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Freeman & Mills, Inc. v. Belcher Oil Co.: Yes, the Seaman's Tort Is Dead

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Freeman & Mills, Inc. v. Belcher Oil Co.: Yes, The Seaman's Tort Is Dead*

Robert L. Rancourt, Jr.**

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* The title refers to the question posed by Dana Rae Landsdorf in her Comment, *California's Detortification of Contract Law: Is the Seaman's Tort Dead?*, 26 LOY. L.A. L. REV. 213 (1992).

** B.A., George Mason University, 1992; J.D., University of the Pacific, McGeorge School of Law, to be conferred 1997. I must thank my wife for her love of and devotion to an undeserving husband, and my parents, who always pushed me to be my best. This project is dedicated to my father, Robert L. Rancourt, Sr., whose recent untimely demise took a great man from this world; I am forever indebted to him.

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The duty to keep a contract at common law means a prediction that you must pay damages if you do not keep it—and nothing else.

Oliver Wendell Holmes, Jr.¹

I. INTRODUCTION

The civil defense bar must have cringed on the day the California Supreme Court handed down its opinion in *Seaman’s Direct Buying Service v. Standard Oil Co.*² Although *Seaman’s* was a contract case, it created tort liability, in the form of punitive damages, for a defendant’s bad faith denial of the existence of a contract.³ The newfound liability in *Seaman’s* gave plaintiffs another pigeon-hole through which they could expose the deep pockets of corporate defendants to punitive damages awards.⁴ However, it was evident right from the start that the

1. Oliver W. Holmes, Jr., *The Path of the Law*, 10 HARV. L. REV. 457, 462 (1897).

2. 36 Cal. 3d 752, 686 P.2d 1158, 206 Cal. Rptr. 354 (1984).

3. *Id.* at 769, 686 P.2d at 1167, 206 Cal. Rptr. at 363.

4. See STEVEN J. BURTON & ERIC G. ANDERSEN, CONTRACTUAL GOOD FAITH §§ 9.2.3, 9.2.3.1, at 400-01 (asserting that *Seaman’s* encouraged expansion of tortious breach of contract, and visions of huge damages awards inspired plaintiffs to bring *Seaman’s* actions). The sizes of some punitive damages awards sustained by the courts are certainly alluring. See, e.g., TXO Prod. Corp. v. Alliance Resources Corp., 509 U.S. 443, 465-66 (1993) (plurality opinion) (sustaining a punitive damages award of \$10 million); Browning-Ferris Indus. v. Kelco Disposal, Inc., 492 U.S. 257, 280 (1989) (affirming a \$6 million punitive damages award); Robertson Oil Co. v. Phillips Petroleum Co., 14 F.3d 373, 376-80 (8th Cir. 1993) (upholding a total of \$8 million in punitive damages); Hasson v. Ford Motor Co., 32 Cal. 3d 388, 403, 650 P.2d 1171, 1180, 185 Cal. Rptr. 654, 663 (1982) (holding that the evidence was sufficient to support the jury’s award of \$4 million in punitive damages); Pennzoil Co. v. Texaco, Inc., 729 S.W.2d 768, 866 (Tex. Ct. App. 1987) (sustaining Texaco’s point of error that the trial court abused its discretion by failing to suggest a remittitur, and reducing the jury’s original \$3 billion punitive damages verdict to \$1 billion on a tortious interference with contract claim). But see BMW, Inc. v. Gore, 116 S. Ct. 1589, 1603-04 (1996) (reversing a \$2 million punitive damages award

new *Seaman's* tort would have difficulty ripening into a full-fledged theory of tort liability in contract cases.⁵ Indeed, California courts expressed reluctance to apply the tort, sister states refused to adopt the tort, and legal commentators leveled heavy criticism at the new tort.⁶ Suggestions that the state high court reconsider or eliminate the new tort came from all parts of the legal community.⁷ The California Supreme Court heeded these requests when it overruled *Seaman's* in its recent decision of *Freeman & Mills, Inc. v. Belcher Oil Co.*⁸

As discussed in Professor Kelso's prologue, this case forms part of the significant imprint left on California jurisprudence by retiring Chief Justice Malcolm Lucas.⁹ This Casenote specifically reviews the legal landscape of the *Seaman's* tort, from its inception through its demise in *Freeman & Mills*, in Part II. The thrust of the note, Part III, is a consideration of the *Freeman & Mills* case itself. Part IV discusses legal and economic ramifications likely to flow from the decision. Part V concludes by praising California's high court for restoring adherence of contract and tort remedies to the goals of contract and tort law, and returning needed economic stability in commercial contractual settings.

II. BACKGROUND

A. *Traditional Prohibition of Punitive Damages Awards in Contract Cases*

The common law has typically limited punitive damages remedies in actions based upon contract.¹⁰ California has adopted the common law approach.¹¹ The

against a car manufacturer, who failed to disclose to a purchaser that the purchased car had been damaged and repainted prior to delivery, as grossly excessive in light of the defendant's low level of reprehensible conduct and the five hundred to 1 ratio of punitive damages to actual damages).

5. See *infra* notes 68-73 and 89-146 and accompanying text.

6. See *infra* notes 89-172 and accompanying text.

7. E.g. *Freeman & Mills, Inc. v. Belcher Oil Co.*, 33 Cal. App. 4th 837, 840, 33 Cal. Rptr. 2d 585, 586 (1994), *aff'd*, 11 Cal. 4th 85, 103, 900 P.2d 669, 680, 44 Cal. Rptr. 2d 420, 431 (1995); Okun v. Morton, 203 Cal. App. 3d 805, 826, 250 Cal. Rptr. 220, 233 (1988); Landsdorf, *supra* note *, at 236-39 (advocating that the California Supreme Court overrule *Seaman's*); C. Delos Putz, Jr., & Nona Klippen, *Commercial Bad Faith: Attorney Fees—Not Tort Liability—Is the Remedy for "Stonewalling,"* 21 U.S.F. L. REV. 419, 499 (1987) (advising the state high court to correct its misstep in *Seaman's*); William W. Oxley, *Seaman's Overboard*, L.A. LAW., Sept. 1995, at 44, 78 (urging the California Supreme Court, in *Freeman & Mills*, to fix its mistake of inventing the *Seaman's* tort).

8. 11 Cal. 4th 85, 900 P.2d 669, 44 Cal. Rptr. 2d 420 (1995).

9. See J. Clark Kelso, *A Tribute to Retiring Chief Justice Malcolm M. Lucas*, 27 PAC. L.J. 1395 (1996) [hereinafter *Tribute*].

10. Professor Farnsworth, renowned contracts professor, author of a leading treatise on contracts, and reporter for the Restatement, Second, of Contracts, traces the earliest application of this rule to *Addis v. Gramophone Co.*, [1909] App. Cas. 488 (H.L.), in which an English appellate court denied granting punitive damages to a plaintiff-employee even though the defendant-employer wrongfully discharged the employee in an unnecessary and humiliating manner. 3 E. ALLAN FARNSWORTH, FARNSWORTH ON CONTRACTS § 12.8, at 189 n.16 (1990). American cases have also followed this trend. See *Den v. Den*, 222 A.2d 647, 648 (D.C. 1966) (refusing to allow punitive damages for a plaintiff-wife against the defendant-husband regardless of the

California Supreme Court has expressed two primary rationales for this tenet of

latter's bad motives in failing to make alimony payments under the parties' separation agreement); *Eskew v. Camp*, 204 S.E.2d 465, 465 (Ga. Ct. App. 1974) (denying punitive damages for a carpenter's breach of contract since the homeowner's cause of action arose from a contract, rather than from a tort); *White v. Benkowski*, 155 N.W.2d 74, 77 (Wis. 1967) (disallowing award of punitive damages for the defendant's willful denial of the plaintiff's rightful use of a water supply).

Several other authorities similarly agree that punitive damages are generally not among the available remedies to plaintiffs in contract actions. RESTATEMENT (SECOND) OF CONTRACTS § 355 (1979) (prohibiting punitive damages for a breach of contract "unless the conduct constituting the breach is also a tort for which punitive damages are recoverable"); 25 C.J.S. *Damages* § 120 (1955) (prohibiting exemplary damages, also known as punitive damages (BLACK'S LAW DICTIONARY 390 (6th ed. 1990)) for breach of contract, but allowing them "in tort cases incidentally involving a contract where the requisite aggravating circumstances are present"); 5 ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 1077 (1950) (asserting that punitive damages are not recoverable for a breach of contract, but a certain class of cases allows them when elements are present that fall "within the field of tort or as closely analogous thereto"); 11 SAMUEL WILLISTON & WALTER H. E. JAEGER, A TREATISE ON THE LAW OF CONTRACTS § 1340 (3d ed. 1968) (restating the general rule that punitive damages are unavailable as a remedy for contract breach except in certain instances involving wanton behavior by public utilities or marriage promisors); see U.C.C. § 1-106(1) (1990) (forbidding punitive damages unless otherwise provided by law).

11. CAL. CIV. CODE § 3294(a) (West Supp. 1996); see *Croghan v. Metz*, 47 Cal. 2d 398, 405, 303 P.2d 1029, 1033 (1956) (denying the plaintiff, a buyer, punitive damages even though the defendant, a real estate broker with whom the plaintiff shared a fiduciary relationship, covertly received extra profits from the transaction); *Chelini v. Nieri*, 32 Cal. 2d 480, 482, 486-87, 196 P.2d 915, 916, 918-19 (1948) (reversing a punitive damages award against a mortician who intentionally promised the plaintiff that the defendant would embalm the body of the plaintiff's deceased mother so that it would "keep almost forever," and that the defendant would provide a hermetically sealed casket, although evidence showed that the defendant-mortician never had any intention of fulfilling these promises and knew that such promises were impossible to fulfill).

The courts have historically permitted punitive damages in actions based upon tort, however, since one goal of tort law is deterrence of unfavorable, injurious conduct. See *Molzof v. United States*, 502 U.S. 301, 306 (1992) (quoting *Day v. Woodworth*, 13 How. 363, 371 (1852)) (noting that "[i]t is a well-established principle of the common law, that in actions of trespass and all actions on the case for torts, a jury may inflict what are called exemplary, punitive, or vindictive damages upon defendant, having in view the enormity of his offense rather than the measure of compensation to the plaintiff"); see also J. Clark Kelso, *Sixty Years of Torts: Lessons for the Future*, 29 TORT & INS. L.J. 1, 4-5 (1993) [hereinafter *Sixty Years of Torts*] (calling compensation and deterrence the "twin pillars of tort law," and explaining that courts have experienced difficulty in achieving the proper balance of the two). Punitive damages make an example of a particular defendant's conduct that the law disfavors, thus achieving the deterrence goal of tort law. W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 2, at 9 & n.21 (5th ed. 1984). Punitive damages may be awarded in tort cases only when the defendant's conduct is particularly egregious, outrageous, malicious, fraudulent, or evil. *Id.* at 9-10. See generally CAL. CIV. CODE § 3294(a), (c)(1)-(3) (West Supp. 1996).

In an action for the breach of an obligation not arising from contract, where it is proven by clear and convincing evidence that the defendant has been guilty of oppression, fraud, or malice, the plaintiff, in addition to the actual damages, may recover damages for the sake of example and by way of punishing the defendant.

...

"Malice" means conduct which is intended by the defendant to cause injury to the plaintiff or despicable conduct which is carried on by the defendant with a willful and conscious disregard of the rights or safety of others.

"Oppression" means despicable conduct that subjects a person to cruel and unjust hardship in conscious disregard of that person's rights.

"Fraud" means an intentional misrepresentation, deceit, or concealment of a material fact known to the defendant with the intention on the part of the defendant of thereby depriving a person of property or legal rights or otherwise causing injury.

Id.

contract law.

The first rationale promulgated by the court is the importance of promoting certainty and predictability regarding the costs of transacting commercial business by way of legal contracts.¹² Punitive damages, after all, introduce an element of speculation into the parties' transaction because the assessment of punitive damages is usually left to the jury's discretion and is, therefore, inherently uncertain; they are also often inexplicably larger than compensatory damages.¹³

The second rationale expressed by the court for prohibiting punitive damages in contract actions is that damages are awarded to plaintiffs in breach of contract actions *only* to compensate them for failed expectations, rather than to punish the breaching party.¹⁴ The whole idea of contract law is to compensate parties for

12. *Foley v. Interactive Data Corp.*, 47 Cal. 3d 654, 683, 765 P.2d 373, 389, 254 Cal. Rptr. 211, 227 (1988).

13. See *International Bhd. of Elec. Workers v. Foust*, 442 U.S. 42, 50 & n.14 (1979) (noting that the broad discretion accorded to juries both as to the imposition and amount of punitive damages makes their awards unpredictable, and the inappropriate passion or prejudice of juries toward unions, management, or minority views may find its expression in punitive damages awards); *Gertz v. Robert Welch, Inc.*, 418 U.S. 323, 350 (1974) (asserting that jury discretion in awarding punitive damages is tempered only by "the gentle rule that they not be excessive," that juries' assessments of this kind of damages are unpredictable because they often bear no relation to the harm caused by defendant, and that juries may "use their discretion selectively to punish expressions of unpopular views"); *KEETON ET AL.*, *supra* note 11, § 2, at 11-12 & n.49 (describing how punitive damages are awarded in civil cases without the procedural safeguards found in criminal cases, such as proof beyond a reasonable doubt, the privilege against self-incrimination, and the double jeopardy rule, since, except in Indiana, these defendants can be re-prosecuted for a crime even though they may have already been found guilty in a tort action and paid punitive damages); see also *Rosener v. Sears Roebuck and Co.*, 110 Cal. App. 3d 740, 762-63, 168 Cal. Rptr. 237, 250-51 (1980) (Elkington, J., concurring) (noting inexplicable ratios of punitive to actual damages imposed by juries, and calling punitive damages "an immovable and treacherous Sword of Damocles" imposed by "perhaps the misguided verdict of a jury"). See generally Malcolm E. Wheeler, *The Constitutional Case for Reforming Punitive Damages Procedures*, 69 VA. L. REV. 269 (1983) (noting an increase in size and frequency of punitive damages awards, urging a reassessment of the utility of punitive damages remedies, recognizing arbitrariness and prejudice inherent in many punitive damages verdicts, and concluding that current procedures prevalent in awarding punitive damages are constitutionally inadequate). But see *JOHN W. WADE ET AL.*, *PROSSER, WADE AND SCHWARTZ'S CASES AND MATERIALS ON TORTS* 531 (9th ed. 1994) (describing the benefits of punitive damages as follows: a salutary method of discouraging bad or evil motives, a remedy for the unfortunate American rule of civil procedure that attorney's fees are generally not recoverable against the defendant, a channeling device since plaintiff's desire for revenge is brought through peaceful channels, and an incentive to try a long array of petty cases of outrage and oppression, which prosecutors do not have time to pursue and private litigants would otherwise find inconvenient).

Just recently, the Supreme Court has finally gotten around to creating a legal mechanism that will hopefully offer some control over the often inexplicably large size of punitive damages awards. Its effectiveness, of course, remains to be seen. See *BMW, Inc. v. Gore*, 116 S. Ct. 1589, 1598-1603 (1996) (providing three "guideposts" for a court to determine whether a punitive damages award comports with the Supreme Court's notion of constitutional fairness whereby a person must receive fair notice of the conduct that will subject the actor to punishment and of the severity of the penalty that states may impose: (1) The degree of reprehensibility of the defendant's conduct; (2) the ratio between the plaintiff's compensatory damages and the amount of punitive damages; and (3) the difference between the punitive damages award and the civil or criminal sanctions that could be imposed for comparable misconduct).

14. *Foley*, 47 Cal. 3d at 683, 765 P.2d at 389, 254 Cal. Rptr. at 227 (emphasis added).

reasonable reliance on the promises of others.¹⁵ Punitive damages are given, however, to punish parties for behavior that society deems contemptuous, and to deter others from acting similarly.¹⁶ Punishment and deterrence serve more of a purpose in the criminal law, where the law seeks to vindicate the interests of the public at large rather than those between individual parties.¹⁷ In this sense, punitive damages are inconsistent with the goal of contract remedies—individual compensation for failed expectations. Professor Corbin stated the reason for the lack of recoverability of punitive damages for contract breach another way: “Breaches of contract . . . do not in general cause as much resentment or other mental and physical discomfort as do the wrongs called torts and crimes.”¹⁸

For these reasons, punitive damages have usually been unavailable as a remedy for the breach of a contract. Instead they have remained primarily a creature of tort remedies. In certain tort cases, and even a few contract cases, such as those about to be discussed, punishment and deterrence of a defendant’s wrongful behavior, however, are remedies the law seeks to advance.

B. The Exception Allowing Punitive and Other Tort Damages in Insurance Contract Cases

Of course, there are always exceptions to rules. Prior to *Seaman’s*, California courts made one notable exception to the rule denying punitive damages awards in contract cases: cases involving insurance contracts.¹⁹

15. See *infra* note 245 and accompanying text (describing this goal as one of the chief purposes of contract law).

16. *Memphis Community Sch. Dist. v. Stachura*, 477 U.S. 299, 306 n.9 (1986); *Adams v. Murakami*, 54 Cal. 3d 105, 110, 813 P.2d 1348, 1350, 284 Cal. Rptr. 318, 320 (1991); RESTATEMENT (SECOND) OF TORTS § 908(1) (1979); KEETON ET AL., *supra* note 11, § 2, at 9 & n.21.

17. See KEETON ET AL., *supra* note 11, § 2, at 7 (describing the purpose of a criminal prosecution as vindication of the interests of the public as a whole, whereas a civil tort action is designed to compensate an individual for damages suffered at the hands of certain defendants); WAYNE R. LAFAYE & AUSTIN W. SCOTT, JR., SUBSTANTIVE CRIMINAL LAW §§ 1.3(b), 1.5, at 17, 30-40 (1986) (differentiating criminal law, with its aim toward protection of the public against harm, from tort law, with its emphasis on the conflicting interests of individuals, and discussing the various theories of punishment advanced to serve the purpose of the criminal law: to prevent certain undesirable conduct and thus to protect various interests of society); see also Henry M. Hart, Jr., *The Aims of the Criminal Law*, 23 LAW & CONTEMP. PROBS. 401, 402-04 (1958) (recognizing the distinction between criminal and contract and tort law; that crimes constitute injuries to society in general, whereas contract or tort actions are concerned with individuals; finding the distinction unhelpful; and calling the method of the criminal law a series of “commands, formulated in general terms, telling people what they must or must not do[:] . . . [t]hey speak to members of the community, . . . in the community’s behalf, with all the power and prestige of the community behind them”).

18. 5 CORBIN, *supra* note 10, § 1077.

However valid these [punitive] policy objectives might be in respect to pure torts involving conduct of an extraordinary and outrageous character, they have little relevance in the area of contract law, where breaches of contract do not ordinarily engender as much resentment or mental or physical discomfort as do torts of the former variety.

General Motors Corp. v. Piskor, 381 A.2d 16, 22 (Md. 1977).

19. 3 FARNSWORTH, *supra* note 10, § 12.8, at 192-94.

The landmark California case that gave birth to this exception is *Communale v. Traders & General Insurance Co.*²⁰ In *Communale*, the California Supreme Court allowed monetary recovery against an insurer in excess of its contractually-obligated amount under the insurance policy.²¹ The court reasoned that the insurance company wrongfully declined to defend its insured because the insurance policy contract expressly obligated the insurance company to provide for the insured's representation if a personal injury action was brought against the insured.²² Further, the insurance company refused a reasonable settlement offer well within policy limits, knowing that a judgment well in excess of those policy limits would most likely be rendered against the insured if settlement failed.²³ Although the court did not call the recovery punitive damages, it recognized that, under traditional contract theory, recovery would be limited to the amount of the policy.²⁴ The court disagreed with the conventional view, instead, permitting recovery beyond the contractually-obligated policy amount.²⁵ The high court's rationale for allowing recovery was its position that the covenant of good faith and fair dealing implied by law in every contract²⁶ requires an insurer to consider the interest of its insured at least as much as its own interests when deciding whether a claim should be compromised.²⁷ This consideration in turn requires the insurer to settle a claim against its insured if the settlement is within policy limits and there is great risk of recovery beyond those policy limits.²⁸

Communale was a third-party case. The third party, an injured person, recovered against the responsible party's insurer. However, the court was quick to

20. 50 Cal. 2d 654, 328 P.2d 198 (1958).

