EKONOMISTA | **ARTYKUŁY**

2026, 3, 311–331
DOI: 10.52335/ekon/226493

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Economic Contract Theory and Law and Economics of Contracts: Are they twins or separate approaches? Selected overview of literature in the last decade

Ekonomiczna teoria kontraktów a ekonomiczna analiza prawa umów: bliźniacze czy jedynie spokrewnione podejścia? Wybrany przegląd literatury z ostatniej dekady

Abstract

This paper takes a closer look at the divergence of economic approaches towards contracts (agreements) with various developments of Economic Contract Theory and Law and Economics of Contracts. In order to observe the multifaceted nature of Economic Contract Theory, its three main directions are discussed, namely incentive theory, incomplete theory and transaction cost theory. To track the evolution of these two approaches, a selected survey of publications that appeared over the past decade in leading scientific journals was conducted. We conclude that Economic Contract Theory forms a distinct economic approach in contracts in comparison to Law and Economics of Contracts, but there are noticeable similarities.

Keywords: Microeconomics, Economic Analysis of Contracts, Economic Contract Theory, Law and Economics.

JEL: B40, K00, K12

Streszczenie

W niniejszym artykule bliżej przyglądamy się rozbieżnościom podejść ekonomicznych do kontraktów (umów) w kontekście różnych kierunków rozwoju teorii kontraktów ekonomicznych (Economic Contract Theory) oraz Ekonomicznej Analizy Prawa Umów. W celu uchwycenia wieloaspektowej natury teorii kontraktów ekonomicznych, omówiono jej trzy główne kierunki, a mianowicie teorię bodźców (incentive theory), teorię niekompletności (incomplete theory) oraz teorię kosztów transakcyjnych (transaction cost theory). Następnie przeprowadzono przegląd literatury mający ukazać ewolucję obu podejść, uwzględniający publikacje, które ukazały się w trakcie ostatniej dekady w wiodących czasopismach naukowych. Na koniec stwierdzamy, że – jakkolwiek zauważalne są podobieństwa – teoria kontraktów ekonomicznych stanowi odrębne podejście ekonomiczne w porównaniu z metodą używaną w Ekonomicznej Analizie Prawa Umów.

Słowa kluczowe: mikroekonomia, Ekonomiczna Analiza Prawa Umów, Ekonomiczna Teoria Kontraktów, Ekonomiczna Analiza Prawa.

JEL: B40, K00, K12

1. Introduction

If one were to ask an economist what is meant by a *contract*, the answer would very likely boil down to the following definition: *an agreement by which two parties mutually commit their behaviour*, which could be coined as a *bilateral coordination arrangement* (Brousseau & Glachant, 2002, p. 3). Further elaborating on this definition, the economist would point to actions to be taken by the parties at different times (*actions*), but would also list conditions that include uncertain future events (*contingencies*), commitment of the parties, etc. (Bag, 2018, p. 2). The above approach differs from the definition of a *contract* that a lawyer would give. The latter would refer to the existence of a *legal bond between two or more parties each of which is obliged to waive or transfer legal rights in favour of the other party (or parties*) (Posner, 2016, p. 5). Domestically, a native Polish lawyer would point to *consensual declarations of will of two or more parties (consensus)*, which constitutes *an independent and integral whole that only shapes the* legal *relationship defined in its content* (Radwański, 2009, p. 288).

This does not mean, of course, that the differences in the economic approach compared to the legal one are limited to the recognition or otherwise of the multiplicity of parties that can enter into a contract, as for economics such cases are also taken into account and subjected to an in-depth analysis (see e.g. Bolton & Dewatripont, 2005, p. 239 sq.). The difference in the two approaches, however, relates respectively to the perspective of exchange and the manner of enforcement. However, if one were to consult one of the scholarly publications on *Economic Contract Theory* (ECT), the multitude of approaches might be surprising. It might also be difficult to determine the relationship with the *Economic Analysis of Contract Law* (*Law & Economics of Contracts*, or *L&EC*). This paper explores in more detail what approach has been taken in ECT, how it differs from the Economic Analysis of Contract Law perspective, and how they have both evolved in the recent decade in the literature. For the former, it appears to be limited to the study of the state of efficient exchange, while the latter focuses on the analysis of existing contract law insofar as it contributes to such exchange within the welfare economics framework forming traditionally the foundations of Law & Economics[1].

Nevertheless, ECT does not constitute a homogeneous theory. Depending on the approach taken, one can distinguish between a static or dynamic perspective, bilateral or multilateral, and whether it is a complete or incomplete contract. The latter approach seems to unite lawyers and economists. Indeed, the former have long used the notion of a self-executing contract, i.e. one that anticipates future events and introduces all sorts of ways to resolve them. In this sense, a contract is complete, whereas a contract which does not fully define the obligations of the parties is an incomplete contract (Salanié, 2005, p. 4). Moreover, it does not matter whether it is a short-term or long-term legal relationship as long as the cooperation

[1] We note the discussion in the literature on the potential differences between the terms *Law & Economics* and *Economic Analysis of Law*, e.g. Marciano and Harnay (2019), but for the sake of clarity we do not distinguish between the two terms here and we use them intercheangably, which relates to contracts too.

between the parties can be enforced by a legal sanction (Bag, 2018, p. 2). However, the completeness or incompleteness of a contract is approached in a different way by economists from the long-term perspective, and thus even if the contract is based on unobservable relationships, it may still be complete as long as the court is able to verify them. This, of course, represents a certain simplification of the legal permissibility of interfering with a private contractual relationship, although the court may in some cases make additions to the content of the contract. Economists also place more emphasis on the possibility of renegotiating or breaching the contractual relationship originally agreed in the case of an incomplete contract, while lawyers focus on assessing the consequences in the event of a dispute arising from gaps in an incomplete contract.

