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Fusing the Equitable Function in Private Law

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Abstract: Whether and to what extent we should desire the fusion of law and equity depends on the function it serves. This paper draws on systems theory to show how equity is a second-order check on the workings of the law, when complex problems such as party opportunism call for such targeted intervention. Seen from this standpoint, the substantive distinctiveness of equity is potentially valuable even if it is administered in a unified court system. Because this function has not been sufficiently recognized, fusion has been carried too far, especially in the United States. Symptoms of an undertheorized excessive fusion of law and equity include multi-factor balancing tests, a polarization of formalism and contextualism, and a flattening of the law's approach to remedies.

Introduction

Is the fusion of law and equity a fact, a fallacy, or a fantasy? All can agree that the stakes are high in the fusion of law and equity and that something happened between the days of separate equity jurisdiction and the present. Beyond that, however, the terrain is hotly contested.

One conventional story has it that the old law and equity divide was a historical happenstance. There was nothing truly special about equity in a substantive sense, and so the whole point of fusion was to meld the two bodies of law into a seamless whole.¹

And yet there are holdouts — those who see something as lost if equity is not kept separate in some fashion. Historically there are those who have advocated for separate equity courts,² and even these days some judges and commentators believe that fusion

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¹ See, eg. Anthony Mason, 'Fusion,' in Simone Degeling & James Edelman (eds), *Commercial Law* (Sydney, Lawbook Co., 2005) 11; Andrew Burrows, 'We Do This at Common Law but That in Equity' (2002) 22 *Oxford Journal of Legal Studies* 1 (arguing that the law-versus-equity distinction is arbitrary, multiplies terminology and prevents desirable fusion).

² See *The Federalist No. 83* (Alexander Hamilton); Joseph Story, *The Miscellaneous Writings of Joseph Story* (William W. Story (ed), Boston, Charles C. Little and James Brown, 1852) 148, 169–79.

should be regarded as an administrative convenience.³ On this view, any mixing of the streams of law and equity is inherently illegitimate. The disagreement about fusion extends to the case law, resulting in some sharp judicial exchanges.⁴

Whether one takes one of these polar positions or one in between turns in part on one's view about equity itself. Throughout the history of equity jurisdiction, controversy has raged over whether equity involved too much judicial discretion and whether it undermined rather completed the common law — subversion rather than supplementation.⁵ On this negative view, fusion is an unmitigated blessing. Fusion can defang the equitable monster.

Ironically, those who are the biggest enthusiasts of judicial discretion can also find much to like in fusion. Antiformalists tend to see separate jurisdiction itself as empty formalism.⁶ And the perceived freedom of the equity judge to do justice can be extended over all of the law with the advent of fusion.⁷ It is no accident that fusion was

³ This brand of anti-fusionism is strongest in Australia. See generally Paul M. Perell, *The Fusion of Law and Equity* (Toronto, Butterworths, 1990); see also J.D. Heydon, M.J. Leeming & P.G. Turner, *Meagher, Gummow, and Lehane's Equity* (Chatswood, NSW, LexisNexis Butterworths, 5th ed., 2015).

⁴ Compare *United Scientific Holdings Ltd v Burnley Borough Council* [1978] AC 904 (HL) 925 (Diplock, J.) ('The waters of the confluent streams of law and equity have surely mingled now'.) with *G R Mailman & Assocs Pty Ltd v Wormald (Aust) Pty Ltd* [1991] 24 NSWLR 80, 99 (Meagher, J.) ('[In *United Scientific Holdings v Burnley Borough Council*] Lord Diplock . . . expressed the remarkable view that the [Judicature Act 1873] effected a "fusion" of law and equity so that equity as a distinct jurisprudence disappeared from English law. That view is so obviously erroneous as to be visible, and one may confidently anticipate that no Australian court will ever follow it in that regard'.).

⁵ See, eg, FW Maitland, *Equity: A Course of Lectures* (A.H. Chaytor & W. J. Whittaker (eds), 2d ed rev by Brunyate, 1949) 17 ('[T]he first thing we have to observe is that [the relationship between law and equity] was not one of conflict. Equity had come not to destroy the law, but to fulfil it.');

Stephen N. Subrin, 'How Equity Conquered Common Law: The Federal Rules of Civil Procedure in Historical Perspective' (1987) 135 *University of Pennsylvania Law Review* 909, 973–1000 (arguing that '[t]hrough the Federal Rules, equity had swallowed common law', *ibid* at 974).

⁶ See, eg, Burrows, above n 1 at 4–5 ('[W]e as academics, judges, legislators and practitioners are simply not doing enough to eradicate the needless differences in terminology used, and the substantive inconsistencies, between common law and equity.').

⁷ Roscoe Pound, 'The End of Law as Developed in Legal Rules and Doctrines' (1913) 27 *Harvard Law Review* 195, 226 ('Equity sought to prevent the unconscientious exercise of rights; today we seek to prevent the anti-social exercise of rights.');

id. at 227 ('Equity imposed moral limitations. The law today is beginning to impose social limitations.');

see Owen M. Fiss, *The Supreme Court, 1978 Term — Foreword: The Forms of Justice*, (1979) 93 *Harvard Law Review* 1, 2 ('The structural suit is one in which a judge, confronting a state bureaucracy over values of constitutional dimension, undertakes to restructure the organization to eliminate a threat to those values posed by the present institutional arrangements. The injunction is the means by which these reconstructive directives are transmitted.').

But see *Bisciglia v. Kenosha Unified Sch. Dist. No. 1*, 45 F.3d 223, 228 (7th Cir. 1995) (denying temporary injunction in suit over employment termination and stating: '[T]his court does not possess a roving commission to do good. It must make a decision based upon the record and the law.' (citation omitted)); Douglas Laycock, 'The Triumph of Equity' (Summer 1993) 56 *Law and Contemporary Problems* 53, 73 (denying 'that a court of

completed in the United States during the era of Legal Realism, notably with the adoption in 1937 of the Federal Rules of Civil Procedure. Fusion is the occasion for equity to slip its bounds — to die and to triumph at the same time.

Upon closer look, the debate between fusionists and anti-fusionists does not take place on the same plane. Fusionists are typically interested in function and see fusion as a way to enshrine the correct approach — whether formalist or contextualist, or conceivably in between — into a streamlined and unified law and legal system. Anti-fusionists seek to preserve something special about equity, and yet it is hard to convince the uninitiated to value what that is. Is equity a repository for conscience, and, if so, whose?⁸ It may well be that '[e]quity is not a set of rules but a state of mind,'⁹ as Lord Millett would have it. If so, how to answer those who see conscience and states of mind as too amorphous, too expansive, and too impenetrable to value for their own sake?

This paper will present a functionalist case for skepticism about substantive fusion. This may seem doubly contrarian or even perverse. After all, if there is one thing most people agree on, especially in the United States, it is that there really is no identifiable equitable function. Perhaps what equity courts did was valuable, but it is hard to argue that it can be explained with any specificity. Perhaps it is inherently unmeasurable — because it is too ethereal or because it does not exist.

Not so fast. There is an equitable function. This function is not unrelated to separate equity jurisdiction, but it does not require separate courts. Equity in a functional sense was not the exclusive preserve of equity judges — common law courts could be functionally equitable — and equity judges did more than dispense equity. So what is equity?

I argue that equity is a limited second-order intervention to solve a class of problems characterized by both complexity and uncertainty. Legal decision-making takes place on several related levels. Within the law, rights and duties form a primary stratum of legal relations between legal actors. Powers and the like are second order in that a power works a change in rights rather than the other way around: to formulate a power one needs to make reference to rights, but to formulate a right there is no need to refer to a power.¹⁰ The power is at a 'meta' level. In terms of common law decision-

equity has a roving commission to do good once it identifies a threshold violation of law that justifies its intervention').

⁸ Irit Samet, 'What Conscience Can Do for Equity' (2012) 3 *Jurisprudence* 13 (arguing that Kantian conscience can supply the standard for a distinct equity); P.G. Turner, "'Mending Men's Bargains" in Equity: Mortgage Redemption and Relief Against Forfeiture' (2014) *Law Quarterly Review* 188 (analyzing *Cukurova Finance International Ltd v Alfa Telecom Turkey Ltd* [2013] UKPC 20).

⁹ Lord Millett, 'The Common Lawyer and the Equity Practitioner,' (2015) *UK Supreme Court Yearbook* 193

¹⁰ See Wesley Newcomb Hohfeld, 'Fundamental Legal Conceptions as Applied in Judicial Reasoning' (1913) 23 *Yale Law Journal* 16, 44-58; Ugo Pagano, 'Public Markets, Private Orderings and Public Governance' (2000) 20 *International Review of Law and Economics* 453, 459-65; Ted M. Sichelman,

making, one could regard the generation of new ‘rules’ to be a higher-order part of the common law: common law rules operate on one level, and courts will sometimes will modify and create new rules. The similarity to legislation has often been remarked upon. What is special about the equitable function is that it is highly applied and fact-oriented, like the application of common law to facts, and yet it is, as I will argue, second-order like the quasi-legislative component of the common law. Indeed pre-fusion equity was a source of new common law rules.

When is the second-order equitable function needed? Going back to Aristotle — often invoked by equity judges and commentators — we can start with the notion that equity intervenes into law where it fails owing to its generality.¹¹ Why does the law fail for being general? Many answers have been offered, some of which — such as unfairness and changed circumstances — lead to a very expansive equity. The account I offer here and in related work,¹² equity as a second-order safety valve, focuses on how the ‘regular’ part of the law, precisely because it aspires to be general, faces problems with hard-to-foresee problems that disturb the stable relationships between activities. To be general, the law has to assume that situations fall into probabilistically meaningful categories. To take an example, any system of liability that excuses violations of a right as *de minimis* or as in good faith has to face the possibility that informed actors can commit a violation that appears innocent but that is actually knowing and harmful. Signs that something is *de minimis* or in good faith can be mimicked by the opportunist. Or, to take another example, if damages in tort serve any deterrent function, many, especially in law and economics, take comfort from the idea that incentives will be correct if damages are calculated correctly on average: before the act, in expectation, the actor will face the cost of the harm that would otherwise be externalized.¹³ However, a clever actor, knowing how damages are measured, can cherry-pick rights to violate, such that the harm is systematically undervalued.¹⁴

Quantifying Legal Entropy (May 22, 2013), San Diego Legal Studies Paper No. 13-128, available at SSRN: <http://ssrn.com/abstract=2293015>.