21. *Communale*, 50 Cal. 2d at 661, 328 P.2d at 202. *Contra* State Farm Mut. Auto. Ins. Co. v. Skaggs, 251 F.2d 356, 359-60 (10th Cir. 1957) (holding that an insurer who breaches its contract by refusing to defend an action brought against its insured for a covered accident and who wrongfully denies coverage is liable only to the extent of the insurer's liability under the policy limits); Fidelity & Casualty Co. v. Gault, 196 F.2d 329, 330 (5th Cir. 1952) (refusing to attach tort liability to an insurer that failed to investigate an allegedly covered accident and refused to defend a subsequent suit against its insured, even assuming that the insurer breached its contract).

22. *Communale*, 50 Cal. 2d at 660, 328 P.2d at 201.

23. *Id.* at 660-61, 328 P.2d at 202.

24. *Id.* at 659-60, 328 P.2d at 201.

25. *Id.* at 660-61, 328 P.2d at 201-02.

26. Implied in all contracts is an obligation of "good faith and fair dealing that neither party will do anything which injures the right of the other to receive the benefits of the agreement." *Brown v. Superior Court*, 34 Cal. 2d 559, 564, 212 P.2d 878, 881 (1949); accord CAL. COM. CODE § 1203 (West 1964); U.C.C. § 1-203 (1990); RESTATEMENT (SECOND) OF CONTRACTS § 205 (1979). The covenant often serves as a basis for the provision of certain rights under commercial law, such as a seller's right to cure a defective delivery of goods to a buyer. *E.g.* CAL. COM. CODE § 2508 (West 1964); U.C.C. § 2-508 (1990). The good faith and fair dealing requirement, however, serves only to assist courts in interpreting rights and remedies. It is thus not an independent cause of action by which a plaintiff can recover separate damages for its breach. U.C.C. § 1-203 cmt. (1990) (emphasis added).

27. *Communale*, 50 Cal. 2d at 659, 328 P.2d at 201.

28. *Id.*

apply the tortious breach of the implied covenant theory²⁹ to first-party cases, in which the insured sues its insurer. The seminal case in the first-party context is *Crisci v. Security Insurance Co.*,³⁰ in which the high court awarded mental suffering damages for an insurer's wrongful refusal to settle.³¹ In *Crisci*, the plaintiff owned an apartment building on which she carried a \$10,000 general liability policy issued by the defendant. A tenant on the property fell when the wooden staircase she was descending collapsed. The tenant sued Crisci for negligence. The defendant insurance company, pursuant to the policy, retained counsel to represent its insured, plaintiff Crisci. The tenant's suit requested damages of \$400,000, but Crisci's counsel anticipated that, realistically, a verdict of \$100,000 could probably be rendered against Crisci. The tenant made reasonable settlement offers, one for \$10,000 and another for \$9000, and, at this point, Crisci herself even offered to pay \$2500 toward a \$9000 settlement. The insurance company refused to settle for more than \$3000, the insurer let the action go to trial, and the jury awarded a total of \$101,000 against Crisci. In Crisci's subsequent action against her insurer, she sued for \$91,000, the entire judgment against her less the \$10,000 the insurer paid from the policy. Mrs. Crisci won, even though the contractual policy limits were only \$10,000.³² The court further sustained Crisci's

29. Courts and commentators alike seem to use the terms tortious breach of contract and bad faith breach of contract interchangeably to describe the availability of tort remedies for breach of the covenant of good faith and fair dealing implied in all contracts. See James H. Cook, Comment, *Seaman's Direct Buying Service, Inc. v. Standard Oil Co.: Tortious Breach of the Covenant of Good Faith and Fair Dealing in a Noninsurance Commercial Contract Case*, 71 IOWA L. REV. 893, 894 n.12 (1986) (deciding to refer to tortious breach of contract as bad faith breach, and noting that varying terms have been used by different courts at different times to refer to the same tort theory of bad faith breach of contract); Susan D. Gresham, Note, "*Bad Faith Breach*": A New and Growing Concern for Financial Institutions, 42 VAND. L. REV. 891, 892 & n.5 (1989) (naming jurisdictions that followed California's lead in allowing tort recovery for breach of the implied covenant of good faith and fair dealing in insurance contracts, and noting that tortious breach of the implied covenant of good faith and fair dealing has been referred to under various labels, including bad faith breach and the tort of bad faith); see also *supra* note 26 (defining the covenant of good faith and fair dealing implied in all contracts). Ms. Gresham stated succinctly the evolution of the tortious breach of the implied covenant of good faith and fair dealing theory:

A majority of courts have determined that all contracts impose on the parties to the contract an implied covenant of good faith and fair dealing in their actions with each other. This implied covenant prohibits a contracting party from injuring another party's right to receive the benefits of the agreement. Breach of this implied covenant usually creates a cause of action based on contract rights. Moreover, California courts maintain that breach of the implied covenant of good faith and fair dealing creates a tort action as well. The California courts initially limited these tort actions to claims against insurance companies. Other states have followed California in allowing tort recovery for breach of the implied covenant of good faith and fair dealing in insurance contracts. The imposition of tort liability in contract suits has allowed courts to award the injured party all damages proximately caused by breach of the contract, as well as punitive damages.

Gresham, *supra*, at 891-92.

30. 66 Cal. 2d 425, 432-33 & n.3, 426 P.2d 173, 178 & n.3, 58 Cal. Rptr. 13, 18 & n.3 (1967).

31. *Crisci*, 66 Cal. 2d at 425, 426 P.2d at 173, 58 Cal. Rptr. at 13.

32. *Id.* at 433-34, 426 P.2d at 179, 58 Cal. Rptr. at 19. The court relied heavily on *Commune v. Crisci*, 66 Cal.2d at 429-32, 426 P.2d at 176-77, 58 Cal. Rptr. at 16-17.

mental suffering damages of \$25,000, finding tort remedies appropriate since an action for wrongful refusal to settle sounds in both contract and tort.³³ The court stated that if Mrs. Crisci elected the contract remedy, the mental suffering damages could be sustained by relying on the line of cases permitting mental suffering damages for breach of contracts directly concerning the comfort, happiness, or personal esteem of one of the parties.³⁴ If Mrs. Crisci elected the tort remedy, the court noted that it had long permitted mental suffering damages for actions based upon tort.³⁵

Another subsequent first-party insurance case that expanded tort remedies in the insurance contract context is *Fletcher v. Western National Life Insurance Co.*³⁶ The plaintiff purchased from the defendant a disability insurance policy that provided monthly payments for two years in the case of sickness and thirty years in the case of injury in the event of the plaintiff's total disability.³⁷ All physicians examining the plaintiff agreed that he suffered permanent injury due to an on-the-job accident about two years after he obtained the disability policy. Since the disability insurance policy listed a hernia as a sickness, the defendant used one of the plaintiff's medical reports listing a hernia as a related injury to the accident, in order to pay the plaintiff under the sickness provision rather than the disability provision. Under the policy, the defendant would only have to pay the plaintiff

33. *Crisci*, 66 Cal.2d at 432-33 & n.3, 426 P.2d at 178 & n.3, 58 Cal. Rptr. at 18 & n.3. The court also found plaintiff's mental suffering damages award analogous to its line of cases permitting mental suffering recovery for invasion of property rights rather than personal rights. *Id.* at 432-33, 426 P.2d at 178, 58 Cal. Rptr. at 18. Mrs. Crisci, as a result of the original award against her and in partial fulfillment of the judgment against her, assigned 40% of her interest in a piece of property to the tenant who sued her. *Id.* at 429, 426 P.2d at 176, 58 Cal. Rptr. at 16. See generally *Acadia, Cal., Ltd. v. Herbert*, 54 Cal. 2d 328, 337-38, 353 P.2d 294, 299-300, 5 Cal. Rptr. 686, 691-92 (1960) (allowing mental suffering damages for defendant's malicious failure to abide by prior agreement to supply plaintiff with water essential to use of his land); *Kornoff v. Kingsburg Cotton Oil Co.*, 45 Cal. 2d 265, 271-75, 288 P.2d 507, 511-13 (1955) (permitting damages for discomfort and annoyance because defendant's cotton gin operation constituted a nuisance and caused plaintiffs injury to their homes and furniture); *Herzog v. Grosso*, 41 Cal. 2d 219, 225-26, 259 P.2d 429, 433-34 (1953) (sustaining plaintiffs' damages for annoyance and discomfort due to defendant's blocking the road to plaintiffs' property).

34. *Crisci*, 66 Cal. 2d at 434, 426 P.2d at 179, 58 Cal. Rptr. at 19. The court cited *Chelini v. Nieri*, 32 Cal. 2d 480, 196 P.2d 915 (1948), as representative of its line of cases permitting mental suffering damages for breach of a personal comfort contract. See *supra* note 11 (citing *Chelini*); *infra* note 269 (same). *Chelini* actually authorizes damages for physical suffering or illness in such cases. *Chelini*, 32 Cal. 2d at 482, 196 P.2d at 916. The *Crisci* court failed to state expressly whether mental suffering damages and damages for physical suffering or illness are one and the same. The *Chelini* court reversed the plaintiff's award of punitive damages, finding them unavailable for breach of contract. *Chelini*, 32 Cal. 2d at 486-87, 196 P.2d at 918-19. In any event, the facts of the *Chelini* case, relating to a defendant-mortician's ill-advised promises to an emotional plaintiff that the defendant could make the body of the plaintiff's deceased mother "keep almost forever," make it worth reading. Interestingly, the now famous Melvin M. Belli represented the plaintiff in *Chelini*.

35. *Crisci*, 66 Cal. 2d at 433, 426 P.2d at 178-79, 58 Cal. Rptr. at 18-19. The court cited several of its own cases permitting mental suffering damages in tort actions based on either personal injuries or tortious interference with property rights.

36. 10 Cal. App. 3d 376, 89 Cal. Rptr. 78 (1970).

37. The foregoing and following facts of the *Fletcher* case are paraphrased from *Fletcher*, 10 Cal. App. 3d at 386-94, 89 Cal. Rptr. at 83-88.

for two years under the sickness provision, rather than thirty years under the disability provision. Another related injury, which the accident exacerbated, was the plaintiff's congenital back ailment. The plaintiff never realized he had this pre-existing condition, so he failed to list it on the disability application. The defendant further seized upon this to inform the plaintiff that he had made misrepresentations upon the application. Accordingly, the defendant would now contest the claim in its entirety, and would consider suing for restitution of the payments paid to the plaintiff to date on the ground of this misrepresentation. However, the defendant offered to allow the plaintiff, in exchange for canceling the policy and releasing defendant from the contract, to retain the payments the plaintiff had already received, without receipt of any further benefits. The plaintiff declined the offer and sued instead. The court relied on *Crisci* to uphold the plaintiff's punitive damages award for the insurer's unjustified refusal to pay the disability insurance claim.³⁸ The court reiterated that the implied covenant of good faith and fair dealing requires an insurer to act reasonably and in good faith to settle claims. The *Fletcher* court reasoned that:

The violation of that duty sounds in tort notwithstanding that it may also constitute a breach of contract We think that . . . the implied-in-law duty of good faith and fair dealing imposes upon a disability insurer a duty not to threaten to withhold or actually withhold payments, maliciously and without probable cause, for the purpose of injuring its insured by depriving him of the benefits of the policy.³⁹

Three years later, in *Gruenberg v. Aetna Insurance Company*,⁴⁰ the California Supreme Court granted mental distress damages against an insurer that encouraged the filing of criminal charges against its insured who made a claim on a fire policy; the insurer falsely implied that the insured may have committed arson since he had excessive coverage under his fire insurance policies.⁴¹ The insurer further manipulated its right to an examination of its insured, Mr. Gruenberg, by timing the examination during the pendency of the criminal charges against the insured, correctly suspecting that, having to deal with the criminal charges, its insured would not show up for the examination, and then used the failure to appear as a pretense for denying the claim.⁴² The court justified its holding by relying on *Communale* and *Crisci*, reasoning that the insurer had

38. *Id.* at 401-02, 89 Cal. Rptr. at 93-94.

39. *Id.* at 401, 89 Cal. Rptr. at 93 (citing *Crisci*, 66 Cal. 2d at 432-34, 426 P.2d at 178-79, 58 Cal. Rptr. at 18-19).

40. 9 Cal. 3d 566, 510 P.2d 1032, 108 Cal. Rptr. 480 (1973).

41. *Gruenberg*, 9 Cal. 3d at 570, 510 P.2d at 1034, 108 Cal. Rptr. at 482.

42. *Id.* at 570-71, 510 P.2d at 1034-35, 108 Cal. Rptr. at 482-83.

breached its implied duty of good faith and fair dealing to its insured and was thus liable in tort.⁴³

Similarly, the court allowed tort remedies in *Egan v. Mutual of Omaha Insurance Company*,⁴⁴ in which a punitive damages award against a disability insurer was approved on appeal, albeit reversed for being too excessive, after a finding that the insurer had breached the implied covenant of good faith and fair dealing.⁴⁵ There, the insurance adjuster called the plaintiff a fraud, told him that he was claiming disability only to avoid working, and advised the plaintiff that the insurer's prior payments to him were unwarranted, and that the plaintiff would not receive them any longer, despite the plaintiff's legitimate claim due to a bona fide, substantiated injury.⁴⁶ Further, irrespective of the plaintiff's valid claim, the insurer offered a final settlement check to the plaintiff if he would agree to surrender the policy.⁴⁷ These actions were sufficient to constitute a breach of the implied covenant of good faith and fair dealing, and to subject the insurer to punitive damages liability in excess of its original, contractually-obligated amount of liability.⁴⁸

Several rationales emerge that justify awarding punitive and other tort damages in the insurance line of cases. One rationale is the special relationship between the insurer and the insured.⁴⁹ This special relationship, along with the obligation of good faith and fair dealing, require the insurer to act with decency and humanity.⁵⁰ Another rationale is the fact that insurance contracts are largely contracts of adhesion;⁵¹ the relationship between the insurer and insured is

43. *Id.* at 575, 510 P.2d at 1038, 108 Cal. Rptr. at 486.

44. 24 Cal. 3d 809, 620 P.2d 141, 160 Cal. Rptr. 691 (1979).

45. *Egan*, 24 Cal. 3d at 823, 620 P.2d at 148, 169 Cal. Rptr. at 698.

46. *Id.* at 821, 620 P.2d at 147, 169 Cal. Rptr. at 697.

47. *Id.* at 822, 620 P.2d at 147, 169 Cal. Rptr. at 697.

48. *Id.* at 819, 823, 620 P.2d at 146, 148, 169 Cal. Rptr. at 696, 698.

49. *Id.* at 820, 620 P.2d at 146, 169 Cal. Rptr. at 696. Several factors culminate to constitute this special relationship: for example, the insurance company is in a superior bargaining position since it dictates the terms of its insurance contracts, with the insured merely "signing upon the dotted line;" the insured's position is further weakened by the fact that the individual is obtaining a necessary service or product, which is often compulsory under state motor vehicle law; and the insurer is essentially a fiduciary since the insured places its trust and confidence in the insurer, who agrees to be responsible for the insured's accidents. *See Foley*, 47 Cal. 3d at 690, 765 P.2d at 394, 254 Cal. Rptr. at 232-33 (citing Charles M. Louderback & Thomas W. Jurika, *Standards for Limiting the Tort of Bad Faith Breach of Contract*, 16 U.S.F. L. REV. 187, 227 (1982)) (recounting these aspects of the special relationship).

50. *Egan*, 24 Cal. 3d at 820, 620 P.2d at 146, 169 Cal. Rptr. at 696 (quoting William M. Goodman & Thom G. Seaton, *Foreword: Ripe for Decision, Internal Workings and Current Concerns of the California Supreme Court*, 62 CAL. L. REV. 309, 346-47 (1974)).

51. California courts define a contract of adhesion as "a standardized contract, which, imposed and drafted by the party of superior bargaining strength, relegates to the subscribing party only the opportunity to adhere to the contract or reject it." *Neal v. State Farm Ins. Cos.*, 188 Cal. App. 2d 690, 694, 10 Cal. Rptr. 781, 784 (1961) (citing Friedrich Kessler, *Contracts of Adhesion—Some Thoughts About Freedom of Contract*, 43 COLUM. L. REV. 629, 629 (1943)). While adhesion contracts are not per se illegal, since, after all, "[m]ost contracts which govern our daily lives are of a standardized character," courts usually scrutinize them because

inherently unbalanced and the insurer is in an automatically superior bargaining position.⁵² Also of note is the fact that the weaker party to the contract, the insured, enters into the contract not to make a profit, but rather to obtain a necessary service or product: financial security or peace of mind.⁵³ In light of these rationales, punitive damages serve their deterrent effect by requiring insurers not to take advantage of their insureds and to act in good faith with their insureds, or else risk exposure to punitive damages liability.⁵⁴ Although expansion of the punitive remedy in the contractual setting seemed plausible,⁵⁵ punitive damages remedies remained unavailable outside the insurance context, until *Seaman's*.

C. *A Tort Is Born*

The tough economic times⁵⁶ surrounding the transactions underlying *Seaman's* caused plaintiff's request for punitive damages for breach of a non-insurance contract to fall on sympathetic ears. In 1971, *Seaman's Direct Buying Service, Inc. (Seaman's)*, sought to lease a part of a new marina that the City of Eureka (City) had just built to operate a marine fuel dealership.⁵⁷ However, before the City would approve the lease, it pressured *Seaman's*, for bonding purposes, to secure evidence of a binding agreement with an oil supplier that would provide the necessary fuel. *Seaman's* consulted Standard Oil Company of California

they stand theoretically opposite to our "freedom in bargaining and equality of bargaining which are the theoretical parents of the American law of contracts." *Neal*, 188 Cal. App. 2d at 694, 10 Cal. Rptr. at 784; see *Spence v. Omnibus Indus.*, 44 Cal. App. 3d 970, 974, 119 Cal. Rptr. 171, 174 (1975) (stating that "[t]he use of standardized or mass-produced agreements containing a profusion of provisions which allow the stronger party to dictate the terms to the weaker party is viewed with judicial concern").

52. *Egan*, 24 Cal. 3d at 820, 620 P.2d at 146, 169 Cal. Rptr. at 696.

53. *Id.* at 819, 620 P.2d at 146, 169 Cal. Rptr. at 696; *Louderback & Jurika*, *supra* note 49, at 227.

54. See *supra* note 16 and accompanying text (describing the purpose of punitive damages as punishment for behavior society deems contemptuous and as deterrence of such behavior by others in the future).

55. See *Tameny v. Atlantic Richfield Co.*, 27 Cal. 3d 167, 179 n.12, 610 P.2d 1330, 1337 n.12, 164 Cal. Rptr. 839, 846 n.12 (1980) (inferring that the covenant of good faith and fair dealing implied in employment contracts might give rise to tort remedies if breached).

56. See *Transcript of President Nixon's November 7 National Television Address on Nation's Energy Crisis and Oil Shortage*, N.Y. TIMES, Nov. 8, 1973, at 32 (detailing numerous aspects of the nation's then energy crisis: the Middle East oil producers cut off petroleum shipments to the United States; the oil supply fell 10% to 17% short of the winter's anticipated demand; the reduction of heat in homes, offices, factories, and commercial establishments became necessary; proposals existed to reduce domestic airline flights by 10%; efforts were made to prevent industries and utilities from converting from coal to oil; highway speed limits were reduced; a need existed for faster licensing and construction of nuclear power plants; a proposal suggested staggering working hours to encourage use of public transportation and car pools; there was a general recognition of a long-term and current energy shortage; and an executive order reduced temperatures in all federal government offices to no more than 68 degrees).

