minnesota's New Rule for Interpreting Anti-Assignment Clauses in* Travertine Corp. v. Lexington-Silverwood, 32 WM. MITCHELL L. REV. 1435, 1437 (2006).

170. 757 A.2d 526, 529 (Conn. 2000) (alteration in original).

171. 1 GILMORE, *supra* note 17, at § 7.9 (construing prohibitions on assignments as mere personal covenants is "more a tribute to judicial ingenuity in avoiding results sensed to be undesirable than to judicial skill in unveiling the true intent of the parties").

172. *See* Anderson, *supra* note 169, at 1460 (noting that "the obligor often will not be quantifiably harmed by an assignment").

173. *See* Bank of Am., N.A. v. Moglia, 330 F.3d 942, 948 (7th Cir. 2003) (noting that limiting the promisor to a damages remedy in that case would have rendered it a general creditor of a bankrupt entity).

damages remedy is clearly inadequate to protect the obligor's interests, yet many courts are willing to refuse the equivalent of a specific performance remedy by finding the assignment invalid. The practice can hardly be justified as an attempt to give effect to the words chosen by the parties to embody their agreement; rather, it is a fairly transparent attempt to achieve a policy result by the use of normative canons of interpretation.

The "modern view" trips up even the most sophisticated contract drafters. In one construction case, the parties had used a standard-form contract provided by the American Institute of Architects (AIA), which contained a clause stating that neither party "shall assign the Contract."[174] The AIA made the "classic mistake" of failing to include the magic words denoting voidness or invalidity,[175] and the clause was therefore read to preserve the power to assign.[176] The treatment of nonassignment clauses appears to be an exception to Robert Scott's claim that "[t]hrough the process of common-law adjudication, these industry-wide prototypes [including the AIA's standard forms] have received plain meaning legal recognition, thereby reducing the risks associated with their use by subsequent contracting parties."[177]

2. Construing "Assignment" as "Delegation"

As the *Restatement (Second)* itself makes clear, the word "assignment" refers to a transfer of rights to a third parties, whereas the word "delegation" refers to the performance of a duty by a third party.[178] Given this terminological clarification, one might think that if the parties agreed that the contract shall not be assignable, the court would understand the parties to have intended to bar assignment. Nevertheless, many courts will construe such a clause as an attempt to bar only the delegation of duties but not the assignment of rights.[179] This practice is approved by the *Restatement (Second)*, which provides that "[u]nless the circumstances indicate the contrary, a contract term prohibiting assignment of 'the contract' bars only the delegation to an assignee of the performance by the assignor of a duty or condition."[180] The U.C.C. has an almost identical provision,[181] but it also provides

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174. Oliver/Hatcher Const. & Dev., Inc. v. Shain Park Assocs., No. 275500, 2008 WL 2151716, at *3 (Mich. Ct. App. May 22, 2008).

175. *Id.* (quoting SWEET ON CONSTRUCTION INDUSTRY CONTRACTS: MAJOR AIA DOCUMENTS, § 23.19, p 485 (4th ed. 2000)).

176. *Id.* at *4.

177. Scott, *supra* note 82, at 870.

178. RESTATEMENT (SECOND) OF CONTRACTS §§ 317–318 (AM. LAW. INST. 1981).

179. Aldana v. Colonial Palms Plaza, Ltd., 591 So. 2d 953, 955 (Fla. Dist. Ct. App. 1991) ("As a rule of construction . . . a prohibition against assignment of the contract (or in this case, the lease) will prevent assignment of contractual duties, but does not prevent assignment of the right to receive payments due . . . ."); Wonsey v. Life Ins. Co. of N. Am., 32 F. Supp. 2d 939, 943 (E.D. Mich. 1998) ("The modern trend with respect to contractual prohibitions on assignments is to interpret these clauses narrowly, as barring only the delegation of duties, and not necessarily as precluding the assignment of rights from assignor to assignee.") (emphasis omitted).

180. RESTATEMENT (SECOND) OF CONTRACTS § 322(1) (AM. LAW. INST. 1981).

181. U.C.C. § 2-210(3) (AM. LAW INST. & UNIF. LAW COMM'N 2017).

that "[a]n assignment of 'the contract' . . . is an assignment of rights." [182] There could hardly be a clearer illustration of policy-motivated interpretation: the same word means different things depending on whether the court is interpreting a clause seeking to prohibit assignment or whether a party has actually purported to achieve an assignment.

3. Permitting Assignments of Money Claims

The default construction of a contractual prohibition on assignment, according to the *Restatement (Second)*, "does not forbid assignment of a right to damages for breach of the whole contract or a right arising out of the assignor's due performance of his entire obligation."[183] The idea is that parties are more likely to wish to restrict transfer of rights to performance than they are to wish to restrict claims for damages for breach. Likewise, a change in the identity of the right holder is less significant when the promisor's only obligation is to pay money for work already done: "[I]t should make no difference to [the promisor] whether [the promisee] or an assignee sues to recover money allegedly owed under a fully performed contract."[184]

Drawing a distinction between assignments at different stages of a contract's life often makes sense. In an insurance contract, for example, the insurer's decision to cover the relevant risk and its decision about the premium to charge are usually based on information the insurer has gathered about the applicant. Evidently, it would undermine the whole arrangement if the original insured had the power to transfer the policy itself to another person, whose risk profile may be different from the original holder.[185] Post-loss assignments, however, do not alter the likelihood of the covered risk occurring, so the insurance company has less reason to wish to avoid assignment.[186] The courts have recognized this distinction, and as a result, "[t]he great weight of authority distinguishes between assignment of an insurance policy before loss occurs and assignment after loss."[187]

While it may make sense for the parties to distinguish between assignments before and after breach, it is at least highly questionable whether the courts should impose this distinction where the parties have not explicitly selected it. As an illustration, in

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182. *See id*. § 2-210(5).

183. RESTATEMENT (SECOND) OF CONTRACTS § 322(2)(a) (AM. LAW. INST. 1981). *E.g.,* SME Indus., Inc. v. Thompson, Ventulett, Stainback & Assocs., Inc., 28 P.3d 669, 674 (Utah 2001) ("As a general rule, a contract provision prohibiting the assignment of the contract itself, or of rights and privileges under the contract, does not, unless a different intention is manifested, prohibit the assignment of a claim for damages on account of breach of the contract."); Berschauer/Phillips Const. Co. v. Seattle Sch. Dist. No. 1, 881 P.2d 986, 994 (Wash. 1994) ("[A] general anti-assignment clause, one aimed at prohibiting the assignment of a contractual performance, does not, absent specific language to the contrary, prohibit the assignment of a breach of contract cause of action.").

184. Omicron Safety and Risk Techs., Inc. v. Univ. Chi. Argonne, LLC, 181 F. Supp. 3d 508, 511 (N.D. Ill. 2015).

185. 17 WILLISTON ON CONTRACTS, *supra* note 123, § 49:126.

186. *Id.*

187. Antal's Restaurant, Inc. v. Lumbermen's Mut. Cas. Co., 680 A.2d 1386, 1388 (D.C. App. 1996); *see also* Millard Gutter Co. v. Farm Bureau Prop. & Cas. Ins. Co., 889 N.W.2d 596 (Neb. 2016).

one case, a contractor and project owner agreed that neither party would assign "this Contract" without the prior written consent of the other party.[188] The contractor then assigned its claims for breach of contract against the project owner to a bank.[189] The project owner found itself on the receiving end of an arbitration claim by the bank and pointed to the seemingly unlimited nonassignment clause in an effort to resist the claim.[190] The court, however, ruled that the nonassignment clause did not prevent "post-contract assignment of the related chose in action";[191] because "restraints on alienation of property should be strictly construed against the party urging the restriction."[192] This process of strict construction must seem like mere legal verbiage to a project owner who reads the actual text of the contract.