¹¹ Aristotle, *The Nicomachean Ethics* (J.L. Ackrill & J.O. Urmson (eds), trans. David Ross trans., Oxford, Oxford University Univ. Press, rev. ed., 1980).

¹² Henry E. Smith, ‘Why Fiduciary Law Is Equitable’ in Andrew S. Gold & Paul B. Miller (eds), *Philosophical Foundations of Fiduciary Law* 261–84 (Oxford, Oxford University Press 2014); Henry E. Smith, *Equity as Second-Order Law: The Problem of Opportunism* (January 15, 2015) (unpublished manuscript), <http://ssrn.com/abstract=2617413>.

¹³ Louis Kaplow & Steven Shavell, ‘Property Rules Versus Liability Rules: An Economic Analysis’ (1996) 109 *Harvard Law Review* 713, 725; A. Mitchell Polinsky & Steven Shavell, ‘Punitive Damages: An Economic Analysis’ (1998) 111 *Harvard Law Review* 869, 877–81. For a more thorough exposition of this theory, see Steven Shavell, *Economic Analysis of Accident Law* (Cambridge, Mass., Harvard University Press, 1987).

¹⁴ Henry E. Smith, ‘Property and Property Rules’ (2004) 79 *New York University Law Review* 1719, 1774–85.

Law's generality is thus vulnerable to what in institutional economics is termed 'opportunism' and what the equity lawyers of old called 'constructive fraud'.¹⁵ Those who may (or may not) stay within the letter of the law by taking advantage of it to impose an unfair result on someone else are inherently difficult to deter with ex ante rules. It is hard to defeat opportunists who themselves exploit the system as a whole without going ex post and to a higher level to meet them on their own ground. Some measure of targeted discretion to defeat them can be more beneficial than costly in terms of destabilizing the system.

Although I will consider mainly equitable anti-opportunism, the theory here is about the class of problems that require second-order intervention. Other such problems include those that Lon Fuller termed polycentric and those involving conflicting rights.¹⁶ When a problem involves multiple parties interacting in highly dependent ways, it is difficult to deal with on its own terms: a component that can refer to and control the primary law makes sense — a law about law, a meta law. That is the equitable function, or so I argue.

This paper will first set forth the equitable function in Part I. It will show how providing a limited second-order safety valve was a large part of the business of equity courts and how separate equitable jurisdiction leads naturally to emphasizing equity's second-order character, even though separate courts or even a distinct jurisdiction are not strictly necessary for such a second-order function. Part II will then show how fusion, particularly as implemented in the United States, has gone too far. In their fixation on substantive fusion, courts and commentators have partially effaced the second-order equitable function. Part III draws out some implications of identifying the equitable function and its partial submergence in fusion. These include the rise of standards and multi-factor balancing tests, the polarization of courts and commentators into formalist and contextualist camps, and the flattening of the law of remedies. The paper ends with some concluding thoughts on the place of equity within a legal system.

I. The Equitable Function

The question of fusion makes little sense without some idea of what is being fused. For many, and for the most ardent pro-fusionists, there is nothing particularly special about equity from a substantive point of view. Something unspecial need not be kept distinct, either in separate courts or as a separate element of a legal system entrusted to a single set of courts. In contrast, for those who are skeptical or even opposed to fusion, arguments tend to be made 'from within' the system. Anti-fusionists appeal to tradition, or they rely on notions of conscience and states of mind that make sense to those already steeped in the world of equity. But such invocations of equity run the risk of preaching to the choir, and not making many converts.

¹⁵ Oliver E. Williamson, *The Economic Institutions of Capitalism* (New York, Free Press, 1985) 47.

¹⁶ Lon L. Fuller, 'The Forms and Limits of Adjudication' (1978) 92 *Harvard Law Review* 353.

I argue that equity does have a distinct function. I thus give it an external justification. This is not meant to supplant an internal and interpretive perspective that elaborates equity doctrine from within. At a time of widespread uncertainty about equity's status, though, a grounding of equity in distinct functional concerns would be a plus.¹⁷

As with other parts of the legal system, it is important to keep in mind the difference between the purpose of equity and how it serves that purpose. This is especially tricky when it comes to equity, because equity has more direct recourse to purposes than do other parts of the law. The 'equity of the statute' is a traditional form (much contested) of purpose-driven statutory interpretation, and in general equity looks to the spirit rather than the letter of the law. It lends the system of the law a great deal of its openness. One useful definition of formalism is relative invariance to context.¹⁸ Thus, natural language — with pronoun reference and implied meaning — is less formal than computer languages. The language of everyday mathematics is less formal than that of published proofs. Systems generally need some external anchor, and equity is more outward looking — to morality, custom, common sense — than the regular more formal parts of the law.

It is therefore only a starting point to identify the purpose of equity. We need also to explore how it works. The 'how' of equity used to depend on separate jurisdiction. Now that it cannot, we need a better theory of equity's function. Let me first endorse a moderate view of equity's purpose and then turn to a theory of the workings of equity.

Many discussions of equity, both in the courts and the commentary, start with Aristotle's definition of equity (*epieikeia*) as intervening into 'law where law is defective because of its generality'.¹⁹ Law's generality can cause problems for many reasons. The legislator may not have foreseen a particular problem or have failed to avoid ambiguity ('no vehicles in the park'). Or someone may be trying to take unfair advantage of the law being, as Aristotle would have it, a 'stickler in a bad way'.²⁰ Opportunists are looking for

¹⁷ cf Lionel Smith, 'Fusion and Tradition' in Simone Degeling & James Edelman (eds), *Equity in Commercial Law* (Sydney, Lawbook Co., 2005) 19.

¹⁸ Francis Heylighen, 'Advantages and Limitations of Formal Expression (1999) 4 *Foundations of Science* 25, 25, 37 (1999); Henry E. Smith, 'Property, Equity, and the Rule of Law' in Lisa M. Austin & Dennis Klimchuk (eds) *Private Law and the Rule of Law* (Oxford, Oxford University Press, 2014) 224–46.

¹⁹ Aristotle, above n 11 at 133; see also, e.g., *Riggs v. Palmer*, 22 N.E. 188, 189 (N.Y. 1889) (quoting Aristotle on equity); Eric G. Zahnd, 'The Application of Universal Laws to Particular Cases: A Defense of Equity in Aristotelianism and Anglo-American Law' (Winter 1996) 59 *Law and Contemporary Problems* (documenting influence of Aristotelian equity on Anglo-American law) 263, 270–75; but cf Darien Shanske, 'Four Theses: Preliminary to an Appeal to Equity' (2005) 57 *Stanford Law Review* 2053 (arguing that Aristotle's equity was not primarily legal).

²⁰ Aristotle, above n 11; see also Dennis Klimchuck, 'Equity and the Rule of Law' in Lisa M. Austin & Dennis Klimchuk (eds), *Private Law and the Rule of Law* (Oxford, Oxford University Press, 2014) 247; Dennis Klimchuk, 'Is the Law of Equity Equitable in Aristotle's Sense?' 4 (June 2011) (unpublished).

weak points in the law to exploit, and plugging every loophole in advance is somewhere between impractical and impossible. As I have argued elsewhere, without some protection from something like equity, the general law on its own cannot serve the rule of law values of stability and certainty.²¹

Legal sources, and courts and commentators in particular, often relatedly invoke a stock formula for the domain of equity. Equity intervenes in cases of ‘fraud, accident, and mistake’.²² Sometimes the triad emphasizes confidence rather than mistake as in the poetic version attributed to Thomas More, the first lawyer to serve as Chancellor: ‘Three things are to be helpt in Conscience; Fraud, Accident and things of Confidence’.²³ The theme is lack of foreseeability and surprise coupled with some element of potential deceit.

In later sources, a catch-all for much of the domain of equity was ‘constructive fraud’. To take a famous American example, Justice Story emphasized ‘constructive fraud’ (what we would call opportunism) and the role of equity in defeating it:

There is always fraud presumed or inferred from the circumstances or conditions of the parties contracting, weakness on one side, usury on the other, or extortion or advantage taken of that weakness. There has always been an appearance of fraud from the nature of the bargain, even if there be no proof of any circumvention, but merely from the intrinsic unconscionableness of the bargain.

manuscript) (on file with the author), <http://www.law.ucla.edu/workshops-colloquia/Documents/Klimchuk.%20Is%20the%20Law%20of%20Equity%20Equitable%20in%20Aristotles%20Sense.pdf> (‘Correction is sometimes necessary because all law is universal and, owing to its universality, can lead to error in particular cases.’).

²¹ Smith, above n 18.

²² 47 *American Jurisprudence 2d* ‘Judgments’ § 718, Westlaw (database updated Nov. 2015) (‘Generally, claimants seeking equitable relief from judgments through independent actions must meet three requirements[, the third of which is that] they must establish a recognized ground, such as fraud, accident, or mistake, for the equitable relief.’) (footnotes omitted, citing cases); see also William F. Walsh, *A Treatise on Mortgages* (Chicago, Callaghan and Co., 1934) 6, 11 (relief from mortgages in equity on grounds of fraud, accident, or mistake); Val D. Ricks, ‘American Mutual Mistake: Half-Civilian Mongrel, Consideration Reincarnate’ (1998) 58 *Louisiana Law Review* 663, 717 & n.277 (speculating that Chief Justice Allen in *Swift v. Hawkins*, 1 Dall. 17 (Pa. 1768), ‘considered “mistake” to be representative of all categories of equity’).

²³ 1 Rolle’s Abridgement 374; see also *Coco v AN Clark (Engineers) Ltd*, [1969] RPC 41, 46 (Ch Div) (Justice Megarry) (quoting More’s couplet); Anthony Laussat, Jr., *An Essay on Equity in Pennsylvania* (Philadelphia, Robert Desilver, 1826) 67 (stating that ‘Sir Thomas More used to say that the following doggerel contained all the heads of chancery jurisdiction’). William Blackstone, more a fan of the common law than of equity, gets a little defensive in making the legitimate point that the triggers for equity were not ignored by the common law. 3 William Blackstone, *Commentaries* *431.