This paper is organised as follows. In the first part, we focus on importance of the existence of contracts in economic analysis from the viewpoint of history. In the second part we delve into the roots of L&EC. We then focus on three theories which are associated with ECT. In the fourth part, in order to reassess the findings, we conduct an overview of literature within the leading journals for over a decade within which we analyse conducted research both in ECT and L&EC. Conclusions are presented at the end.

2. The Emergence of Importance of Contracts in Economic Analysis – Historical Perspective

The importance of the existence of contracts in understanding the functioning of decentralised social systems, including markets, has been present since the time of the philosophers of the Enlightenment, but it is only relatively recently that economists have moved in a similar direction in their analysis to recognise the role of contracts. Indeed, they had previously focused on the notion of a market and a price system, which amounted to a simplistic observation of supply and demand around an agreed price, and did not fully capture the essence of a decentralised economy. This classical approach attributed to Adam Smith was developed primarily by the 19th century French economist Léon Walras, who is widely accepted as the founder of the mathematical theory of economic equilibrium. This approach, however, is criticised for failing to take into account the costs of market functioning, and for assuming the existence of collective coordination with the effective participation of all market participants, reducing this to an unrealistic model where exchanges occur out of equilibrium in a bilateral context.

Opposition to this simplistic approach, referred to in the economic literature as the *Walrasian Theory*, led to a number of publications, of which Coase's attempt to explain the rationale for the existence of firms played a particular role. He demonstrated as early as 1937 that the presence of coordination costs in functioning markets leads to various coordination mechanisms in a decentralised economy, in particular with regard to hierarchical coordination within the firm (Coase, 1937). It was this research that initiated further a non-price explanation of the existence of firms in the market.

The breakthrough, however, came with the emergence of two new strands of research in economic science in relation to contracts, which covered both theoretical and empirical studies. The former focused on explaining the way in which participants operating in the market determine ownership rights, volumes and prices fleeced among themselves, taking into account the transaction costs that may be involved. In addition to such transaction costs, they also began to analyse the investment costs that should be reflected in the price, which was not predicted by the Walras equilibrium model. To a large extent, the development of this research focusing on price theory extended to cover the analysis of economic aggregates shaped in this way was contributed to by the economics of information, influenced by the research carried out by Akerlof and others on second-hand car markets and Arrow and Stiglitz on insurance markets (respectively Akerlof, 1970; Arrow, 1971; Stiglitz, 1977).

Empirical research linked to competition law, on the other hand, has led to a reanalysis of various contractual relationships that had hitherto been considered to reduce competitiveness, e.g. long-term cooperation agreements, because the positive effects they could potentially bring to society were not sufficiently recognised at the time (Brousseau & Glachant, 2002, p. 4). A change was made by scholars such as Demsetz and Willamson, but also Laffont and Tirole, who ultimately contributed to the emergence of the *Economics of Regulation* (Demsetz, 1976; Williamson, 1975; Laffont, 1984; Tirole, 1988).

In the same vein as suggested in the literature, we could recognise three strands within ECT, namely *Incentive Theory*, *Incomplete Contract Theory* and *Transaction Cost Theory*. These theories differ in their assumptions and consequently focus on different aspects of contracting. Importantly, the dividing line runs through such fields as the understanding of rationality, the extent of information available to parties acting in the market, and the type of external institutions in place.

Rationality within the framework of these theories is captured here according to the assumptions of Savage (Savage, 1954) or Simon (Simon, 1947). As a reminder, the former believed that market participants are endowed with a substantial rationality, which results from the complete information available to them regarding the issue they face, together with their unlimited computational capacities and with a complete and ordered set of preferences. In contrast, the latter assumed that market participants have limited computational capacity, operating in an environment where they do not know the structure of the issues that arise, leaving them in a state of uncertainty that does not allow them to enter into complete contracts. In other words, they have bounded rationality.

Subsequently, these theories differ in the extent of information available to market participants. There are several possible combinations, which lead to the variants of completeness or incompleteness together with symmetric or asymmetric availability of information. The question of the extent of the existence of external institutions and the fundamental issues on which the above theories focus will be discussed separately, as it requires an in-depth explanation which we provide in part three of this paper.

3. Law and Economics of Contracts

The Economic Analysis of Contract Law branched out naturally from the Law and Economics movement which is generally coined contemporarily as the second wave of Law and Economics (Richardson & Hadfield, 1999). Its foundations were structured within the textbooks among which Posner's Economic Analysis of Law is regarded as the most prominent (Posner, 1972). However, if one looks at the latter's contents there is only one extensive chapter devoted to the contracts following the structure of legal textbooks. It discusses the main features and problems of contractual obligations that neglect any economic foundations. However, there are some examples of other textbooks which concentrate on the bargain theory and others which prove the presence of contracts as necessary to execute binding contractual obligations (Cooter & Ulen, 1988). This appears to be exceptional, as others simply assume the existence of contracts and focus only on its economic role (Mackaay, 2013) or even limit their importance, reducing it to the relationship with responsibility (Deffains & Langlais, 2009). Even such important sources as the Oxford Handbook of Law and Economics do not pay too much attention to the economic concept of a *contract* (Parisi, 2017). although some economic foundations could be found further in more specific monographs (Kronman & Posner, 1979), again the concept of contract within Law & Economics is being missed. However, Schaffer and Ott refer to the complete contract as the blueprint for the Law & Economics analysis (Schäffer & Ott, 1986), and they refer their further analysis to this concept and how the legal system should adjust to it. Interestingly, they reconstruct theoretically the complete contract through discovery of what the parties did not explicitly or implicitly agree upon at the time of its conclusion (Bełdowski et al., 2024, p. 244).