57. The foregoing and following facts of the *Seaman's* case are paraphrased from *Seaman's Direct Buying Serv. v. Standard Oil Co.*, 36 Cal. 3d 752, 759-62, 686 P.2d 1158, 1160-62, 206 Cal. Rptr. 354, 356-58 (1984).

(Standard) for this purpose. After preliminary negotiations with Standard, Seaman's explained the City's insistence on evidence of a written agreement and requested Standard to prepare something to show the City. Standard responded with a letter of intent that explicitly provided that the terms were not binding. Since Seaman's needed to show the City a binding commitment, further negotiations with Standard ensued and culminated in another letter of intent prepared by Standard in 1972. This letter of intent contained language that the agreement between Seaman's and Standard was conditioned upon mutual satisfaction with the specific wording of the final contract, endorsement by the appropriate government agencies, and continued approval of the credit status of Seaman's. Seaman's presented this letter to the City, the City approved the letter as sufficiently binding, and Seaman's and the City entered into a forty-year lease.

Due to market fluctuations in the oil industry and what eventually came to be known as the oil crisis of the 1970s,⁵⁸ Seaman's and Standard never executed the final contract contemplated by the second letter of intent.⁵⁹ A federal program designed to control the crisis went into effect in late 1973 and mandated allocation of petroleum products among existing consumers. Standard then informed Seaman's that Standard could no longer supply Seaman's with fuel, since the federal regulations required suppliers to supply only those purchasers to whom they sold petroleum products during the base period of 1972, a criterion Seaman's did not meet. Standard contended this was the only bar to its continuing to do business with Seaman's.

Seaman's successfully petitioned the federal government in early 1974 to allow Standard to supply Seaman's with fuel. Standard responded by changing position, denying that it had ever reached a binding agreement with Seaman's, and appealing the government's decision because Standard did not want to take on any new business. Communications between Standard and Seaman's grew adverse. Standard was successful on its appeal of the federal government's order in Seaman's favor.

Seaman's then appealed the government order again and won on the condition that it file a court decree with the federal government to the effect that a valid contract existed between Standard and Seaman's under state law. Seaman's asked Standard to stipulate to the existence of a contract since it could not afford a trial on the matter. The Standard representative responded by laughing and saying "see you in court."⁶⁰

58. See *supra* note 56 (describing the crisis).

59. However, in 1973, Standard did execute a temporary marine dealership agreement to supply Seaman's with the fuel necessary to run its station while the new marina remained under construction. *Seaman's*, 36 Cal. 3d at 761, 686 P.2d at 1162, 206 Cal. Rptr. at 358.

60. *Id.* at 762, 686 P.2d at 1162, 206 Cal. Rptr. at 358. The *Seaman's* court characterized this expression as "adopting a 'stonewall' position" in its opinion. *Id.* at 769-70, 686 P.2d at 1167, 206 Cal. Rptr. at 363. The Court of Appeal subsequently defined "stonewalling" as the "unreasonable denial of liability without a substantial defense." *Okun v. Morton*, 203 Cal. App. 3d 805, 824, 250 Cal. Rptr. 220, 232 (1988).

Seaman's ceased operations in early 1975 and thereafter sued Standard. Seaman's alleged breach of contract, fraud, tortious breach of the implied covenant of good faith and fair dealing, and intentional interference with the contractual relationship of Seaman's with the City. Seaman's recovered on all but the fraud theory.⁶¹ It received compensatory damages for breach of contract, tortious breach of the implied covenant of good faith and fair dealing, and intentional interference with an advantageous business relationship. The jury awarded Seaman's punitive damages on both the tortious breach of the implied covenant and intentional interference with contractual relations counts. Although Seaman's consented to a remittitur⁶² for excessive punitive damages, Standard appealed.

The California Supreme Court affirmed the action for breach of contract, but reversed the tortious breach of the implied covenant and the intentional interference with an advantageous business relationship causes of action due to erroneously prejudicial jury instructions.⁶³ The thrust of the appeal was "whether, and under what circumstances, a breach of the implied covenant of good faith and fair dealing in a commercial contract may give rise to an action in tort."⁶⁴ The court knew it was treading on new ground since it was dealing with a commercial rather than an insurance contract,⁶⁵ but the high court asserted that it was unnecessary to decide the broad question posed by the thrust of the appeal.⁶⁶ Instead, the state high court merely declared that "[i]t is sufficient to recognize that a party to a contract may incur tort remedies when, in addition to breaching

61. Seaman's declined to appeal the fraud cause of action, limiting its cross-appeal to only the merits of the trial court's order reducing the amount of punitive damages awarded. *Seaman's*, 36 Cal. 3d at 774 n.11, 686 P.2d at 1170 n.11, 206 Cal. Rptr. at 366 n.11.

62. The term "remittitur" refers to "[t]he procedural process by which an excessive verdict of the jury is reduced." BLACK'S LAW DICTIONARY 1295 (6th ed. 1990). Remittiturs are authorized in California by statute. CAL. CIV. PROC. CODE § 666 (West 1987).

63. The court affirmed the breach of contract cause of action after finding Standard's statute of frauds defense without merit. *Seaman's*, 36 Cal. 3d at 762-66, 686 P.2d at 1162-64, 206 Cal. Rptr. at 358-60. The court then held that the intent element of the tort of intentional interference with contractual relations requires that a defendant's intentional acts of purposeful design disrupt the contractual relationship. *Id.* at 766, 686 P.2d at 1164-65, 206 Cal. Rptr. at 360-61. The high court reversed this cause of action because it found that the trial court's instruction, that the intent element could be satisfied if defendant knew that interference with the contractual relationship was substantially certain to result from its conduct, failed to comply with the proper definition of intent for this tort: the defendant must intentionally act with purposeful design to disrupt the contractual relationship. *Id.* at 767, 686 P.2d at 1165-66, 206 Cal. Rptr. at 361-62. Finally, on the tortious breach of the implied covenant of good faith and fair dealing count, the court held that recovery could only be found if Standard denied the existence of its contract with Seaman's *in bad faith*; since the trial court's charge failed to specify that the denial must be in bad faith, the high court reversed for further proceedings consistent with its decision. *Id.* at 767-74, 686 P.2d at 1166-70, 206 Cal. Rptr. at 362-66 (emphasis added).

64. *Id.* at 767, 686 P.2d at 1166, 206 Cal. Rptr. at 362.

65. *Id.* at 768-69, 686 P.2d at 1166-67, 206 Cal. Rptr. at 362-63.

66. *Id.* at 769, 686 P.2d at 1167, 206 Cal. Rptr. at 363.

the contract, it seeks to shield itself from liability by denying, in bad faith and without probable cause, that the contract exists.⁶⁷

Hence, the *Seaman's* tort was born, seemingly out of thin air,⁶⁸ since the court failed to rely on the implied covenant of good faith and fair dealing theory in establishing the tort. Little did the California Supreme Court know that its new tort would lead a short and tumultuous life. Had the court relied on the implied covenant of good faith and fair dealing as the basis for tort liability, perhaps its new tort would have lived longer, because courts would then have had a framework within which to apply the new tort.

D. *The Fatal Flaw of Seaman's*

It was evident from the *Seaman's* decision that the new tort theory of liability would pose difficulty in its application to ordinary commercial contract cases. The major problem, which proved to be the fatal flaw of *Seaman's*, was the court's failure to rely on the implied covenant of good faith and fair dealing theory as its rationale for applying tort remedies in commercial contract settings. Use of the implied covenant of good faith and fair dealing as a basis for tort liability proved successful in its insurance contract line of cases.⁶⁹ So too would it probably have been in the *Seaman's* line of cases.

Chief Justice Rose Bird recognized the flaw immediately by way of her dissent from the part of the court's opinion creating the new tort.⁷⁰ Although the ultimate disposition of the case was faulty, under either the majority or the concurring and dissenting opinion, at least the Chief Justice realized the anomaly of allowing a tort remedy for denial of existence of a contract without providing a solid framework by which to apply this remedy.⁷¹ Courts would need a test to

67. *Id.*

68. Economics may help to explain the reason for the court's sudden inclination to expand tort remedies for contract plaintiffs. While the actual controversy underlying *Seaman's* occurred during the tougher economic days of the early 1970s oil crisis, see *supra* note 56 for a description of the crisis, the high court decided *Seaman's* in better economic times: the 1980s, the decade of "greed." Courts are much more willing to expand tort liability during better economic times on the theory that business and industry can absorb new costs by distributing them through insurance and price increases. However, during more difficult economic periods, such as 1995, the year of *Freeman & Mills* and slow economic recovery from a late 1980s-early 1990s recession, courts restrict tort liability because business and industry may suffer and be unable to absorb any new costs of doing business. See *Sixty Years of Torts*, *supra* note 11, at 8 (asserting that during "times of plenty," courts ignore industry complaints that tort liability is too burdensome, but during "periods of recession or very slow growth," courts are more likely to respond to business complaints by restricting tort liability).

69. See *supra* notes 19-55 and accompanying text (discussing the insurance contract line of cases).

70. *Seaman's*, 36 Cal. 3d at 775, 686 P.2d at 1171, 206 Cal. Rptr. at 367 (Bird, C.J., concurring and dissenting).

71. See *id.* (stating that the majority opinion in *Seaman's* "refuses to acknowledge that its holding is compelled by this court's past decisions analyzing the scope of the implied covenant of good faith and fair dealing"). This clash between the majority and concurring and dissenting opinions is undoubtedly to what the Lucas court refers in its majority opinion in *Freeman & Mills* when it states "[s]ubsequent opinions of this

determine how to apply the tort, such as utilizing the implied covenant of good faith and fair dealing theory as a basis of liability, and recognizing that a breach of contract could constitute a tortious breach of the implied covenant under certain circumstances.⁷² Without such a theory to apply the *Seaman's* tort, lower courts would be confused, and history proved this to be the case.⁷³

The Chief Justice's dissent, however, would be only the first of many criticisms of the court's analysis in *Seaman's*. Since the other criticisms leading up to *Freeman & Mills* are addressed at length in the *Freeman & Mills* opinion itself, it is helpful to consider the criticisms of *Seaman's* as they are discussed in *Freeman & Mills*.

III. THE DEATH OF SEAMAN'S

A. *The Facts of Freeman & Mills*⁷⁴

Defendant Belcher Oil Company (Belcher) retained a law firm, Morgan, Lewis & Bockius (Morgan), to represent its interests in a lawsuit in Florida. Morgan then retained an accounting firm, plaintiff Freeman & Mills, Inc. (Freeman & Mills), to provide financial analysis and litigation support for the suit, after obtaining Belcher's authorization through its general counsel. Belcher was to pay for costs incurred on its behalf, including fees for accountants, pursuant to a letter of understanding executed by Belcher's general counsel and a Morgan partner.

Subsequently, general counsel for Belcher, with whom the Morgan partner had dealt, left Belcher, and was replaced. Belcher thereafter became dissatisfied with Morgan's representation and fired the firm, requesting summaries of both its work and Freeman & Mills's work. Belcher ultimately refused to pay both Morgan and Freeman & Mills, claiming Belcher was not consulted about the extent of Freeman & Mills's services. Belcher suggested to Freeman & Mills that it look to Morgan for payment.

court indicate a continuing reluctance, *originally reflected in Seaman's itself*, to authorize tort recovery for noninsurance contract breaches." *Freeman & Mills, Inc. v. Belcher Oil Co.*, 11 Cal. 4th 85, 93, 900 P.2d 669, 674, 44 Cal. Rptr. 2d 420, 425 (1995) (emphasis added).

72. *Seaman's*, 36 Cal. 3d at 775, 686 P.2d at 1171, 206 Cal. Rptr. at 367 (Bird, C.J., concurring and dissenting). Chief Justice Bird applied the implied covenant of good faith and fair dealing theory to reason that Standard violated the good faith and fair dealing requirement by attempting to avoid all liability for a contract breach by denying, in bad faith, the very existence of the contract, which "violates the nearly universal expectation that the injured party will be compensated for losses caused by the breaching party's failure to perform"). For a discussion of expectation damages, see *infra* notes 246-49 and accompanying text (describing expectation damages theory).

73. See *infra* notes 115-46 and accompanying text (discussing the various Court of Appeals opinions that interpreted the *Seaman's* opinion, and noting the confusion and inconsistency among them).

74. The following facts of the *Freeman & Mills* case are paraphrased from *Freeman & Mills*, 11 Cal. 4th at 88-89, 900 P.2d at 670-71, 44 Cal. Rptr. 2d at 421-22.

Freeman & Mills sued Belcher, alleging causes of action for breach of contract, “bad faith denial of contract,” and quantum meruit.⁷⁵ The jury returned a verdict for Freeman & Mills on the breach of contract count, and found that Belcher had denied the existence of the contract in bad faith, and had acted with fraud, oppression, or malice in so doing. The jury then awarded Freeman & Mills \$400,000 in punitive damages.

Belcher appealed the judgment in its entirety. The Court of Appeal reversed on the bad faith denial of contract claim, finding an absence of the “special relationship”⁷⁶ it thought necessary between the parties to justify tort remedies under *Seaman’s*.⁷⁷ In so doing, the appellate court suggested, “it is time for the Supreme Court to re-examine the tort of ‘bad faith denial of contract.’”⁷⁸ The California Supreme Court did exactly that, and overruled *Seaman’s* in its decision of August 31, 1995. The *Seaman’s* tort is dead.

B. *The Freeman & Mills Majority Opinion—An Assault on Seaman’s*

1. *Seaman’s and Stare Decisis*

Using its signature Lucas methodology for overturning far-reaching Bird court decisions,⁷⁹ the *Freeman & Mills* majority opinion, written by Chief Justice Malcolm Lucas, began by reviewing the court’s holding in *Seaman’s*.⁸⁰ This review consisted of a restatement of the facts of *Seaman’s*,⁸¹ and a lengthy quote of the part of the opinion in which the court created the new tort.⁸²

75. *Id.*, 11 Cal. 4th at 89, 900 P.2d at 671, 44 Cal. Rptr. 2d at 422. The equitable doctrine of quantum meruit, literally meaning “as much as deserved,” provides the plaintiff with damages reasonably tantamount to the amount of goods or services the plaintiff has provided the defendant, regardless of whether an express contract exists. The plaintiff can usually recover quantum meruit damages in circumstances under which the defendant would be unjustly enriched by retaining the benefits accorded the defendant by the plaintiff’s material or labor. BLACK’S LAW DICTIONARY 1243 (6th ed. 1990).

76. See *supra* note 49 and accompanying text (defining the special relationship); *infra* notes 100, 127-29, 149 and accompanying text (describing various court appraisals of the special relationship).

77. *Freeman & Mills*, 11 Cal. 4th at 90, 900 P.2d at 671, 44 Cal. Rptr. 2d at 422.

78. *Freeman & Mills, Inc. v. Belcher Oil Co.*, 33 Cal. App. 4th 837, 840, 33 Cal. Rptr. 2d 585, 586 (1994), *aff’d*, 11 Cal. 4th 85, 900 P.2d 669, 44 Cal. Rptr. 2d 420 (1995).

79. See *Tribute*, *supra* note 9 (discussing the Lucas approach to overruling prior decisions of the California Supreme Court).

80. This part of the *Freeman & Mills* opinion is not discussed here since *Seaman’s* has already been addressed. See *supra* notes 63-67 and accompanying text.

81. See *supra* notes 56-60 and accompanying text (recounting the facts of *Seaman’s*).

82. The quoted portion is from *Seaman’s Direct Buying Serv. v. Standard Oil Co.*, 36 Cal. 3d 752, 768-70, 686 P.2d 1158, 1166-67, 206 Cal. Rptr. 354, 362-63 (1984). See *supra* notes 64-67 and accompanying text (analyzing this part of the *Seaman’s* decision).

The court then addressed the doctrine of stare decisis.⁸³ It acknowledged that “[i]t is . . . a fundamental jurisprudential policy that prior applicable precedent usually must be followed even though the case, if considered anew, might be decided differently by the current justices.”⁸⁴ The court conceded that the rationale behind the doctrine is the law’s important goal of promoting certainty and predictability so that parties can guide their conduct and relationships with assurance of established rules of law.⁸⁵

However, the court also averred that the doctrine of stare decisis does not “shield court-created error from correction.”⁸⁶ The court couched its decision to re-examine *Seaman’s* in terms of subsequent developments that indicated *Seaman’s* was decided incorrectly.⁸⁷ The subsequent developments to which the court refers are rejection and criticism of the *Seaman’s* holding from all legal corners.

83. Stare decisis literally means “[t]o abide by, or adhere to, decided cases.” BLACK’S LAW DICTIONARY 1406 (6th ed. 1990). A well-respected authority on stare decisis offered an excellent description of the doctrine this way:

A deliberate or solemn decision of a court or judge, made after full argument on a question of law fairly arising in a case and necessary to its determination, is an authority or binding precedent in the same court, or in other courts of equal or lower rank within the same jurisdiction, in subsequent cases where the very point is again presented; but the degree of authority belonging to such a precedent depends, of necessity, on its agreement with the spirit of the times or the judgment of subsequent tribunals upon its correctness as a statement of the existing or actual law, and the compulsion or exigency of the doctrine is, in the last analysis, moral and intellectual, rather than arbitrary or inflexible.

Daniel H. Chamberlain, *The Doctrine of Stare Decisis as Applied to Decisions of Constitutional Questions*, 3 HARV. L. REV. 125, 125 (1889).

84. *Freeman & Mills*, 11 Cal. 4th at 92, 900 P.2d at 673, 44 Cal. Rptr. 2d at 424 (quoting *Moradi-Shalal v. Fireman’s Fund Ins. Cos.*, 46 Cal. 3d 287, 296, 758 P.2d 58, 62, 250 Cal. Rptr. 116, 121 (1988)); see *Planned Parenthood v. Casey*, 505 U.S. 833, 854-55 (1992) (promulgating the following factors to be considered in deciding whether to overrule precedent: (1) Whether the current rule is unworkable; (2) whether the established precedent is relied upon to such an extent that its overruling would cause hardship; (3) whether principles of law related to the existing doctrine have developed to the point of rendering it legally insignificant; and (4) whether facts or circumstances have changed such that the rule no longer has vitality or applicability).

One writer asserted that, indeed, “it is highly unlikely that [*Seaman’s*] would be decided the same way today.” Landsdorf, *supra* note *, at 222.

85. *Freeman & Mills*, 11 Cal. 4th at 93, 900 P.2d at 673, 44 Cal. Rptr. 2d at 424 (quoting *Moradi-Shalal*, 46 Cal. 3d at 296, 758 P.2d at 62-63, 250 Cal. Rptr. at 121); see *Planned Parenthood*, 505 U.S. at 854 (offering a prudential and pragmatic rationale for stare decisis, stating “that no judicial system could do society’s work if it eyed each issue afresh in every case that raised it,” and asserting that the rule of law contemplated by the Constitution requires continuity over time such that a respect for precedent is indispensable with reference to the court’s legitimacy).

86. *Freeman & Mills*, 11 Cal. 4th at 93, 900 P.2d at 673, 44 Cal. Rptr. 2d at 424 (quoting *Cianci v. Superior Court*, 40 Cal. 3d 903, 924, 710 P.2d 375, 388, 221 Cal. Rptr. 575, 587 (1985)).