Story sees equity's emphasis on constructive fraud, which takes up the bulk of his treatise, as a way of countering it.²⁴ Indeed, he sees confidence as a core radiating out to 'mistake, accident, and fraud', summing up that:

many cases of penalties and forfeitures; many cases of impending irreparable injuries, or meditated mischiefs; and many cases of oppressive proceedings, undue advantages and impositions, betrayals of confidence, and unconscionable bargains; in all of which Courts of Equity will interfere and grant redress; but which the Common Law takes no notice of, or silently disregards.²⁵

Story gives qualified endorsement to Lord Cowper's expansive language in *Dudley v. Dudley*, sounding in anti-opportunism:

Now equity is no part of the law, but a moral virtue, which qualifies, moderates, and reforms the rigour, hardness, and edge of the law, and is an universal truth; it does also assist the law where it is defective and weak in the constitution (which is the life of the law) and defends the law from crafty evasions, delusions, and new subtillies, invented and contrived to evade and delude the common law, whereby such as have undoubted right are made remediless; and this is the office of equity, to support and protect the common law from shifts and crafty contrivances against the justice of the law. Equity therefore does not destroy the law, nor create it, but assist it.²⁶

Dudley itself was about opportunism and anti-evasion, in that the heir in that case tried to invoke a technicality that would delay a widow's remedy on her dower rights for 99 years — which the chancery court prevented.²⁷

²⁴ See Robert Lowry Clinton, 'Classical Legal Naturalism and the Politics of John Marshall's Constitutional Jurisprudence' (2000) 33 *John Marshall Law Review* 935, 948 (discussing Carl Dibble's identification of a 'moderate Enlightenment' tradition of legal interpretation associated with Grotius, Blackstone, and Marshall, that emphasized the role of equity and located the need for interpreting laws not in the ambiguity of language but in the possibility 'that corrupt, duplicitous persons will "treat the law in a sophisticated manner" in order to advance their own individual interests' (quoting Carl M. Dibble, *The Lost Tradition of Modern Legal Interpretation* 5 (1994) (unpublished essay prepared for delivery at the 1994 Annual Meeting of the American Political Science Association))).

²⁵ See Joseph Story, *Commentaries on Equity Jurisprudence: as Administered in England and America*, Boston, Hillard, Gray & Co., 1836) § 29.

²⁶ *Dudley v Dudley* (1705) 24 Eng Rep 118, 119 (Ch), *quoted in* 1 Story, above n 25, § 17.

²⁷ Story hesitates to endorse the tight connection between equity and morality and sees this accordingly as a bit broad. On another interpretation, the type of morality being invoked here is not that broad — it is the kind of morality that protects the regular or formal law. This narrower version features in Justice Roujet Marshall's opinion for the Wisconsin Supreme Court in *Harrigan v. Gilchrist*, 99 N.W. 909 (Wis. 1904): The text-writers disagree, in some respects, in the manner of stating this, but are in harmony in this: While new principles are not to be added to those long established for the government of equitable remedies, the rules, not the precedents, are to control. There is no vitality in precedents; there is in rules. They are susceptible of expansion along every line necessary to reach new conditions. *The ingenuity of man in devising new forms of wrong cannot outstrip such development.* In all situations and under all circumstances, whether new or old, the principles of

Story ties equity's open-ended nature to the need to deal with constructive fraud and the crafty evasions of opportunists. Quoting Lord Hardwicke, he notes that '[f]raud is infinite' given the 'fertility of man's invention'.²⁸ As a result, equity cannot announce in advance all its particulars:

Accident, mistake, and fraud, are of infinite variety in form, character, and circumstances; and are incapable of being adjusted by any single and uniform rule. Of each of them, one might say, *Mille trahit varios adverso sole colores*. The beautiful character, or pervading excellence, if one may so say, of Equity Jurisprudence is, that it varies its adjustments and proportions, so as to meet the very form and pressure of each particular case in all its complex habitudes.²⁹

Equity needs to be ex post and tailored to the situation, because opportunism calls for that kind of response. Moreover, in Story's view, the rise of industry and commerce increase the danger of opportunistic invocation of the letter of the law.³⁰

This anti-opportunism version of equity lends a somewhat expansive gloss on traditional formulations of equity. As Chancellor Ellesmere put the point: 'The Cause why there is a Chancery is, for that Mens Actions are so divers and infinite, That it is impossible to make any general Law which may aptly meet with every particular Act, and not fail in some Circumstances'.³¹ Aristotle analogized equity's tailored ex post nature to the leaden rulers of the builders of Lesbos, which could be fitted to individual

equity will point the way to justice where legal remedies are infirm. Precedents will be a constant guide, but never a bar. Where a new condition exists, and legal remedies afforded are inadequate or none are afforded at all, the never-failing capacity of equity to adapt itself to all situations will be found equal to the case, extending old principles, if necessary, not adopting new ones, for that purpose. That is a very old doctrine.

Ibid at 937 (emphasis added). The opinion is 334 pages long and is described by his rival Chief Justice Winslow as a 'compendium of legal lore'. 'Roujet D. Marshall' in Trina E. Gray (ed), *Portraits of Justice: The Wisconsin Supreme Court's First 150 Years* (Madison, Wis., Wisconsin Historical Society Press, 2002) 26.

²⁸ 1 Story, above n 25, § 186 (quoting a Letter from Lord Hardwicke to Lord Kames (June 30, 1759)).

²⁹ Ibid at § 439. Story is evidently quoting Vergil's *Aeneid*, bk 5, line 89 ('It gets a thousand various colors from the sun', author's translation), in a passage likening the surface of a snake (!) to a rainbow.

³⁰ To this effect Story quotes from a Report by a committee he chaired on equity courts:

These are a few of the numerous cases in which universal justice requires a more effectual remedy than the courts of common law can give. In proportion as our commerce and manufactures flourish and our population increases, subjects of this nature naturally accumulate; and, unless the legislature interpose, *dishonest and obstinate men may evade the law and intrench themselves within its forms in security*.

Joseph Story, *The Miscellaneous Writings of Joseph Story* (William W. Story (ed), Boston, Charles C. Little and James Brown, 1852) 148, 175 (emphasis added).

³¹ *The Earl of Oxford's Case* (1615) 21 Eng Rep 485, 486 (Ch).

stones in order to pick the exactly right one.³² Problems like opportunism point to a particular problem with the generality of law, and it calls for a particular type of second-order solution.

We see, then, in the writings of Story and of others elucidating the nature of constructive fraud,³³ the beginnings of a functional theory of equity as responding to a special kind of problem that is not handled well by the law. Because equity is a function rather than essentially jurisdictional, that function can sometimes be served by the common law courts. And indeed some of the most ardent defenders of the common law and opponents of equity jurisdiction courts could at times sound a functionally equitable note, as when Coke saw ‘discretion [as] a science or understanding to discern between falsity and truth, between wrong and right, between shadows and substance, between equity and colourable glosses and pretences, and not to do according to their wills and private affections’.³⁴ Here again discretion, often thought a hallmark of equity for good and for ill, is tied to something quite close to our notion opportunism, which is often a matter of ‘colourable glosses and pretences’.

The starting point for the functional theory of equity is to recognize that there is a special class of problems calling for a more ‘meta’ kind of solution than the law normally provides. Polycentric tasks, conflicting rights, and opportunism all involve great complexity and uncertainty.³⁵ In systems theory they are problems associated with high variability. The question is what mechanism for control we need, and this can either be improvements to the system — better and more elaborate versions of the rules that give rise to the complex variable problem — or moving to a higher level.³⁶ In the systems theory and cybernetic literatures this is called hierarchy.³⁷ Certain problem call for hierarchy because the cost of setting up a higher level and the noise associated with a new higher-level set of devices is worth incurring in light of the better handling of the complex variable problems.³⁸

³² Aristotle, above n 11 at 133.

³³ L.A. Sheridan, *Fraud in Equity: A Study in English and Irish Law* (London, Pitman & Sons, 1957)

³⁴ *Rooke’s Case* (1597) 5 C. Rep 99b, 100a; 77 Eng Rep 209, 210 (KB).

³⁵ Examples of polycentric tasks might include violations of community custom or certain kinds of accounting (as opposed to compensatory damages), and conflicting potential rights often arise in nuisance. See Smith, *Equity as Second-Order Law*, above n 12.

³⁶ See, e.g., Karl Ludwig von Bertalanffy, *General System Theory* (New York, Braziller, 1968); see also John H. Holland, *Hidden Order* (Reading, Mass., Addison-Wesley, 1995) 11–12 (discussing second-order agents and properties).

³⁷ See, e.g., Francis Heylighen & Cliff Joslyn, ‘Cybernetics and Second-Order Cybernetics’ in Robert A. Myers (ed), *Encyclopedia of Physical Science & Technology* (San Diego, Academic Press, 3d ed., 2002).

³⁸ See A.Y. Aulin-Ahmavaara, ‘The Law of Requisite Hierarchy’ (1979) 8 *Kybernetes* 259.

Consider opportunism in particular. What is opportunism? It is a term much disputed in economics, and notably Nobel laureate Oliver Williamson defines opportunism as ‘self-interest seeking with guile’.³⁹ This definition turns out to be too broad for our purposes, because to Williamson any rule breaking is opportunism. And yet not all rule breaking causes complexity and uncertainty calling for second-order solutions. Other definitions based on contravening the spirit of the law or defeating a counterparty’s legitimate expectations are likewise potentially broad enough to go beyond any need for the second-order solutions.⁴⁰ Some of these definitions are nonetheless too narrow if they do not include situations where full-blown deception may not be present but someone is taking advantage of an unexpected change in conditions or a hard to discover loophole.⁴¹

Because of this feature, opportunism is hard to capture explicitly ex ante. Elsewhere I have defined opportunism as ‘behavior that is undesirable but that cannot be cost-effectively captured — defined, detected, and deterred — by explicit ex ante rulemaking. . . . It often consists of behavior that is technically legal but is done with a view to securing unintended benefits from the system, and these benefits are usually smaller than the costs they impose on others’.⁴² The response needs to be ex post, and partially discretionary. It also needs to make reference to the law: the law is the vocabulary, the input, to the equitable function. Equity is higher order.

This brings us to the nature of equitable devices. Equity is, in general, second order. This is potentially destabilizing absent severe limits on what one can do at the higher level. These limits are built into the proxies and presumptions that implement equity and are now only semi-familiar in American law.

Turning first to the overall structure, the fact that equity courts usually and eventually won the battle with the common law courts can be seen as reflecting equity’s

³⁹ Williamson, above n 15 at 47.