The missing conceptualisation of contracts within L&EC may be explained from the perspective of welfare economics, as Law and Economics has adopted this perspective since the beginning (Coase, 1960, Calabresi, 1961) and it has been reaffirmed numerous times (see e.g. Shavell, 2003). In this sense, the individual contractual obligation is important as long as it contributes positively to society (see e.g. Espozito, 2022). In this vein, individual contractual obligation analysis shall be focused on the complete contract, as this may inform a judge how to adjudicate the conflict among the parties, and a legislator how to design the contractual law accordingly, to the greatest benefit for society.

Now we will look at some selected economic concepts which are utilised within ECT.

4. The Three Directions in ECT

4.1. Incentive Theory

Incentive Theory (IT) refers to the Walrasian theory in recognising that market participants and economic agents are rational in Savege's sense of the term, in particular possessing complete information with respect to the issues they face in the market

with unlimited calculating power and endowed with a complete and ordered set of preferences. Completeness of information, however, is understood to mean that although they cannot predict the future, which is random (stochastic) in nature, they do know the range of issues that may arise on the probability calculus side without being able to predict their sequence (Brousseau & Glachant, 2002, p. 8). However, the two parties to the contract do not have access to the same information, meaning that there is asymmetry, which makes the earlier Walrasian approach more realistic. Using economic terminology, if both parties had symmetric information, then they would know about each party's private information, e.g. their order of preference, the quality of the service offered or product sold, or their willingness to pay the price.

IT is built on a principal-agent model in which the former is under-informed, causing it to be forced to introduce a system of incentives so that the agent, i.e. the informed party, discloses information or aligns its behaviour with the principal's expectations consistent with its interests. The payment thus depends on the signals that result from the agent's behaviour, which is captured as *the selection of options from a list of proposals captured as a menu of contracts or as the visible result of the effort expended insofar as such a result is not* visible (Brousseau & Glachant, 2002, p. 9). However, this wording is subject to two assumptions, i.e. that the uninformed principal puts himself in the position of the agent in order to predict behaviour according to a structure or payment scheme and makes a choice, and that there is an implicit but competent and voluntary institutional framework that causes the principal to respect his commitments, and the payment scheme is based on verifiable information, i.e. observable by a third party.

4.2. Incomplete Contract Theory

Like IT, ICT navigates rationality in Savege's sense and the completeness and asymmetry of information available to market participants. At its roots, it draws on the economic direction of *property rights* research focusing on the effects of the allocation of such rights on the distribution of residual surplus among agents and on incentives to invest. Its basic premise is the impossibility of achieving a complete contract state if a third party cannot verify *ex-post* the correct value of the variables that are central to the interaction between the parties to the contract (Brousseau & Glachant, 2002, p. 10). The solution to the problem explicitly refers to a judge who holds the authority to enforce their performance, but has no way of verifying certain variables, such as the level of commitment or investment. This leads to the conclusion that contracting based on unverifiable variables is without purpose and that other means must be sought to ensure effective coordination.

Furthermore, ICT assumes that there is no asymmetry of information between the parties. In this institutional view, it implies uncertainty, because each party must act on the basis of an unverifiable contractual variable in the absence of complete information as to its behaviour, for it cannot predict how the other party will behave. This is captured in two time steps. In the first, the parties make unverifiable investments, and in the second they focus on trading (*trade*) expressed in terms of price and quantity as the only verifiable variables. This leads to a dilemma, because

if contracting is done solely on the basis of verifiable variables, commitment only occurs in the second stage, so the level of investment depends on the amount of trade that occurs in the second stage. As a result, if the level of investment in the first stage is known, then *ex-ante the* level of turnover in the second stage is sub-optimal and therefore the level of turnover should be renegotiated *ex-post,* but the parties envisaging the possibility of renegotiation will have no incentive to invest efficiently *ex-ante*, since the contracted level of turnover is no longer reliable.

In the search for a solution to the problem described above, it is postulated that an obligation limiting the scope of *ex-post* negotiations be adopted in order to incentivise the parties to invest optimally *ex-ante*. This means affording one party the power to estimate the effective level of turnover *ex-post*, as the default option protects the interests of the other party to determine the minimum level of turnover. Following this line of reasoning, two models dominate the economic literature, the first of which, by Hart-Moore, boils down to the fact that the efficient level of investment is not achieved from the beneficiary of the default option because it does not sufficiently incentivise him to invest at the optimal level under the existing conditions (see Hart & Moore, 1988). The second model, which is an extension of the work of Aghion, Dewatripont and Rey, focuses on a default option that may encourage its beneficiary to invest optimally, with the assumption that the judge will be able to enforce such an option and prevent renegotiation (Aghion et al., 1994).

