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Beyond Traditional Methods of Judicial Interpretation and Adaptation

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Abstract

The impact of the unforeseen on “economy of the contract” is a practical problem, where the unexpected event destroys the economic balance negotiated by the parties. To mitigate this, the contracting entities include adaptation clauses, designed to safeguard the internal economy of the contract. However, most of these mechanisms are poorly drafted, often leading to disputes regarding their true meaning. Consequently, the choice of the interpretive method by the judge, the lens through which he is going to use to read the clauses, has a major impact on how he enforces them. Traditional interpretative methods tend to treat the contract as a static text or subjective puzzle, resulting in judgments that are legally correct but economically absurd, which led some judges to adopt an economic method that treats the contract as an economy. This point highlights the central challenge that this paper addresses: To what extent does the economic method outperform traditional approaches in enhancing accuracy, reducing unpredictability of outcomes when courts interpret and enforce adaptation clauses? Methodologically, this study employs a dual approach: it combines a critical doctrinal analysis, utilizing a comparative review to illustrate divergent outcomes, and a normative Law and Economics framework. This framework explains why the “economy of the contract” is a superior method, offering a direct practical outcome by enhancing both fairness and predictability in judicial decisions. Consequently, this paper contributes to critical debates regarding the failure

of traditional methods, arguing that their rigid application often precipitates the economic destruction of the agreement.

Keywords: Contract law, unforeseen events, adaptation, law and economics

Introduction

Contract law is built on the foundation of predictability, yet the last two decades have been marked by profound instability. The 2009 global financial crisis demonstrated it with brutal clarity: how even the most well-negotiated contracts drafted by big international law firms using advanced technologies were rendered economically nonsensical overnight as global credit markets froze and asset values collapsed.

The impact of these unforeseen events on the “economy of the contract” can be devastating, ranging from making it expensive to execute to turning the contract itself into an economically meaningless operation. In this context, the economy of the contract refers to the underlying commercial rationale and financial equilibrium that parties seek to achieve when entering the agreement. This vulnerability of the contracts is not the result of parties’ incompetence in most cases, but a fundamental problem explained by the economic analysis of the law: all contracts are inherently “incomplete” (Frydlinger & Hart, 2024) since it is economically unprofitable for them to insure the contract against every possible contingency, and because there are inherent limits to human cognition in anticipating all future events. As a result, contractual gaps are an inevitable feature of complex agreements (Mouzas & Naidu, 2024).

In response, when negotiating the agreement, the parties include clauses that allow them to adapt it to the new reality that is changed by the unforeseen event, with the objective of protecting the internal economy from outside shocks or, when failing that, to allow the termination of the contract when it becomes meaningless. This is what we call an “impossible economy”: when the impact of the unforeseen event is so strong that the contract becomes economically impossible to perform. In this context, some legal systems, such as France with its theory of *imprévision* allow the judge to adapt the contract even without the existence of an adaptative clause.

However, when the unforeseen disrupts the economy of the contract, the signatories find themselves with a vague drafting or deliberate incompleteness of the clauses, an “agree to disagree” strategy that enables opportunism (Parisi et al., 2024). In such cases, judges are compelled to interpret and enforce these vague clauses, a task that can be difficult when dealing with complex contracts that include risk allocation mechanisms.

The choice of interpretive method by the judge, the lens through which he is going to use to read the clauses, has a major impact on how he will

enforce them, while some judges adopt traditional methods, such as textualism (where only the word of the contract matters) or purposivism (where the reasoning is based on what the parties want from the contract), others have adopted another approach, an economical approach, where contracts are considered an economy, and thus interpreted and adapted using an economic logic, as mentioned in the ruling by the French Court of Appeal in 1894: "to recognize the true meaning of a convention, it is necessary to study its general economy."

Choosing the correct method is not a minor theoretical debate, but a profound practical problem. A judge who applies a textual reading to a contract that was negotiated by the parties based on an economic logic that goes beyond the words of the contract will risk being legally correct but commercially absurd. Conversely, a judge who applies purposivism can create uncertainty because it will be left to their appreciation of the situation.

This point highlights the central challenge that this paper addresses: To what extent does the economic method outperform traditional approaches in enhancing accuracy, reducing unpredictability of outcomes when courts interpret and enforce adaptation clauses?

This study hypothesizes that the use of economic rationale by judges increases contract fairness and flexibility while ensuring the legality and predictability of outcomes. And so, by considering economic interpretation and adaptation as pragmatic legal tools, this paper contributes to ongoing debates on how the brute use of traditional methods has disastrous economic effects on the contract.