⁴⁰ See, eg, George M. Cohen, ‘The Negligence-Opportunism Tradeoff in Contract Law’ (1992) 20 *Hofstra Law Review* 941, 957 (defining ‘opportunism’ as ‘any contractual conduct by one party contrary to the other party’s reasonable expectations based on the parties’ agreement, contractual norms, or conventional morality’) (footnote omitted); Timothy J. Muris, ‘Opportunistic Behavior and the Law of Contracts’ (1981) 65 *Minnesota Law Review* 521, 521 (defining ‘opportunism’ as conduct that is ‘contrary to the other party’s understanding of their contract, but not necessarily contrary to the agreement’s explicit terms’); see also, eg, Samuel W. Buell, ‘Good Faith and Law Evasion’ (2011) 58 *UCLA Law Review* 611, 623 (‘In common parlance, the evasive actor is one whose project is to get around the law. She seeks to avoid sanction while engaging, in substance, in the very sort of behavior that the law means to price or punish.’). For a wider definition, see, for example, Richard A. Posner, *Economic Analysis of Law* § 4.1, at 103 (New York, Aspen Law & Business, 5th ed., 1998) (defining ‘opportunism’ in the contracting context as ‘trying to take advantage of the vulnerabilities created by the sequential character of the contract’).

⁴¹ There is a tendency to call any nefarious behavior with an element of concealment ‘fraud’, which includes breach of trust and underground mining. See *Livingston v. Rawyards* (1880) LR 5 App Cas 34 (quoted in *Marengo Cave Co. v. Ross*, 10 N.E.2d 917, 923 (Ind. 1937)).

⁴² Smith, Equity as Second-Order Law, above n 12 at 10–11.

second-order aspect: equity can make reference to and alter a legal result (at least in effect), but not vice versa. Substantively, it has been noticed that law and equity are not on the same plane. Equity is ‘law about law’. I have characterized equity as a safety valve, and a safety valve has to be a safety valve on something else. As Maitland, no proponent of a special equitable function, put it, if equity had been abolished, ‘in some respects our law would have been barbarous, unjust, absurd’, but still ‘the great elementary rights against violence, to ownership, and so on, would have been enforced’. By contrast, abolishing common law would have meant ‘anarchy’, because ‘[a]t every point equity presupposed the existence of common law’.⁴³ In his famous formulation, ‘equity without common law would have been a castle in the air, an impossibility’.⁴⁴

As a second-order intervention, equity is potentially a powerful tool. This power has always called forth detractors who see equity as too unconstrained. From the chancellor’s foot to fears of judicial overreach,⁴⁵ the open-endedness of equity requires constraints on equity that are key to its viability.

The second-order equitable element in the legal system can be treated as a safety valve, and we will see that traditional equity in large part acted in this fashion. As I discuss elsewhere, many of the central features of equity have the effect of deepening and narrowing it. To start with, ‘equity acts in personam’ limits its reach to parties before the court. Importantly, equity does not alter entitlements with in rem effect.⁴⁶ From the point of view of duty bearers, the substantive and informational impact of in rem rights is heavier: more people are impacted and their social distance from the transaction creating the right (or other legal relation) makes the informational burden greater.⁴⁷ The hurdles to get into equity — notably the irreparable injury requirement — also have the effect of

⁴³ Maitland, above n 5 at 19.

⁴⁴ Ibid.

⁴⁵ See J.H. Baker, *An Introduction to English Legal History* (London, Butterworths, 3d ed., 1990). The most famous critique of equity is Selden’s:

Equity is a Roguish thing: for law we have a measure, know what to trust to; Equity is according to the Conscience of him that is Chancellor, and as that is larger or narrower, so is Equity. ’Tis all one as if they should make the Standard for the measure we call a Foot, a Chancellor’s Foot; what an uncertain Measure would be this. One Chancellor has a long Foot, another a short Foot, a Third an indifferent Foot: ’Tis the same thing in the Chancellor’s Conscience.

John Selden, ‘Equity’ in *Table-Talk: Being the Discourses of John Selden, Esq.* (London, J.M. Dent & Co., 2d ed., 1689) 43, 43–44.

⁴⁶ See Charles M. Gray, ‘The Boundaries of the Equitable Function’ (1976) 20 *American Journal of Legal History* 192, 202–06 (illustrating how courts of equity were prohibited from addressing real estate disputes).

⁴⁷ See Thomas W. Merrill & Henry E. Smith, ‘Optimal Standardization in the Law of Property: The *Numerus Clausus* Principle’ (2000) 110 *Yale Law Journal* 1, 4, 33; Thomas W. Merrill & Henry E. Smith, ‘The Property/Contract Interface’ (2001) 101 *Columbia Law Review* 773; Henry E. Smith, ‘The Language of Property: Form, Context, and Audience’ (2003) 55 *Stanford Law Review* 1105.

narrowing equity.⁴⁸ The flip side of this is the inadequacy of the legal remedy requirement. On the theory offered here, the question being asked is whether it really is necessary to leave the primary level and go to meta-law in order to solve a problem.

Less obviously but crucially, many of the more substantive triggers and presumptions in equity serve to fashion it into a second-order safety valve. Equity involves rules of thumb, as expressed in maxims such as clean hands. It also provides for a flow chart of presumptions, which vary somewhat depending on the subject matter at hand. The triggers for presumptions are proxies for opportunism, and they sound in good or bad faith and disproportionate hardship. Take, for example, building encroachments. The law-and-economics literature treats problems of remedies in areas like nuisance and building encroachments as involving two settings: property rules that force duty bearers to get the consent of the entitlement holder, and liability rules that allow duty bearers to take the entitlement and pay an officially determined price.⁴⁹ The literature is vast, but one point of agreement is that liability rules are appropriate in situations of high transaction costs in markets, such as with bilateral monopolies, holdouts, and free riders.⁵⁰ Hence the supposed trend towards giving damages in building encroachment cases.

The traditional equitable approach to building encroachments was a more sophisticated second-order safety valve.⁵¹ The basic baseline theoretically is that equity will not enjoin a mere trespass. Nevertheless, for repeated and continuing trespasses the presumption is for issuing an injunction, and this presumption covers building encroachments, which are certainly continuing trespasses. Of course, ordering a building torn down is wasteful, but the traditional equitable test was not directly about waste. In a targeted fashion, equity provides a defense of disproportionate (or undue) hardship: if the injunction would harm the encroacher far more than it would benefit the movant (especially if the encroachment is slight), then a court may deny the injunction and give only damages.⁵² However, if the encroachment was not in good faith — if the encroaching party had notice of the violation before engaging in it — the defense of disproportionate hardship does not apply, and the injunction will issue. This mechanism is designed to deal with potential opportunism on both sides — the opportunism of the

⁴⁸ Douglas Laycock, *The Death of the Irreparable Injury Rule* (New York, Oxford University Press, 1991); Douglas Laycock, 'The Death of the Irreparable Injury Rule' (1990) 103 *Harvard Law Review* 687, 688–701 (1990); but see Smith, Equity as Second-Order Law, above n 12.

⁴⁹ Guido Calabresi & A. Douglas Melamed, 'Property Rules, Liability Rules, and Inalienability: One View of the Cathedral' (1972) 85 *Harvard Law Review* 1089.

⁵⁰ See, eg, Ian Ayres, *Optional Law: The Structure of Legal Entitlements* (Chicago, University of Chicago Press, 2005); Ian Ayres & Eric Talley, 'Solomonic Bargaining: Dividing a Legal Entitlement to Facilitate Coasean Trade' (1995) 104 *Yale Law Journal* 1027; Kaplow & Shavell, above n 13.

⁵¹ Smith, Equity as Second-Order Law, above n 12.

⁵² Douglas Laycock, 'The Neglected Defense of Undue Hardship (and the Doctrinal Train Wreck in *Boomer v. Atlantic Cement*)' (Dec. 2011) 4 *Journal of Tort Law* Art. 3.

rights violator and the ex post exploitation of holdout power by the landowner. As argued below, this approach to injunctions, using shifting presumptions based on proxies for opportunism, handles the remedial problem here in a potentially better — in a more tailored and less destabilizing way — than do more ‘modern’ approaches in the case law or commentary.

The equitable function is not limited to torts and property. A prototypical category of traditional constructive fraud was contractual unconscionability. Unconscionability involves advantage taking, especially of the vulnerable. Interestingly, theories of unconscionability offered by Arthur Leff and Richard Epstein track traditional equity and are targeted at what I am calling opportunism.⁵³ Their version of unconscionability can be regarded as special case of constructive fraud,⁵⁴ and their theories are instances of the equitable function. As in other contexts, unconscionability employs proxies based on disproportionate hardship and bad faith to shift the presumption against the possible opportunist; more particularly, certain classes of people, such as the very young and very old, sailors on leave, and so on, will more easily raise the presumption of opportunism.⁵⁵

To carry out the equitable function in contracts, it makes sense for a court to go one level up, to meet the opportunists who take a comprehensive view of the situation. Indeed, unconscionability and equity are needed most where one party is ill-informed or otherwise vulnerable. Even for sophisticated parties, the reluctance to allow parties to bargain out of the contractual duty of good faith altogether may be rooted in a sense that even in contexts of apparent availability of information, one party may have found an unanticipated avenue of advantage taking. Moreover, as Epstein analogizes unconscionability to the statute of frauds,⁵⁶ the question we need to ask is whether there is a category of transactions that is so fraught with near-fraud that it is worthwhile not enforcing such bargains despite the few beneficial deals that may be swept in the net.

One virtue of the traditional set of proxies and presumptions in a second-order safety valve is its modular quality. In general, modularity is an important tool for managing complexity in systems.⁵⁷ By dividing a set of interactions into components —

⁵³ Arthur Allen Leff, ‘Unconscionability and the Code—The Emperor’s New Clause’ (1967) 115 *University of Pennsylvania Law Review* 485, 539; Richard A. Epstein, ‘Unconscionability: A Critical Reappraisal’ (1975) 18 *Journal of Law & Economics* 293, 293, 293–301; see also Henry E. Smith, ‘The Equitable Dimension of Contract’ (2012) 45 *Suffolk University Law Review* 897, 902–07.

⁵⁴ Story, above n 25 at § 221.

⁵⁵ Leff, above n 53 at 532.

⁵⁶ Epstein, above n 53 at 302.