Thus, within ICT, we observe a link between the judge's ability to assess the parties' obligations and the effectiveness of the contract. Since some variables are unobservable, contracts are incomplete, but institutional capacity allows us to assess the complexity of the default option that motivates the efficient behaviour of a party that does not gain from being assigned the power to renegotiate (Brousseau & Glachant, 2002, p. 12).

4.3. Transaction Cost Theory

In contrast to IT and ICT, *Transaction Cost Theory* (TCT) makes the assumption of rationality in *Simon's* sense, i.e. its finite state, as well as the incompleteness and asymmetry of the information available to market participants. Market participants move in a space of unpredictability and are therefore unable to enter into complete contracts, and *institutional failure* contributes to this. External institutions (institutional frameworks) responsible for enforcing contracts are unable to do so because of unverifiable variables, which means that their performance is not guaranteed (Brousseau & Glachant, 2002, p. 13). In the world of an incomplete contract understood in this way, the parties must, on the one hand, ensure *ex-post* procedures indicating certain behaviours and, on the other hand, put in place such measures that ensure the fulfilment of such *ex-post* obligations. This results in the contract having to allocate such powers in three possible ways. The first is to allocate the power to one party, the second is to allocate it to both parties (with provision for negotiation), and the third is to allocate it to a third party, who cannot be the judge. This leads to the creation of a *private order* in which it is the parties who assure each other as to the coordination of their behaviour *ex-post*.

As part of TCT, there are a few assumptions regarding contracts. For example, it emphasises protecting a party to a contract against the opportunistic behaviour of the other party, while introducing incentives to fulfil the commitment, which is achieved by *manipulating the cost of breach of commitment* through margin hedging or irreversible instruments within the commitment length. It also points out that the longer the commitment period, the more difficult it is to predict effective future adjustments. Therefore, it is necessary to redefine the parties' obligations during the commitment period. In addition, it forces a private dispute resolution to be found, as the judge will not be able to fully enforce such a commitment due to the limited rationality (Brousseau & Glachant, 2002, p. 13–14).

Paradoxically, TCT seems to be the closest to L&EC as described above, which, although it uses the efficiency criterion, adopts a welfare economics perspective by focusing on the analysis of existing contract law. However, TCT goes beyond the analysis of the structure of the law by extending it to include the institutional structure to which reference must be made, as the tools of bilateral coordination between the parties are not perfect. The institutional structure thus has a significant role to play in the contracting process, as it provides a basic *set of coordination rules*, which relieves the parties of the need to be innovative in this respect, e.g. by having technical standards to refer to it. In addition, the institutional structure reinforces the credibility of sanctions that guarantee the performance of contractual obligations, which may involve reputation, self-regulation of selected professions, and the power to regulate and coerce (Brousseau & Glachant, 2002, p. 13). This again confirms a broader approach than solely relying on the legal system extending to various collective formal institutions, e.g. the mentioned codes of selected professions, and informal institutions, e.g. specific modes of behaviour imposed by professional groups, ethnic groups, etc. (see North, 1990).

4.4. Competition within ECT

The above-mentioned three economic theories attempt to explain the nature and role of the contract in the economy. They are also complementary when viewed from the perspective of the fundamental issue on which they focus, in particular IT on payment schemes, ICT on provisions relating to renegotiation, and TCT on the assignment of different powers to a party or parties in order to perform a contract. This does not mean that these theories do not compete with each other either. Hence there is no surprise that there is a dispute in the literature between representatives of the different strands. In particular, proponents of IT accuse representatives of ICT of inaccuracies in the proposed model. The most relevant objections still seem to be framed by Tirole, who pointed out the logical inconsistency between the assumption of rationality of market participants within the framework of ICT and their inability to introduce an *ex-ante* disclosure mechanism leading to such disclosure to the judge of the true level of their investment *ex-post*, which would result in the elimination of unverifiability (Tirole, 1999). The representatives of ICT reject this objection, pointing out that the disclosure mechanism cannot be renegotiated *ex-post,* as this would be tantamount to ascribing to the judge verification capabilities that

it does not have (Brousseau & Glachant, 2002, p. 12). However, such a demarcation between the rationality of market participants and the refusal to accept it vis-à-vis the referee may be regarded as an inconsistency of the incomplete contract model, so it is not surprising that it is proposed that this assumption should be replaced by an assumption of the existence of bounded rationality as in the case of TCT (Brousseau & Fares, 2000). Now we turn to the overview of literature which evolved over the last decade in order to find out what topics currently attract scholars' interests.

5. Overview of Literature Devoted to the ECT and L&EC over the Last Decade

5.1. Data and Method

To conduct an overview of the recent literature, we have selected eight leading journals in the field for the period 2016–2026[2], namely the Journal of Economic Theory (JET), Rand Journal of Economics (RAND), Journal of Law and Economics (JLE), Journal of Law, Economics, and Organization (JLEO), International Review of Law and Economics (IRLE), Review of Law and Economics (RoLE), European Journal of Law and Economics (EJLE), and American Law and Economics Review (ALER). Further, we have implemented three-stage filtering for each journal within the period indicated with the JEL codes (D86/D82/D23/K12) or keywords related to contracts. Moreover, the pool of papers obtained was subject to manual screening on an abstract level in order to remove false positives and to recover those missed. Finally, this produced a result of 197 papers and the procedure is summarised below (see table 1).