Methodology

Methodologically, this paper combines a critical doctrinal analysis with a normative Law and Economics framework. The doctrinal inquiry is not merely descriptive; rather, it is employed to critique traditional methods (Textualism and Purposivism). This analysis is paired with a normative economic framework to argue for how courts ought to interpret adaptation clauses to maximize efficiency.

Justification of Jurisdictional Scope: To this end, the study focuses on the United Kingdom and France as representative archetypes. The United Kingdom serves as the model for strict interpretation judgments, highlighting the friction between text and commercial context. France acts as the counter-model, selected specifically for its judicial application of the "economy of the contract". This concept is analyzed not merely as a theory, but as a practical mechanism that guides judges in how to adapt the contract's terms to restore the parties' original equilibrium.

Case Law Selection Criteria: Within these jurisdictions, case law was chosen through purposive selection, specifically targeting "hard cases" such

as *Rainy Sky S.A. and Arnold v Britton*. These examples were selected to illustrate instances where traditional interpretive methods produce legally correct yet economically absurd outcomes, thereby isolating the specific failures of current approaches and justifying the need for the economic method proposed in this study.

This article will proceed as follows: (i) It examines the traditional methods and shows, through case studies, why they fail as mechanisms for interpreting and adapting contracts after unforeseen events. (ii) Introduce and defend the use of the economic approach as a superior analytical framework for interpreting and adapting contracts to a new reality.

1. The failure of traditional methods:

A. Textualism:

Textualism, also referred to as formalism, is the traditional and most rigid method of contractual interpretation in this context. It should be mentioned that this method is mainly limited to interpretation, but it directly impacts how adaptive clauses will be enforced. Its philosophy is based on one simple premise: a contract is a written instrument whose meaning lies in its text, and so the judge, when interpreting the contract, should enforce that language as agreed upon, without looking at any other subjective elements (Al-Owaid, 2017). This method aims to maintain the primacy of contractual language by using a strict toolkit that includes the “four corners” rule, which prevents the judge from referring to any evidence outside of the contract itself, and the “parol evidence rule,” which prevents the judge from relying on pre-contractual documents that contradict the final text (Schroeter, 2010; Gilson et al., 2017).

This method has been supported by several authors who consider it to carry a strong efficiency-based rationale. Schwartz and Scott (2010) contend that by solely referring to the contract, it provides predictability and reduces both drafting and litigation costs. Some authors, such as Antonin Scalia (1997), argue that allowing judges to search for subjective elements such as what the parties might want from a contract is “thoroughly evil,” because it encourages them to substitute their own subjective “virtues” and policy preferences, which he considered “lawless.” Textualism has strong proponents in some courts, such as in the US, where judges explicitly prioritize this method. Antonin Scalia, a judge of the Supreme Court of Justice, one of the most influential advocates of modern textualism, argued that judges should give effect to the ordinary meaning of the text and avoid using other methods. Empirical studies prove this shift towards textualism, in a study conducted in 2025 by James J. Brudney, who analyzed 664 decisions from 1969 to 2023. The reliance on textualism has increased from 48.5% in 1969 to 75% in 2023.

However, when interpreting contracts that include adaptation clauses, this method faces significant limitations (Silverstein, 2021). Since when the judge applies a blind textual reading to clauses that were negotiated using economic logic that goes beyond the text, he risks reaching results that are “legally correct but commercially absurd”, this was pointed out even by judges themselves, such as Judge Posner in 2016, who considered textualism a “flawed” theory because it ignores the economic context that gives words their meaning, leading to pragmatically inefficient results. This failure is a result of many reasons, like the exclusion of the commercial context and reality. Adaptation clauses are fundamentally designed to address the disruption in the contract’s economic balance (Alsharqawi et al., 2025). However, most of these clauses cannot perform unless we look outside the contract itself, since we need a reference like the commercial reality the parties were in when negotiating the contract, or the industry norms to determine that the contract became excessively expensive to execute and imbalanced. And so, by refusing to take into consideration these elements, these clauses become “impracticable”.

Another reason behind the failure of this method is the idea that textualism promotes neutrality by limiting the judge to the text of the contract. The supporters of this method claim that the judgments are fair and not affected by any biases. However, empirical analysis suggests the failure of this claim (Silverstein, 2021). In practice, when the judge interprets the contract, he uses a dictionary that helps him define every term of the contract. But every dictionary has a different view of terms, and so the judge can go back and forth between this collection of dictionaries to “cherry-pick” the definitions to either support or deny an adaptation claim. And so, when the adaptation clause includes a term like “expensive to execute,” the judge can pick a dictionary that is rigid or more open to what this term can possibly mean.