⁵⁷ See, e.g., 1 Carliss Y. Baldwin & Kim B. Clark, *Design Rules: The Power of Modularity* (Cambridge, Mass., MIT Press, 2000); Raghu Garud, Arun Kumaraswamy & Richard N. Langlois (eds), *Managing in the Modular Age: Architectures, Networks and Organizations* (Malden, Mass., Blackwell, 2002); Herbert A. Simon, *The Sciences of the Artificial* (Cambridge, Mass., MIT Press, 2d ed., 1981) 195–200; Richard N. Langlois, ‘Modularity in Technology and Organization’ (2002) 49 *Journal of Economic Behavior &*

modules — that can interact only in certain ways across interfaces, the system can be modified and understood much more cost-effectively. Activity including innovation can occur in one module or a few modules without destabilizing ripple effects throughout the system. Think of the brakes and the ignition system of a car. Each can operate and be modified without worrying too much about the other. In private law, information is managed through modularity — not just in property, but tort, and contract as well.⁵⁸

Equity's safety valve is modular. The combination of domain-defining rules (in personam, irreparably injury) and the flowchart of proxies and presumptions allow equity to operate in greater isolation and with less destabilizing effect than it would otherwise. There are many situations in which equity is simply not relevant, and that can be known *ex ante*. By intervening at a second level, equity allows the law to be more general than it would be otherwise. The alternative to protecting the law against evasion through equity is to either allow the evasion or to make the law very complicated and specific *ex ante*. Allowing evasion can bring the law into disrepute.⁵⁹ And trying to head off every possible avenue of evasion is difficult without making the law either very complex or very blunt (with extreme prophylaxis). And most legal actors do not need to be policed with equitable interventions most of the time, and, unlike the opportunists, find the moral tone of equity reassuring.⁶⁰ Moreover, such a version of the law is likely to be very rigid and fail to remain responsive to change in background conditions. The very generality and simplicity that serve rule of law values may even be harder to implement without the backstop of equity. As is generally the case with modularity, some functional (if not jurisdictional) separation of regular law and equity can allow for specialization. The law can achieve generality, simplicity, publicity and the like, while equity targets its intervention against opportunism in a deep and through fashion. Equity's intervention can go further where it applies, because it does need not be generalized across the board.

If one regards the equitable function as that of a second-order safety valve to deal with complex and uncertainty-ridden problems like opportunism, that does not mean one can square the circle. Equity does involve judicial discretion and it does have some destabilizing effect. Instead, the account being offered allows us to state the tradeoff in equity in a precise form that draws on a well-developed framework of systems theory. Do the benefits from specialization at two levels — greater generality at the primary level and greater targeting of contextual intervention at the second level — exceed the costs of

Organization 19; Ron Sanchez & Joseph T. Mahoney, 'Modularity, Flexibility, and Knowledge Management in Product and Organization Design' (Special Issue Winter 1996) 17 *Strategic Management Journal* 63.

⁵⁸ Henry E. Smith, 'Property as the Law of Things' (2012) 125 *Harvard Law Review* 1691; see also Henry E. Smith, 'Modularity and Morality in the Law of Torts' (Sept 2011) 4 *Journal of Tort Law* Art. 5, <https://dash.harvard.edu/bitstream/handle/1/8789603/Modularity.pdf?sequence=1>; Henry E. Smith, 'Modularity in Contracts: Boilerplate and Information Flow' (2006) 104 *Michigan Law Review* 1175.

⁵⁹ Matthew Harding, 'Equity and the Rule of Law' (forthcoming 2016) 132 *Law Quarterly Review*.

⁶⁰ Yuval Feldman & Henry E. Smith, 'Behavioral Equity' (2014) 170 *Journal of Institutional and Theoretical Economics* 137.

setting up a second level and the costs of the targeting of equity's contextualized intervention? This also helps explain what courts have traditionally done. Although the equitable function was not exclusive to equity courts and was not absent from common law courts, the structure of the traditional doctrine can be explained and justified in terms of equity as a second-order safety valve. In separate work, I survey equity from this point of view.⁶¹ Here I wish to focus on what fusion risks giving up — and has to an alarming degree already done so in the United States — in the rush to deny any special differentiated role for equity in the legal system as a whole.

II. Carrying Fusion Too Far

There are many ways to carry out fusion. Some of them are extreme enough that the function of equity as a second-order safety valve is put in peril. That, I argue, is exactly what has happened in the United States, and it is a tendency in other jurisdictions as well.

Separate equity jurisdiction is perhaps sufficient (or at least helpful) for keeping the safety valve function of equity robust.⁶² It is certainly not necessary. Civilian legal systems largely did without separate equity courts, and yet doctrines like of abuse of right and abuse of law serve a similar second-order safety valve function. They are directed at opportunists, and the same concern with evasion and 'fraud on the law' pops all over in this part of the civil law.⁶³ Some of the same proxies relating to good faith and disproportionate hardship feature strongly in abuse of law in the civil law as well. To be sure, as in post-fusion common law jurisdictions, there is a tendency for some of these doctrines to expand beyond the function of a second-order safety valve. Nevertheless, it is possible to maintain a separate second-order element of a system that is jurisdictionally unified.

Such could be the case in the United States, but fusion has typically been pushed further and in a non-reflective fashion. The fusion of law and equity happened over a period extending from the mid-nineteenth to the early mid-twentieth century.⁶⁴ The

⁶¹ Smith, *Equity as Second-Order Law*, above n 12.

⁶² Besides highlight equity's distinct role, separate equity courts can afford consistency among equitable decision-makers and might lessen the tendency to stretch equity in the course of regular legal decision-making. How much scope to give the equitable function, whether in one court or two, will also depend on the degree of background consensus on matters like commercial morality and judicial decision-making, which is likely to be less now than in the era prior to fusion. *Ibid.*

⁶³ *Contra legem facit qui id facit quod lex prohibet; in fraudem vero qui salvis verbis sententiam eius circumvenit* (D. 1.3.29, Paul) ('The one who does what the law prohibits acts against the law; but the one who keeping to its terms gets around its spirit acts in fraud of the law'); see also D. 1.3.30; W.W. Buckland, *Equity in Roman Law* (London, University of London Press, 1911) 112–14; Henri Desbois, *La Notion de Fraude à la Loi et la Jurisprudence Française* (Paris, Dalloz, 1927); Oliver Heeder, *Fraus legis* (Frankfurt am Main, Lang, 1998).

⁶⁴ For the United States, see Federal Rules of Civil Procedure (1938); New York Code of Procedure of 1848, N.Y. Laws ch. 379 (Field Code); Ralph E. Kharas, 'A Century of Law-Equity Merger in New York'

conventional story has it that during this time a ‘Grand Style’ of moralism and policy-making judging was replaced by legal science and formalism, which was supplanted by waves of progressivism and Legal Realism.⁶⁵

From the earliest days of the Field Code through the Legal Realist era, fusion was presented as an unalloyed good. The more fusion the better. Fusion was regarded as almost a panacea for the problems of the justice system.⁶⁶ Impatience with the (supposedly) slow pace of fusion in the courts was palpable among commentators, with Charles Clark going so far as to claim that ‘[i]n fact it is unfortunate to continue to speak of law and equity, since that naturally tends to preserve old distinctions. The former principles of equity jurisprudence are now a part of our one body of applicable legal rules’.⁶⁷

Legal Realists believed in drawing upon equity to give their policy-oriented, judicially-driven reform some historical pedigree. This openness to equity did not extend to seeing a function to equity separable from the rest of the law. Some saw in the rising administrative state the new equity that would reform the law.⁶⁸

Law schools took equity out of the curriculum at the time. It was thought anachronistic to keep a separate equity course, and the material in such a course could be blended into various substantive courses. It is not atypical of this era when all Laswell and MacDougal can say of Equity is ‘What useful purpose is served by putting this rag-bag of stuff between two covers?’⁶⁹ Like restitution, substantive equity was folded into

(1949) 1 *Syracuse Law Review* 186. For England, see Supreme Court of Judicature Act 1873, 36 & 37 Vict, c 66; Supreme Court of Judicature Act 1875, 38 & 39 Vict., c. 77; Baker, above n 45, at 108–09; Stephen Waddams, ‘Equity in English Contract Law: The Impact of the Judicature Acts (1873-75)’ (2012) 33 *Journal of Legal History* 185.

⁶⁵ See, eg, Grant Gilmore, *The Ages of American Law* (New Haven, Yale University Press, 1977); Morton J. Horwitz, *The Transformation of American Law, 1870–1960: The Crisis of Legal Orthodoxy* (New York, Oxford University Press, 1992); Duncan Kennedy, ‘Form and Substance in Private Law Adjudication’ (1976) 89 *Harvard Law Review* 1685, 1725–40.

⁶⁶ See, eg, Edward Robeson Taylor, ‘The Fusion of Law and Equity’ (1917) 66 *University of Pennsylvania Law Review* 17, 17 (‘In the fusion of law and equity lies, in the opinion of the writer, the one great object to be achieved, if we would reach anything like a true reformation of the evils of the present administration of justice’.); Charles T. McCormick, ‘The Fusion of Law and Equity in United States Courts’ (1927) 6 *North Carolina Law Review* 283, 285 (‘Any separation of the stream of equity from the main channel of legal administration is today seen to be unjustifiable as an administrative device and explainable only as a historical survival from an era of multitudinous separate courts. [P] The desirability of reforming the practice in Federal Courts by abolishing the formal distinctions between proceedings at law and in equity, in harmony with the modern practice in England and most of the States, seems too clear for argument’.).

⁶⁷ Charles E. Clark, ‘The Union of Law and Equity’ (1925) 25 *Columbia Law Review* 1, 5.

⁶⁸ Henry E. Smith, ‘Equity and Administrative Behavior’ in *Equity and Administration* (P.G. Turner (ed), Cambridge, Cambridge University Press, forthcoming Apr 2016).

⁶⁹ Harold D. Lasswell & Myres S. McDougal, ‘Legal Education and Public Policy: Professional Training in the Public Interest’ (1943) 52 *Yale Law Journal* 203, 255.

the course on Remedies and then that course fell out of fashion, dealing equity a second death in the curriculum.⁷⁰ Even with some revival of the Remedies class of late, the leading casebook, by Douglas Laycock, is not organized around the old jurisdictional divide, in favor of a more modern and (supposedly) more functional organization around concepts like ‘in kind’ versus ‘compensatory’ remedies.⁷¹

I will turn to some implications of fusion in the next Part, but the conventional wisdom in our post-fusion era is that law and equity have been fused procedurally and equity won.⁷² In terms of substance, there is agreement that there are vestiges of equity here and there, but they are unjustified and are largely perpetuated out of inertia and the need to keep track of legal versus equitable issues for purposes of the right to a jury trial (where jury trial has not been extended to all claims legal or equitable).⁷³

III. Implications

Fusion has been taken far but is not complete. I argue that some characteristic contours of fusion in the United States stem from effacing equity as a second-order safety valve, and that this made fusion less successful than it should be.