Table 1.
Literature query procedure

Stage	Description	Note
Step 1 - Formal filter	eight journals, 2016-2026 (JET, RAND, JLEO, EJLE, RoLE, IRLE, JLE, ALER)	Full RePEc/IDEAS series listings screened
Step 2 - Metadata filter	JEL codes OR keywords (contract theory, moral hazard, hold-up, contract law...)	Disjunction used because JEL codes are missing for parts of the corpus
Step 3 - Manual substantive screening	Abstract-level review: false positives removed, missed contract papers recovered	Verified on source page (RePEc / publisher / Crossref)

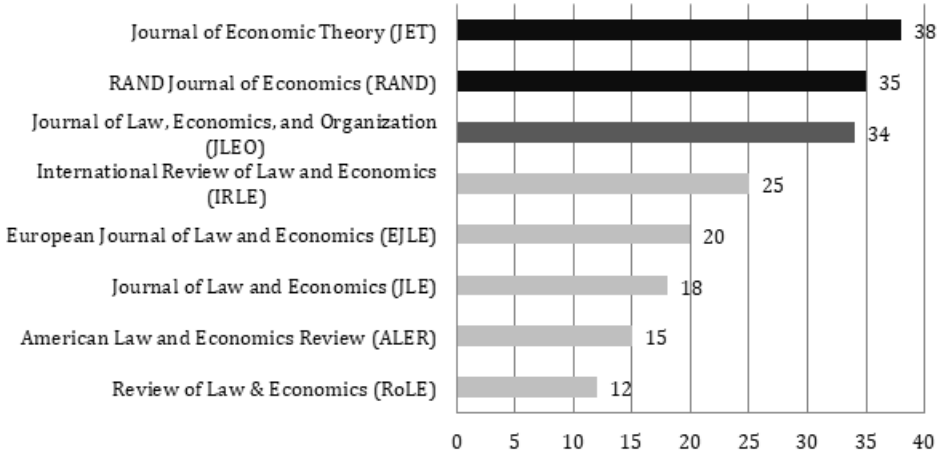
Source: own work.

[2] The year of 2026 covers January-June only.

5.2. Scale, composition and Evolution over Time

The pool of papers obtained indicates two equal currents, giving 101 papers on ECT and 94 papers on L&EC respectively with the border pool of two papers to be observed in JLEO (Beshkar, 2016; Arruñada et al., 2019)[3]. The field is in fact bipolar. In addition, there is significant concentration of certain streams in some journals, with JET and RAND publishing 73 papers on ECT with ninety papers on L&EC in five other journals (JLE, IRLE, RoLE, EJLE and ALER) as well as JLEO which is already indicated as a bridging journal.

Figure 2.
Articles by journal in the period of 2016–2026

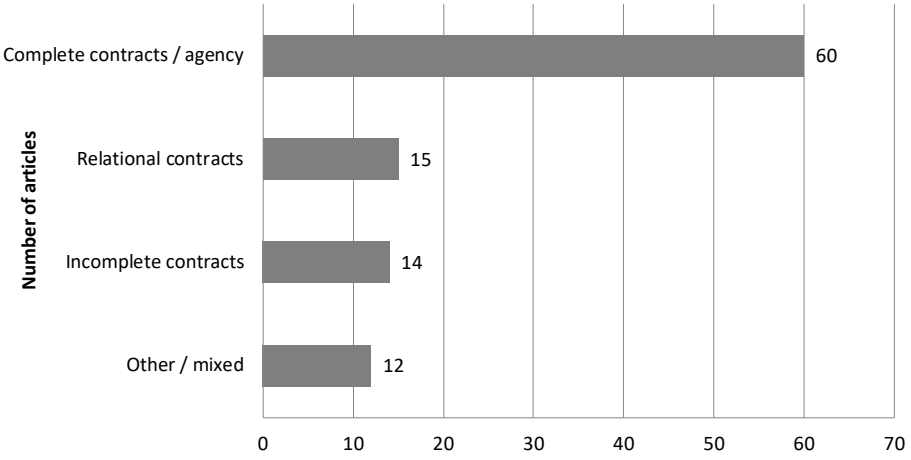


Source: own work.

Within ECT we could further indicate that the predominant topic is agency theory (sixty papers) with incomplete contracts (twelve papers) and relational contracts (fifteen papers) in the minority. The first group covers complete contracts in more detail (moral hazard, adverse selection, mechanism design) and the latter's self-enforcement, repeated games and hold-up, renegotiation and property rights respectively.

[3] The *border* classification comes from the fact that each of the papers indicated as such simultaneously builds an economic optimal-contract model and uses it to rank a specific legal rule on efficiency grounds which appear to form a bridge between ECT and L&EC.

Figure 3.
Economic stream by modelling approach (n = 101)



Source: own work.

From the Law & Economics perspective a more diversified approach was identified, which we group into five lines of topics with the first one related to breach of contract, remedies and default rules as well as contract interpretation and drafting (24 papers), the second one – incomplete contract, relational contracts, hold-up, transactions costs, franchising and private public partnerships (nineteen papers), the third one – consumer protection and behavioural contract law studies (seventeen papers), the fourth one – information asymmetry, agency contracts and corporate governance (sixteen papers) and the last one covering contract regulation and enforcement within labour, credit and debt relations – non-competition clauses, judicial enforcement, covenants and debt agreements (eighteen papers).