Case study: Arnold v Britton

In the 1970s, a group of tenants took 99-year leases. The contracts included an adaptive clause under which the tenants agreed to pay a service charge of £90, increasing by 10% per annum compounded. However, this adaptive clause was negotiated in 1970, when inflation skyrocketed. As inflation fell during the 1980s and the 1990s (from 25% to 5%), the application of the clause produced an economically disproportionate outcome, as the tenants would eventually end up paying more than £11.27 million in total (for reference, a house in that period used to cost between 57k and 59k).

The Supreme Court, led by Lord Neuberger, delivered a landmark textualist judgment in which he explicitly rejected the tenants’ reliance on “commercial common sense,” stating that it “should not be invoked to undervalue the importance of the language”. This case demonstrates the

limitations of a purely textual approach: while the court's interpretation was legally precise regarding the syntax, it enforced a financial obligation that diverged significantly from the underlying commercial context.

B. Purposivism:

The philosophy of purposivism is that language is an imperfect tool for capturing human intention. In other words, the content of the contract is insufficient to understand the contractual relationship between the parties. Therefore, judges often assume what the parties wanted to complete and understand the contract, using what is called "commercial common sense" (Al-Owaid, 2017).

In this approach, the judge's role is not only to read the text in isolation but also to look for the real commercial purpose that the parties were trying to achieve. This method is considered more economically fair than a strict literal interpretation, since courts do not directly enforce the clause word for word, but instead try to find a balance between the content of the contract and what the parties intended, by filling the gaps they left in their incomplete contracts (Anderlini et al., 2003).

However, this method also failed when dealing with adaptation clauses, for the opposite reason that textualism failed. If textual interpretation is too rigid, purposivism is too flexible, which depends heavily on the judge's personal appreciation or sense of fairness. This creates uncertainty, since the result of each case depends more on the judge than on the contract itself. Some judges will apply the clauses literally, while others will use commercial common sense to complete them. This narrative creates two main problems: First, it incentivizes parties to litigate and to conduct many expensive research and investigations in hopes of manufacturing ambiguity to influence the judge's interpretation, rather than settling amicably. The second point is that the law itself can change depending on the judge's view. These inconsistent outcomes make the legal system unstable, and so each court will give a different interpretation to the same facts. In some countries, like the United Kingdom, this problem became serious enough that the courts had to correct it. In *Arnold v Britton* (2015), Lord Neuberger ended what was called the "era of purposivism" by stating that commercial common sense should not be used to undervalue the importance of the language itself.

Case study: Rainy Sky S.A. v Kookmin Bank

The potential instability of purposivism is illustrated by cases in which different courts looked at the same contract and reached completely different conclusions. The *Rainy Sky S.A. v Kookmin Bank* case is the best example of this problem.

In 2001, Rainy Sky S.A. agreed to buy ships from Jinse Shipbuilding Co. Ltd., paying in advance in five instalments of \$6.66 million each (each vessel cost \$33.3 million). The contract required Kookmin Bank to issue “advance payment bonds” to guarantee that the money would be repaid if the shipbuilder defaulted. These terms were stated in Article X.8, which stated that the builder must provide refund guarantees before the buyers paid the first instalment, and in Article XXII.3, which said that if the builder became insolvent, it had to refund the payments plus interest. However, when the bank issued the bonds, the language was unclear, and the refund conditions were confusing.

In 2008, the builder ran into financial problems and, in 2009, entered a debt workout process. The buyers treated this as insolvency and demanded a full refund, as Article XXII.3 required. When the builder refused, the buyers asked the bank to pay under the bonds, but the bank refused, saying that this type of insolvency was not covered by the bond’s wording.

The judicial discord throughout the appellate process highlights the subjectivity of the interpretive method in the High Court. Judge Simon J ruled for the buyers, reasoning that the bond made no sense if it did not cover the same risks as the main contract, and that it was not a separate contract but part of the same transaction. This decision was based on commercial common sense. When the bank appealed, the Court of Appeal, led by Patten LJ and Thorpe LJ, focused strictly on the wording of the bond and decided that it was clear enough to exclude insolvency, so the bank did not have to pay.

When the case reached the Supreme Court, the reasoning changed again. The judges returned to commercial common sense and focused on the purpose of the bond. They asked, “Why would a buyer pay millions for a refund guarantee that does not cover the builder’s bankruptcy, which is the most obvious risk?” They concluded that there was no reasonable commercial explanation; therefore, the bank had to pay.