4. Permitting Assignment by Another Name

Another way, approved by the English courts, for promisees to evade a prohibition on assignment is for the assignor to declare itself a trustee of the claim it has against the obligor.[193] This subterfuge was approved in *Barbados Trust Co. v. Bank of Zambia*.[194] The case concerned a loan to the government Bank of Zambia in 1985; the loan documents permitted the lender to assign its rights only to another bank or financial institution.[195] As the trial court judge pointed out, "[a]ny borrower, but particularly a central bank, may be concerned to ensure that its affairs and obligations are known and owed to and only enforceable by established and authorised institutions."[196] The purpose of the clause, it appears, was to prevent assignment to vulture funds. Like American courts, the English courts nominally purport to honor freedom of contract in this area, stating that there is "no policy reason why a contractual prohibition on assignment of contractual rights should be held contrary to public policy."[197] The Bank of Zambia must have felt confident that it could not be liable to suit by vulture funds.

Nevertheless, a majority of the judges in the *Bank of Zambia* case agreed that the nonassignment clause did not prevent a bank holding the right—in this case, Bank of America—from evading the clause by declaring that it was a trustee of its debt claim for a vulture fund. The court reached this conclusion on the basis of the "true construction" of the clause: if the parties had wished to bar declarations of trust in

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188. Missouri Bank & Trust Co. v. Gas-Mart Dev. Co., 130 P.3d 128, 134 (Kan. Ct. App. 2006).

189. *Id.* at 130.

190. *See id.* at 132 ("[The project manager's] motion framed the issue as whether the construction contract's express prohibition on assignment precluded the assignment of the contractor's right, title, and interest in the arbitration proceedings.").

191. *Id.*

192. *Id.* at 134.

193. *See* Don King Prods. Inc. v. Warren [2000] Ch 291 (CA) 388 (Eng.).

194. [2007] EWCA (Civ) 148 (Eng.).

195. *Id.* at 434.

196. *Id.* at 438.

197. Linden Gardens Trust Ltd. v. Lenesta Sludge Disposals Ltd. [1994] 1 AC 85 (HL) 107 (Lord Browne-Wilkinson) (appeal taken from Eng.).

addition to assignments, they should have done so explicitly.[198] Yet the same judges agreed that as the beneficiary of a trust, the vulture fund could bring an action directly against the Bank of Zambia, just as an assignee could.[199] As a dissenting judge pointed out, the effect of this construction was to permit precisely the same legal result—liability to suit by a vulture fund—that the clause was meant to prevent.[200] While the majority's reasoning was nominally tied to contract interpretation and party intent, it was clearly motivated by hostility to prohibitions on assignment.[201]

D. Mandatory Assignability Rules

Assignability is also promoted by explicit mandatory rules. In the nineteenth century, the newly widespread ability to assign contractual rights was coupled with an understanding that the parties could choose to make rights nonassignable if they so wished. In the early twentieth century, however, many courts embraced the notion that attempts to restrict the assignability of debt claims must be disregarded.[202] This change in the law appears to have been prompted by the rise of accounts-receivable financing, whereby a business uses claims against its customers as collateral to obtain a loan. In addition to common-law development, changes in financing practice also prompted state legislatures to enact statutory provisions declaring certain classes of debt assignable regardless of party agreement.[203]

Today's mandatory assignability rules are contained mostly in the U.C.C., first published in 1952 and eventually adopted throughout the United States. Under U.C.C. Article 2, in a contract for the sale of goods, "a right to damages for breach of the whole contract or a right arising out of the assignor's due performance of his entire obligation can be assigned despite agreement otherwise."[204] This provision converts the canon of construction, discussed in Section II.C.3 above, into a mandatory rule, but only for sales-of-goods contracts. Article 9's mandatory assignability rules are of broader significance. Following their revision in 2001, these rules are "horribly complicated";[205] a relatively brief description will suffice for present purposes.[206]

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198. *Bank of Zam.*, [2007] EWCA (Civ) at 451–52 (Waller LJ).

199. The right of a beneficiary of a trust to bring an action against the obligor was established in *Vandepitte v. Preferred Accident Ins. Corp.* [1933] AC 70 (PC) 79 (appeal taken from B.C.).

200. *Bank of Zam.*, [2007] EWCA (Civ) at 477–78 (Hooper LJ, dissenting).

201. One of the majority judges stated that "[i]f a prohibition on assignment carried all before it . . . it seems to me that the public interest in freedom of contract and the freedom of markets could be severely prejudiced." *Id.* at 470 (Rix LJ).

202. An article published in 1934 stated: "So available is a debt for assignment, that if the originating contract should forbid the assignment of the obligation when it has taken form, the majority rule is that the stipulation is unenforceable." Glenn, *supra* note **Error! Bookmark not defined.**, at 622.

203. *See* 1 GILMORE, *supra* note 17, at 308.

204. U.C.C. § 2-210(2) (AM. LAW INST. & UNIF. LAW COMM'N 2017).

205. 4 WHITE & SUMMERS, *supra* note 106, at 382.

206. For a more detailed account of the revisions to Article 9's provisions on non-assignability, see Cohen & Henning, *supra* note 23.

Article 9 primarily concerns security interests in personal property, but it also applies to many other kinds of transaction whose purpose is financing. Hence, the original Article 9 covered not only transactions granting security interests but also outright sales of "accounts" and of "chattel paper."[207] The initial bar on nonassignment clauses, former section 9-318(4), provided that "[a] term in any contract between an account debtor and an assignor is ineffective" in two circumstances.[208] First, a term would be ineffective if it prohibited assignment of an "account," whether by sale or as a security.[209] Due to the definition of "account," the provision's main effect was to invalidate attempts to restrict the assignability of rights to payment for goods and services rendered.[210] Grant Gilmore—a Co-Reporter for Article 9 and evidently the driving force behind this explicit incursion on freedom of contract—explained that its purpose was to support accounts receivable financing.[211] Secondly, a term was ineffective if it prohibited the creation of a *security interest* in a "general intangible for money due or to become due."[212] Clauses restricting the outright sale of general intangibles involved neither a prohibition on a sale of an account nor the creation of a security interest, and were thus exempt from the ban.[213]

Further changes in commercial practice led to a perceived need to expand the bar on restrictions of assignability. In particular, the rise of securitization meant that much financing was achieved through sales of receivables not covered by former Article 9's definition of "account," including credit-card receivables, insurance premiums, and rights to payment on energy contracts.[214] Hence, revised Article 9 greatly expanded the definition of "account" and now contains two complex provisions affecting restrictions on assignment.

The first restriction in revised Article 9—section 9-406—is a hard rule that simply invalidates contractual restrictions on the transfer of accounts (other than health-care receivables) and chattel paper. [215] The new definition of "account" includes almost any right to payment other than under a loan.[216] Section 9-406 also invalidates contractual restrictions on the creation of security interests in "payment intangibles" and promissory notes.[217] The second provision—section 9-408—applies to restrictions on the transfer of health-care receivables and to outright sales of payment

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207. U.C.C. § 9-102(1)(b) (1972) (AM. LAW INST. & UNIF. LAW COMM'N, amended 2010).

208. *Id.* § 9-318(4) (1972) (AM. LAW INST. & UNIF. LAW COMM'N, amended 2010).

209. *Id.*

210. The original U.C.C. defined "account" as "any right to payment for goods sold or leased or for services rendered which is not evidenced by an instrument or chattel paper not yet earned by performance." *Id.* § 9-106 (1962) (AM. LAW INST. & UNIF. LAW COMM'N, amended 2010).

211. Gilmore, *supra* note 160, at 1118–21.

212. U.C.C. § 9-318(4).

213. *See* Cohen & Henning, *supra* note 23, at 358.

214. *Id.* at 360; Paul M. Shupack, *Making Revised Article 9 Safe for Securitizations: A Brief History*, 73 AM. BANKR. L.J. 167, 174–76 (1999).

215. U.C.C. § 9-406(f) (2005) (AM. LAW INST. & UNIF. LAW COMM'N, amended 2010).

216. *Id.* § 9-102(2) (2005) (AM. LAW INST. & UNIF. LAW COMM'N, amended 2010); *see* Cohen & Henning, *supra* note 23, at 360–61.