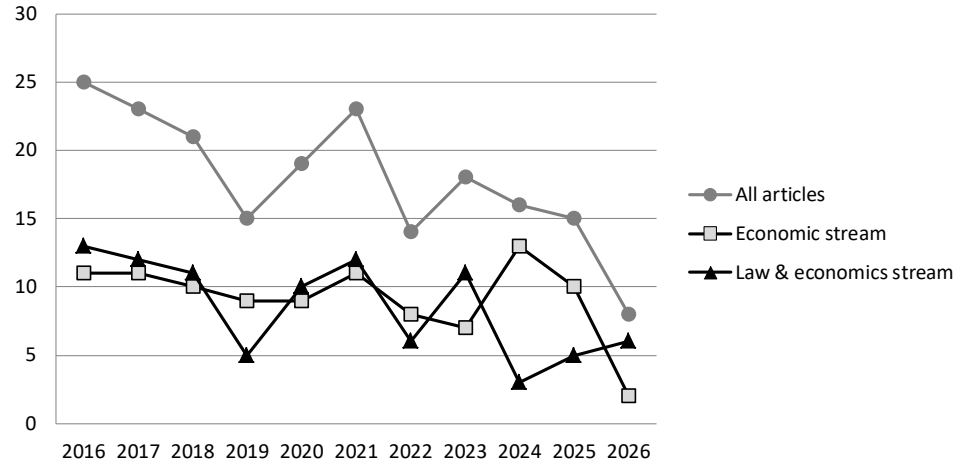
Table 2.
Law & Economics stream by modelling approach (n = 94)

Line of topics (number)	Key topics	Number of articles
1	breach of contract, remedies, default rules, contract interpretation and drafting	24
2	incomplete contract, relational contracts, theory of firm, hold-up, transactions costs, franchising and private public partnerships	19
3	consumer protection and behavioural contract law studies	17
4	contract regulation and enforcement in labour, credit, and debt contracting	16
5	contract regulation and enforcement in labour, credit and debt relations – non-competition clauses, judicial enforcement, covenants and debt agreements	18
	Together	94

Source: own work.

Also, both currents appear to be mature with stable, slightly decreasing rates of production (25 → ~15/year). However, it is interesting to note that L&EC appears to be stronger at the beginning of the covered period, whereas ECT towards its end (see for instance 2024: 13 vs 3).

Figure 4.
Annual Scientific Production in the period 2016–2026



Source: own work.

The number of selected papers prevents us from summarising all of them, hence a selected subjective overview is given below with the most noticeable advancements.

5.3. ECT Literature Developments

The literature of ECT has various streams which relate to the concepts established therein. The predominant one is the incomplete contract which is covered, for example from the angle of observable, but unverifiable performance leading to the optimal contract. Empirical research found that some firms under certain domestic circumstances may use ambiguity to circumvent the legal constraints (Sanga, 2018). In the same vein, the concept of a *continuing contract* is now being revisited, with the employment contract as a leading example. Such a contract can reduce (re)negotiation costs relative to a short-term or long-term perspective, but it may generate inefficient outcomes (Halonen-Akatwijuka & Hart, 2020). In general, the research into ECT also scrutinises the equilibrium condition in the choice between binding and non-binding contracts. The findings point to some beneficial role of contract-enforcing institutions, but in some circumstances the result may be less effective (D'Agostino & Lisciandra, 2018).

As indicated above, the agency theory is clearly visible and predominates. For instance, a complete information game with multiple principals and multiple common agents is under investigation (Lavi & Shamash, 2022). Another example could

be a study concerning a principal-agent model where the agent is better informed about the prospects, and the project needs an observable and unobservable input (Rietzke & Chen, 2020). In contrast, a game between several principals with their limited knowledge and one agent is being scrutinised (Marku et al., 2024). There is also research devoted to the incentive compensation in a static principal-agent moral hazard setting where both players are prudent with the concave function being introduced (Sinclair-Desgagné & Spaeter, 2018). The agents' incentives to form horizontal coalitions ahead of given vertical contracts by a principal are also under scrutiny (Harstad & Mideksa, 2024). Similarly, the adoption of indemnification clauses in research and development contracts is under investigation (Guo et al., 2022).

Another stream of literature relates to bilateral trade involving a short-term commitment when the seller is more "patient" than the buyer, as it impacts the optimal selling and renting mechanisms. Contrary to the common view, it has been established that the restriction on price-posting is harmless and that informational asymmetries are more persistent in renting than in selling (Beccuti & Möller, 2018). There was also some focus on the sequential screening problem when *ex-post* participation constraints were present. The findings are that within the static contract the buyers are not screened with respect to their interim type, and the object is sold at a posted price in contrast to the sequential contract (Bergemann et al., 2020). This is also a matter of subjective evaluations covered within the incentive contract with stochastic compensation which does not require third-party payments to deliver some similar results (Lang, 2023). When examined in detail, there were also contracts under two risk-neutral parties with bounded bonus payments when scrutinised. If the agent's behaviour satisfies a novel condition, the optimal contract is shaped within a simple form irrespective of a first-order approach (Chi & Olsen, 2025).