The outcome of this case depended entirely on how the judges chose to read the contract. This shows that purposivism creates major uncertainty: Two or three courts can read the same clause in completely different ways. This makes the law unpredictable and confusing for businesses that depend on clear rules.

2. The economic approach as a superior analytical framework:

A. How the method works:

The economic method of contractual analysis is an analytical approach that integrates economic reasoning into the process of interpretation and adaptation of contracts. It enables judges to consider the contract not as a text or a combination of clauses, but as a coherent “economic structure” (Brousseau, 2002), a micro-economy structured around the allocation of risk,

performance, and incentives designed to generate mutual gains from exchanges.

This method was first used as early as 1984 in the French court of appeal, stating that: “to recognize the true meaning of a convention, it is necessary to study its general economy.” This formulation is marked as the first explicit invocation of the idea that the contract interpretation should be guided not by just literal wording but by the overall economic purpose and balance of the agreement.

The interpretation in this legal economic mindset is a process of ensuring that the agreement functions as an effective tool for exchange (Sugianto, 2024), assuming that both parties are “rational” and entered the agreement to achieve the most satisfying results based on profit and loss consideration (Sugianto, 2025), and so, when the judge is faced with an ambiguity or gap, assuming the “Pareto efficiency,” the judge ensures that interpretation is done in good faith and so the exchange is beneficial economically to both parties (Martimort et al., 2025).

The judge studies the contract on two levels: one is quantitative and objective, and the other is qualitative and subjective. In the first stage (quantitative objective), the judge determines the quantitative impact of the unforeseen event on the contract by establishing the “Economic Baseline,” the original equilibrium negotiated by the parties when forming the contract, which now works as a reference point allowing the judge to distinguish between a structural imbalance inherent in the contract (in the case of a bad bargain) and an external shock. Once the baseline is determined, the judge measures the deviation caused by an unforeseen event. Economically speaking, every contract involves risks and losses; however, there is a difference between ordinary losses and abnormal ones. Generally, when it exceeds the norms that a reasonable person would expect, this step is crucial since most adaptation clauses are conditioned on proving that the change in circumstances surpasses the threshold of normal commercial risk.

In the second stage (qualitative and subjective), based on the original equilibrium, the judge interprets each clause of the contract with the assumption that the parties are rational economic actors “Homo economicus” (Brousseau, 2002), and so any clause that is economically absurd is considered incorrect because no rational agent would consent to a deal that guarantees their own financial destruction. In this context, the judges read the contract with the assumption of good faith.

We can demonstrate this process by an example: an agreement between a supplier and a construction firm. Under this contract, the supplier agrees to sell steel at \$600 per ton, leaving a normal profit margin of \$100 per ton. This margin becomes the economic baseline, representing the equilibrium that both parties expect rationally. Two years later, due to an unforeseen cost

increase, the supplier's cost rises to \$750 while the contract price remains fixed at \$600. This means that the cost increased by 50%, and the contract became economically meaningless for the supplier who reasonably expected profit. However, this contract contains two clauses: an adaptation clause: "In the event of significant changes in market conditions, the parties shall consider in good faith any necessary adjustments to maintain the contractual balance" and an absurd clause: "The supplier shall bear all market risks, regardless of magnitude, without the right to revision or termination." Applying the Homo economicus assumption, for the first clause, the judge will benchmark the 50% increase to what we consider a "normal increase" in the supplying industry. For the second clause, the judge will consider it invalid since the court presumes that no rational actor would include a clause like that with the possibility of adaptation.

When it comes to the adaptation phase, using the economic method, the judges have different possibilities, noting that they can be limited by the phrasing of the clause, mainly three. The first possibility is the modification of the obligations, and it is not limited to reducing them, but also to lowering the quality or increasing the payment by the other party. Applying this to our example, the judge, for example, can order the construction firm to pay to match the increase that the supplier is giving, or allow the supplier to buy a lower quality of iron at a lower price. Another option given to the judge is the redistribution of losses, and so to protect the supplier from going bankrupt, the judge can make the construction firm pay for a part of the increase. The last option, which is only used when the contract is beyond saving, not from a physical impossibility but from an economic one, is that the judge allows the suspension of the contract if he presumes that this unforeseen event's effect isn't permanent, or the termination when the adaptation is impossible and it would fundamentally alter the contract's nature.

B. Why the Method is superior:

The economic approach is not merely a theoretical alternative to the traditional methods; it's a must-have tool that should be made available to judges. Its superiority rests on three pillars: objectivity, cost minimization, and, most importantly, fairness and efficiency.