217. U.C.C. § 9-406.

intangibles, health-care receivables, and promissory notes.[218] This provision renders restrictions on assignment ineffective to the extent that they would "impair the creation, attachment, or perfection of a security interest" but, unlike section 9-406, it is not binding on the promisor, who can continue to pay the promisee.[219] Under section 9-408, unless the promisor agrees to pay the assignee, the assignee is limited to asserting its interest against the proceeds of the assignment once they have been paid to the promisee. Because it preserves the promisor's ability to assert a contractually agreed restriction on assignment, section 9-408 does not bear directly on the main issue addressed by this Article. Section 9-406 is, however, a direct interference with freedom of contract.

Some state laws have extended mandatory assignability even beyond the U.C.C.'s already-broad scope. In the 1970s, the Supreme Court of Oklahoma declared "any contract provisions which prohibit or restrict the assignability of accounts or contract rights to be contra to the law, and thus null and void and of no effect."[220] By statute, Arkansas law provides that "[a]ll bonds, bills, notes, agreements, and contracts, in writing, for the payment of money or property, or for both money and property, shall be assignable."[221] Arkansas courts ruled that this provision requires administrators of employee-benefit plans that are covered under the Employee Retirement Income Security Act (ERISA) to honor assignments of insurance claims by plan beneficiaries despite provisions in the plan preventing assignment.[222] To that extent, the federal courts later ruled that the Arkansas statute was preempted by ERISA.[223]

While the United States seems to have been the world leader in overriding restrictions on assignment, many other jurisdictions have adopted similar mandatory rules. As noted above, the English courts have bent over backwards to validate assignments in the teeth of nonassignment clauses,[224] and the U.K. government has recently enacted regulations invalidating clauses purporting to restrict the assignment of receivables.[225] The perceived need to override freedom of contract extends beyond common-law jurisdictions. In Germany, a 1994 law renders ineffective attempts to restrict the assignment of claims resulting from reciprocal commercial transactions.[226] Moreover, to meet a perceived need for international uniformity to facilitate cross-border assignability, two international conventions have been drafted, and each includes a restriction on freedom of contract. The Ottawa Convention on International Factoring contains an optional provision overriding nonassignment

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218. *Id.* § 9-408 (2005) (AM. LAW INST. & UNIF. LAW COMM'N, amended 2010).

219. *Id.* § 9-408(a), (d).

220. Am. Bank of Commerce v. City of McAlester, 555 P.2d 581, 585 (Okla. 1976).

221. ARK. CODE. ANN. § 4-58-102 (West 2011).

222. Am. Med. Int'l v. Arkansas Blue Cross & Blue Shield, 773 S.W.2d 831, 834 (Ark. 1989).

223. Arkansas Blue Cross & Blue Shield v. St. Mary's Hosp., Inc., 947 F.2d 1341 (8th Cir. 1991).

224. *See supra* Section II.C.4.

225. *See* Business Contract Terms (Assignment of Receivables) Regulations 2018, SI 2018/1254 (Eng. & N. Ir.).

226. Hugh Beale & Wolf-Georg Ringe, *Transfer of Rights and Obligations*, *in* THE COMMON EUROPEAN SALES LAW IN CONTEXT: INTERACTIONS WITH ENGLISH AND GERMAN LAW 540 (Gerhard Dannemann & Stefan Vogenauer, eds., 2013).

clauses, and three countries (France, Latvia, and Belgium) have decided to sign up to the Convention but opt out of the override.[227] The U.N. Convention on the Assignment of Receivables in International Trade similarly contains an optional provision that overrides restrictions on assignment. [228]

III. POSSIBLE JUSTIFICATIONS FOR THE PRO-TRANSFERABILITY POLICY

The law's policy of encouraging—and sometimes demanding—transferability is thus well entrenched. But what, if anything, justifies it? Professor Gilmore, who was largely responsible for Article 9's prohibitions on nonassignment clauses,[229] seemed unable to explain it. "To rehearse social and economic arguments designed to prove that the position is sound would not be helpful. On propositions of so fundamental an order, belief is instinctive and irrational, not logical and reasoned."[230] Gilmore did gesture towards an instrumental argument in favor of his position, stating that "[t]he social or economic utility of permitting creditors to transfer rights is believed to outweigh the utility of permitting obligors to forbid the transfer."[231] But the claim that the utility of transferability outweighed the utility of promisors able to prevent it "lies beyond demonstration and proof."[232] The purpose of Part III is to figure out whether any such demonstration might be available now, especially given advances in the economic analysis of law since Gilmore's discussion, which was published in 1965.

Modern economic analysis supports a general presumption in favor of enforcing contract terms as agreed: assuming the parties know their own desires, enforceability generally makes them better off, without making anyone worse off.[233] Yet contract law properly contains some mandatory rules (with which parties cannot dispense by agreement) and quasi-mandatory rules (with which parties can only dispense by agreement with difficulty).[234] Within the economic framework, there are two main potential justifications for mandatory or quasi-mandatory rules: (i) to protect the interests of a party to the contract (paternalism); and (ii) to protect the interests of third parties (externalities).[235] A pro-assignability rule might be justified as a paternalistic step to help promisees or as an externality-minimizing measure to protect the interests of transferees and potential transferees.

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227. *Status—Unidroit Convention On International Factoring (Ottawa, 1988)*, UNIDROIT, https://www.unidroit.org/status-1988-factoring [https://perma.cc/3WMW-BDTF].

228. *See* N. Orkun Akseli, *The United Nations Convention on the Assignment of Receivables in International Trade and Small Businesses*, *in* SECURED TRANSACTIONS LAW REFORM: PRINCIPLES, POLICIES AND PRACTICE (Louise Gullifer & Orkun Akseli, eds., 2016).

229. 1 GILMORE, *supra* note 17, at 211

230. *Id.* at 212.

231. *Id.*

232. *Id*. at 212–13.

233. *See, e.g.*, ROBERT COOTER & THOMAS ULEN, LAW AND ECONOMICS 223 (6th ed. 2012) ("Economic efficiency usually requires enforcing a promise if the promisor and promisee both wanted enforceability when it was made.").

234. Ayres, *supra* note 163.

235. *Id.* at 2084.

To the extent judges and scholars have tried to justify the law's transferability bias, they have focused more on externalities than on paternalism, but both potential bases for overriding nonassignment clauses might be relevant. As outlined below, early justifications for the pro-transferability bias made a simple analogy between contractual rights and tangible property.[236] Behind this conceptual argument lies the intuition that restricting the transfer of contract rights is economically wasteful. Simplistic externality-based arguments[237] refer solely to the interests of transferees in being able to acquire contractual rights. More sophisticated externality-based arguments in favor of transferability might rely on a general market interest in reducing information costs for potential transferees.[238] Finally, paternalism-based arguments have recently surfaced, as defenders of receivables financing seek to invoke the interests of small-business promisees in transferring their rights to financial institutions.[239]

A. Contractual Rights as "Property"

The simplest version of the argument against enforcing nonassignment clauses goes as follows. Contract rights are property.[240] The law limits the extent to which parties to contracts can restrict the alienation of other kinds of property.[241] Likewise, the law must limit restraints on the alienation of contractual claims.[242]

In the United States, this idea was given its most prominent expression by Justice Holmes in his opinion for the U.S. Supreme Court in *Portuguese-American Bank v. Welles*.[243] The case concerned a construction contract with a prohibition on the assignment of payment rights without the promisor's consent. The promisee nevertheless purported to assign the payment rights. When the promisee entered bankruptcy proceedings, the assignee sought to claim priority over the proceeds of the debt. The nonassignment clause was evidently inserted for the promisor's benefit and, as it turned out, the promisor was happy to pay either the promisee or the

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236. *See infra* Section III.A.

237. *See infra* Section III.B.