Some of the aftermath of fusion is, as noted earlier, a Realist-inspired removal of the constraints on equity. Also, to the extent that the Realists and their successors saw the administrative state as dispensing the ‘new equity’, the action shifts from courts to agencies and the political and judicial control (or not) of those agencies. In both the administrative arena and in the case law since the Realist Era, one can discern an expansionist strand of equity as an all-purpose fix-it for problems arising in the legal system. In the early days of Realism, invocations of the ‘equity of the statute’ were popular, as were implications of equity as a response to change, in this case social and economic change.⁷⁴

So part of the aftermath of fusion is a greater tolerance for discretion. There is nothing particularly structural or bi-level about this version of equity. There is nothing

⁷⁰ See Lester B. Orfield, ‘The Place of Equity in the Law School Curriculum’ (1949) 2 *Journal of Legal Education* 26.

⁷¹ Douglas Laycock, *Modern American Remedies: Cases and Materials* (New York, Aspen, 4th ed, 2010).

⁷² Laycock, above n 7 at 53 (‘The distinctive traditions of equity now pervade the legal system. The war between law and equity is over. Equity won.’).

⁷³ See Fleming James, Jr., ‘Right to A Jury Trial in Civil Actions’ (1963) 72 *Yale Law Journal* 655, 663 (‘Under a merged procedure, few if any of the differences between law and equity continue to have any vitality, except the question of mode of trial.’); Laycock, *The Death of the Irreparable Injury Rule*, above n 48 at 696 & n.39 (presenting equitable relief as a tool to ‘manipulate jurisdiction or avoid jury trial’); *ibid* at 757–60 (same).

⁷⁴ See sources cited above n 7.

stopping us from implementing vague ex post standards at the primary level of regular law, and to some extent that is what has happened. Think unconscionability. If it is an all things considered fairness review — as it may be in some courts and not others — then one can say the bi-level structure has been flattening and equity expanded at the primary level. This triumph (if that is what it is) of equity is mirrored by the adoption of equity procedures (discovery, interpleader, class actions) over the more rigid ones of the common law.⁷⁵ It also reflects fusion statutes apparently directing courts to apply the equitable rule when law and equity conflict. This expansion of substantive standards is, however, something very different from the structural second-order safety valve identified here as an equitable function, and reflected in part in traditional equity.

There is more to the story than ever-expanding standards. Courts are still responsive to the considerations of the rule of law, or at least their appearance, and have had to contend in more recent decades with a backlash against unbounded judicial discretion. In this Part, I diagnose how some of the discontents in current American private law stem from our misguided approach to the fusion of law and equity.⁷⁶ Three principal aftershocks of fusion are the proliferation of standards and multifactor tests, the polarization of formalism and contextualism, and the flattening of the law of remedies.

A. Multi-Factor Balancing Tests

Few things are as notorious as the multi-factor test, especially the multi-factor ‘balancing’ test. It is easy to roll one’s eyes about them, but they are very hard for courts to resist. If one does not want to take a ‘tough luck’ approach to what Carol Rose calls ‘crystals’,⁷⁷ and yet one wants to provide some guidance to judicial decision makers, the multifactor test is a typical result. Even if they do not constrain judicial decision makers, they at least give the appearance something more constrained than total discretion.

Let me advance the hypothesis that much of substantive equity was replaced by multifactor tests and standards because when it comes to the equitable function, that is the closest mono-level substitute for a second-order safety valve. Although I do not argue that multi-factor balancing tests are never justified, the general sense that they have proliferated too far dovetails with an account of equity as a historical and functional substitute.

⁷⁵ Patricia I. McMahon, *The Fusion Fallacy Revisited: A Purposive Approach to the Fusion of Law and Equity Under the Judicature Acts, 1873–1875* (30 Sept 2015) (unpublished manuscript) (on file with the author).

⁷⁶ The implications of fusion in jurisdictions without a tradition of Realism tend to combine standards with finely tuned complex doctrine. See Joshua Getzler, ‘Patterns of Fusion’ in Peter Birks (ed), *The Classification of Obligations* (Oxford, Clarendon Press 1997) 157, 192–93.

⁷⁷ For Rose, ‘crystals’ are the ‘hard-edged doctrines that tell everyone exactly where they stand’ that are especially prevalent in the common law of property. Carol M. Rose, ‘Crystals and Mud in Property Law’ (1988) 40 *Stanford Law Review* 577, 577.

Examples of multifactor balancing tests are legion, and their virtue is their flexibility. This is sometimes termed ‘equitable’ in the sense of tailored and flexible — like Aristotle’s leaden rulers of the builders of Lesbos.⁷⁸ Thus, in a well-known example, courts have gravitated toward a multifactor balancing test for lawyer liability to third parties for malpractice, to replace the older privity rules,⁷⁹ with the California Supreme Court treating the question of potential liability as ‘a matter of policy and involv[ing] the balancing of various factors, among which are ‘the extent to which the transaction was intended to affect the plaintiff, the foreseeability of harm to him, the degree of certainty that the plaintiff suffered injury, the closeness of the connection between the defendant’s conduct and the injury, and the policy of preventing future harm’,⁸⁰ as well as ‘whether the recognition of liability to beneficiaries of wills negligently drawn by attorneys would impose an undue burden on the profession’.⁸¹ The traditional approach would be to apply privity as a legal matter but look beyond the formal privity in cases of unclean hands and constructive fraud.⁸²

Often the balancing approach takes the form of new tort liability based on standards in place of an older equitable devices like the constructive trust in restitution. John Goldberg and Robert Sitkoff argue that the new tort adopted in some states of interference with inheritance is a poor substitute for older approaches sounding in restitution and equity.⁸³ Goldberg and Sitkoff note that William Prosser, an early proponent of the new tort, recharacterized equity cases resting on constructive trust to prevent unjust enrichment as *de facto* tort decisions.⁸⁴ Goldberg and Sitkoff locate the problem in a Legal Realist vision of torts:

that . . . drains tort law of its doctrinal structure and content, leaving only an open-ended license for courts to shift losses and mete out punishment. On this view, a tort plaintiff need only prove a loss or a setback owing to the defendant's

⁷⁸ See above n 32 and accompanying text.

⁷⁹ See Tom W. Bell, ‘Limits on the Privity and Assignment of Legal Malpractice Claims’ (1992) 59 *University of Chicago Law Review* 1533 (discussing the expansive trend of lowering the privity bar and arguing that privity should be relaxed only ‘when equity demands’, *id.* at 1548); Lynn Curtis, ‘Changing Standards of Third-Party Liability in Estate Planning’ (1998) 66 *UMKC Law Review* 863, 864–65 (noting the trend since the 1970s toward multi-factor balancing tests for attorney third-party liability and arguing this provides for more ‘equitable’ results).

⁸⁰ *Lucas v. Hamm*, 364 P.2d 685, 687 (Cal. 1961) (in bank).

⁸¹ *Ibid* at 688.

⁸² See, eg, *Nat’l Sav. Bank of D.C. v. Ward*, 100 U.S. 195, 205 (1879) (‘Where there is fraud or collusion, [an attorney] will be held liable, even though there is no privity of contract; but where there is neither fraud or collusion nor privity of contract, the [attorney] will not be held liable.’).

⁸³ John C.P. Goldberg & Robert H. Sitkoff, ‘Torts and Estates: Remediating Wrongful Interference with Inheritance’ (2013) 65 *Stanford Law Review* 335.

⁸⁴ *Ibid* at 360–61.

antisocial conduct. Core concepts that have historically defined tortious conduct — such as duty, breach of duty, proximate cause, and injury — are reduced to empty labels. Tort is converted into the ‘chancellor’s foot’ caricature of old equity. It becomes an unstructured loss-shifting apparatus that has the potential to swallow better-defined fields of law, in this instance probate and restitution.⁸⁵

Not all multifactor tests are balancing tests. Sometimes courts strive mightily to capture what was once equitable with ex ante rules, but these tend to be complex multi-prong tests. The evolution of hot new misappropriation provides a high-profile example. In the leading case and fountainhead for modern misappropriation doctrine, *International News Service v. Associated Press*,⁸⁶ the U.S. Supreme Court held that one news service engaged in misappropriation by using the other’s ‘hot news’. Although this case is taken as being about property rights in news, the Court itself went to great pains to emphasize that the case was brought in equity and that the decision was an equitable one: ‘The transaction speaks for itself and a court of equity ought not to hesitate long in characterizing it as unfair competition in business’.⁸⁷ In the course of the majority opinion, the Court repeatedly makes reference to equity.⁸⁸ The reasoning of the Court sounds in desert for labor and the need for an incentive to gather news, and the result is a ‘quasi-property’ right in the news not availing against others generally (which would be in rem) but only those in direct competition. In his dissent, Justice Brandeis hits a number of cautionary themes and argued for a baseline of information being ‘free as the air to common use’.⁸⁹ Later, the Second Circuit, especially speaking through Judge Learned Hand, cut back the implications of this doctrine to the narrow context of hot news,⁹⁰ a remarkable feat for a lower court.

The fusion of law and equity has had unfortunate effects on misappropriation doctrine.⁹¹ First, the equitable aspect of the opinion and the doctrine have largely been lost, which means that some of the sources and limitations are lost as well. The original equitable doctrine is not as expansive as some might fear.⁹² Second, and relatedly, the

⁸⁵ Ibid at 392 (citation omitted). Goldberg and Sitkoff cite to Grant Gilmore’s *Death of Contract*, which argued that tort swallowed contract. Notice that the supposed vehicles for doing so — promissory estoppel and unconscionability — trace back to equity.

⁸⁶ 248 U.S. 215 (1918).

⁸⁷ 248 U.S. at 240.

⁸⁸ Ibid at 237–38; Ibid at 240 (twice).

⁸⁹ Ibid at 250 (Brandeis, J., dissenting).

⁹⁰ See, eg, *Cheney Bros. v. Doris Silk Corp.*, 35 F.2d 279 (2d Cir. 1929) (Hand, J.).