87. *Freeman & Mills*, 11 Cal. 4th at 93, 900 P.2d at 673, 44 Cal. Rptr. 2d at 424. The court cited *People v. Anderson*, 43 Cal. 3d 1104, 1138, 742 P.2d 1306, 1327, 240 Cal. Rptr. 585, 605 (1987), for the proposition that subsequent developments, showing that a prior decision was unsound, require re-examination of precedent. The court there overruled a prior decision holding that intent to kill is an element of the felony-murder special circumstance in light of subsequent Supreme Court opinions expressing sentiments to the contrary. *Id.*

2. *Subsequent Developments: Rejection and Criticism of Seaman's*

a. *Supreme Court Decisions—Rejection of Seaman's*

The high court began the thrust of its opinion by discussing its own opinions subsequent to *Seaman's* that evinced reluctance to sanction tort remedies for non-insurance contract⁸⁸ breaches.⁸⁹ Notably, the court decided the opinions to which it refers *after* Lucas assumed the helm of the Supreme Court. It comes as no surprise that the Lucas Supreme Court will go down in history for its conservative shift in ideology from its liberal predecessor, the Bird Supreme Court.⁹⁰ The most obvious decision that exemplified this shift is *Foley v. Interactive Data Corp.*,⁹¹ written by Lucas, which the court reviewed only a year and a half after California voters ousted former Chief Justice Rose Bird, which resulted in then-Governor George Deukmejian appointing Malcolm Lucas as the new chief justice.⁹²

88. Based upon the court's lack of discussion of the bad faith insurance contract cases, its recurring references to "noninsurance" contracts in its analysis, and its repeated intimations about the ordinary commercial setting in which *Seaman's* allowed tort recovery, punitive damages are clearly still allowed in bad faith insurance contract cases. In fact, at the end of its opinion, the court stated "that nothing in this opinion should be read as affecting the existing precedent governing enforcement of the implied covenant [of good faith and fair dealing] in insurance cases." *Freeman & Mills*, 11 Cal. 4th at 103, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431.

89. *Id.* at 93-95, 900 P.2d at 674-75, 44 Cal. Rptr. 2d at 425-26.

90. Undoubtedly, the conservative trend of the state high court is an unspoken "subsequent development" that contributed to the death of *Seaman's*. As one writer put it, "Chief Justice Malcolm Lucas will always be remembered for presiding over a conservative shift in California Supreme Court jurisprudence following the liberal and controversial era of Chief Justice Rose Bird." Scott Graham, *Lucas' Biggest Impact Came Outside Courtroom; But Some Important Projects Remain 'Works in Progress'* S.F. RECORDER, Oct. 3, 1995, at 1.

91. 47 Cal. 3d 654, 765 P.2d 373, 254 Cal. Rptr. 211 (1988). Appellate courts recognized that *Foley* had a significant impact on the state's tortious breach of the implied covenant of good faith and fair dealing jurisprudence. *See, e.g., Copesky v. Superior Court*, 229 Cal. App. 3d 678, 688, 280 Cal. Rptr. 338, 344 (1991) (stating that the "winds of change blew in 1988 with the publication of *Foley*," noting that only two of the seven justices that decided *Foley* took part in *Seaman's*, and further noting that the court took an entirely new approach to the implied covenant of good faith and fair dealing after *Seaman's*, by emphasizing the difference between contract and tort remedies, and asserting that normally only contract remedies are available for breach of the implied covenant of good faith and fair dealing); *Price v. Wells Fargo Bank*, 213 Cal. App. 3d 465, 477-78, 261 Cal. Rptr. 735, 740-41 (1989) (stating that the "evolution of the [tortious breach of the implied covenant of good faith and fair dealing] law was dramatically upset last year by *Foley* . . . [; t]he impact of the *Foley* decision cannot be assessed with certainty . . . [and t]he decision surely precludes the sort of loose extension of tort recovery, based on 'quasi-fiduciary' relationship, sanctioned in [other earlier cases]").

92. *See* Claire Cooper, *State High Court Chief Will Retire*, SACRAMENTO BEE, Oct. 1, 1995, at A1 (describing Lucas's ascension to the chief justice position). Former Chief Justice Rose Bird and two other then-associate justices, Cruz Reynoso and Joseph Grodin, failed to win "a bitterly contested and expensive 1986 election centering on voters' perception that the court had not enforced the death penalty sufficiently." Karl Olson, *Change and Constancy; Now Most Frequently a Liberal Dissenter Among Conservatives, Stanley Mosk's Legacy Over 30 Years on the Supreme Court May Be Clouded*, S.F. RECORDER, Aug. 17, 1994, at 6. In fact, during the period from 1979 to 1986, the California Supreme Court reviewed 64 death penalty verdicts and upheld only five of them. Gerald F. Uelman, *Review of Death Penalty Judgments by the Supreme Courts of California: A Tale of Two Courts*, 23 LOY. L.A. L. REV. 237, 237 (1989).

The *Freeman & Mills* court noted its previous refusal in *Foley* to extend the ordinary commercial contracts holding of *Seaman's* to employment contracts. *Foley* involved an employment contract in which a discharged employee alleged wrongful termination.⁹³ The employee had informed his employer that the employee's supervisor was under investigation by the Federal Bureau of Investigation for embezzlement from a former employer.⁹⁴ Plaintiff, the employee, alleged that the defendant, the employer, fired him for this reason, while the defendant maintained that the termination resulted from the plaintiff's poor job performance.⁹⁵ The *Foley* court declined the *Seaman's* invitation⁹⁶ to extend tort remedies for breach of the implied covenant of good faith and fair dealing in employment contracts.⁹⁷

In doing so, the court first paid homage to two essential tenets of contract law: the importance of certainty and predictability about the cost of doing business by way of legal contracts, and the traditional restriction of contract remedies to compensate the aggrieved party rather than to punish the breaching one.⁹⁸ These concepts provided the court with the impetus it needed to limit tort remedies for contract breach. The *Foley* court then considered an attempted analogy of employment contracts to insurance contracts to determine whether employment contracts merited tort remedies for bad faith breach, as insurance contracts had.⁹⁹ The court concluded that employment contracts do not have the special relationship component that insurance contracts do, a factor the court had emphasized in permitting tort remedies for bad faith breach of insurance contracts.¹⁰⁰ The court reasoned that employment contracts are not contracts of adhesion, since standardized forms are not always used and the employer often does not dictate the contract's terms.¹⁰¹ Further, employees are usually not in as disastrous a dilemma as insureds are if their employment contracts are breached, since employees can look for other employment while insureds cannot find other

93. *Foley*, 47 Cal. 3d at 662, 765 P.2d at 373, 254 Cal. Rptr. at 212.

94. *Id.* at 664, 765 P.2d at 375, 254 Cal. Rptr. at 213.

95. *Id.* at 664, 765 P.2d at 375-76, 254 Cal. Rptr. at 213-14.

96. See *Seaman's Direct Buying Serv. v. Standard Oil Co.*, 36 Cal. 3d 752, 769 n.6, 686 P.2d 1158, 1166 n.6, 206 Cal. Rptr. 354, 362 n.6 (1984) (reiterating its intimation in *Tameny v. Atlantic Richfield Co.*, 27 Cal. 3d 167, 179 n.12, 610 P.2d 1330, 1337 n.12, 164 Cal. Rptr. 839, 846 n.12 (1980), that breach of the implied covenant of good faith and fair dealing might permit tort remedies, since the employer-employee relationship "has some of the same characteristics as the relationship between insurer and insured"); see also *supra* note 55 (recounting the *Tameny* footnote).

97. *Foley*, 47 Cal. 3d at 693, 765 P.2d at 396, 254 Cal. Rptr. at 234-35.

98. *Id.* at 683, 765 P.2d at 389, 254 Cal. Rptr. at 227; see *supra* notes 14-18 and accompanying text (discussing the punishment goal of punitive damages, and its inconsistency with contract law's compensatory goal).

99. *Foley*, 47 Cal. 3d at 690-93, 765 P.2d at 393-96, 254 Cal. Rptr. at 232-35; see *supra* notes 19-55 and accompanying text (discussing punitive damages and other tort remedies for bad faith breach of an insurance contract).

100. See *supra* notes 19-55 and accompanying text.

101. *Foley*, 47 Cal. 3d at 691, 765 P.2d at 394, 254 Cal. Rptr. at 233.

insurers to pay for their already-sustained loss.¹⁰² Thus, *Foley* marked the beginning of a trend toward limiting tort recovery for bad faith contracting.

The *Freeman & Mills* majority then devoted two paragraphs to *Hunter v. Up-Right, Inc.*,¹⁰³ a case involving employer misrepresentations¹⁰⁴ made to induce termination of employment.¹⁰⁵ The court there held that *Foley* precludes an award of punitive damages in such a scenario.¹⁰⁶ The *Freeman & Mills* majority thought it significant that *Hunter* failed to mention *Seaman's*, noting that, "with the exception of insurance contracts, remedies for breach of the implied covenant [of good faith and fair dealing] 'have almost always been limited to contract damages.'"¹⁰⁷ The court further noted its reasoning in *Hunter* that the defendant's misrepresentations were merely a means used to achieve an end to the contractual relationship and that the *Hunter* court would not allow this to be used as a predicate for tort damages.¹⁰⁸ Again, the state high court had refused to allow tort remedies for a bad faith breach of contract. Two concurring justices in *Freeman & Mills*, however, would have a different opinion about the applicability of *Hunter*.¹⁰⁹

The last California Supreme Court opinion that the Lucas court considered is *Applied Equipment Corp. v. Litton Saudi Arabia Ltd.*,¹¹⁰ in which the high court held that a contracting party may not be held liable in tort for conspiring with another to interfere with its own contract. The *Freeman & Mills* court noted its rationale in *Applied Equipment* that commercial activity is fostered by limiting contract remedies to damages reasonably foreseeable at the time of a contract's execution.¹¹¹ This limitation is grounded in the notion that foreseeability of contract damages for breach enable parties to gauge ahead of time the fiscal risk of entering into the contract.¹¹² The court further noted its statement in *Applied Equipment* that tort remedies for a breach of contract could be recovered only when the breach constitutes a violation of some independent duty arising out of tort law.¹¹³

102. *Id.* at 692, 765 P.2d at 396, 254 Cal. Rptr. at 234.

103. 6 Cal. 4th 1174, 864 P.2d 88, 26 Cal. Rptr. 2d 8 (1993).

104. A misrepresentation is a manifestation by words or conduct that constitutes an untrue assertion of fact. BLACK'S LAW DICTIONARY 1001 (6th ed. 1990).

105. *Freeman & Mills*, 11 Cal. 4th at 94, 900 P.2d at 674, 44 Cal. Rptr. 2d at 425.

106. *Hunter*, 6 Cal. 4th at 1185, 864 P.2d at 93, 26 Cal. Rptr. 2d at 13.

107. *Freeman & Mills*, 11 Cal. 4th at 94, 900 P.2d at 674, 44 Cal. Rptr. 2d at 425 (quoting *Hunter*, 6 Cal. 4th at 1180, 864 P.2d at 90, 26 Cal. Rptr. 2d at 11).

108. *Freeman & Mills*, 11 Cal. 4th at 94, 900 P.2d at 674, 44 Cal. Rptr. 2d at 425.

109. See *infra* notes 182-201 and accompanying text.

110. 7 Cal. 4th 503, 869 P.2d 454, 28 Cal. Rptr. 2d 475 (1994).

111. *Applied Equipment*, 7 Cal. 4th at 515, 869 P.2d at 460, 28 Cal. Rptr. 2d at 481.

112. *Id.*

113. *Id.* For example, regardless of the promise that the promisor makes the promisee in a contract, the law imposes on the promisor the general tort duty to exercise reasonable care to avoid physical harm to persons and tangible things when acting to perform the promise. KEETON ET AL., *supra* note 11, § 92, at 657. Thus, the

The *Freeman & Mills* majority believed that these opinions, *Foley*, *Hunter*, and *Applied Equipment*, viewed cumulatively, stood for the proposition that recovery of tort damages should be limited to insurance contract cases unless some duty arises on the part of the defendant out of tort law. In such a scenario, when the defendant breaches the contract, the defendant also breaches this tort duty, and the plaintiff may recover tort remedies accordingly.¹¹⁴

The high court thus concluded a review of its own recent decisions that evinced reluctance to extend tort remedies for bad faith breach of contract. The *Freeman & Mills* majority then turned to various Court of Appeal decisions interpreting *Seaman's*.

b. Court of Appeal Decisions—More Rejection of Seaman's

The California Supreme Court, in *Freeman & Mills*, noted that the Court of Appeal opinions evinced obvious confusion concerning the *Seaman's* holding.¹¹⁵ It cited numerous appellate cases that raised important questions regarding the tort of bad faith denial of contract.¹¹⁶ For instance, one question that the lower courts attempted to resolve was whether the *Seaman's* tort was based on a breach of the implied covenant of good faith and fair dealing or some other independent tort duty.¹¹⁷ The Second District Court of Appeal, in *Okun v. Morton*,¹¹⁸ decided that the tort was indeed based upon the implied covenant of good faith and fair dealing,¹¹⁹ while its sister court in the Fifth District, in *Quigley v. Pet, Inc.*,¹²⁰ concluded to the contrary.¹²¹ Another question that the appellate courts answered inconsistently was whether the *Seaman's* tort encompassed bad faith denial of liability under a contract, such as posing a defense in bad faith, as well as denial of a contract's existence in bad faith.¹²² The court in *DuBarry International, Inc.*

promisor is liable for both his promises imposed by the contract as well as any breach of this general tort duty imposed by law in carrying out the promise. This independent tort duty exists in traditionally contractual contexts such as a lawyer or an abstractor examining title to property, a doctor treating or diagnosing a patient, an engineer surveying land, and a bill collector settling an account. *Freeman & Mills*, 11 Cal. 4th at 106, 900 P.2d at 682, 44 Cal. Rptr. 2d at 433 (Mosk, J., concurring and dissenting); KEETON ET AL., *supra*, § 92, at 657.

114. *Freeman & Mills*, 11 Cal. 4th at 95, 900 P.2d at 675, 44 Cal. Rptr. 2d at 426.

115. See *infra* notes 116-29 and accompanying text (examining the appellate decisions).

116. *Freeman & Mills*, 11 Cal. 4th at 96-97, 900 P.2d at 676, 44 Cal. Rptr. 2d at 427.

117. *Id.* at 96, 900 P.2d at 676, 44 Cal. Rptr. 2d at 427. This Casenote maintains that the *Seaman's* court did not rely on the implied covenant of good faith and fair dealing theory as the basis for its holding. This is the "fatal flaw" of *Seaman's*. See *supra* notes 69-73 and accompanying text.

118. 203 Cal. App. 3d 805, 250 Cal. Rptr. 220 (1988).

119. *Okun*, 203 Cal. App. 3d at 824, 250 Cal. Rptr. at 232; *accord Koehrer v. Superior Court*, 181 Cal. App. 3d 1155, 1170, 226 Cal. Rptr. 820, 829 (1986) (finding it "difficult otherwise to understand" the *Seaman's* court's repeated references to "good faith" and "bad faith" if the court did not in fact find it necessary to base its decision on the implied covenant of good faith and fair dealing).

120. 162 Cal. App. 3d 877, 208 Cal. Rptr. 394 (1984).

121. *Quigley*, 162 Cal. App. 3d at 889, 208 Cal. Rptr. at 401.

122. *Freeman & Mills*, 11 Cal. 4th at 96, 900 P.2d at 676, 44 Cal. Rptr. 2d at 427.

*v. Southwest Forest Industries, Inc.*¹²³ determined that *Seaman's* could only extend to bad faith denial of a contract's existence, not a party's bad faith denial of liability under a contract.¹²⁴ Another appellate court, however, in *Multiplex Insurance Agency, Inc. v. California Life Insurance Co.*,¹²⁵ concluded that bad faith denial of liability under a contract was enough for remedies under *Seaman's* to attach.¹²⁶ Finally, another recurring, problematic question of which the *Freeman & Mills* majority took notice was whether a "special relationship" between the contracting parties, analogous to insurer and insured, was a necessary element of the *Seaman's* tort.¹²⁷ While both the *Multiplex* and *Quigley* courts found a special relationship unnecessary to a *Seaman's* action,¹²⁸ the *Okun* court ruled that a special relationship was a prerequisite to *Seaman's* liability.¹²⁹

The *Freeman & Mills* court then pointed to policy reasons that these appellate decisions underscored for abrogating *Seaman's*.¹³⁰ For example, the *DuBarry* court, in holding that *Seaman's* did not apply to bad faith defenses to claims of

123. 231 Cal. App. 3d 552, 282 Cal. Rptr. 181 (1991).

124. *DuBarry*, 231 Cal. App. 3d at 571, 282 Cal. Rptr. at 193.

125. 189 Cal. App. 3d 925, 235 Cal. Rptr. 12 (1987).

126. *Multiplex*, 189 Cal. App. 3d at 939, 235 Cal. Rptr. at 21.

127. *Freeman & Mills*, 11 Cal. 4th at 97, 900 P.2d at 676, 44 Cal. Rptr. 2d at 427. Perhaps one reason why the appellate courts applying *Seaman's* encountered such confusion over the special relationship question is the fact that, after *Seaman's*, plaintiffs who were victims of bad faith commercial contract breach often pleaded tortious breach of the implied covenant of good faith and fair dealing. Although the results were mixed, and the cases were not technically *Seaman's* actions because the defendants breached in bad faith, rather than denied in bad faith, their contracts, the Courts of Appeal focussed on the characteristics of the relationship of the contracting parties in determining recovery, as had the Supreme Court in *Seaman's* and the insurance line of cases. See *Rogoff v. Grabowski*, 200 Cal. App. 3d 624, 630, 632-33, 246 Cal. Rptr. 185, 189-91 (1988) (declining to permit the plaintiff's tort remedy for breach of the implied covenant of good faith and fair dealing in an oral limousine rental contract, by emphasizing that the parties, a consumer and a driver with a limousine, were not in unequal bargaining positions, since the plaintiff enjoyed access to and from the car while the defendant partially performed the contract, and remanding to determine whether the plaintiff stated a statutory cause of action under California Public Utilities Code § 5360, since the court found a reasonable inference that the defendant was a carrier of persons for reward or a charter-party carrier of passengers); see also *Commercial Cotton Co. v. United Cal. Bank*, 163 Cal. App. 3d 511, 514, 209 Cal. Rptr. 551, 554 (1985) (upholding the plaintiff's cause of action for tortious breach of the implied covenant of good faith and fair dealing against the defendant-bank, who claimed nonexistent legal defenses to its negligent disbursement of the Plaintiff's funds, by reasoning that the relationship of bank to depositor is at least quasi-fiduciary); *Wallis v. Superior Court*, 160 Cal. App. 3d 1109, 1119, 207 Cal. Rptr. 123, 129-30 (1984) (allowing recovery in tort against an employer that breached its agreement to pay its employee severance pay on the ground that the parties shared a relationship analogous to that of a disability insurer and insured). Of course, *Foley* rained on the tortious breach of the implied covenant of good faith and fair dealing parade. See *Price v. Wells Fargo Bank*, 213 Cal. App. 3d 465, 478, 261 Cal. Rptr. 735, 741 (1989) (stressing that a likely impact of *Foley* is to quash further extension of tort recovery for breach of the implied covenant of good faith and fair dealing based on "quasi-fiduciary relationship," similar to that of the bank and depositor in *Commercial Cotton*).

128. *Multiplex*, 189 Cal. App. 3d at 939, 235 Cal. Rptr. at 21; *Quigley*, 162 Cal. App. 3d at 890, 208 Cal. Rptr. at 401.

129. *Okun*, 203 Cal. App. 3d at 825, 250 Cal. Rptr. at 233.

130. *Freeman & Mills*, 11 Cal. 4th at 97-98, 900 P.2d at 676-77, 44 Cal. Rptr. 2d at 427-28.

breach of contract,¹³¹ stated that, to rule otherwise, “any party attempting to defend a disputed contract claim would risk . . . exposure to the imposition of tort damages and an expensive and time-consuming expansion of the litigation into an inquiry as to the motives and state of mind of the breaching party.”¹³² This, according to the *DuBarry* court, would be bad public policy because the line between contract and tort, both as to actions and damages, would be blurred, which would constitute a disservice to the goals served by contract and tort law and “their purposefully different measures of damages.”¹³³ Such a rule would also upset the reliability of commercial transactions and would give more work to an already overburdened court system.¹³⁴

The *Freeman & Mills* majority also recognized other meritorious policy reasons for overruling *Seaman's* that the court in *Harris v. Atlantic Richfield Co.*¹³⁵ had expounded.¹³⁶ In *Harris*, the plaintiff operated an AM/PM mini-market under a franchise agreement with the Atlantic Richfield Co. (ARCO).¹³⁷ The plaintiff alleged that ARCO failed to repair and renovate his store as promised in retaliation for the plaintiff's failure to comply with ARCO's pricing policy, and for his report to the authorities of an underground gasoline leak at the facility. The plaintiff sued ARCO for breach of contract, tortious breach of contract in violation of public policy, bad faith denial of contract, and fraud. The court upheld the breach of contract action in the plaintiff's favor, upheld both the tortious breach of contract in contravention of public policy and the bad faith denial of contract claims against the plaintiff, and remanded on the fraud cause of action. The *Seaman's* action was denied because the jury found there was no consideration for the underlying contract that ARCO had allegedly denied. The *Harris* court engaged in a thorough policy analysis, however, to decide whether tortious breach of contract in violation of public policy should be extended beyond the employer-employee relationship, which the Supreme Court had sanctioned in *Tameny v. Atlantic Richfield Co.*¹³⁸ In declining the invitation to

131. *DuBarry*, 231 Cal. App. 3d at 569, 282 Cal. Rptr. at 192.