238. *See infra* Section III.C.

239. *See infra* Section III.D.

240. The assertion also appears in more qualified, less objectionable, forms. *See, e.g.*, E. ALLAN FARNSWORTH, CONTRACTS §11.1, at 745 (1982) ("Since a contract right is one kind of property, many of the rules governing its transfer are similar to the rules of property law governing the alienation of land and chattels."); SCOTT & KRAUS, *supra* note 26, at 1004 ("An executory contract is a valuable property right, and, as with most such rights, it is (within certain limitations) transferable to third parties.").

241. *See, e.g.*, RESTATEMENT (SECOND) OF PROPERTY: DONATIVE TRANSFERS § 4 (AM. LAW. INST. 1983).

242. Glenn, *supra* note 115, at 623 ("It requires a statute to impair that freedom of transfer, which is part of the concept that a chose in action is really 'property' and, being such, is by its very nature assignable.").

243. 242 U.S. 7 (1916). A decade earlier, an English judge had expressed the same idea, claiming that "a debt must be regarded as a piece of property capable of legal assignment in the same sense as a bale of goods." Fitzroy v. Cave, [1905] 2 K.B. 364 (CA) 373 (Eng.). *Fitzroy*, did not involve a nonassignment clause. *Id.*; *see also supra* text accompanying notes 122–125.

assignee. The assignee had a strong case that the nonassignment clause was simply irrelevant to the dispute over the proceeds of the debt.[244] Justice Holmes's pronouncements in favor of the assignee's position, however, went well beyond the context in which the dispute arose. He stated that a debt is "property in the hands of the creditor" and that it was "not illogical" to treat it like a chattel.[245] In the same way that a contract for the sale of a horse cannot restrain the future alienation of the horse in the buyer's hands, he said, a contract cannot restrain the future alienation of claims to debts arising under that contract.[246]

Holmes is right to say that it is "not illogical" to treat a debt claim as being relevantly similar to a horse. But it is also "not illogical" to treat it differently from a horse. In more famous writings, Holmes himself stressed the limits of this kind of logical claim in law.[247] Legal rules are determined less by syllogism than by "[t]he felt necessities of the time, the prevalent moral and political theories, institutions of public policy, avowed or unconscious, even the prejudices which judges share with their fellow men."[248] In *Portuguese-American Bank*, however, Justice Holmes does not elaborate on the underlying reasons, felt necessities, theories, or prejudices that had motivated judges to move all the way from the idea that debt claims could not be assigned to an approach that all debt claims must be assignable. Presumably, the underlying idea is that the reasons for ensuring the alienability of rights in tangible property apply with the same force to in personam contractual claims. Yet contractual claims are at least potentially different from tangible property in multiple respects. For example, as an English judge has pointed out, "[i]n the case of real property there is a defined and limited supply of the commodity . . . . But no such reason can apply to contractual rights: there is no public need for a market in choses in action."[249]

There are at least two problems with the use of the property idea to justify the law's pro-transferability policy. First, it is not the case that categorizing a right as "property" means it must be alienable without restriction.[250] Second, even if property is, by necessity, transferable, it is not clear that contractual rights are property rights in the *relevant* sense of the term. The argument that contract is property thus assumes what it seeks to establish: that contractual rights are transferable. Calling contractual rights property in this context is therefore more of a rationalization or a rhetorical flourish rather than an independently significant idea. Later courts and commentators have generally abandoned it—the *Restatement (Second)*, for example, states that proprietary reasoning has "limited application" to contractual rights.[251]

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244. *See* 1 GILMORE, *supra* note 17, at § 7.8.

245. *Portuguese-Am. Bank*, 242 U.S. at 11.

246. *Id.*

247. OLIVER WENDELL HOLMES, THE COMMON LAW 1 (1882).

248. *Id.*

249. Linden Gardens Trust v. Lenesta Sludge Disposals Ltd., [1994] 1 AC 85 (HL) 107 (appeal taken from Eng.).

250. *E.g.*, Susan Rose-Ackerman, *Inalienability and the Theory of Property Rights*, 85 COLUM. L. REV. 931 (1985).

251. RESTATEMENT (SECOND) OF CONTRACTS § 322 cmt. a (AM. LAW INST. 1981).

B. Protecting Transferee Interests

The analogy to property law's rules on alienation suggests that the pro-transferability policy might be based on an externalities rationale. Certainly, the content of contract law may be affected by the interests of third parties. Where, for example, a contract inflicts a harm on a third party, it might be made criminal or unenforceable, or it might be interpreted in such a manner as to avoid harm to the third party.[252] It would be a stretch to say that the decision of the parties to create a nontransferable right "harms" a potential transferee. Still, if a contractual right is nonassignable, its lack of assignability makes the person who would otherwise acquire that right worse off than she otherwise would be. And indeed, mandatory assignability is sometimes justified on the simple ground that it will improve the position of transferees of contractual rights. This seems to be what defenders of the policy of free assignability mean when they say, for example, that the policy "go[es] to the root of freedom and sanctity of contract which are cornerstones of market based economies,"[253] or that "lenders and assignees who engage in legitimate and useful business operations should be protected and such lenders and assignees are potentially at risk from nonassignment clauses."[254]

The weakness of this argument is that it gives no systematic reason to favor the interests of potential transferees over those of promisors who wish to avoid being liable to such a transferee. And where the parties have agreed to a nonassignment clause, there is a systematic reason to think that the transferee's interest is weaker. To the extent that making a right transferable will increase the value of that right,[255] the interests of a transferee who would be willing to purchase it are already represented in the contractual negotiation. The promisee, anticipating potential gains from the transfer, has an incentive to bargain for transferability.[256] If the parties to the contract nevertheless agree on non-transferability, the fact that someone else would prefer the right to be transferable is not a genuine externality.[257]

Non-transferability could, however, harm a transferee in another way. If non-transferability comes as a surprise, the transferee might have paid money to the promisee in the erroneous belief that the right was transferable, and it may now find itself unable to recoup its money. But if the purported transferee knows or could have readily discovered that the right is transferable, its interests are adequately protected. Consider *Bank of America, N.A. v. Moglia*, which concerned an attempt to grant a

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252. Aditi Bagchi, *Other People's Contracts*, 32 YALE J. ON REG. 211, 212 (2015) (arguing that "[t]extual ambiguity should be resolved to avoid compromising the legally-recognized interests of third parties").

253. Akseli, *supra* note 19, at 662.

254. McCormack, *supra* note 51, at 426. McCormack is reciting, rather than embracing this argument.

255. *See supra* Section I.A.

256. *Cf.* Merrill & Smith, *supra* note 21, at 30 ("The costs [of idiosyncratic property rights] to potential successors in interest will … be mediated through the price mechanism.").

257. Beale, Gullifer, and Paterson support the nullification of nonassignment clauses by saying that such clauses "seem to have an effect on receivables financing that is out of proportion to the benefits that the [nonassignment clause] will bring to the customer." Beale, Gullifer & Paterson, *supra* note 53, at 229. The basis for this comparative judgment is unclear.

security interest in assets held on trust for the corporation's executives.[258] The contract between the corporation and the trustee stated:

> [The] Trust Corpus . . . shall remain at all times subject to the claims of the general creditors of [the corporation]. Accordingly, [the corporation] shall not create a security interest in the Trust Corpus in favor of the Executives, the Participants [a term that apparently refers to retired executives] or any creditor.[259]

Despite this clear prohibition, the corporation nevertheless purported to create a security interest in favor of Bank of America. Because the clause did not contain the "magic words," discussed in Section II.C.1 above, the bank argued that the clause should be interpreted to preserve the assignability of the right.[260] However, unlike many other jurisdictions, Illinois law does not require "magic words" to convince the court that a right is nonassignable.[261] The Seventh Circuit thus gave effect to the nonassignment clause and refused to recognize the bank's security interest in the trust.