⁹¹ Henry E. Smith, ‘Equitable Intellectual Property: What’s Wrong With Misappropriation?’ in Shyamkrishna Balganesh (ed), *Intellectual Property and the Common Law* (Cambridge, Cambridge University Press, 2013) 42.

⁹² Equitable features — notably its action in personam, not in rem — limit the operation of the misappropriation doctrine more than its critics admit. See Harold Greville Hanbury & Ronald Harling

case is not really about property rights: equity was not supposed to declare in rem rights and the Court did not do so in *INS*. Third, once the doctrine is not equitable, the two-tier structure and safety valve nature of equity have to be replaced by something. In this case, the best replacement to date has been the Second Circuit's influential restatement of the law of misappropriation in Judge Winter's opinion in *National Basketball Association v. Motorola*.⁹³ The opinion seeks to capture hot news misappropriation in a five-prong test:

(i) a plaintiff generates or collects information at some cost or expense; (ii) the value of the information is highly time-sensitive; (iii) the defendant's use of the information constitutes free-riding on the plaintiff's costly efforts to generate or collect it; (iv) the defendant's use of the information is in direct competition with a product or service offered by the plaintiff; (v) the ability of other parties to free-ride on the efforts of the plaintiff or others would so reduce the incentive to produce the product or service that its existence or quality would be substantially threatened.⁹⁴

As we will see with injunctions, courts try to put some structure into what appears unstructured now that equity as a safety valve is no longer familiar.⁹⁵ For something as open-ended and closely tied to commercial morality as misappropriation, the *NBA v. Motorola* test may be the best that can be done, as a mono-level legal test. Nevertheless, the original equitable approach is, I have argued, more apt for situations of opportunism, and misappropriation is indeed about both ethics and efficiency.⁹⁶

Maudsley, *Modern Equity* (London, Stevens, 10th ed., 1976) 15 ('The key to understanding the nature of equitable remedies is the appreciation of the importance of the maxim that "Equity acts in personam." This has been the basis of the jurisdiction from the earliest days; and is so today.');

see also Gray, above n 46 (offering a historical account of equity's refusal to create property rights). The *INS* Court hinted at this restriction when it emphasized that 'a court of equity concerns itself only in the protection of property rights', not in their creation. 248 U.S. at 236. By acknowledging that misappropriation gives rise only to quasi-property whose duty holders were those in direct competition, the Court cabined the class of people affected by its intervention to AP's competitors, who opportunistically manipulated an existing, customary framework of private rights. See Smith, above n 91 at 57–62.

⁹³ 105 F.3d 841 (2d Cir. 1997). This is true whether, as the Second Circuit suggested recently, is a set of 'sophisticated observations in aid' of an analysis of preemption. *Barclays Capital Inc. v. Theflyonthewall.com, Inc.*, 650 F.3d 876, 901 (2d Cir. 2011); but see *ibid* at 911 (Raggi, J., concurring) (arguing that the five-part test was necessary to the result in *NBA*). One could say that the statement in the majority opinion in *Barclay*'s itself was dictum. See Shyamkrishna Balganes, 'The Uncertain Future of "Hot News" Misappropriation after *Barclays Capital v. theflyonthewall.com*' (2012) 112 *Columbia Law Review Sidebar* 134, http://columbialawreview.org/wp-content/uploads/2012/06/134_Balganes.pdf.

⁹⁴ 105 F.3d at 852 (citations omitted).

⁹⁵ The ahistorical and misleading four-factor test for injunctions recently adopted by the Supreme Court is the most recent example. *eBay v. MercExchange*, 547 U.S. 388, 390 (2006). See Mark P. Gergen, John M. Golden & Henry E. Smith, 'The Supreme Court's Accidental Revolution? The Test for Permanent Injunctions,' (2012) 112 *Columbia Law Review* 203.

⁹⁶ The *NBA* opinion is fusionist in disavowing ethics and speaking about property rather than quasi-property: '*INS* is not about ethics; it is about the protection of property rights in time-sensitive information so that the

As mentioned earlier, opportunism is not the only problem calling for a second-order equitable intervention. Situations of conflicting rights also can be amenable to resolution at a higher level. Indeed, traditional nuisance law took such an approach, with courts deciding nuisance cases on the basis of invasion (mini-trespass) shading off into a complex reconciliation of conflicting use rights.⁹⁷ For example, in *Campbell v. Seaman*,⁹⁸ a decision enjoining the sulfuric fumes from a brick-making works, the court invokes the locality rule, shutdown costs, uniqueness of the location, irreparable injury, a threatened multiplicity of suits, and (absence of) disproportionate hardship. The analysis is quite ‘meta’ and sophisticated, much more so than the more recent *Boomer v. Atlantic Cement*,⁹⁹ which appears to endorse damages instead of injunctions when the plaintiffs are numerous, a flat single-level decision if there ever was one.¹⁰⁰

Nuisance these days is in flux, and as with other echoes of equity, the multifactor balancing test looms large in theory if not exactly in practice. Notably the Restatements, especially the Second Torts Restatement, have advocated balancing tests for nuisance.¹⁰¹ Under the Second Restatement, a nuisance is a substantial nontrespassory interference with the use and enjoyment of land that is caused either by intentional and unreasonable activities, or negligent, reckless, or ultrahazardous activities. As is often the case, the key to intentional nuisances largely turns on reasonableness:

An intentional invasion of another’s interest in the use and enjoyment of land is unreasonable if
(a) the gravity of the harm outweighs the utility of the actor’s conduct, or
(b) the harm caused by the conduct is serious and the financial burden of compensating for this and similar harm to others would not make the continuation of the conduct not feasible.¹⁰²

information will be made available to the public by profit seeking entrepreneurs.’ 105 F.3d at 853. The court may have meant ‘property rights’ in an economic sense.

⁹⁷ Henry E. Smith, ‘Exclusion and Property Rules in the Law of Nuisance’ (2004) 90 *Virginia Law Review* 965.

⁹⁸ 63 N.Y. 568 (1876).

⁹⁹ 257 N.E.2d 870 (N.Y. 1970).

¹⁰⁰ The decision has been wildly popular in law and economics, *see* Calabresi & Melamed, above n 49, and the case and this commentary have been persuasively critiqued by Laycock, *see* Laycock, above n 52.

¹⁰¹ *Restatement (Second) of Torts* §§ 822, 826 (1939).

¹⁰² *Ibid* § 826; *see also* *Ibid* § 827 (setting out factors relating to gravity of the harm, including the social value of the plaintiff’s use); *id.* § 828 (setting out factors relating to utility of actor’s conduct, including its social value); 6A *American Law of Property* § 28.22, at 66, § 28.26, at 75–77 (A. James Casner (ed), Boston, Little Brown, 1954) (emphasizing the vagaries associated with, and importance of, a determination as to whether a defendant’s conduct is unreasonable); 1 Fowler V. Harper & Fleming James, Jr., *The Law of Torts* § 1.24, at 70–74 (Boston, Little Brown, 1956) (discussing the importance of reasonableness consideration in nuisance cases). *See generally* Jeff L. Lewin, ‘Boomer and the American Law of

Restatements are known for multifactor balancing tests as well as standards as opposed to rules.¹⁰³ The fusion of law and equity may well have furnished a lot of the material for these tests.

Pushing fusion to the point of erasing its second-order function does not cause the problems calling for second order solutions to simply vanish. Instead, they still need solving and all that's left are solutions at the same level as the problem. Standards and multifactor tests are among the main avenues remaining, once equity in the safety valve sense has been fused out of existence.

B. Polarization of Formalism and Contextualism

The formalist-contextualist debate continues, especially in the area of statutory interpretation.¹⁰⁴ In the post-fusion era when Legal Realists and their successors argue for maximal potential use of context, they are in a sense arguing for equity all the time.¹⁰⁵ This has the potential of undermining the simplicity and stability (otherwise) of the relatively formal parts of the law. On the other side, formalists will be driven to more elaborate ex ante formulations in the face of party opportunism. The result tends to be multifactor tests or, to be very formal, rules that are not tailored toward goals. The debate also rages in law and economics, and I have suggested that the new formalism has also mistakenly dismissed hybrid decision-making featuring equity as anti-opportunism. These debates extend importantly to corporate law, in which an explicitly equitable court, the Delaware Court of Chancery, does exhibit an anti-opportunism theme in its corporate jurisprudence, to the delight of some and consternation of others.¹⁰⁶

Nuisance: Past, Present and Future' (1990) 54 *Albany Law Review* 189, 212–14 (documenting the limited adoption of the balance of the utilities test for reasonableness, and citing cases). Courts may invoke the Restatement formulation but not actually engage in the cost-benefit test, instead following a more traditional approach to nuisance. See, eg, *Morgan v. High Penn Oil Co.*, 77 S.E.2d 682 (N.C. 1953).

¹⁰³ See Alan Schwartz & Robert E. Scott, 'The Political Economy of Private Legislatures' (1995) 143 *University of Pennsylvania Law Review* 595 (evaluating the taxonomy of rules produced by private law-making groups such as the American Law Institute, which puts out the Restatements).

¹⁰⁴ See, eg, Guido Calabresi, *A Common Law for the Age of Statutes* (Cambridge, Mass., Harvard University Press, 1982) 5–7; William N. Eskridge, Jr., *Dynamic Statutory Interpretation* (Cambridge, Mass., Harvard University Press, 1995); Richard A. Posner, *The Problems of Jurisprudence* (Cambridge, Mass., Harvard University Press, 1990) 247–309; Antonin Scalia, *A Matter of Interpretation* (Princeton, Princeton University Press, 1998); Adrian Vermeule, *Judging under Uncertainty* (Cambridge, Mass., Harvard University Press, 2006); Abbe R. Gluck, 'The States as Laboratories of Statutory Interpretation: Methodological Consensus and the New Modified Textualism' (2010) 119 *Yale Law Journal* 1750; John F. Manning, 'What Divides Textualists from Purposivists?' (2006) 106 *Columbia Law Review* 70; Caleb Nelson, 'What Is Textualism?' (2005) 91 *Virginia Law Review* 347.

¹⁰⁵ Smith, above n 47, at 1177–83; Smith, Modularity in Contracts, above n 58; see also sources cited above n 7.

¹⁰⁶ See Andrew S. Gold and Henry E. Smith, *The Equity in Corporate Law* (unpublished manuscript) (on file with the authors).