The relation contract is also under investigation in this stream of the literature. The research conclusions point to the fact that under the optimal relational contract the bond between the parties may not last and such a relationship is less efficient (Fong & Li, 2017). In addition, the relation contract is placed within the conservative agreements framework understood as some arrangement between a local community and an outside party with costly monitoring borne by the latter, but with a weak enforcement system, albeit with the option to renegotiate constantly (Gjersten et al., 2021). Interestingly, experimental economics is represented within the relational contracts as well. In effect, the personal and impersonal relations contracts are created with the notion that their overall effect depends on the relative competition and enforceability (Muñoz-Herrera & Reuben, 2024). The previous experiments for the idea that contracts are reference points for trading relations are also being replicated with some mixed results (Hippel & Hoeppner, 2021). However, experimental evidence explains why people keep their promises (Mischowski et al., 2019).

In addition, the blueprint topics embedded in economic theory are also linked with contracts, in particular the moral hazard problem. In one paper, the possibility of private observation of the performance by the principal is being investigated in a static environment with multiple agents (Ishiguro & Yasuda, 2023). Another example is a hold-up problem in procurement auctions of incomplete contracts (An & Tang, 2019) as well as adverse selection in insurance markets (Saltzman, 2021).

5.4. L&EC Developments

The L&EC literature followed the concepts forged there accompanied by legal ones. The first step could be to highlight the survey relating to publications examining whether contract law should prioritise maximisation of efficiency and social welfare over justice and fairness (Parisi & Bix, 2026). This could be followed by examination of the good faith principle for example from the economic perspective. The findings prove that this principle is being used to curb opportunistic behaviour in some domestic jurisdictions, which is in line with the foundations of Law & Economics (Schäfer & Aksoy, 2015). However, the prominent example of the Law & Economics concept itself is the efficient breach theory linked with material or fundamental breach of contract. As the breach may take different forms, in one paper it has been evaluated with regard to defective delivery (Ganglmair, 2017). In general, there is also research examining under what circumstances promises retaliate to breach and to what extent expectation damages fulfil the function of limiting such retaliatory behaviour (Mittlaender & Buskens, 2019). In this direction there was a delve into the tensions between self-interested incentives to break them and moral ones to keep them in relation to the third parties' behaviour. As a result, it was observed that promissory norms enhance cooperative behaviour (Atkinson et al., 2026).

In the same group of literature, the L&EC literature traditionally focused on damages within the game theory framework (Schweitzer, 2020), but it also examines whether uniform or variable liability rules enhance welfare with some mixed answers provided (Chen & Hua, 2026). From a different angle, the damages due to the misrepresentation have been analysed with the conclusion that its common law approach to prove reliance shall be abandoned and replaced by the new concept of *price impact*. This examines whether the statement led to an increase in the market price (Klement et al., 2018). In another paper, reliance has been analysed, with some focus on the comparison between reliance damages and expectation damages. The authors come to the conclusion that introducing some additional mechanism, e.g. a losing contract, may make the expectation damages more efficient (Ok, 2026). The expectation damages are also scrutinised in relation to the disgorgement remedy. However, both incentives draw overreliance and the choice between them depends on the higher costs on either side (Givati & Kaplan, 2018).

A significant portion of L&EC literature covers consumers as contractual actors. To give an example, consumers are tested with the projection bias (exaggeration of future tastes with the current ones) under long-term contracting. As a consequence, legal intervention is recommended only in some circumstances which depend on the market characteristics and the bias itself (Bienenstock & Ropaul, 2018). This matter is also analysed from the perspective of withdrawal right under EU consumer law in distance sales. This is not the predominant conclusion of authors in Law & Economics theory. Personalised mandatory rules and the mandated-choice model are an optimal solution, but some newly tailored *risk allocation* rules are proposed (Karampatzos & Ilić, 2023). Another example is the consumer's right to early repayment of mortgage loans without damage compensation to the creditor

in the European Union. Hence a panel study on monthly mortgage interest rates of 23 EU member states between 2005 and 2017 found that the spread was linked to the level of consumer protection (Schäfer & Wulf, 2022). Furthermore, the topic of destandardisation of digital contracts is scrutinised in relation to consumer protection and overall efficiency. This means that the *numerus clausus* principle in the digital sphere is recommended (Bucaria & Gottardo, 2023). Consumers and contracts concluded with them are being tied with litigation, too. In particular, they are linked with some impact of sanctions when abusive contract terms are imposed within a litigation model where there is asymmetric information on consumers' ability to go to court. The findings go beyond its enforceability and explore an additional sanction for the unenforceability of such an abusive contract term which may worsen the utilities of some consumers and has mixed effects on welfare (Bienenstock & Desrieux, 2022).

Another stream of literature concentrates on incomplete contracts as well as relational contracts, with some focus on hold-up and transaction costs. For instance, there is some historical research on the relationship between the agent and the principal in medieval paintings in Renaissance Italy. Taking into account the sample of existing documents, the patrons used formal contracts to mitigate painters' opportunism. However, there is limited evidence to show whether the reputation of an artist played any role in its enforcement (Piano & Piano, 2023). Based on historical archives, an analysis of prior appropriation water rights was conducted in the nineteenth century in the Western United States of America was conducted too. The authors found that such prior appropriation facilitated cooperation through contracting, and this led to increasing infrastructure investment and promotion of irrigated agriculture (Leonard & Liebacamp, 2019). Interestingly, it has also been confirmed that the enforceability of (incomplete) contracts depends on the quality of the drafting (Beuve & Chever, 2017).