The court in *Moglia* had little sympathy for the bank's attempt to evade the nonassignment clause. Judge Posner pointed out that the bank "knew, if it bothered to read the trust agreement along with the other documents that defined [the corporation's] assets, as it should have done and no doubt did do, that the security interest it was acquiring would not cover the . . . trust."[262] The bank was thus not in a position analogous to that of a good-faith purchaser without notice of the restriction. Moreover, "if the recipient's purchaser knows exactly what he is (not) getting, a refusal to enforce the restriction merely confers a windfall on him."[263] The *Moglia* case was governed by Illinois law; had it been governed by the law of a state adopting the "modern view," the bank would have gained precisely such a windfall.

C. Increasing Liquidity by Reducing Information Costs

The *Moglia* case suggests a way for the externalities argument to be stated in a more compelling form. It illustrates that if the parties to contracts are free to determine whether or not the rights they create are transferable, a potential transferee is required to check whether or not the right it seeks to acquire is transferable. As Max Weber noted, "[a]dvanced trade . . . needs not only the possibility of transferring legal claims but also, and quite particularly, a method by which transfers can be made legally secure and which eliminates the need of constantly testing the title of the transferor."[264] The problem with contractually agreed restrictions on alienation, the

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258. 330 F.3d 942, 942 (7th Cir. 2003).

259. *Id.* at 946 (fourth alteration in original) (emphasis omitted).

260. *Id.* at 946 ("[The bank] argues that Illinois law . . . will enforce a contractual antiassignment provision . . . against an assignee only if the provision states that the assignor has no power, and not merely no right, to assign.").

261. *See, e.g.*, *In re* Nitz, 739 N.E.2d 93, 96, 101 (Ill. Ct. App. 2000)

262. *Moglia*, 330 F.3d at 948.

263. *Id.*

264. MAX WEBER, ON LAW IN ECONOMY AND SOCIETY 122 (Max Rheinstein, ed. 1967).

argument might go, is that their very possibility makes it costly for potential transferees to determine whether or not a given contractual right is subject to such a restriction. This rise in transaction costs means that even where the parties *do* seek to create a transferable right, efficient transfers may not occur because potential transferees find it too costly to verify that they are transferable. This may be what defenders of the pro-transferability policy mean when they refer to the "argument about liquidity and cost of credit and the need for the workings of private law to foster the former and lower the latter,"[265] or when they say that it is "important that legal rules based on freedom of contract do not impair the free flow of intangibles in the stream of trade."[266]

The argument seems to have appeared only in a terse, intuitive form, but it might draw support from recent work on the economics of property rights by Merrill and Smith.[267] Merrill and Smith explain why freedom of contract does not and should not always prevail in the creation of property rights. The law of estates in land, for example, limits the parties to a fixed list of possible interests: fee simple, defeasible fee simple, life estate, and lease. In explaining why property rights, unlike contract rights, are restricted to a limited number of standardized forms, Merrill and Smith suggest that "[t]he root of the difference . . . stems from the in rem nature of property rights: When property rights are created, third parties must expend time and resources to determine the attributes of these rights, both to avoid violating them and to acquire them from present holders."[268] In making the case for the law to insist on standardized bundles of rights, Merrill and Smith stress the informational advantages for three classes of persons: potential duty holders, potential transferees, and other market participants dealing with similar kinds of assets.[269] Crucially, Merrill and Smith contend that those who create property rights lack adequate incentive to conform to the optimal standard-form bundles of rights.[270] Accordingly, the law limits party choice by only permitting a closed list or *numerus clausus* of property rights to bind third parties.

The information-cost considerations explored by Merrill and Smith are undoubtedly relevant to the transferability of contractual rights. For one thing, the original parties to a contract will often themselves wish to reduce information costs for third parties by opting in to standard-form transferable contracts—for example, in financial markets.[271] Moreover, Merrill and Smith contend that some form of legally mandated standardization prevails in the law of assignment. While the parties are free to customize the terms of the contract, promisees appear not to be able to

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265. Akseli, *supra* note 19, at 652.

266. Goode, *supra* note 51 at 300.

267. Merrill & Smith, *supra* note 21. *see also* Smith, *supra* note 24, at 148.

268. Merrill & Smith, *supra* note 21, at 8 (emphasis omitted).

269. *Id.* at 27–28.

270. *Id.*

271. The need for standard terms in investment markets was noted by Karl N. Llewellyn, *What Price Contract?—An Essay in Perspective*, 40 YALE L.J. 704, 721 (1931). For a more recent discussion, see Kenneth Ayotte & Patrick Bolton, *Covenant Lite Lending, Liquidity, and Standardization of Financial Contracts*, *in* RESEARCH HANDBOOK ON THE ECONOMICS OF PROPERTY LAW 174 (Ayotte & Smith eds., 2011).

create complex forms of ownership in contractual rights.[272] In assignment, the assignee "steps into the shoes" of the transferor and becomes something like a fee simple owner. The law does not recognize complex forms of future interest in contractual rights. This simplification relieves non-parties of the burden of grasping an extra layer of complexity, though they must still "process" the contract terms themselves.[273]

To this, Merrill and Smith might have added that the law recognizes a second standard form of transfer for contractual rights to payment: the negotiable instrument.[274] By choosing to embody a promise to pay in the recognized form, the parties opt in to a set of transfer rules, including one that precludes the promisor from raising claims and defenses that it would have against the promisee. The transferee of a negotiable instrument who qualifies as a holder in due course does not simply step into the shoes of the promisee: her position may be better, because the right to payment does not depend on whether the promisee has done what is necessary under the contract to earn the right to payment. This feature of negotiable instruments greatly economizes on information costs: the transferee need not concern herself with the contents of the contract or the relationship between the promisor and promisee.

Information-cost concerns, however, seem unlikely to justify the current law's mandatory and quasi-mandatory rules in favor of transfer. First, information costs are so significant in property law because the rights in question are rights in rem. Contractual rights, by contrast, are typically rights in personam corresponding to duties owed by a single person. The class of parties potentially affected by confusion is thus smaller: it is essentially limited to potential transferees of the right and to others dealing in similar assets. [275] Moreover, it is usually not difficult to discern whether a contractual right is subject to a nonassignment clause: such clauses are easily discoverable by a quick review of the contractual text.[276] To understand what she might be acquiring, a potential transferee of a contractual right will typically wish to inspect the contract anyway.[277]

Moreover, as Merrill and Smith stress, the law's aim is not to standardize property rights but to encourage the optimal degree of standardization.[278] Limiting party

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272. *See* Merrill & Smith, *supra* note 21, at 55; *see also* Smith, *supra* note 24, at 151.

273. Merrill & Smith, *supra* note 21, at 55.

274. *See supra* text accompanying notes 111–115.

275. Contractual rights also entail tortious duties in third parties not to intentionally induce the promisor to breach the contract, but these duties add little by way of information costs to third parties because they apply only where the third party is aware of the contract. *See* Smith, *supra* note 24, at 151.

276. Richard Calnan, *Ban the Ban: Prohibiting Restrictions on the Assignment of Receivables*, 3 J. BUTTERWORTHS INT'L BANKING & FIN. L. 136 (2015). Admittedly, under current law, it is often difficult to predict whether an assignment is permissible, but most of this uncertainty derives from the refusal of many (but not all) courts to give nonassignment clauses their conventional meaning. *See supra* Section II.C.

277. *See* Beale, Gullifer & Paterson, *supra* note 53, at 219 (presenting empirical evidence that financial institutions in England considering taking assignments of receivables search the supplier's contracts for nonassignment clauses, but also for other kinds of problematic clauses).

278. Merrill & Smith, *supra* note 21, at 38 ("[W]hat we want is not maximal standardization—or no standardization—but optimal standardization.").

choice economizes on information costs, but it increases "frustration costs" by preventing the parties from doing what they wish. Merrill and Smith contend that these frustration costs are not so great in the case of a *numerus clausus* of rights in rem.[279] The *numerus clausus* rarely stops parties from doing as they wish; rather, it makes it more difficult or costly to achieve their goals, requiring them to combine the standardized building blocks of property law.[280] The equivalent position in the area of assignability would be for the law to channel the parties into a limited number of permissible forms or "boxes," some of which would permit assignability and some of which would not.