132. *Id.* This feature of the *Seaman's* tort runs counter to the fundamental tenet of contract law that the objective standard governs whether a contract exists and, thus, its terms and their meaning. *See, e.g.,* *New York Trust Co. v. Island Oil & Transp. Corp.*, 34 F.2d 655, 656 (2d Cir. 1929); *Lucy v. Zehmer*, 84 S.E.2d 516, 521-22 (Va. 1954).

133. *DuBarry*, 231 Cal. App. 3d at 569, 282 Cal. Rptr. at 192.

134. *Id.*

135. 14 Cal. App. 4th 70, 17 Cal. Rptr. 2d 649 (1993).

136. *Freeman & Mills*, 11 Cal. 4th at 98, 900 P.2d at 676-77, 44 Cal. Rptr. 2d at 427-28.

137. The foregoing and following facts of the *Harris* case are paraphrased from *Harris*, 14 Cal. App. 4th at 72, 17 Cal. Rptr. 2d at 650.

138. 27 Cal. 3d 167, 610 P.2d 1330, 164 Cal. Rptr. 839 (1980). *Tameny*, another Bird Court decision that expanded tort liability, concerned a terminated employee's allegations against ARCO that it had wrongfully fired him for refusing to participate in an illegal scheme to fix gasoline prices. *Tameny*, 27 Cal. 3d at 169, 610 P.2d at 1330-31, 164 Cal. Rptr. at 840. Although the trial court held that the plaintiff could not recover in tort since only breach of an employment contract was at issue, the Supreme Court reversed, holding that the employee could maintain the tort action on a wrongful discharge theory. *Id.* at 178-79, 610 P.2d at

extend tort recovery for breach of contract in violation of public policy, the *Harris* court pointed to the efficient breach theory as an important reason for keeping contract and tort remedies separate,¹³⁹ since the efficient breach theory is recognized in contract law but not in tort law.¹⁴⁰ The court further noted that the goal of contract remedies, compensation of the aggrieved party, offers contracting parties predictability of the consequences of actions, which promotes commercial stability.¹⁴¹ The *Harris* court also underscored the potential of turning almost every contract breach into a claim for punitive damages, which seems like an unfair tool of coercion for plaintiffs.¹⁴² Finally, the court concluded by stating its preference for judicial restraint as another beneficial policy principle that militates against making tort remedies available for the bad faith breach of a contract in contravention of public policy.¹⁴³ The *Harris* court thought it more appropriate to defer to the state legislature when it comes to making important policy judgments affecting commercial relationships that dictate expansion of tort remedies in contract law.¹⁴⁴ The legislative forum provides the opportunity to collect empirical evidence, unrestricted by evidentiary rules; the chance to solicit expert advice; and the occasion to hold hearings in which all pertinent parties may be heard and all issues may be fully debated.¹⁴⁵ Hence, the *Freeman & Mills* court concluded its review of the cases interpreting *Seaman's* on this note, stating that "the foregoing policy considerations fully support our decision to overrule *Seaman's* rather than attempt to clarify its uncertain boundaries."¹⁴⁶

1336-37, 164 Cal. Rptr. at 846. The high court reasoned that tort recovery was appropriate in a situation in which an employer essentially demanded that its employee commit criminal acts to further the employer's interest, which the court found violated fundamental tenets of public policy. *Id.* at 173, 610 P.2d at 1333, 164 Cal. Rptr. at 842. The *Tameny* court declined to address the issue whether the employee could maintain an action against the employer on a tortious breach of the implied covenant of good faith and fair dealing theory. *Id.* at 179 n.12, 610 P.2d at 1337 n.12, 164 Cal. Rptr. at 846 n.12; *see supra* note 55 (noting the court's intimation in the *Tameny* footnote that the implied covenant of good faith and fair dealing in employment contracts might give rise to tort remedies if breached).

139. *Harris*, 14 Cal. App. 4th at 77, 17 Cal. Rptr. 2d at 653-54.

140. *See infra* notes 285-99 and accompanying text (discussing the efficient breach theory in contract law); *see also Freeman & Mills*, 11 Cal. 4th at 106, 900 P.2d at 682, 44 Cal. Rptr. 2d at 433 (Mosk, J., concurring and dissenting) (viewing the intentional breach of contract as a morally neutral act but the intentional tort as a reprehensible act, since economics supports the idea that an intentional breach of contract may create net benefits for society); RESTATEMENT (SECOND) OF CONTRACTS, ch. 16 introductory note at 100 (1979) (describing contract law's acceptance of economically efficient, intentional breaches of contract).

141. *Harris*, 14 Cal. App. 4th at 81, 17 Cal. Rptr. 2d at 656.

142. *Id.*

143. *Id.* at 81-82, 17 Cal. Rptr. 2d at 656-57.

144. *Id.* at 82, 17 Cal. Rptr. 2d at 656-57.

145. *Id.* at 82, 17 Cal. Rptr. 2d at 657.

146. *Freeman & Mills*, 11 Cal. 4th at 98, 900 P.2d at 677, 44 Cal. Rptr. 2d at 428.

c. *Persuasive Authority—Criticism of Seaman's*

The Supreme Court's majority opinion in *Freeman & Mills* then looked at persuasive authority from other jurisdictions that supported the overruling of *Seaman's*.¹⁴⁷ The court noted its position of almost complete solitude in having recognized a tort cause of action for bad faith denial of a contract's existence.¹⁴⁸ It described how, other than California, only Montana had recognized the tort, and even then, that state had limited the tort to those situations in which the contracting parties had a special relationship.¹⁴⁹

The majority then observed critical commentary directed at *Seaman's* by colleagues on the federal bench.¹⁵⁰ Most notably, Judge Kozinski of the United States Court of Appeals for the Ninth Circuit made negative remarks about California's newest tort in *Oki America, Inc. v. Microtech International, Inc.*¹⁵¹ The distinguished federal jurist believed *Seaman's* to be flawed because he found the distinction between bad faith denial of a contract and lawful denial of liability under a contract impossible to make.¹⁵² The only test Judge Kozinski could extract from *Seaman's* to make this distinction was whether a defendant's conduct "offends accepted notions of business ethics," which simply "gives judges license to rely on their gut feelings in distinguishing between a squabble and a tort."¹⁵³ The *Freeman & Mills* court also took notice of Judge Kozinski's further thought that *Seaman's* liability interfered with the business community's important freedom to contract by injecting court-made business etiquette into the law of contracts.¹⁵⁴ Judge Kozinski explained that it is "most troubling" that courts subordinate parties' voluntary contractual arrangements to the court's own sense of public policy and proper business decorum, which deprives parties of the important right to adjust legal relationships freely by mutual agreement.¹⁵⁵

147. *Id.* at 98-102, 900 P.2d at 677-79, 44 Cal. Rptr. 2d at 428-30.

148. *Id.* at 98, 900 P.2d at 677, 44 Cal. Rptr. 2d at 428; see Landsdorf, *supra* note *, at 235 & n.182 (explaining that Montana was the only other state recognizing a *Seaman's*-type tort).

149. *Freeman & Mills*, 11 Cal. 4th at 98, 900 P.2d at 677, 44 Cal. Rptr. 2d at 428 (citing *Story v. Bozeman*, 791 P.2d 767, 776 (Mont. 1990)); see *supra* notes 49, 76, 100, 127-29 and accompanying text (discussing the special relationship concept).

150. *Freeman & Mills*, 11 Cal. 4th at 99, 900 P.2d at 677, 44 Cal. Rptr. 2d at 428.

151. *Oki Am., Inc. v. Microtech Int'l, Inc.*, 872 F.2d 312 (9th Cir. 1989).

152. *Id.* at 315 (Kozinski, J., concurring). Indeed, Judge Kozinski's remarks are telling: "In inventing the tort . . . , the California Supreme Court has created a cause of action so nebulous in outline and so unpredictable in application that it more resembles a brick thrown from a third story window than a rule of law." *Id.*

153. *Id.* (quoting *Seaman's*, 36 Cal. 3d at 770, 686 P.2d at 1167, 206 Cal. Rptr. at 363).

154. *Oki America*, 872 F.2d at 316 (Kozinski, J., concurring).

155. *Id.*

Finally, the court observed Judge Kozinski's ability to predict the future when he concluded, "'*Seaman's* is a prime candidate for reconsideration."¹⁵⁶

The majority proceeded to consider another federal judge's critical remarks of *Seaman's* in *Air-Sea Forwarders, Inc. v. Air Asia Co., Ltd.*¹⁵⁷ Circuit Judge Hall had criticized *Seaman's* for what this author calls its "fatal flaw,"¹⁵⁸ by writing "[t]he *Seaman's* opinion . . . is ambiguous as to the origin of [its] holding."¹⁵⁹ The *Freeman & Mills* court acknowledged Judge Hall's criticism that the failure of *Seaman's* to rely on the implied covenant of good faith and fair dealing theory as the basis for tort liability, or to justify the expansion of tort liability for bad faith denial of contract versus bad faith dispute of contractual terms, caused confusion for courts attempting to interpret *Seaman's*.¹⁶⁰

The last persuasive decision the majority recognized is *Elxsi v. Kukje America Corp.*¹⁶¹ There, Judge Aguilar found fault with *Seaman's* for the same reason as his counterparts in the Ninth Circuit.¹⁶² Courts faced a formidable task under *Seaman's* in trying to make the elusive distinction between bad faith denial of existence of a contract and bad faith denial of liability under a contract.¹⁶³ The *Freeman & Mills* majority finally concluded this section of its opinion by realizing that its holding in *Seaman's* must have been flawed since so many courts of other jurisdictions had rejected or criticized it.¹⁶⁴

d. *Legal Literature—More Criticism of Seaman's*

Lastly, in the *Freeman & Mills* majority opinion, the California Supreme Court reviewed the plethora of scholarly commentary that its decision in *Seaman's* had generated.¹⁶⁵ It cited thirteen law review articles that criticized *Seaman's*.¹⁶⁶ For instance, several commentators criticized the *Seaman's* holding for its infamous failure¹⁶⁷ to provide guidance for making the difficult distinction

156. *Freeman & Mills*, 11 Cal. 4th at 99, 900 P.2d at 677, 44 Cal. Rptr. 2d at 428 (quoting *Oki America*, 872 F.2d at 317) (Kozinski, J., concurring)).

157. *Air-Sea Forwarders, Inc. v. Air Asia Co.*, 880 F.2d 176 (9th Cir. 1989).

158. *See supra* notes 69-73 and accompanying text (defining the "fatal flaw" of *Seaman's*).

159. *Air-Sea Forwarders*, 880 F.2d at 184.

160. *Freeman & Mills*, 11 Cal. 4th at 99, 900 P.2d at 677-78, 44 Cal. Rptr. 2d at 428-29 (citing *Air-Sea Forwarders*, 880 F.2d at 184 n.11).

161. 672 F. Supp. 1294 (N.D. Cal. 1987).

162. *Elxsi*, 672 F. Supp. at 1296; *see supra* notes 152-54, 160 and accompanying text (recounting the criticisms of Judge Kozinski and Circuit Judge Hall with regard to *Seaman's*).

163. *Elxsi*, 672 F. Supp. at 1296.

164. *Freeman & Mills*, 11 Cal. 4th at 100, 900 P.2d at 678, 44 Cal. Rptr. 2d at 429.

165. *Id.* at 100-02, 900 P.2d at 678-79, 44 Cal. Rptr. 2d at 429-30.

166. *Id.* at 100-01, 900 P.2d at 678-79, 44 Cal. Rptr. 2d at 429-30.

167. *See supra* notes 122-26, 152-53, 160 and accompanying text (describing the infamous failure of *Seaman's* as it does not provide direction for distinguishing between illegal denial of a contract's existence and lawful denial of liability under a contract's terms).

between bad faith denial of contract and bad faith denial of liability under a contract.¹⁶⁸ Others generally criticized *Seaman's* because of the confusion it created¹⁶⁹ and the questions it left unanswered.¹⁷⁰ The *Freeman & Mills* majority concluded "the breadth of the criticism . . . is disturbing and . . . is pertinent to our determination whether or not to reconsider [*Seaman's*]."¹⁷¹ As the court noted at the outset of its *Freeman & Mills* opinion, when developments subsequent to a decision show that the decision may have been unsound or that it has become ripe for reconsideration, reexamination of the opinion is proper.¹⁷²

3. Assault Complete—*Seaman's Is Overruled*

Given the expansive assault the court had just launched on *Seaman's*, in what is referred to as "subsequent developments" in the *Freeman & Mills* opinion, but what was really rejection and criticism of *Seaman's* from all directions, the court overruled *Seaman's*.¹⁷³ The new rule in California is that tort remedies, in the form of punitive damages, are not available for either bad faith denial of a noninsurance contract's existence, or bad faith denial of liability under a noninsurance contract, unless a plaintiff can plead and prove some independent tort duty arising on the part of the defendant, and that duty was breached when the defendant breached the contract.¹⁷⁴

168. See, e.g., Putz & Klippen, *supra* note 7, at 459; John A. Sebert, Jr., *Punitive and Nonpecuniary Damages in Actions Based upon Contract: Toward Achieving the Objective of Full Compensation*, 33 UCLA L. REV. 1565, 1640-41 (1986); Sandra Chutorian, Note, *Tort Remedies for Breach of Contract: The Expansion of Tortious Breach of the Implied Covenant of Good Faith and Fair Dealing into the Commercial Realm*, 86 COLUM. L. REV. 377, 401-02 (1986); Landsdorf, *supra* note *, at 223-28; John Monaghan, Note, *Extending the Bad Faith Tort Doctrine to General Commercial Contracts*, 65 B.U. L. REV. 355, 376 (1985).

169. See, e.g., Sebert, *supra* note 168, at 1640-41; Raymond Wallenstein, *Breach of the Implied Covenant of Good Faith and Fair Dealing in Commercial Contracts: A Wrong in Search of a Remedy*, 20 U. WEST L.A. L. REV. 113, 124 (1988-1989); Landsdorf, *supra* note *, at 223 & n.79; Eileen A. Scallen, Comment, *Sailing the Uncharted Seas of Bad Faith: Seaman's Direct Buying Service, Inc. v. Standard Oil Co.*, 69 MINN. L. REV. 1161, 1175 (1985); Mark Snyderman, Comment, *What's So Good About Good Faith? The Good Faith Performance Obligation in Commercial Lending*, 55 U. CHI. L. REV. 1335, 1363 (1988); see also Oxley, *supra* note 7, at 44.

170. See, e.g., Landsdorf, *supra* note *, at 227-31 (discussing such dilemmas as what quantum of proof is required to establish denial of a contract's existence and whether a special relationship is a necessary element of the *Seaman's* tort); Kurt E. Wilson, *How Contracts Escalate into Torts*, CAL. LAW., Jan. 1992, at 59-60 (attempting to harmonize the various unanswered questions concerning the required elements of a *Seaman's* cause of action); *supra* notes 122-26 and accompanying text (raising the question whether the tort applies to only bad faith denial of a contract's existence or bad faith denial of liability under a contract); see also *supra* notes 115-46 and accompanying text (reviewing how the Courts of Appeal grappled with the several questions left unanswered in *Seaman's*).

171. *Freeman & Mills*, 11 Cal. 4th at 102, 900 P.2d at 679, 44 Cal. Rptr. 2d at 430 (quoting *Moradi-Shalal*, 46 Cal. 3d at 299, 758 P.2d at 65, 250 Cal. Rptr. at 123).

172. *Freeman & Mills*, 11 Cal. 4th at 93, 900 P.2d at 673, 44 Cal. Rptr. 2d at 424.

173. *Id.* at 102-03, 900 P.2d at 679-80, 44 Cal. Rptr. 2d at 430-31.

174. *Id.*

The court again underscored the “infamous failure” of *Seaman’s*.¹⁷⁵ It recited the anomaly of extending tort remedies to bad faith denial of a contract yet treating as only contractual, with only contract remedies, bad faith denial of liability under a contract; an aberration others had already criticized.¹⁷⁶ Further, the court poked fun at the *Seaman’s* definition of bad faith: committing acts offensive to “accepted notions of business ethics.”¹⁷⁷ The *Freeman & Mills* court thought such a definition could turn every contract breach into a tort because “stonewalling,” as the *Seaman’s* court had called it, is fairly common in the business world.¹⁷⁸ After all, a defendant’s statement to a prospective plaintiff of “see you in court,” could incidentally accompany every breach of contract.¹⁷⁹ Finally, the court concluded by stating its preference for legislative, rather than judicial, activity in this area.¹⁸⁰ Nothing prevents the state legislature, it asserted, from enacting measures to provide attorneys fees for noninsurance bad faith cases, to extend compensatory damages to certain attenuated damages like lost profits, or to even reinstate *Seaman’s*.¹⁸¹

C. *The Freeman & Mills Concurring Opinion—Disagreement Over Hunter*

Justice Kennard, joined by Justice Arabian, wrote separately to concur in the majority’s disposition of *Freeman & Mills*.¹⁸² Both justices disagreed with the majority’s discussion of *Hunter v. Up-Right, Inc.*¹⁸³

In *Hunter*, an employee sued his former employer for breach of contract, breach of the implied covenant of good faith and fair dealing, and fraud.¹⁸⁴ The plaintiff claimed that he worked well with his coworkers and received excellent evaluations; yet one day his supervisor advised him that his position was being

175. See *supra* notes 122-26, 152-53, 167-68 and accompanying text (describing the infamous failure of *Seaman’s* as not providing direction for distinguishing between illegal denial of a contract’s existence versus lawful denial of liability under a contract’s terms).

176. *Freeman & Mills*, 11 Cal. 4th at 102-03, 900 P.2d at 679-80, 44 Cal. Rptr. at 430-31.

177. *Id.* at 103, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431; *Seaman’s*, 36 Cal. 3d at 770, 686 P.2d at 1167, 206 Cal. Rptr. at 363.

178. *Freeman & Mills*, 11 Cal. 4th at 103, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431; see *supra* note 60 and accompanying text (defining “stonewalling”).

179. *Freeman & Mills*, 11 Cal. 4th at 103, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431; see *supra* note 60 and accompanying text (describing the “see you in court” position).

180. *Freeman & Mills*, 11 Cal. 4th at 103, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431.

181. *Id.* The majority seemed pleased to note that, so far, the state legislature has failed to express an intention “either to expand contract breach recovery or to provide tort damages for ordinary contract breach.” *Id.* See *infra* notes 275-76 for a discussion of the various instances in which attorney’s fees are currently permitted by law.

182. *Freeman & Mills*, 11 Cal. 4th at 104, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431 (Kennard, J., concurring).

183. *Id.*; 6 Cal. 4th 1174, 864 P.2d 88, 26 Cal. Rptr. 2d 8 (1993).