The classical approach in L&EC has been enriched by the behavioural one which produced several observations in the last decade. For instance, it was indicated that non-compete contract effectiveness derives from employees' beliefs about the likelihood of a lawsuit or legal enforcement resulting in a decline in competitor offers (Starr et al., 2021). In contrast, in another paper in which a behavioural approach was not implemented, it was established that the effectiveness of non-compete contracts depends on liquidity constraints (Wickelgren 2018). Following the behavioural research framework, three areas of contracts, namely formation, performance and remedies, were compared with the rational choice theory. The result is the recommendation of a shifting existing paradigm in Law & Economics to accommodate the behavioural findings (Ulen, 2021). One paper takes a more detailed look at the potential endowment effect of contractual default rules. This was explored by observing a significant gap caused by default rules (Marcin & Nicklisch, 2017).

The second stream focuses on agency contracts. In particular, the duty of care and the duty of loyalty are modelled with regard to corporations. The former is aligned with moral hazard where the principal induces the costly effort on the agent, but the result is unobserved by the principal whereas the latter is a response to adverse

selection with the principal's expectation that the agent will provide true information. Loyalty is further extended to corporate loyalty. It differs from the former one as it requires, *inter alia*, a third-party audit technology such as the court system. The author argues that the optimal judicial approach would highlight the duty to monitor as a part of loyalty due care with limited legal mechanisms available (Buntinga, 2021). In another paper it is suggested that by controlling the owner's limited liability it would be possible to correct the externalities which are being imposed by the firm (Asai, 2020). Interestingly, agency contracts have been approached from a slavery angle too. To understand them better, this was compared with free labour contracts and it was found that relation-specific investment produces high turnover costs to push principals towards slavery (Dari-Matiacci & de Oliveira, 2021).

Contracts within the financial market are also paid attention in the literature. For example, the strength of a creditor's rights are being tested. It was examined whether it could prevent some strategic default and this correlation was established in some cases in India (Tantri, 2020). The introduction of debt recovery tribunals in India also had a positive effect on product innovation there within the large firms, along with secured borrowing and new long-term loans (Jain et al., 2025). However, short-term loans to risky debtors may be highly overcollateralised and contain many restrictive covenants to produce repayment risk near zero, albeit with spread averages significantly above the average (Eckbo et al., 2023).

Incidentally, it is no surprise that the papers published in Law & Economics journals are also embedded in certain laws, in particular of American origin. This is due to the fact that the majority are established in the United States of America. It is not surprising that the papers concentrate on federal and state laws in America, for instance the matter of termination of publishing contracts in which publishers may internalise the harm caught the attention of scholars (Karas & Kristein, 2016). In addition, contracts under American law were empirically analysed with reference to the arbitration clause versus the domestic court system one. The latter were found to dominate the market, as the American court system is solid and reliable (Nyarko, 2019). A more specific topic is being investigaged with the change in Nevada, as the effect on state corporate law was reduction of the legal liability of directors and officers for breaching fiduciary duties towards a corporation. This change is examined with regard to loan contract terms and related borrower-lender agency conflicts, and the conclusion is that it had a negative impact in both aspects (Chen et al., 2020). In a broader approach, restrictions on the ability of franchisors to terminate franchise contracts in America are being tested. In the authors' opinion this has led to increased concentration in a large number of markets (Murry & Newberry, 2022). Moreover, the language of a standardised term in America is being investigated within the rational design model, but the data supports the evolution of boilerplate language to be closer to random mutation rather than rational design (Choi et al.,2018). Nevertheless, broader topics are also being evaluated with some comparison to other systems, e.g. the possibility to contractually re-allocate legal fees which is to opt out of the American rule and follow the *English rule*. It has been observed that this possibility is irrelevant for cases involving a defendant with weak grounds for a case (Ayouni et al., 2020).

6. Conclusions

Taking into account the overview of literature, we confirm that the contract itself is currently an enduring reference point within economic analysis. However, there are differences between ECT and L&EC. The latter does not produce any sophisticated foundation, simply assuming the aim of a complete contract, whereas the former involves a variety of concepts. ECT tends to be detached from the black letter laws and strives to model the contractual obligations theoretically, albeit with some examples of empirical proof. It is dominated by the agency theory and draws various inroads to the information economics. In contrast, L&EC is heterogenous thematically, but is embedded in national laws, in particular American law. It is also noticeable that ECT has diverse trends. Over the past decade, it has stayed firmly theoretical, consolidating around agency and mechanism-design models and pushing into dynamic and relational contracting and the treatment of information and data as contractible objects, while the older incomplete-contracts approach has receded. L&EC, meanwhile, has taken a decisively empirical turn, testing the real-world effects of legal rules through natural experiments, cross-jurisdictional variation (notably non-compete enforceability), and large-scale analysis of contract text. Indeed, both streams merge in some border papers, but it is also important to point out that both also refer to relational contracts, agency theory, complete or incomplete contracts, and other associated economic concepts. However, the difference appears to be still methodological. ECT characterises the optimal contract under informational and enforcement constraints without tying the analysis to, or passing judgment on, any particular legal regime while L&EC takes existing legal rules — remedies, default rules, enforceability — as its object and evaluates them against an efficiency benchmark. The relationship between the two may be described as neither twins nor separate siblings, but cousins who meet from time to time.

Acknowledgements

The author would like to thank Łukasz Dąbroś and Michalina Waclaw for their valuable comments as well as technical support.

Data availability

This study did not use any data other than publicly available databases of scientific publications.

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