By contrast, the law's insistence on mandatory assignability entails large frustration costs. Parties who wish to make rights, falling within the scope of these rules, nontransferable appear to have no way of achieving their aim. Supporters of mandatory transferability sometimes contend that the harm of overriding a nonassignment clause is minimal—especially where the promisor's duty is simply to pay money.[281] Such arguments underestimate the significance and breadth of reasons that promisors wish to avoid transfer.[282]

To the extent that the law's policy is expressed in quasi-mandatory rules, one might say that these simply raise the cost of achieving the parties' goals: one can often restrict transferability if one finds and pays a lawyer with knowledge of the canons of construction deployed by many courts. Still, the effect of these quasi-mandatory rules is often to frustrate party intention. The modest information-cost savings to be gained from relieving transferees of the burden of looking at contracts and finding nonassignment clauses seem unlikely to outweigh the large frustration costs inflicted on parties who wish to restrict transfer but are unable to do so—and in particular, on those who reasonably but wrongly believe that they have done so.

D. Paternalism for Promisees

While most attempts to defend compulsory transferability focus on externalities, some recent arguments focus on the interests of promisees. Defenders of bans on nonassignment clauses, for example, speak generally about the need for businesses to obtain credit using their contractual rights as security or collateral for loans. Allowing a nonassignment clause to take effect "may increase the cost of credit" to the promisee who has agreed to it.[283] Over time, the promisee may become concerned that the promisor will become insolvent and may wish to shift the risk to a transferee in exchange for a lower recovery.[284] To be sure, this possibility gives a concerned promisee reason to bargain for the insertion of an express assignment clause or, at the least, to refuse to agree to a nonassignment clause.

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279. *See id.* at 55–57.

280. *See id.* at 55.

281. For example, Kramer argues that the cost of bare rights to payment does not vary with the other party's conduct, and suggests that this consideration supports Article 9's mandatory assignability rule. Kramer, *supra* note 24, at 57–58.

282. *See supra* Section I.A.

283. Akseli, *supra* note 19, at 662.

284. *Id.* at 662–63.

Again, however, any systematic analysis must weigh the advantages of transferability against the economic benefits that accrue to the promisor from a valid nonassignment clause. The advantages of transferability do not alone provide any general reason to think that promisees who wish to have the power to assign their rights cannot adequately protect themselves by bargaining for assignability. Where the parties have chosen to prohibit assignability, we can generally assume that the benefit to the promisor of keeping the contractual relationship between the original parties exceeds the benefit to the promisee of being able to transfer rights to someone else.

An argument based on the interests of promisees, then, must provide a special justification for contract law to depart from its usual assumptions and to engage in a form of paternalism. Along these lines, in recent debates outside the United States, mandatory assignability rules have sometimes been justified with reference to the needs of small-business promisees. Recent efforts to introduce a mandatory assignability rule for receivables in the United Kingdom have been largely justified on this basis.[285] The "small-business" rationale has also been used to support the U.N. Convention on Assignment of Receivables in International Trade,[286] even though the Convention applies only to cross-border financing transactions to which small businesses are unlikely to be parties.[287]

Inequality of bargaining power between businesses is not generally considered a sufficient reason to invalidate contract terms.[288] So why might nonassignment clauses be singled out for such treatment? As far as I am aware, supporters of mandatory assignment rules have not addressed this question. But they might argue that promisees who would be harmed by nonassignment clauses are systematically unlikely to consider cases outside the usual run of contractual performance between two parties.[289] Moreover, nonassignment clauses usually form part of standard form contractual documents. In some instances, it may be because nonassignment suits the interests of powerful purchasers of goods and services who have the power to require suppliers to agree to a barrage of terms.

Still, it is unlikely that the current mandatory or quasi-mandatory assignability rules, which apply regardless of whether the promisee is a small business, actually serve the interests of small businesses. Small businesses are often debtors rather than creditors in contracts for goods and services, and like large businesses, they may have a host of reasons to restrict the assignment of rights against them.[290] Moreover,

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285. Beale, Gullifer & Paterson, *supra* note 53, at 205 (referring to "a concern that [bans on assignments] at best increase the cost of an essential form of credit and at worst starve businesses of credit—in particular, smaller businesses which are most dependent on their receivables to raise financing").

286. *See* Akseli, *supra* note 19, at 651–52.

287. Akseli recognizes this point but suggests that the Convention may aid small businesses indirectly, by encouraging developing countries to follow its lead in their domestic laws. *Id.* at 661.

288. Daniel D. Barnhizer, *Inequality of Bargaining Power*, 76 U. COLO. L. REV. 139, 144 (2005).

289. *See* Melvin Aron Eisenberg, *The Limits of Cognition and the Limits of Contract*, 47 STAN. L. REV. 211, 240 (1995).

290. Calnan, *supra* note 276, at 137.

policies that either render nonassignment clauses explicitly ineffective or interpret them in a manner contrary to their apparent meaning are likely to fall harder on smaller businesses who do want to restrict assignability. In contrast, large businesses are more likely to be advised of the law and hence less likely to trade away some other contractual term in return for an (ineffective) nonassignment clause.

Note that small businesses may also be prejudiced by express clauses that make rights against them assignable, but there appears to be no clamor to protect them from such clauses. When one combines these observations with the fact that contract law rarely declines to enforce terms simply because they are unfavorable to small businesses,[291] it is fair to suspect that the "small business" argument often serves as a fig leaf for the interests of large, well-organized financial institutions whose interests as transferees would be served by mandatory and quasi-mandatory assignability rules.

IV. IMPLICATIONS

If the law is unduly weighted towards transferability, how should the balance be redressed? It is easier to show that the current regime is unjustified than to figure out what exactly should replace it. Nevertheless, in Part IV, I examine, in turn, whether any mandatory assignability rules are justified,[292] how courts should interpret clauses concerning assignment, [293]and the default rules courts should apply where the parties have not provided guidance on the assignability issue.[294] In addition, I suggest that a closely analogous area of the law, agency law's doctrine of the undisclosed principal, is similarly biased towards an impersonal view of contractual rights and is likewise in need of reform.[295]

A. Mandatory Assignability Rules

As argued above, the current, wide-ranging mandatory assignability rules recognized by U.C.C. Article 9 do not appear to be justified either by an externalities-based or a paternalism-based rationale.[296] It may be possible, however, to justify more narrowly drawn exceptions to freedom of contract.

The perceived need to ensure that small businesses have access to receivables financing, for example, might conceivably justify a specific mandatory rule directly aimed at helping such businesses. If policymakers conclude that large-business promisors systematically force their small-business promisee-suppliers to accept nonassignment clauses, legislative action might be justified on paternalism grounds. Recent experience in England may prove instructive. There, the U.K. government initially sought to introduce a general mandatory assignability rule for receivables,

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291. *See* Larry T. Garvin, *Small Business and the False Dichotomies of Contract Law*, 40 WAKE FOREST L. REV. 295, 297 (2005).

292. Section IV.A.

293. Section IV.B.

294. Section IV.C

295. Section IV.D.

296. *See supra* Sections III.B–D; *see also* Ayres, *supra* note 163, at 2087 ("[P]aternalism and externalities provide the ur-justifications for both mandatory rules and sticky defaults").

justifying the proposed rule with reference to the needs of small businesses.[297] Critics of the reform noted that the initial proposals restricted contractual freedom whether the promisee was a large business or a small business.[298] In response to these criticisms, the government revised the rules so that, as enacted, they exempt contracts where the promisee is a large enterprise.[299]

Even when a mandatory assignability rule is limited to circumstances where the promisee is a small or medium-sized business, the arguments in favor of overriding freedom of contract must overcome the standard objections to helping "weaker" parties avoid contract terms that disserve their interests.[300] Declining to enforce a particular term does not change the parties' bargaining power. If "stronger" promisors know that they are unable to restrict transferability, they are likely to pass the cost of this limitation on to the "weaker" promisees, either by lowering the prices that they pay for the promisee's goods or services or by insisting on other terms that are less favorable to the promisee. Moreover, if the U.K. government's reform were genuinely motivated by an interest in helping small businesses—rather than by the financial-institution transferees who would certainly benefit from a mandatory rule—proponents of such a rule would have to explain why this kind of term has been singled out for special treatment over other unfavorable terms offered to small businesses.