184. *Hunter*, 6 Cal. 4th at 1179, 864 P.2d at 89, 26 Cal. Rptr. 2d at 9.

eliminated and that, if he did not resign, he would be fired.¹⁸⁵ To the contrary, the supervisor testified that he had disciplined Hunter for absenteeism, that Hunter told the supervisor that he was contemplating quitting due to personal problems, and that eventually Hunter did exactly that.¹⁸⁶ At trial, the jury found for Hunter for breach of the implied covenant not to terminate employment without good cause, breach of the implied covenant of good faith and fair dealing, and fraud, awarding contract and tort damages of \$120,000.¹⁸⁷ The Court of Appeal affirmed and the California Supreme Court granted review to consider *Foley's* effect on a terminated employee's action for fraud.¹⁸⁸

The high court reversed the holding on the fraud cause of action.¹⁸⁹ The majority reasoned that *Foley* precluded awarding tort remedies for fraud by employer misrepresentations made to induce termination of an employment contract. The court found that the plaintiff, in order to recover tort remedies, would have to plead and prove fraud by misrepresentation *separate* from the termination of the employment contract.¹⁹⁰ The majority stated that the employer "simply employed a falsehood to do what it otherwise could have accomplished directly," that Up-Right's misrepresentation was essentially a constructive termination, and, as such, Hunter could not prove that he detrimentally relied on Up-Right's false statements, an essential element of a fraud action.¹⁹¹ The majority further noted that, in the context of employment contracts, "it is difficult to conceive of . . . a misrepresentation made by the employer to effect termination [that] could ever rise to the level of a separately actionable fraud."¹⁹²

Justice Arabian concurred in Justice Mosk's dissent in *Hunter* and Justice Kennard dissented separately. Both dissenting opinions disagreed with the majority's premise that *Foley* controlled the case.¹⁹³ The dissenters further agreed

185. *Id.* at 1179, 864 P.2d at 89, 26 Cal. Rptr. 2d at 10.

186. *Id.* at 1179, 864 P.2d at 89-90, 26 Cal. Rptr. 2d at 10.

187. *Id.* at 1180, 864 P.2d at 90, 26 Cal. Rptr. 2d at 10.

188. *Id.* at 1183, 864 P.2d at 92, 26 Cal. Rptr. 2d at 13; *see also supra* text accompanying notes 91-102 (discussing *Foley*).

189. *Hunter*, 6 Cal. 4th at 1187, 864 P.2d at 95, 26 Cal. Rptr. 2d at 15.

190. *Id.* at 1184-85, 864 P.2d at 93-94, 26 Cal. Rptr. 2d at 13-14.

191. *Id.* at 1184, 864 P.2d at 93, 26 Cal. Rptr. 2d at 13. A claim of fraud in California requires that the plaintiff establish five elements: (1) The defendant's misrepresentation; (2) the defendant's knowledge of its falsity; (3) the defendant's intent to induce the plaintiff's reliance on the misrepresentation; (4) the plaintiff's justifiable reliance on the defendant's misrepresentation; and (5) the plaintiff's resulting damages. *Watts v. Crocker-Citizens Nat'l Bank*, 132 Cal. App. 3d 516, 522 n.2, 183 Cal. Rptr. 304, 307 n.2 (1982).

192. *Hunter*, 6 Cal. 4th at 1184-85, 864 P.2d at 93, 26 Cal. Rptr. at 13.

193. *Id.* at 1187, 864 P.2d at 95, 26 Cal. Rptr. 2d at 15 (Mosk, J., dissenting); *id.* at 1196, 864 P.2d at 101, 26 Cal. Rptr. 2d at 21 (Kennard, J., dissenting); *see supra* notes 91-102 and accompanying text (addressing the *Freeman & Mills* majority opinion discussion of *Foley*). Justice Mosk found that fraud existed in *Hunter* and distinguished *Foley* in that "*Foley* nowhere held that actions for traditional intentional torts which might accompany a wrongful discharge are barred." *Id.* at 1188, 864 P.2d at 96, 26 Cal. Rptr. 2d at 16 (Mosk, J., dissenting). Justice Kennard merely agreed with Justice Mosk's statement that *Hunter's* result is not dictated by *Foley*. *Id.* at 1196, 864 P.2d at 102, 26 Cal. Rptr. 2d at 22 (Kennard, J., dissenting).

that, on the facts before them in *Hunter*, a cause of action for fraud existed. Justice Mosk asserted that the employer's statements in *Hunter* constituted promissory fraud and, thus, tort recovery is allowed.¹⁹⁴ Justice Kennard disagreed with the majority's characterization of Up-Right's statements to induce Hunter's termination as a constructive wrongful termination.¹⁹⁵ Instead, she maintained that constructive wrongful discharge amounts to the *legal consequence* of the employer's conduct, not the employer's conduct itself.¹⁹⁶ She disagreed with giving Up-Right's statements, which included that Hunter's position was being eliminated and that if he did not quit he would be fired, legal recognition as constructive wrongful termination. She then distinguished the employer's conduct in *Hunter* from other cases in which the court found that constructive wrongful termination had occurred.¹⁹⁷

Even after *Freeman & Mills*, all California Supreme Court justices still currently agree that the violation of some independent duty imposed by tort law gives rise to tort remedies, even if the defendant's conduct also constitutes a breach of contract.¹⁹⁸ The reason for the concurring opinion in *Freeman & Mills* is best understood in light of this notion. Justice Kennard and Justice Arabian, like the majority, found that Belcher's conduct did not rise to the level of a tort; therefore, the plaintiff accounting firm could not recover punitive damages.¹⁹⁹

194. *Id.* at 1191, 1193-94, 864 P.2d at 98, 99-100, 26 Cal. Rptr. 2d at 18, 20 (Mosk, J., dissenting). "Promissory fraud" is a subspecies of the action for fraud and deceit. A promise to do something necessarily implies the intention to perform; hence, where a promise is made without such intention, there is an implied misrepresentation of fact that may be actionable fraud." *Lazar v. Superior Court*, 12 Cal. 4th 631, 638, 909 P.2d 981, 985, 49 Cal. Rptr. 2d 377, 381 (1996). Promissory fraud is a tort and, if proven, the plaintiff may recover tort damages; but the plaintiff may be limited to an election of remedies between recovery on the contract or on the tort. *Id.*

195. *Hunter*, 6 Cal. 4th at 1196, 864 P.2d at 102, 26 Cal. Rptr. 2d at 22 (Kennard, J., dissenting).

196. *Id.* at 1197, 864 P.2d at 102, 26 Cal. Rptr. 2d at 22 (Kennard, J., dissenting).

197. *Id.* at 1196-97, 864 P.2d at 102, 26 Cal. Rptr. 2d at 22 (Kennard, J., dissenting). Justice Kennard defined constructive wrongful discharge as an employee's forced resignation "as a result of actions or conditions so intolerable that a reasonable person in the employee's position would have resigned, and the employer—with actual or constructive knowledge of the intolerable actions or conditions and their impact on the employee—could have remedied the situation but did not." *Id.* at 1196, 864 P.2d at 102, 26 Cal. Rptr. 2d at 22 (Kennard, J., dissenting).

198. *Freeman & Mills*, 11 Cal. 4th at 102, 900 P.2d at 679-80, 44 Cal. Rptr. 2d at 430-31 (Lucas majority opinion); *id.* at 104, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431 (Kennard concurring opinion, in which Arabian joined); *id.* at 104, 900 P.2d at 681, 44 Cal. Rptr. 2d at 432 (Mosk concurring and dissenting opinion); see RESTATEMENT (SECOND) OF CONTRACTS § 355 (1979) (forbidding punitive damages "for a breach of contract unless the conduct constituting the breach is also a tort for which punitive damages are recoverable"); 25 C.J.S. *Damages* § 120 (1955) (prohibiting punitive damages for breach of contract but allowing them "in tort cases incidentally involving a contract where the requisite aggravating circumstances are present"); 5 CORBIN, *supra* note 10, § 1077 (asserting that punitive damages are not recoverable for a breach of contract, but certain cases allow them when elements are present that fall "within the field of tort or as closely analogous thereto").

199. *Compare Freeman & Mills*, 11 Cal. 4th at 104, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431 (Kennard, J., concurring) (explaining that "the conduct complained of by plaintiff here . . . does not amount to the violation of any independent duty arising from principles of tort law") with *id.* at 90, 900 P.2d at 671, 44 Cal.

Unlike the majority here and in *Hunter*, Justice Kennard and Justice Arabian found that Up-Right's statements in *Hunter* had amounted to commission of the tort of fraud.²⁰⁰ They therefore wrote separately to note that they disagreed with the *Freeman & Mills* majority opinion discussion of *Hunter*, but that they agreed with the disposition of *Freeman & Mills* on its facts.²⁰¹

D. The Concurring and Dissenting Opinion—For Consistency's Sake

Justice Mosk, consistent with his membership in the majority of *Seaman's* itself, dissented because he disagreed with overruling *Seaman's*.²⁰² Instead, he thought the court should have clarified the *Seaman's* holding.²⁰³ As the sole dissenting justice, Justice Mosk offered his understanding of *Seaman's* to be that it stood for the proposition "that a contract action may also sound in tort when the breach of contract is intentional and in bad faith, and is aggravated by certain particularly egregious forms of intentionally injurious activity."²⁰⁴ Since Justice Mosk found no such "intentionally injurious activity" by Belcher, he concurred in the majority's disposition of the case in Belcher's favor.²⁰⁵

In a well-structured opinion, Justice Mosk first explained the noninsurance contract circumstances under which he believes tortious breach of contract may occur.²⁰⁶ After discussing the underlying purposes served by contract and tort law,

Rptr. 2d at 422 (majority opinion) (affirming appellate court's verdict for defendant and finding tort recovery unavailable in the instant case).

200. *Hunter*, 6 Cal. 4th at 1197, 864 P.2d at 102, 26 Cal. Rptr. 2d at 22-23 (Kennard, J., dissenting); see *id.* (finding fraud on the part of defendant); *id.* at 1193-94, 864 P.2d at 99-100, 26 Cal. Rptr. 2d at 20 (Mosk, J., dissenting, in which Arabian, J., concurred) (finding all elements of fraud present).

201. *Freeman & Mills*, 11 Cal. 4th at 104, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431 (Kennard, J., concurring).

202. No doubt Justice Mosk's general inclination toward expanding tort liability had something to do with his opinion in favor of retaining *Seaman's*. See Olson, *supra* note 92, at 6 (comparing Justice Mosk to former Chief Justices Roger Traynor, Donald Wright, and Rose Bird in terms of willingness to expand tort liability).

203. *Freeman & Mills*, 11 Cal. 4th at 104, 900 P.2d at 680-81, 44 Cal. Rptr. 2d at 431-32 (Mosk, J., concurring and dissenting).

204. *Id.* at 105, 900 P.2d at 681, 44 Cal. Rptr. 2d at 432 (Mosk, J., concurring and dissenting). Notice that *Seaman's* explicitly held only that a contracting party could be liable for tort remedies when it denies the existence of the contract in bad faith and without probable cause (*Seaman's Direct Buying Serv. v. Standard Oil Co.*, 36 Cal. 3d 752, 769, 686 P.2d 1158, 1167, 206 Cal. Rptr. 354, 363 (1984)), and said nothing about denials aggravated by "egregious forms of intentionally injurious activity." Perhaps Justice Mosk derives these aggravating circumstances proposition from the statute governing when punitive damages are available, which refers to oppression, fraud, or malice as the requisite circumstances that must be present for a plaintiff to plead punitive damages *in actions for the breach of obligations not arising from contract*. See CAL. CIV. CODE § 3294(a) (West Supp. 1996).

205. *Freeman & Mills*, 11 Cal. 4th at 105, 900 P.2d at 681, 44 Cal. Rptr. 2d at 432 (Mosk, J., concurring and dissenting).

206. *Id.* at 105-13, 900 P.2d at 681-87, 44 Cal. Rptr. 2d at 432-38 (Mosk, J., concurring and dissenting).

and their fundamental differences,²⁰⁷ Justice Mosk recognized, as had his colleagues in their separate opinions, that a party to a contract can seek tort remedies for breach of the contract if the behavior constituting the contract breach violates some independent duty imposed by tort law.²⁰⁸ Justice Mosk cited Prosser's rule that tort liability for the misperformance of a contract will generally attach whenever there would be liability for gratuitous performance without the contract—when the misperformance creates foreseeable, unreasonable risk of harm to the plaintiff's interests.²⁰⁹

Again, however, the justices are not in disagreement over this proposition. Rather, one point of division between Justice Mosk and his colleagues seems to be the willingness to impose tort liability for certain intentional breaches of contract by deeming a contract defendant's conduct socially wrong or "deviati[ng] from socially useful business practices"²¹⁰ Justice Mosk cited two Court of Appeal cases in support of the view that contract law imposes tort liability when a defendant's conduct constitutes a distinct social wrong apart from the breach of contract.²¹¹ The majority, however, pointed to the high court's own cases, such

207. See KEETON ET AL., *supra* note 11, § 1, at 5-6 (describing the function of contract law as protecting the single, limited interest in having the promises of others performed while the law of torts allocates losses arising out of human activities, protecting individuals for losses "suffered within the scope of their legally recognized interests generally, rather than one interest only").

208. *Freeman & Mills*, 11 Cal. 4th at 106, 900 P.2d at 682, 44 Cal. Rptr. 2d at 433 (Mosk, J., concurring and dissenting); see *supra* note 113 and accompanying text (discussing availability of tort remedies when a contract breach violates some independent tort duty imposed by law, and giving examples).

209. *Freeman & Mills*, 11 Cal. 4th at 107, 900 P.2d at 682, 44 Cal. Rptr. 2d at 433 (Mosk, J., concurring and dissenting) (quoting KEETON ET AL., *supra* note 11, § 92, at 660-61); see *infra* note 269 (citing examples of these types of situations).

210. *Freeman & Mills*, 11 Cal. 4th at 109, 900 P.2d at 684, 44 Cal. Rptr. 2d at 435 (Mosk, J., concurring and dissenting); see *supra* note 202 (noting Justice Mosk's preference for expanding tort liability).

211. *Freeman & Mills*, 11 Cal. 4th at 108, 900 P.2d at 683-84, 44 Cal. Rptr. 2d at 434-35 (Mosk, J., concurring and dissenting). Justice Mosk cited *Walker v. Signal Companies, Inc.*, 84 Cal. App. 3d 982, 149 Cal. Rptr. 119 (1978), for the rule that a plaintiff may recover punitive damages when a defendant induces the breached contract by promissory fraud, a rule justified "by the fact that the breach of a fraudulently induced contract is a significantly greater wrong, from society's standpoint, than an ordinary breach." *Freeman & Mills*, 11 Cal. 4th at 108, 900 P.2d at 684, 44 Cal. Rptr. 2d at 435 (Mosk, J., concurring and dissenting). In *Walker*, the court held that the plaintiff presented sufficient evidence to establish a claim of fraud by satisfying its five elements. *Walker*, 84 Cal. App. 3d at 995, 149 Cal. Rptr. at 125; see *supra* note 191 (listing the elements of fraud). The *Freeman & Mills* majority would agree, however, that tort remedies may be recovered when plaintiff pleads and proves fraud, apart from the breach of contract. See, e.g., *Hunter v. Up-Right, Inc.*, 6 Cal. 4th 1174, 1184-85, 864 P.2d 88, 93-94, 26 Cal. Rptr. 2d 8, 13-14 (1993) (reasoning that the plaintiff would have to prove fraud separate from breach of contract to recover tort remedies for breach of an employment agreement). Furthermore, a different court found that the rule is justified not by the "greater wrong" involved but rather by the fact that California Civil Code § 3294 lists the word "fraud" alone as an adequate basis for awarding punitive damages. CAL. CIV. CODE § 3294(a) (West Supp. 1996); *Glendale Fed. Sav. & Loan Ass'n v. Marina View Heights Dev., Inc.*, 66 Cal. App. 3d 101, 135, 135 Cal. Rptr. 802, 822 (1977).

The other appellate case Justice Mosk cited, *Las Palmas Assocs. v. Las Palmas Ctr. Assocs.*, 235 Cal. App. 3d 1220, 1 Cal. Rptr. 2d 301 (1991), similarly involved a fraud claim in the context of a real estate contract. The court affirmed the fraud cause of action after finding the evidence sufficient to meet the elements of fraud. *Las Palmas Assocs.*, 235 Cal. App. 3d at 1239, 1 Cal. Rptr. 2d at 311. The court relied on California

as *Foley*, *Hunter*, and *Applied Equipment*, for the proposition that, in fact, the courts should be reluctant to deem a contract defendant's conduct socially wrong and thus to permit tort remedies, the approach taken in the insurance contract cases. Instead, tort recovery for contract breaches should be limited to the insurance area, absent the violation of an independent tort duty.²¹²

Continuing to address the noninsurance contract circumstances under which Justice Mosk asserts that tortious breach of contract may occur, Justice Mosk next considered tortious breaches of contract based on the implied covenant of good faith and fair dealing,²¹³ rather than independent conventional torts like fraud. The associate justice referred to the insurance line of cases as an example of the implied covenant of good faith and fair dealing serving as a predicate to allow tort recovery in contract cases.²¹⁴ Justice Mosk admonished California courts not to be "preoccupied" with limiting the tortious breach of the implied covenant of good faith and fair dealing theory in contract cases, rather than to be "useful" by "identifying *specific practices* employed by contracting parties that merit the imposition of tort remedies."²¹⁵ Justice Mosk then addressed two broad categories of persuasive authority that he saw as expanding the tortious breach of the implied covenant of good faith and fair dealing theory in contract cases. The concurring and dissenting justice cited these categories of persuasive authority in an attempt to bolster his argument that California should not be slow to attach tort liability for breach of the implied covenant of good faith and fair dealing in contract cases. The first category consisted of cases in which tortious means are utilized by one of the contracting parties to deceive the other into foregoing contractual rights. The other category comprised cases of intentional breach in which the breaching party knows that the breach entails attendant consequences to the other party that are especially injurious.

However, at least some of the authority that Justice Mosk cited appears misplaced. For instance, Justice Mosk discussed *Advanced Medical, Inc. v. Arden Medical Systems, Inc.*²¹⁶ as a case representing his first category of cases expanding tort liability for breach of the implied covenant of good faith and fair dealing in contract cases. In this category, tortious means are utilized by one of

Civil Code § 1710(4) for its definition of fraud, which defined "fraud" as "[a] promise, made without any intention of performing it," and California Civil Code § 3294, which permits punitive damages in fraud actions. *Las Palmas Assocs.*, 235 Cal. App. 3d at 1238-39, 1 Cal. Rptr. 2d at 310-11.

212. *Freeman & Mills*, 11 Cal. 4th at 94-95, 900 P.2d at 674-75, 44 Cal. Rptr. 2d at 425-26; see *supra* notes 91-114 and accompanying text (discussing *Foley*, *Hunter*, and *Applied Equipment*).

213. See *supra* note 26 (describing the parameters of the implied-by-law covenant of good faith and fair dealing in all contracts).

214. *Freeman & Mills*, 11 Cal. 4th at 109, 900 P.2d at 684, 44 Cal. Rptr. 2d at 435 (Mosk, J., concurring and dissenting).

215. *Id.*

216. 955 F.2d 188 (3d Cir. 1992).

the contracting parties to deceive the other into foregoing contractual rights.²¹⁷ The plaintiff in *Advanced Medical* sued the defendant for breach of a distribution contract and intentional interference with contractual relations. The defendant attempted to get out of the contract by marketing products designed to compete with the plaintiff, and failed to supply the plaintiff with support services as the contract required.²¹⁸ The *Advanced Medical* court, though, never mentioned the implied covenant of good faith and fair dealing as a predicate for tort liability, instead finding that the plaintiff's right to punitive damages "emanate from plaintiff's tort claim."²¹⁹ All the court found necessary under Pennsylvania law, to sustain the punitive damages award on the plaintiff's tort claim, was the defendant's willful or malicious outrageous conduct.²²⁰

The other category of cases that Justice Mosk found exemplified the expansion of tort liability for breach of the implied covenant of good faith and fair dealing in contract cases was the kind of intentional breach that the breaching party knows involves especially injurious attendant consequences. Here, Justice Mosk cited *K Mart Corp. v. Ponsock*.²²¹ K Mart had employed Ponsock as a forklift driver for a term until his retirement, which the court found amounted to Ponsock being a tenured employee.²²² Subsequently, K Mart fired Ponsock six months prior to his anticipated retirement, after which he would be paid in full by K Mart, for allegedly "defacing company property, forklift, with misappropriated merchandise, paint, on company time."²²³ K Mart had failed, however, to follow the employment agreement that called for its providing assistance and correction notices to Ponsock in the event of his deficient performance.²²⁴ The employment contract also mandated that K Mart could terminate Ponsock only after a series of these correction notices proved that his performance remained unacceptable.²²⁵ Justice Mosk best summarized the court's holding by stating "the Nevada Supreme Court allowed a \$50,000 award of punitive damages to stand when an employer discharged a long-term employee on a fabricated charge for the purpose of defeating the latter's contractual entitlement to retirement benefits."²²⁶ The *Ponsock* court reasoned that punitive damages were available on a "bad faith discharge" theory, since K Mart's real motive was to divest Ponsock of his retirement rights, finding the "bad faith discharge" theory based on the covenant of

217. *Freeman & Mills*, 11 Cal. 4th at 110, 900 P.2d at 684-85, 44 Cal. Rptr. 2d at 435-36 (Mosk, J., concurring and dissenting).