The central weakness of purposivism is its reliance on a judge's subjective perception of what is a "reasonable" or "fair" (Schwartz & Sepe, 2023). Under this approach, judgments can vary from court to court since every person has their own set of values. The economic method, however, corrects this by anchoring interpretation in the ex-ante (pre-contract) economic logic that guided them when forming the contract. As Valsan (2020) emphasizes, the interpreter's role should be restricted to determining the economic intentions that are embedded within their agreement. So instead of

asking “what is fair?”, a vague moral question, the judge asks, “what is the rational economic function of this clause?” This shift reframes interpretation as an efficiency analysis, not a moral one. The focus moves from judicial virtues to rational choice, ensuring that contractual meaning is derived from the incentive structures (Arbel, 2024).

In economic terms, this method grounds interpretation in *ex ante* efficiency. As DiMatteo (2017) argues, contract law interpretation should be predictable, and by reconstructing the contract’s original economic baseline, the judge measures the current dispute against the contract’s intended equilibrium of risk and benefit (Parisi & Bix, 2025). This prevents the court from imposing external values or redistributing risk *ex post*, while still allowing rational adaptation when the equilibrium is destroyed by unforeseen events.

The second advantage of this method is minimizing transaction and litigation costs. Schwartz and Scott (2010) argue that any socially desirable interpretive rule must trade off against accuracy and adjudication costs. Traditional methods fail this trade-off because textualism reduces adjudication costs but increases error costs by enforcing absurd results, as in the Arnold case. Purposivism increases accuracy but spikes litigation costs by requiring endless evidence of “context”. The economical approach represents the best balance because, while having the objective of maximizing surplus as indicated by Cohen (2009), it minimizes total costs: Drafting Costs: Parties do not have to bear the prohibitive cost of drafting a clause for every imaginable “black swan” event since they can be confident that the court will give effect to the economic logic of their deal (Parisi & Bix, 2025). Costs of litigation: The question is one of objective economic data - prices and ratios - rather than open-ended discovery of “intent” or “context”.

Finally, this method is superior because it resolves the false dichotomy between fairness and efficiency. Legal doctrines often treat them as opposing forces. However, the literature demonstrates that they are intrinsically linked. Meyerson (2010) argues that “analysis based on efficiency tends to produce results of fairness.” When economic principles are properly applied, “the concerns of fairness and of efficiency may coincide more often than partisans of either side... have cared to admit” (Meyerson, 1990).

The “Economy of the Contract” proves this: a contract destroyed by an unforeseen event, leaving one party bankrupt, ruined, while the other with an unearned windfall, this situation is inefficient (it destroys the surplus) and unfair (it violates legitimate expectations). Esmail et al. (2022) define justice as a “practical criterion” to prevent the “misuse of contractual power.” Similarly, Mokal (2003) suggests that “legitimacy” in law is a matter of both “fairness” and “efficiency” working together. By adapting the contract to restore its economic balance, the judge serves both masters: preserving the

efficient deal the parties are meant to make, rather than enforcing the broken shell left behind by the unforeseen.

Conclusion

Considering this examination, it can be concluded that the economic interpretation of contracts, especially when applied to adaptation clauses, is generally more capable of protecting the contract's economic balance than traditional methods. In complex, long-term commercial agreements with strong economic content, a purely literal or conventional interpretation of the contract can lead to overlooking the commercial functions of clauses, leading to results that are legally correct but economically unbalanced.

However, this conclusion must be tempered by practical limitations. Applying an economic interpretation can be both expensive and time-consuming, often requiring market data, financial evidence, and expert input, and resources that may not be equally accessible in every case to each party. Courts also face procedural limitations and heavy workloads, which can encourage judges to adopt simpler routes rather than conducting an extensive economic assessment. The challenge, therefore, is not the uselessness of the method, but its workability: The best path forward is to develop streamlined indicators and evidentiary standards that preserve the rigor of economic reasoning while remaining feasible for judicial application.

Therefore, the scope of this applicability must be clearly defined: while traditional methods may remain sufficient for simple or low-value consumer transactions, the economic approach should be viewed as a specialized tool for high-stakes structures where both parties entered the agreement to achieve specific financial benefits. Consequently, the central challenge is not the validity of the method, but its workability. The best path forward is for legal systems to move toward specific judicial reform; rather than relying on abstract reasoning, courts and legislators should develop streamlined indicators and evidentiary standards that preserve the rigor of economic reasoning while remaining feasible for everyday judicial practice.

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