Another plausible candidate for a justifiable mandatory rule concerns promisee bankruptcy. Current bankruptcy law overrides many nonassignment clauses in the event of a promisee's bankruptcy and gives the trustee the power to assign many contractual rights (and duties) that would otherwise be unassignable.[301] The rationale for this interference with freedom of contract is that it facilitates corporate reorganization, serving the public interest by enabling troubled businesses to recover or to increase the amount paid to their creditors. From this perspective, allowing promisors to bargain for a right to veto the sale of the bankrupt entity's assets could be considered a significant externality. Moreover, overriding nonassignment clauses may not entail a major setback to the promisor's interests. Many such clauses are inserted to prevent opportunistic transfers by the promisee herself—the bankruptcy proceeding hands the decision to the bankruptcy trustee, who is also subject to court supervision. Arguably, however, the law should allow parties who wish for the nonassignment clause to apply even on bankruptcy to stipulate for that result by explicit contractual provision, rather than impose the current, fully mandatory rule.[302]

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297. *See* Calnan, *supra* note 276.

298. *See id.*

299. Business Contract Terms (Assignment of Receivables) Regulations 2018, SI 2018/1254, art. 3 (Eng. & N. Ir.).

300. *See, e.g.*, Richard Craswell, *Two Economic Theories of Enforcing Promises*, *in* THE THEORY OF CONTRACT LAW: NEW ESSAYS, 19 (Peter Benson ed., 2001).

301. 11 U.S.C. § 365(f) (2012); *see* Ayotte & Hansmann, *supra* note 24, at 747–49; *see also* Kenneth Ayotte & Henry Hansmann, *A Nexus of Contracts Theory of Legal Entities*, 42 INT'L REV. L. & ECON. 1, 9–10 (2015).

302. *See* Ayotte & Hansmann, *supra* note 24, at 748 n.66 (stating that there are "good reasons" to make bankruptcy override a default rather than a mandatory rule).

B. Interpreting Assignability Clauses

In the absence of a reason based on paternalism or externalities,[303] courts should generally give nonassignment clauses their conventional meaning. Indeed, many commentators have suggested that the argument for a "plain meaning" interpretation is even stronger where, as here, third parties have an interest in understanding what the contract means.[304] Hence, the general trend towards strict construction of nonassignment clauses should be abandoned. Where a contract says that a promisee "shall not assign" or "may not assign" its rights under the contract, this language should be construed to deprive the promisee of the power to assign its rights.[305] The word "assignment" should be construed to mean "assignment" (rather than "delegation").[306] And where a contract purports to bar assignment of rights generally, the bar on assignment should extend to attempted transfers of rights to sue for breach of contract and for money earned under the contract.[307] While these proposals run counter to the prevailing wind, they are far from radical: some courts have declined to adopt the "modern approach" to interpreting nonassignment clauses.[308]

As in the case of fully mandatory rules, more narrowly drawn interpretive practices favoring assignability could potentially be justified. One testing ground for such practices is in litigation over whether blanket nonassignment clauses should be interpreted to include an implied limitation on the right of the promisor to unreasonably refuse consent to an assignment. Courts have sometimes reached this conclusion. In *Larese v. Creamland Dairies, Inc*., the Tenth Circuit found that a franchisor could not unreasonably refuse consent to a franchisee's request to assign its interest, even though the written contract contained no such restriction.[309] The court recognized that its ruling would have been different had the franchisor insisted on an explicit contractual provision allowing it to refuse consent unreasonably.[310] Franchise contracts are almost always drafted by franchisors; thus, the purpose of adopting this sticky default, according to the court, was "to insure that the franchisee

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303. *See* Ayres, *supra* note 163, at 2087 ("[P]aternalism and externalities provide the ur-justifications for both mandatory rules and sticky defaults").

304. *See, e.g.*, Scott, *supra* note 82, at 870.

305. *See supra* Section II.C.1.

306. *See supra* Section II.C.2.

307. *See supra* Section II.C.3.

308. *See, e.g.*, Bank of Am., N.A. v. Moglia, 330 F.3d 942, 948 (7th Cir. 2003) (stating that Illinois law does not adopt the "magic words" canon); Travertine Corp. v. Lexington-Silverwood, 683 N.W.2d 267, 273 (Minn. 2004) (Minnesota law does not adopt the "magic words" canon); Star Windshield Repair, Inc. v. W. Nat. Ins. Co., 744 N.W.2d 237 (Minn. Ct. App. 2008), *rev'd on other grounds*, 768 N.W.2d 346 (Minn. 2009) (finding that general nonassignment clause prohibited post-loss assignment of insurance claim under Minnesota law).

309. 767 F.2d 716, 718 (10th Cir. 1985); *cf.* Taylor Equip., Inc. v John Deere Co., 98 F.3d 1028, 1034 (8th Cir. 1996) (rejecting *Larese* and holding that a facially unrestricted nonassignment clause in a franchise contract was not subject to a reasonableness limitation).

310. *Larese,* 767 F.2d at 718 ("We do not hold that a provision which expressly grants to the franchisor an absolute right to refuse to consent is unenforceable when such an agreement was freely negotiated.").

is put on notice" of the franchisor's broad assignment power.[311] The court's decision was influenced by its characterization of the franchise relationship as near-fiduciary.[312] Its departure from a plain-meaning interpretation of the clause was thus based on a potentially compelling (soft) paternalist rationale rather than on a general belief in free assignability.

C. The Selection of Defaults

This Article has focused mainly on nonassignment clauses because most contemporary written contracts do contain clauses concerning assignment. But some contracts make no such provision, in which case the court will need to fill the gap in the contract where a promisee purports to assign the right and the promisor objects. Additionally, other contracts only make partial provision concerning assignability, in which case a default will again be needed to provide for those cases not covered by the clause.

As noted above, the current default position is that contractual rights are assignable, unless the assignment violates public policy or would result in a material change in the promisor's duty.[313] The current default is heavily weighted towards transferability, especially because the "material change" exception is so narrow. Notably, with respect to money claims, a change in the identity of the right holder is seemingly never regarded as a material change, even though the change, in reality, may be highly consequential.

The selection of default rules is the subject of an extremely large economic literature.[314] The standard approach is that default rules should save on transaction costs, either by attempting to mimic what the individual parties would have contracted for had they reached agreement on the matter (a "tailored default") or by estimating what a majority of parties, to contracts in general or to a certain class of contracts, would have agreed to (an "untailored" majoritarian default).[315] The current assignability rules are not tailored defaults; courts do not seem to make much effort to figure out what the particular parties to the transaction would have wanted. The rules do sort cases governed by the general rule, where assignability is considered an appropriate default, from those governed by the exceptions, for which non-assignability is the default. The virtue of the law's current default approach is that it is reasonably predictable to lawyers familiar with the case law, because the exceptions to the default are so rarely applicable.

It is difficult, however, to argue that the current rules are majoritarian. Would most parties to most contracts agree to assignability? At best, the current default rules could be defended as a crude attempt at capturing generic party intent. But in many

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311. *Id.*

312. *Id.* at 717 ("[W]e find that the franchisor-franchisee relationship is one which requires the parties to deal with one another in good faith and in a commercially reasonable manner.").

313. *See supra* Section II.A.

314. *See, e.g.*, Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules,* 99 YALE L.J. 87, 91–92 (1989); David Charny, *Hypothetical Bargains: The Normative Structure of Contract Interpretation*, 89 MICH. L. REV. 1815 (1991); Scott, *supra* note 82, at 847.