218. *Advanced Medical*, 955 F.2d at 189-91.

219. *Id.* at 202 n.8.

220. *Id.* at 202.

221. 732 P.2d 1364 (Nev. 1987).

222. *K Mart Corp.*, 732 P.2d at 1366.

223. *Id.* at 1367.

224. *Id.* at 1366.

225. *Id.*

226. *Freeman & Mills*, 11 Cal. 4th at 112, 900 P.2d at 686, 44 Cal. Rptr. 2d at 437 (Mosk, J., concurring and dissenting).

good faith and fair dealing implied in contracts.²²⁷ The court found, however, that such tort liability in a contract case, based upon breach of the implied covenant of good faith and fair dealing, could only be found if there existed a special relationship between the parties.²²⁸ On the facts before it, the court found that a special relationship between the parties indeed existed.²²⁹ The California Supreme Court, however, has disagreed with its sister-state supreme court on this point, and has refused to call the employer-employee association a special relationship in the context of tortious breach of the implied covenant of good faith and fair dealing.²³⁰

Justice Mosk concluded the section of his opinion in which he described the noninsurance contract circumstances under which he asserts tortious breach of contract may occur by stating:

In sum, the above cited cases show that an intentional breach of contract may be found to be tortious when the breaching party exhibits an extreme disregard for the contractual rights of the other party, either knowingly harming the vital interests of a promisee so as to create substantial mental distress or personal hardship, or else employing coercion or dishonesty to cause the promisee to forego its contractual rights.²³¹

The associate justice then devoted the next part of his opinion to a reconsideration of *Seaman's*, in light of the first part of his opinion discussing expansion of the tortious breach of the implied covenant of good faith and fair dealing theory in contract cases elsewhere.

Justice Mosk first reviewed the facts of *Seaman's* and its holding.²³² He then bluntly approved of what this Note has referred to as "the fatal flaw of *Seaman's*."²³³ The now dissenting justice found it preferable that the *Seaman's* majority (of which he was a member) had "identif[ied] specific practices used by Standard that violated 'accepted notions of business ethics'"²³⁴ rather than having

227. *K Mart Corp.*, 732 P.2d at 1369-70.

228. *Id.* at 1372.

229. *Id.* at 1370; see *supra* note 49 (discussing California's special relationship factors).

230. *Foley v. Interactive Data Corp.*, 47 Cal. 3d 654, 690-93, 765 P.2d 373, 393-96, 254 Cal. Rptr. 211, 232-35 (1988); see *supra* notes 91-102 and accompanying text (discussing *Foley*).

231. *Freeman & Mills*, 11 Cal. 4th at 113, 900 P.2d at 686-87, 44 Cal. Rptr. 2d at 437-38 (Mosk, J., concurring and dissenting).

232. *Id.* at 113-14, 900 P.2d at 687-88, 44 Cal. Rptr. 2d at 438-39 (Mosk, J., concurring and dissenting); see *supra* notes 56-68 and accompanying text (discussing the facts of *Seaman's* and its holding).

233. See *supra* notes 69-73 and accompanying text (describing the "fatal flaw" of *Seaman's*).

234. The only "specific practices used by Standard that violated 'accepted notions of business ethics'" that the *Seaman's* court identified in its analysis was defendant Standard's adoption of a "stonewalling" position when one of its agents stated "see you in court" without probable cause and with no belief in the existence of a defense. *Seaman's*, 36 Cal. 3d at 769-70, 686 P.2d at 1167, 206 Cal. Rptr. at 363. The *Freeman & Mills* majority rejected limiting the *Seaman's* tort to such "stonewalling" tactics, dismissing such conduct

transformed the implied covenant of good faith and fair dealing theory into a tort *carte blanche* by relying on it.²³⁵ Justice Mosk finally offered his own criticism of *Seaman's*. In his view, *Seaman's* was too narrow because it failed to make a distinction between bad faith denial of the existence of a contract and bad faith denial of liability under a contract.²³⁶ Justice Mosk then admitted that:

Seaman's was overly broad because, for a number of reasons, it appears to have been unwise to impose tort liability for *all* breaches that involve bad faith denial of a contract or liability under the contract. Although the bad faith denial of contractual liability may be ethically inexcusable, we should hesitate to categorically impose tort liability on such activity for fear it may overly deter legitimate activities that we wish to permit or encourage.²³⁷

Ultimately, however, Justice Mosk came to the conclusion that the high court had decided *Seaman's* correctly. The justice explained that some intentional contract breaches in the commercial sphere that cause the injured party emotional distress or personal hardship, such as “the frustrations that attend breached contracts, unreliable suppliers, and the like are part of the realities of commerce.”²³⁸ Justice Mosk noted that society requires the injured party look to the marketplace to seek substitute performance to mitigate losses and to pursue only contract damages for the losses that cannot be mitigated.²³⁹ Justice Mosk continued, however, by citing *Seaman's* as the type of intentional contract breach that is *not* part and parcel of the commercial world: given the oil crisis underway when the *Seaman's* transactions occurred, Standard did more than just breach a contract and cause hardship; Standard knew that its conduct, under the circumstances, would have the practical effect of forcing *Seaman's* out of business.²⁴⁰ Such a case satisfied the elements of the *Seaman's* tort according to Justice Mosk: (1) Intentional breach of contract without probable cause; (2) without belief that the contract does *not* exist; (3) with knowledge or intent that the breach will cause the

as potentially incidental to the breach of every contract. *Freeman & Mills*, 11 Cal. 4th at 103, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431.

235. *Freeman & Mills*, 11 Cal. 4th at 114-15, 900 P.2d at 688, 44 Cal. Rptr. 2d at 439 (Mosk, J., concurring and dissenting) (quoting *Seaman's*, 36 Cal. 3d at 770, 686 P.2d at 1167, 206 Cal. Rptr. at 363).

236. *Freeman & Mills*, 11 Cal. 4th at 115, 900 P.2d at 688, 44 Cal. Rptr. 2d at 439 (Mosk, J., concurring and dissenting); see *supra* notes 167-68 and accompanying text (calling this failure to distinguish between the two types of contractual bad faith the “infamous failure” of *Seaman's*).

237. *Freeman & Mills*, 11 Cal. 4th at 115, 900 P.2d at 688, 44 Cal. Rptr. 2d at 439 (Mosk, J., concurring and dissenting) (emphasis in original); see *infra* notes 295-99 and accompanying text (discussing the chilling economic effect of punitive damages remedies in commercial contractual settings).

238. *Freeman & Mills*, 11 Cal. 4th at 116, 900 P.2d at 689, 44 Cal. Rptr. 2d at 440 (Mosk, J., concurring and dissenting).

239. *Id.*

240. *Id.*; see *supra* notes 57-60 and accompanying text (recounting Standard's conduct).

other party severe damages that are not easily mitigated; and (4) the other party indeed experiences such severe harm.²⁴¹

The final part of Justice Mosk's opinion declared essentially that the facts of *Freeman & Mills* did not establish the just-noted third and fourth elements of the *Seaman's* tort.²⁴² As such, Justice Mosk concurred in the majority's disposition of *Freeman & Mills* in defendant Belcher's favor. Had the courts previously clarified the elements of the *Seaman's* tort, as Justice Mosk did in his *Freeman & Mills* concurring and dissenting opinion, perhaps *Seaman's* would have survived, since lower courts would have been less confused about the parameters of the *Seaman's* tort.²⁴³ At least Justice Mosk's position remained consistent throughout the life of *Seaman's*.

IV. LEGAL AND ECONOMIC RAMIFICATIONS OF *FREEMAN & MILLS*

Well-recognized legal principles and sound economic policy justifies the court's holding in *Freeman & Mills*. The case should prove to be beneficial to contracting parties in general.

A. *Legal Principles*

1. *The Goals of Tort and Contract*

Perhaps the most obvious legal principles that best justify the court's decision in *Freeman & Mills* are the very objectives of tort and contract law. While the threat of punitive damages may serve a proper purpose in the law of tort,²⁴⁴ its presence is inappropriate in the contract context.

Two of the chief purposes of contract law are protection of the reasonable expectations of parties to a bargain and compensation for reasonable reliance on the promises of others.²⁴⁵ Consistent with these goals of contract law, the primary

241. *Freeman & Mills*, 11 Cal. 4th at 116, 900 P.2d at 689, 44 Cal. Rptr. 2d at 440 (Mosk, J., concurring and dissenting). To appreciate the confusion experienced by courts in attempting to define the *Seaman's* tort, compare Justice Mosk's view of the elements of the *Seaman's* tort with a 1992 rendition offered by a legal commentator in the state's bar journal. Wilson, *supra* note 170, at 59 (listing the elements as: (1) An underlying contract; (2) breached by defendant; (3) where defendant denies liability by asserting that the contract does not exist; (4) in bad faith; and (5) without probable cause).

242. *Freeman & Mills*, 11 Cal. 4th at 117, 900 P.2d at 689, 44 Cal. Rptr. 2d at 440 (Mosk, J., concurring and dissenting); *see id.* (finding that Belcher had only intentionally breached the contract and asserted a bad faith defense to contractual liability and that the contract did not exist).

243. *See supra* notes 115-29 and accompanying text (discussing the alleged elements of the *Seaman's* tort that confused appellate courts faced with attempting to apply *Seaman's*).

244. *See supra* note 16 and accompanying text (describing the purpose punitive damages serve).

245. GORDON D. SCHABER & CLAUDE D. ROHWER, *CONTRACTS IN A NUTSHELL* § 88, at 147 (3d ed. 1990); *see Freeman & Mills*, 11 Cal. 4th at 105, 900 P.2d at 682, 44 Cal. Rptr. 2d at 433 (Mosk, J., concurring and dissenting) (finding that contract actions are created to protect the interest in having promises performed);

remedy that the American legal system affords for breach of contract is expectation damages: the placement of the injured party in as good a position as the party would have been had the contract been fully performed.²⁴⁶ This principal remedy of contract law has been historically limited, however, in that damages based upon an aggrieved party's expectation are awarded only to the extent that such damages are reasonably certain and relatively foreseeable.²⁴⁷ Professor

1 FARNSWORTH, *supra* note 10, § 1.6, at 20-21 (recounting the common law development of contract law, noting that the extension of the assumpsit action to the executory exchange of promises had the "important implication" of courts protecting promises by making promisors compensate them for their disappointed expectations, and offering as the rationale for this development of contract law that protection of parties' expectations is "the most effective way of protecting reliance," since contracts are of little use if parties cannot rely on their legal efficacy).

246. See CAL. CIV. CODE § 3300 (West 1970) (delineating the measure of damages for contract breach as the amount that will compensate the injured party for all detriment proximately caused by the breach "or which, in the ordinary course of things, would be likely to result therefrom"); U.C.C. § 1-106(1) (1990) (providing that remedial provisions of the U.C.C. should be liberally administered to place the aggrieved party "in as good a position as if the other party had fully performed"); RESTATEMENT (SECOND) OF CONTRACTS § 347 cmt. a (1979) (interpreting the general measure of contract damages to provide plaintiff with a monetary sum sufficient enough to place plaintiff in as good a position as plaintiff would have been had defendant performed); 3 FARNSWORTH, *supra* note 10, § 12.8, at 186 (asserting that, in most breach of contract cases, the injured party recovers damages sufficient to place the party in as good a position as the party would have been had the contract been performed).

Alternatively, contract plaintiffs who are unable to prove expectation damages may recover "reliance damages," which compensates plaintiff for actual expenses incurred by relying upon the contract. See *Coburn v. California Portland Cement Co.*, 144 Cal. 81, 84, 77 P. 771, 772 (1904) (stating that where there is no market value for goods that are the subject of a contract, or where such market value is not an appropriate or adequate index of damages, the proper measure of damages is recompense for the actual loss suffered); 3 FARNSWORTH, *supra* note 10, § 12.8, at 187 (stating that generally courts allow expectation damages rather than reliance damages); SCHABER & ROHWER, *supra* note 245, § 130, at 263 (discussing reliance damages, which may be assessed when expectation damages are not proven). Since expectation damages are the primary remedy for breach of contract, the other types of contract remedies, such as reliance damages, specific performance, restitution, liquidated damages and penalty clauses, and others, are not discussed here.

247. For the certainty requirement, see, for example: CAL. CIV. CODE § 3301 (West 1970) (declaring that "[n]o damages can be recovered for a breach of contract which are not clearly ascertainable in both their nature and origin"); U.C.C. § 2-204(3) (1990) (stating that leaving one or more terms of a contract open does not prove fatal to formation provided that "there is a reasonably certain basis for giving an appropriate remedy"); RESTATEMENT (SECOND) OF CONTRACTS § 352 (1979) (precluding recovery of damages unless evidence establishes them with reasonable certainty); 3 FARNSWORTH, *supra* note 10, § 12.15, at 252 (discussing uncertainty as a limitation to an award of damages for breach of contract).

For the foreseeability requirement, see, for example: CAL. CIV. CODE § 3300 (West 1970) (imposing expressly a proximate causation prerequisite on plaintiff's recovery of damages for contract breach); U.C.C. § 2-714(1) (1990) (permitting a buyer of goods to recover from the seller losses "resulting in the ordinary course of events"); *Overstreet v. Merritt*, 186 Cal. 494, 502, 200 P. 11, 14 (1921) (holding defendant liable for plaintiff's loss that was the natural result of defendant's breach and that was within the parties' reasonable contemplation upon execution of the contract); *Hadley v. Baxendale*, 9 Ex. 341, 354, 156 Eng. Rep. 145, 151 (1854) (refusing to permit a miller to recover lost profits for closing down his mill due to the defendant-manufacturer's sale to him of a faulty steam engine crankshaft on the ground that the miller failed to notify the defendant his mill was closed and, as such, the closing of the mill could not "have been in the contemplation of both parties, at the time they made the contract as the probable result of the breach of it"); RESTATEMENT (SECOND) OF CONTRACTS § 351(1) (1979) (permitting recovery of only those damages "that the party in breach . . . [had] reason to foresee as a probable result of the breach when the contract was made").

Farnsworth explains that the certainty requirement emerged in early American courts in an effort to control the jury's discretion in awarding damages and to express "a judicial reluctance to recognize interests that are difficult or impossible to measure in money."²⁴⁸ With regard to the unforeseeability requirement, Professor Farnsworth justifies this limitation by asserting "that liability for unforeseeable loss might impose upon an entrepreneur a burden greatly out of proportion to the risk that the entrepreneur originally supposed was involved and to the corresponding benefit that the entrepreneur stood to gain."²⁴⁹ Indeed, both of these limitations on damages for a breach of contract seem fitting in light of contract law's goal of protecting *reasonable* expectations. It would be unfair to subject a contracting party to speculation and discretion in measuring damages and to consequences of which the party had no conceivable idea when it entered into the contract.

The goal of tort law, on the other hand, is a very different one. Rather than imposing liability for breaking voluntary promises made to another, tort law seeks to compensate individuals by legally mandating, based upon then-existing social policy, a duty upon everyone to abstain from injuring the person, property, or other intangible rights of another.²⁵⁰ A corollary of this goal is tort law's function of deterring potential tortfeasors from causing harm in the first instance.²⁵¹ The measure of damages for the commission of most torts is compensation designed to represent the closest possible pecuniary equivalent of the plaintiff's loss—to place the plaintiff in the same position the plaintiff occupied prior to the tort's

248. 3 FARNSWORTH, *supra* note 10, § 12.15, at 252-53 (citing *Griffin v. Colver*, 16 N.Y. 489, 491 (1858), the leading case on the topic).

249. 3 FARNSWORTH, *supra* note 10, § 12.14, at 241.

250. See CAL. CIV. CODE § 1708 (West 1985) (reciting "[e]very person is bound, without contract, to abstain from injuring the person or property of another, or infringing upon any of his rights"); KEETON ET AL., *supra* note 11, § 1, at 6 (asserting that the purpose of tort law is to allocate responsibility for losses arising out of human activities by affording compensation for injuries sustained by one person at the hands of another); WADE ET AL., *supra* note 13, at 1 (including four purposes of tort law: (1) To provide peaceful dispute resolution; (2) to deter wrongful behavior; (3) to encourage socially responsible conduct; and (4) to restore injured parties to their previous state by way of compensation).

251. See RESTATEMENT (SECOND) OF TORTS § 901 cmt. c (1979) (explaining that, unlike the law of contracts or restitution, the law of torts often seeks to punish tortfeasors to deter future tortious acts); KEETON ET AL., *supra* note 11, § 4, at 25-26 (calling the deterrence goal of tort law a "prophylactic" factor designed to prevent future harm and to admonish the wrongdoer; asserting that when court decisions are made, and prospective defendants thereby realize their potential liability, "a strong incentive to prevent the occurrence of the harm" exists; and concluding that punitive damages are sometimes a proper remedy for the commission of torts since the goal of punitive damages is to deter undesirable conduct).

occurrence.²⁵² To this end, the foreseeability²⁵³ and certainty limitations found in contract damages do not exist in tort damages.²⁵⁴ In its quest to make the tort plaintiff whole again, the court assesses damages with little concern for their degree of foreseeability.²⁵⁵ Tort plaintiffs are not required to prove their damages with great certainty.²⁵⁶

Given the different goals and remedies of contract and tort law, the presence of a *Seaman's*-type cause of action muddies the contract waters. As Judge Kozinski put it, "commercial enterprises [cannot] be expected to flourish in a legal atmosphere where every move, every innovation, every business decision must be hedged against the risk of exotic new causes of action and incalculable damages."²⁵⁷ Tort remedies, however, should remain somewhat unpredictable in order to deter risk of harm to others, since the goal of tort law is to prevent risk of harm to others.²⁵⁸ With the economic role that contracts play in today's

252. WADE ET AL., *supra* note 13, at 508; 6 B. E. WITKIN, SUMMARY OF CALIFORNIA LAW, *Torts* § 1319 (9th ed. 1988); see CAL. CIV. CODE § 3333 (West 1970) (authorizing damages for torts in general to be that "amount which will compensate for all the detriment proximately caused" by defendant's "breach of an obligation not arising from contract"); ROBERT L. RABIN, PERSPECTIVES ON TORT LAW 344 (4th ed. 1995) (relating that compensation in "accidental harm" cases is designed to restore the victim of injury to the position the person occupied prior to the accident).

253. Of course, the foreseeability requirement is incorporated into tort law by way of the proximate causation requirement rather than the damages element. KEETON ET AL., *supra* note 11, § 42, at 273 (generalizing about the two contrasting theories of proximate cause: one holds that liability should not extend beyond the scope of foreseeable risks while the other believes that liability should extend only to directly traceable consequences of defendant's act or omission and its indirect consequences that are foreseeable).