Law versus equity features strongly in the debates over formalism and textualism on the one hand and contextualism and purposivism on the other. The conflict was quite overt in the case of *Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc.*,¹⁰⁷ in which the question was the availability of preliminary injunctions to freeze unrelated assets in a suit in which only money damages were being sought. (These are known as *Mareva* injunctions in the UK.¹⁰⁸) The majority per Justice Scalia held that because that power did not exist at equity at the time of the Federal Judiciary Act of 1789, federal courts may not issue such preliminary injunctions.¹⁰⁹ In dissent, Justice Ginsburg favored the availability of such preliminary injunctions based on the flexibility and generativity of the equity power.¹¹⁰ For her, the test for a preliminary injunctions cabined the power enough, but with no apparent structure or bite to these limits. Both polar positions overstate matters. The theory here suggests that equity should be available but only by applying the ‘test’ for preliminary injunctions narrowly. In *Grupo Mexicano*, the defendant was apparently acting quite opportunistically, and the preliminary injunction would serve to protect jurisdiction over assets and prevent judgment-proofness, concerns fitting well within the traditional domain of equity and its role as an anti-opportunism device.

Let me suggest that much of the formalism versus contextualism in American law and jurisprudence is an artifact of the overdoing of fusion. This is as true of contract theory as it is of statutory interpretation. It even extends to jurisprudential *über*-chestnut *Riggs v. Palmer*,¹¹¹ the case of the murdering grandson. In that case the court applied an equitable style of analysis to the interpretation of the wills statute and to the will itself, to prevent the murdering heir from profiting from his own wrong — an equitable maxim relabeled in the opinion as ‘common law’. The dissent vigorously argued for a literal application of the wills statute, leaving punishment of the grandson to the criminal law. The contextualist versus formalist debate relitigates this case repeatedly to this day. Ironically, in an earlier era, the court probably would have treated the transfer to the grandson under the will as valid but would subject him to a constructive trust, as Ames was to argue later.¹¹² It would appear that the court in *Riggs* flattened this structure out to

¹⁰⁷ 527 U.S. 308 (1999). See generally Stephen B. Burbank, ‘The Bitter with the Sweet: Tradition, History, and Limitations On Federal Judicial Power — A Case Study’ (2000) 75 *Notre Dame Law Review* 1291 (analyzing the *Grupo Mexicano* case).

¹⁰⁸ See *Mareva Compania Naviera SA v International Bulkcarriers SA*, 2 Lloyd’s Rep 509 (CA) [1980] 1 All ER 213.

¹⁰⁹ *Ibid* at 332–33. Freezing orders, or *Mareva* injunctions as they are also known, are familiar in Commonwealth jurisdictions.

¹¹⁰ *Ibid* at 342 (Ginsburg, J., dissenting).

¹¹¹ 22 N.E. 188 (N.Y. 1889).

¹¹² James Barr Ames, ‘Can a Murderer Acquire Title by His Crime and Keep It?’ (1897) 45 *American Law Register* 225.

make the transfer void, with potentially problematic consequences, as in third-party purchase situations.¹¹³

C. The Flattening of Remedies

Nowhere are the pernicious effects of flattening the two-level structure of law and equity more apparent than in remedies. Traditionally, rules of thumb, varying somewhat by substantive area, would involve presumptions triggered by irreparable harm, good faith, disproportionate hardship, with defenses of unclean hands and the like. With a few prior hints in the lower courts, the U.S. Supreme Court recently adopted a four-part test for injunctions in *eBay v. MercExchange*.¹¹⁴ Ironically, the court repeatedly invoked the ‘traditional principles of equity’,¹¹⁵ but the test is actually relatively new and is constructed out of the test for preliminary injunctions.¹¹⁶ Under the *eBay* test, the movant must show:

(1) that it has suffered an irreparable injury; (2) that remedies available at law, such as monetary damages, are inadequate to compensate for that injury; (3) that, considering the balance of hardships between the plaintiff and defendant, a remedy in equity is warranted; and (4) that the public interest would not be disserved by a permanent injunction.¹¹⁷

Although motivated by the problem of patent trolls and their alleged misuse of the leverage of an injunction, the test is not confined to patent law or intellectual property. Since it was announced, the Court has now applied it in an administrative environmental case, and the test spreading throughout the federal courts.¹¹⁸

¹¹³ As opposed to voiding title altogether, imposing a constructive trust would give the true owners — in *Riggs*, the murdered grandfather’s daughters — equitable, rather than legal, title to the fraudulently acquired property. The distinction has dramatic consequences for third party purchasers. See Note, ‘Vesting Title in a Murderer: Where Is the Equity in the Georgia Supreme Court’s Interpretation of the Slayer Statute in *Levinson*?’ (2011) 45 *Georgia Law Review* 877; see also Grant Gilmore, ‘The Commercial Doctrine of Good Faith Purchase’ (1954) 63 *Yale Law Journal* 1057, 1059–62 (describing the consequences for third parties who acquire void versus voidable title in fraudulently transferred property — the latter privileges good-faith purchasers for value over true owners). Proponents rationalize this policy as promoting finality in commercial transactions. See Andrew Kull, ‘Rationalizing Restitution’ (1995) 83 *California Law Review* 1191, 1234.

¹¹⁴ 547 U.S. 388, 390 (2006). The Court has reiterated this test outside the patent context. See *Monsanto Co. v. Geertson Seed Farms*, 547 U.S. 139, 156–59 (2010).

¹¹⁵ 547 U.S. at 394. The Supreme Court has of late shown an increased interest, if not understanding, of equity. For an excellent (and in my view quite charitable) analysis, see Samuel L. Bray, ‘The Supreme Court and the New Equity’ (2015) 68 *Vanderbilt Law Review* 997.

¹¹⁶ Gergen, Golden, & Smith, above n 95.

¹¹⁷ *eBay*, 547 U.S. at 291.

¹¹⁸ See, eg, *Monsanto*, 561 U.S. at 156–59; see also Gergen, Golden, & Smith, above n 95.

The test seems to adopt an attitude of equipoise, which is appropriate to the context of a preliminary injunction but not so much to cases involving a proven rights violation, in which the problem is potential opportunism on both sides. Take the ‘balance of the hardships’, which traditionally was about whether the injunction would visit a ‘grossly disproportionate hardship’ on the defendant and so would trigger a defense to a presumption for an injunction against a rights violator.¹¹⁹ In the *eBay* test the tendency is to ask the question without a presumption — asking simply who would be hurt more — and to even to do a mini cost-benefit analysis.¹²⁰

Even worse, notions of good faith and bad faith do not figure directly in the *eBay* test. Proxies relating to good faith are very relevant to equity — that is often what conscience comes down to — and as part of a second-order safety valve, assessing an actor’s good faith can be crucial. For very clear rights violations, such as a building encroachment, simple knowledge in the violator of the violation tips the scale decisively for an injunction. Another irony is that the very problem that motivated the Court to adopt its test in *eBay*, the problem of so-called patent trolls, itself calls for a second-order safety valve. The problem is two-sided potential for opportunism — by the infringer who might violate more if the remedy is inadequate, and the holding-out, troll-like patent owner — and the traditional equitable approach based on good faith and disproportionate hardship is tailor-made for this situation.¹²¹

Another area of remedies in which equity has been flattened out is the constructive trust. Indeed, in *Riggs* itself, the court seems to have been so anxious to relabel equity as ‘common law’ that the transfer to the grandson was treated as void —

¹¹⁹ See, eg, 42 *American Jurisprudence* 2d, ‘Injunctions’ § 35 (2005) (‘Even if the wrongful acts are indisputable, an injunction may be denied if the payment of money would afford substantial redress and if the injunction would subject the defendant to grossly disproportionate hardship.’); see also Richard A. Epstein, ‘A Clear View of *The Cathedral*: The Dominance of Property Rules’ (1997) 106 *Yale Law Journal* 2091, 2102 (arguing that ‘essentially the appropriate solution is to allow injunctive relief when the relative balance of convenience is anything close to equal, but to deny it (in its entirety if necessary) when the balance of convenience runs strongly in favor of the defendant. The usual presumption is that the exploitation risk is greater than the holdout risk. This presumption can be reversed by a showing of the dramatic difference in values . . .’); Herbert F. Schwartz, ‘Injunctive Relief in Patent Infringement Suits’ (1964) 122 *University of Pennsylvania Law Review* 1025, 1045–46 (suggesting a ‘grossly disproportionate hardship’ standard); Henry E. Smith, ‘Institutions and Indirectness in Intellectual Property’ (2009) 157 *University of Pennsylvania Law Review* 2083, 2131 (‘Because equity incorporated a standard of behavior and an injunction implements a sanction rather than a price, it is not surprising that decision making here is not a matter of equipoise but rather a rough matter of avoiding egregious errors in an otherwise robust system of injunctive relief’).

¹²⁰ See, eg, *Warner Bros. Records v. Walker*, 704 F. Supp. 2d 460, 468 (W.D. Pa. 2010) (stating one of the *eBay* factors as ‘whether the balance of the hardships tips in Plaintiffs’ favor’); *AshBritt, Inc. v. U.S.*, 87 Fed. Cl. 344, 378–79 (2009) (requiring movant to show *inter alia* that ‘the balance of the hardships tips in the movant’s favor’).

¹²¹ Smith, above n 119 at 2125–32; Henry E. Smith, ‘Property as Platform: Coordinating Standards for Technological Innovation’ (2013) 9 *Journal of Competition Law & Economics* 1057, 1078–88.

rather than as effective but leading to treatment of the murdering heir as a constructive trustee for the sisters. It would appear that the court was, as usual, overdoing fusion.

Conclusion

Fusion has turned out to be about a lot more than fusion. Recognizing an equitable function of solving complex problems of great uncertainty at a second level allows us to see what needs to be preserved if fusion is to be done right. Equity can be seen as part of a modular private law that manages complexity, rather than as a troublesome wild card. When it comes to problems like opportunism, we are naturally led to solutions like the second-order safety valve, and a strong case can be made that this is the least bad of the alternatives as long as we will have opportunists in our midst. Unfortunately, the general assumption that equity is nothing special has led to an effacement of this structure in both equity and the law. There is no need to resurrect the jurisdictional divide as long as we are clear on what the equitable function is, regardless of the kind of court that is performing it. The hour is late in the United States, where equity is half submerged in multifactor tests, effaced by unproductive debates between formalists and contextualists, and flattened out of a now much cruder law of remedies. Even in other jurisdictions, it is imperative to provide a functional analysis of equity, for in the absence of such a rationale, equity will be increasingly difficult to defend.