315. Ayres & Gertner, *supra* note 314, at 91–92.

cases, the default rules find transferability where the parties would have agreed to non-transferability. In particular, the refusal to countenance a bad-faith exception to the presumption—so, for example, rights can be transferred to the promisor's competitor or enemy—is difficult to justify. From the standpoint of a majoritarian approach to default rules, the case for shifting towards a general starting point of non-assignability, or for at least increasing the size of the exceptions to the assignability default, is thus strong.

To be sure, the literature on contract law also recognizes the possibility that non-majoritarian default rules might be justified in the service of efficiency or fairness. To the extent that the current assignability default does not reflect what the parties to a particular contract would have agreed, could it instead be justified as a deliberately non-majoritarian "penalty default"?[316] The purpose of such a default would be to provide an incentive to the party whose interests are harmed by the default to bargain around it. One potential function for a penalty default is to force a party or parties to disclose information to *third parties*. If a promisor who dislikes the default rule of assignability successfully negotiates a non-assignability clause, the presence of that clause will inform third parties of the parties' agreement, including potential transferees seeking to discern whether or not the right is transferable, and courts later charged with resolving a dispute over whether the rights are transferable or not. Based on the analysis in this Article, however, one might just as easily defend the opposite position as a penalty default. The law could generally assume that rights are nonassignable, unless the parties have agreed otherwise. For a large class of cases, this would be a non-majoritarian default. The promisee who wishes to acquire a transferable right would then bear the burden of insisting on an assignability clause, thereby providing information to potential transferees and to courts later charged with resolving a dispute over the right's transferability.

The current pro-assignability presumption might alternatively be defended as a mechanism for forcing promisors to inform *promisees* of the issue of transferability. Promisees might not otherwise consider the issue during negotiations. By requiring promisors who to restrict assignment to the seek to include a nonassignment clause in the contractual text, the law makes promisors provide notice to promisees, which might prompt the promisee to reject the clause or to bargain for a clause providing for transferability. Again, however, the opposite rule might just as well be appropriate: arguably, promisors who are later surprised by transferability are in greater need of the benefit of an "information-forcing" default than promisees are. That was the conclusion of the Tenth Circuit in the *Larese* case discussed in the previous section;[317] but as that case illustrates, it is difficult to generalize about the relative knowledge of promisors and promisees.

Admittedly, the treatment of express nonassignment clauses provides a more pressing case for reform than the general default rule of assignability. What is crucial is that the parties are generally free to displace the default. Arguably, the most important consideration in the selection of this particular default is clarity so that the parties know whether or not they have the power to assign. Moreover, courts should tread carefully when changing preexisting default rules: however non-majoritarian

316. *Id.* at 98.
317. *See supra* Section IV.B.

the current defaults may be, it is likely that some parties have entered into contracts with the expectation that they will be applied. But the current extent of the pro-assignability default nevertheless sits uneasily with contract law's basic ideas.

D. Agency Law's Undisclosed Principal Doctrine

The argument of this Article also has implications for agency law's undisclosed principal doctrine. T enters into a contract with A believing that A is contracting in her own right. In fact, A is acting as UP's agent. Under the undisclosed principal doctrine, T has entered into a contract with UP even if T knew nothing of UP's existence at the time she entered into the contract.[318] The portion of the doctrine that holds T liable to UP is thus similar to an unexpected assignment.

Unlike the law's transferability bias, the undisclosed principal doctrine has not escaped scholarly criticism.[319] The doctrine has been continually called an "anomaly"[320] that is "inconsistent with the elementary doctrines of the law of contract."[321] The doctrine does not always apply: as in the case of assignability, some rights are considered too personal to be held by undisclosed principals, but, as in the case of assignability, this exception has been construed narrowly.[322] Unlike in the case of assignability, there do not seem to be any mandatory rules preventing the parties' ability to exclude it,[323] but, as in the case of assignability, the courts seem to place a narrow construction on attempts to limit its operation by agreement. For example, the *Restatement (Third) of Agency* states that a nonassignment clause does not exclude the undisclosed principal doctrine[324]—even though the effect of the undisclosed principal doctrine is almost precisely the effect that a nonassignment clause is aimed at avoiding. The effect of these rules is often to bring parties into contractual relationships that can hardly be called consensual.

The undisclosed principal doctrine, to the extent that it confers rights to sue T on UP,[325] has a fundamentally similar effect to the assignability rules considered by this

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318. *See* RESTATEMENT (THIRD) OF AGENCY § 6.03 (AM. LAW INST. 2006) ("When an agent acting with actual authority makes a contract on behalf of an undisclosed principal, (1) unless excluded by the contract, the principal is a party to the contract . . . and (3) the principal, if a party to the contract, and the third party have the same rights, liabilities, and defenses against each other as if the principal made the contract personally.").

319. For an economic defence of the doctrine, see Eric Rasmusen, *Agency Law and Contract Formation*, 6 AM. L. & ECON. REV. 369 (2004) (defending a default rule of liability to the undisclosed principal).

320. *See, e.g.*, James Barr Ames, *Undisclosed Principal—His Rights and Liabilities*, 18 YALE L.J. 443, 443 (1909) (maintaining that the doctrine of the undisclosed principal "ignores . . . fundamental legal principles . . . [and] should be recognized as an anomaly").

321. Frederick Pollock, Note, 3 L.Q. REV. 358, 359 (1887).

322. *See* Sig M. Glukstad, Inc. v. Lineas Aereas Paraguayas, 619 F.2d 457, 458 (5th Cir. 1980) (holding that a freight forwarder, acting as an agent for undisclosed principal, could obtain insurance in its own name on behalf of undisclosed principal).

323. The Restatement recognizes T's ability to protect herself from the doctrine by including an express contractual provision. RESTATEMENT (THIRD) OF AGENCY § 6.03(1).

324. *Id.* § 6.03 cmt. d.

325. The undisclosed principal doctrine also allows T to sue UP once T learns of UP's existence, a rule that is readily defensible if UP can sue T. *See id.* § 6.03(3).

Article. One commentator defending the undisclosed principal doctrine has said that it is "no more inconsistent or anomalous than the rule allowing assignees to bring an action in contract."[326] Indeed, the most common way to defend the undisclosed principal doctrine is by analogy to the law of assignment.[327] According to Randy Barnett, "[t]he close theoretical relationship between undisclosed agency doctrine and the law of assignment also helps explain why and when persons may be 'forced' to deal with parties to whom they might object."[328] To the extent this argument has successfully undercut the argument for the law's pro-transferability bias, then, it also provides new reasons to question the breadth of the undisclosed principal doctrine.

CONCLUSION

This Article has sought to identify and undermine contract law's bias in favor of transferability. If nothing else, it has sought to shine a critical light on a crucial aspect of contract law that has long been taken for granted. The Article can be considered a success if it provokes someone else to develop a more convincing rationale for law's refusal to respect freedom of contract on the issue of transferability. Unless such a rationale is forthcoming, courts and legislatures should work to bring the law of assignability into line with the purposes for which parties enter into contracts.

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326. Tan Cheng-Han, *Undisclosed Principals and Contract*, 120 L.Q. REV. 480, 481 (2004).

327. In addition to those quoted in the text, see Warren A. Seavey, *The Rationale of Agency*, 29 YALE L.J. 859, 879 (1920) ("[B]efore the modern doctrine of the undisclosed principal arose, [the] conception of a personal relationship in contracting parties had been destroyed by allowing contracts to be assigned."); Ernest J. Weinrib, *The Undisclosed Principle of Undisclosed Principals*, 21 MCGILL L.J. 298, 299 (1975) ("[W]e are dealing with an autonomous doctrine in the law of agency, historically derivable from assumpsit, which is similar to, but not identical with, the devices of assignment and trust . . . ." (footnotes omitted)).

328. Barnett, *supra* note 24, at 1989.