254. See *supra* notes 247-49 and accompanying text (discussing these limitations on contract damages).

255. See CAL. CIV. CODE § 3333 (West 1970) (expressly permitting tort damages that will compensate plaintiff "for all the detriment proximately caused" by defendant "whether it could have been anticipated or not"); *Hunt Bros. Co. v. San Lorenzo Water Co.*, 150 Cal. 51, 56, 87 P. 1093, 1095 (1906) (contrasting the foreseeability requirement of contract damages with the tort damages rule that damages need not have been anticipated to be recoverable). Indeed, the tort rule known as the "thin skull doctrine" holds that a defendant must take his plaintiff as the defendant finds the plaintiff, thus making the defendant liable for all of the plaintiff's immediate damages whether they could have been anticipated or not. *McCahill v. New York Transp. Co.*, 94 N.E. 616 (N.Y. 1911).

256. See *Zinn v. Ex-Cell-O Corp.*, 24 Cal. 2d 290, 297-98, 149 P.2d 177, 181 (1944) (holding that tort defendants cannot escape liability merely because plaintiff's damages are not capable of exact measurement); RESTATEMENT (SECOND) OF TORTS § 912 cmt. a (1979) (stating that "[t]here is no general requirement that the injured person should prove with like definiteness the extent of the harm that he has suffered as a result of the tortfeasor's conduct").

257. *Oki Am., Inc. v. Microtech Int'l, Inc.*, 872 F.2d 312, 316 (9th Cir. 1989) (Kozinski, J., concurring); see *Applied Equip. Corp. v. Litton Saudi Arabia Ltd.*, 7 Cal. 4th 503, 515, 869 P.2d 454, 460, 28 Cal. Rptr. 2d 475, 481 (1994) (asserting that the foreseeability limitation on contract damages fosters contractual relationships and commercial enterprise by allowing parties to predict in advance the financial risks of their activities).

258. See WILLIAM M. LANDES & RICHARD A. POSNER, THE ECONOMIC STRUCTURE OF TORT LAW 9-12, 58 (1987) (describing the deterrence rationale of tort law, which is designed to create disincentives for injurious activities); see also *supra* note 251 and accompanying text (calling the deterrence function of tort law a corollary of tort law's main goal of compensation, based on social policy, for breach of the duty to abstain from injuring the person, property, or other intangible rights of others).

commercial realm,²⁵⁹ however, contract remedies should remain stable and predictable to fulfill contract law's goal of encouraging parties to rely on the promises of others with the assurance that their expectations will be fulfilled whether the contract is breached or not. *Freeman & Mills*, thus viewed, serves the goals of both contract and tort by creating certainty and clarity in the remedies of contract and tort.

2. Certainty and Clarity in Contracting

The most beneficial legal effect of the Supreme Court's decision in *Freeman & Mills* is the creation of clarity and the removal of confusion concerning bad faith contract actions in California. Objectivity, often viewed as the hallmark of contract law, requires rules geared toward achieving certainty and clarity. This desired result was indeed the principle force behind the high court's decision to review *Freeman & Mills* and to overrule *Seaman's*.²⁶⁰ The court's retraction of the bad faith denial of contract cause of action frees practitioners and courts from expending an inordinate amount of time and effort in attempting to construe *Seaman's*.²⁶¹ No longer will parties have to guess whether the bad faith denial of contract tort requires a special relationship between the parties.²⁶² Nor will

259. See *infra* notes 285-99 and accompanying text (addressing the economic analysis of contract law and its associated ramifications under *Freeman & Mills*).

260. *Freeman & Mills*, 11 Cal. 4th at 102, 900 P.2d at 679-80, 44 Cal. Rptr. 2d at 430-31 (stressing that the uniform confusion and uncertainty about the scope and application of the *Seaman's* tort, together with doubt concerning the wisdom of the *Seaman's* holding, convinced the court that *Seaman's* should be overruled).

261. See *Oki America*, 872 F.2d at 314-15, 316 (Kozinski, J., concurring). Judge Kozinski's point stressing the time courts and others wasted in applying *Seaman's* is too well-put to paraphrase:

Nowhere but in the Cloud Cuckooland of modern tort theory could a case like this have been concocted. One large corporation is complaining that another obstinately refused to acknowledge they had a contract. For this shocking misconduct it is demanding millions of dollars in punitive damages. I suppose we will next be seeing lawsuits seeking punitive damages for maliciously refusing to return telephone calls or adopting a condescending tone in interoffice memos . . . [T]he case drags on, kept alive by Microtech's vain hope of parlaying a business squabble into a \$3.1 million gold mine. The judicial machinery keeps churning, fueled by the energies of lawyers, the parties, a district judge, three appellate judges, their respective staffs and other myriad components of the judicial process. One shudders to imagine the resources that would be consumed in adjudicating a more colorable *Seaman's* case. We surely have more pressing claims on our limited resources—safeguarding the environment, protecting the rights of the accused, preventing encroachments on constitutionally protected liberties, to name a few—than helping Microtech soothe its bruised feelings over a quarrel with its supplier.

Id.; see Landsdorf, *supra* note *, at 236 (asserting that courts have been judicially inefficient in analyzing *Seaman's* claims in order to restrict the tort).

262. Compare *Multiplex Ins. Agency, Inc. v. California Life Ins. Co.*, 189 Cal. App. 3d 925, 939, 235 Cal. Rptr. 12, 21 (1987) (finding a special relationship unnecessary to *Seaman's*-type recovery) and *Quigley v. Pet, Inc.*, 162 Cal. App. 3d 877, 890, 208 Cal. Rptr. 394, 401 (1984) (same) with *Okun v. Morton*, 203 Cal. App. 3d 805, 825, 250 Cal. Rptr. 220, 233 (1988) (holding that the bad faith denial of contract tort is limited to those situations in which a special relationship exists between the contracting parties); see *supra* notes 127-

litigants have to guess whether the *Seaman's* tort applies to bad faith defenses to formation or bad faith denial of liability under the contract.²⁶³ Whether the Supreme Court erred fatally²⁶⁴ by not basing the *Seaman's* cause of action on the implied covenant of good faith and fair dealing is now a moot point.²⁶⁵ Finally, parties are relieved of facing the prospect that otherwise standard, objective contract litigation will mutate into a subjective inquiry into a party's state of mind, a phenomenon which already overburdens the court's criminal dockets.²⁶⁶ California's highest court has removed the legal community's unwanted burden of confronting these tough issues by eliminating the *Seaman's* tort.

Furthermore, as the *Freeman & Mills* court itself noted, it is anomalous to punish a party with punitive damages for bad faith denial of a contract's existence

29 and accompanying text (addressing the conflicting Court of Appeal decisions over whether a special relationship was a prerequisite to a *Seaman's* action).

263. Compare *DuBarry Int'l, Inc. v. Southwest Forest Ind., Inc.*, 231 Cal. App. 3d 552, 571, 282 Cal. Rptr. 181, 193-94 (1991) (limiting the *Seaman's* cause of action to bad faith denial of a contract's existence rather than assertion of other bad faith defenses to liability) with *Multiplex*, 189 Cal. App. 3d at 939, 235 Cal. Rptr. at 21 (intimating that if appellant denied any liability under the contract in bad faith it could be sanctioned with punitive damages under *Seaman's*); see *supra* notes 122-26 and accompanying text (relating the conflicting Court of Appeal opinions concerning whether the *Seaman's* tort attached to bad faith denial of liability under a contract versus bad faith denial of the contract itself).

264. See *supra* notes 69-73 and accompanying text (introducing the "fatal flaw" of *Seaman's* as failing to base its holding on the implied covenant of good faith and fair dealing).

265. Compare *Okun*, 203 Cal. App. 3d at 824, 250 Cal. Rptr. at 232 (believing the bad faith denial of contract tort to "[fall] squarely within the realm of the covenant of good faith and fair dealing") with *Quigley*, 162 Cal. App. 3d at 890, 208 Cal. Rptr. at 401 (repeating the court's admonition in *Seaman's* that the new bad faith denial of existence of a contract tort is not predicated on breach of the implied covenant of good faith and fair dealing); see *supra* notes 117-21 and accompanying text (addressing the conflicting Court of Appeal decisions with reference to whether the *Seaman's* tort was based on breach of the implied covenant of good faith and fair dealing theory, or violation of some other independent tort theory).

266. See *DuBarry*, 231 Cal. App. 3d at 569, 282 Cal. Rptr. at 192 (declining to hold that *Seaman's* applies to bad faith defenses to contractual liability on the policy ground that imposition of tort damages in such a case would expand the litigation into an "expensive and time consuming" inquiry into the breaching party's motives, and that such an "insult to commercial predictability and certainty" would also make for an enlarged burden on an "already overworked judicial system"); see also *supra* note 261 (making Judge Kozinski's point that the courts have more pressing matters to pursue, such as criminal, constitutional, and civil rights matters, rather than "squabbles" over money). The traditional rule of breach in contract law is that the breaching party's motives or intent is irrelevant. See, e.g., *Applied Equip. Corp. v. Litton Saudi Arabia Ltd.*, 7 Cal. 4th 503, 516, 869 P.2d 454, 461, 28 Cal. Rptr. 2d 475, 482 (1994) (holding that the law generally does not distinguish between good and bad motives for breaching a contract); *Harris v. Atlantic Richfield Co.*, 14 Cal. App. 4th 70, 82, 17 Cal. Rptr. 2d 649, 656-57 (1993) (noting that the extension of tort remedies for bad faith commercial contract breaches represents a substantial departure from the traditional contract tenet of blindness to a party's motives for its breach). Just the fact that the California Supreme Court disposes of far more criminal cases than civil ones represents a greater potential for inquiry into subjective motives and intent, since intent is a crucial element of the criminal law and is often litigated in criminal cases. During the fiscal year of 1993-94, for instance, the California Supreme Court handled, by way of automatic capital appeals, habeas-related automatic capital appeals, petitions for review, or original proceedings, a total of 6366 matters: 4226 of those were criminal (66%), while only 2140 of those were civil (34%). 1995 JUDICIAL COUNCIL OF CAL. ANN. REP. ch. 6, at 45-47.

but yet not to punish it when it denies in bad faith liability under the contract.²⁶⁷ Why, for instance, is it more reprehensible for a party to deny in bad faith a contract's existence than to fabricate an excuse based upon material breach, impossibility, or impracticability, when the breaching party knows or should know that there exists no plausible grounds for its claimed excuse?

Thus, *Freeman & Mills* calms the rough waters left in the wake of *Seaman's* by restoring needed certainty and clarity to contract law. Parties can once again voluntarily adjust their commercial legal relationships through contract with assurance that they may dispute contractual liability if necessary without risking exposure to the looming threat of punitive damages. They can once again accurately gauge how much a commercial contractual venture will cost them in the event breach becomes necessary.

3. Compensation for Bad Faith in Contracting

With its decision in *Freeman & Mills*, the California Supreme Court was able to restore needed certainty and clarity to contract law without sacrificing the potential for compensation when instances of bad faith occur in contract disputes. The entire *Freeman & Mills* court specifically noted the availability of tort remedies when an independent duty arises on the part of the defendant out of tort law.²⁶⁸ Prior California decisions also show that contract plaintiffs may sue in tort, and recover tort remedies, including punitive damages, when they can prove that the defendant committed a tort incidental to the breach of the parties' contract.²⁶⁹

There also remains various exceptions to the rule by which tort remedies are available to plaintiffs arising out of intentional breach of a commercial contract.

267. *Freeman & Mills*, 11 Cal. 4th at 103, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431. Commentators agree that it was inappropriate to single out one type of bad faith breach for punitive damages treatment—bad faith denial of a contract's existence. Oxley, *supra* note 7, at 47, 78.

268. *Freeman & Mills*, 11 Cal. 4th at 102, 900 P.2d at 680, 44 Cal. Rptr. 2d at 430-31 (citing *Applied Equip.*, 7 Cal. 4th 503 at 515, 869 P.2d at 460, 28 Cal. Rptr. 2d at 481); *Freeman & Mills*, 11 Cal. 4th at 104, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431 (Kennard, J., concurring); *see id.* at 104, 900 P.2d at 680, 44 Cal. Rptr. 2d at 432 (Mosk, J., concurring and dissenting) (calling this a "tautological" proposition).

269. *See, e.g.*, *Chelini v. Nieri*, 32 Cal. 2d 480, 486-87, 196 P.2d 915, 918-19 (1948) (striking the plaintiff's punitive damages award in the trial court because he failed to plead a tort cause of action for deceit, although the facts showed that the defendant had indeed committed the tort; had the plaintiff alleged deceit, he would have been able to recover punitive damages since the breach of the contract incidentally involved the tort of deceit); *Haigler v. Donnelly*, 18 Cal. 2d 674, 680, 117 P.2d 331, 335 (1941) (affirming trial court's judgment in awarding the plaintiff punitive damages since the defendant committed the tort of conversion incidental to the breach of the parties' real estate contract); *Southern Cal. Disinfecting Co. v. Lomkin*, 183 Cal. App. 2d 431, 451, 7 Cal. Rptr. 43, 56 (1960) (permitting award of punitive damages against the defendant for fraud even though the tort incidentally involved a contract); *Foster v. Keating*, 120 Cal. App. 2d 435, 454, 261 P.2d 529, 540 (1953) (holding to the same effect).

These include, for instance, the bad faith insurance context,²⁷⁰ public utility cases,²⁷¹ fraud,²⁷² personal comfort contracts,²⁷³ and the instances in which a defendant may be held liable for misfeasance or negligent affirmative conduct in the performance of a promise, such that the actor is liable in tort and contract for physical harm to persons and things.²⁷⁴

270. See *supra* notes 19-54 and accompanying text (discussing the bad faith insurance contract cases that permitted tort remedies, namely punitive damages, for insurers' wrongful denial of benefits under the insurance policy).

271. See, e.g., *Langley v. Pacific Gas & Elec. Co.*, 41 Cal. 2d 655, 662, 262 P.2d 846, 850-51 (1953) (holding that the defendant's breach of contract to supply the plaintiff with power necessary to operate a fish hatchery sounded in both contract and tort, but that damages under either theory were the same since the defendant knew of the unique nature of loss the plaintiff would incur if the defendant breached the contract); *Thompson v. San Francisco Gas & Elec. Co.*, 18 Cal. App. 3d 34-35, 121 P. 937, 939 (1912) (finding a cause of action for civil or ordinary damages resulting from the defendant's refusal to provide the plaintiff's electrical service at his apartment, and holding that the plaintiff's claimed damages of \$540 were sufficient to withstand the defendant's general demurrer); *Fort Smith & W. Ry. Co. v. Ford*, 126 P. 745, 746 (Okla. 1912) (holding that breach of the parties' contract of carriage sounds in tort because a duty arose on the defendant's part out of the parties' contractual relations); see also *KEETON ET AL.*, *supra* note 11, § 92, at 662-63 (describing the scope of tort liability for nonperformance of contracts, or even for refusal to enter into contracts, of public officers, common carriers, innkeepers, public warehousemen, and public utilities, such liability deriving from the common law tort duty to "serve all comers . . . to common callings").

272. See *Munoz v. Kaiser Steel Corp.*, 156 Cal. App. 3d 965, 975-79, 203 Cal. Rptr. 345, 351-54 (1984) (failing to permit the plaintiff's recovery, only because the defendant raised a valid statute of frauds defense, but implicitly recognizing a cause of action for promissory fraud based on allegations of employer-defendant's promise to employ employee-plaintiff for at least three years without intent to perform the contract); see also *KEETON ET AL.*, *supra* note 11, § 92, at 664 (noting tort of deceit as exception to usual nonliability for failure to perform a contract where a promise is made without intent to perform it); cf. *Hydrotech Systems, Ltd. v. Oasis Waterpark*, 52 Cal. 3d 988, 1002, 803 P.2d 370, 379, 277 Cal. Rptr. 517, 526 (1991) (barring a plaintiff-subcontractor's tort claim against a general contractor for false promise to pay only because the plaintiff occupied the status of unlicensed contractor and a state statute expressly forbade recovery for unlicensed construction work).

273. See, e.g., *Wynn v. Monterey Club*, 111 Cal. App. 3d 789, 799-801, 168 Cal. Rptr. 878, 882-84 (1980) (permitting physical and mental suffering damages in excess of the contract's consideration for a gambling club's intentional breach of a contract with its patron, because the patron would repay the gambling indebtedness of the patron's wife incurred at the club in exchange for the club's agreement to refrain from permitting the wife to gamble further in its establishment, on the theory that the club knew that a breach of the contract would cause the patron emotional and physical suffering in the form of marital strife); *Leavy v. Cooney*, 214 Cal. App. 2d 496, 500-02, 29 Cal. Rptr. 580, 583-84 (1963) (upholding mental and emotional suffering damages against a motion picture maker for its intentional breach of contract with a public prosecutor that the movie maker could not show a film the prosecutor agreed to make voluntarily for the movie maker provided it would show or permit to be shown the film only on television and not in any commercial theatre); *Westervelt v. McCullough*, 68 Cal. App. 198, 208-09, 228 P. 734, 738 (1924) (establishing the exception by allowing physical suffering and illness damages for a defendant-homeowner's intentional breach of contract to provide the plaintiff and her family with a place to live by ousting the plaintiff on the theory that the defendant knew of the plaintiff's ill health and old age, and such damages were in contemplation of the parties when they executed the contract).

274. See, e.g., *Bily v. Arthur Young & Co.*, 3 Cal. 4th 370, 406, 834 P.2d 745, 767, 11 Cal. Rptr. 2d 51, 73 (1992) (restricting cause of action in negligence for careless audit reporting to client and auditor, the parties to the contract to audit); *Eads v. Marks*, 39 Cal. 2d 807, 810, 249 P.2d 257, 259 (1952) (recognizing that the same act may constitute both the commission of a tort and the breach of a contract, and permitting tort recovery for the defendant's negligent performance of his contractual duty to supply dairy products to the plaintiff's child); *Ross v. Forest Lawn Mem. Park*, 153 Cal. App. 3d 988, 995, 203 Cal. Rptr. 468, 473 (1984) (holding

Another compensation mechanism for bad faith in contracting may be the award of attorney's fees. Even Justice Mosk recognized in his concurring and dissenting opinion the availability of an attorney's fees award as a sanction for certain types of disfavored civil litigation tactics.²⁷⁵ The award of attorney's fees is already authorized in certain instances.²⁷⁶ Attorney's fees as sanctions are more

that the plaintiff's claim of emotional distress damages for the defendant's negligent breach of its agreement to conduct funeral services for the plaintiff's deceased daughter, by specifically making sure that none of the punk rocker former associates of the plaintiff's deceased daughter would be present at the burial services or would desecrate her daughter's gravesite, which the defendant failed to fulfill, was properly compensable as a result of the breach of contract); *Windeler v. Scheers Jewelers*, 8 Cal. App. 3d 844, 851-52, 88 Cal. Rptr. 39, 44 (1970) (permitting the plaintiff's mental suffering damages for the defendant's breach of contract to repair rings of sentimental value, by losing the rings, on the theory that the defendant knew of the likely special circumstance of emotional or mental suffering on the plaintiff's behalf if the defendant breached the contract); *see also* KEETON ET AL., *supra* note 11, § 92, at 656-57 (stating the proposition and citing examples such as a doctor's tort liability to the patient contracting for medical care when the doctor is negligent in treatment, diagnosis, or the rendering of services without reasonable skill and care).

275. *Freeman & Mills*, 11 Cal. 4th at 115, 117, 900 P.2d at 688, 689, 44 Cal. Rptr. 2d at 439, 440 (Mosk, J., concurring and dissenting). Justice Mosk refers to California Code of Civil Procedure § 128.5(a), which permits an award of attorney's fees against a party to civil litigation who asserts a bad faith defense by acting frivolously or causing unnecessary delay. *See* CAL. CIV. PROC. CODE § 128.5(a) (West Supp. 1996) (permitting attorney's fees as a sanction to remedy bad faith denial of a contract's existence); *see also* Oxley, *supra* note 7, at 77 (noting that California Code of Civil Procedure § 2033(a) allows attorney's fees as a discovery sanction for denial of a contract's existence after an appropriately-worded request for admission).

276. California statutes provide in many instances for the recovery of attorney's fees. *See generally* CAL. CIV. PROC. CODE § 128.5 (West Supp. 1996) (attorney's fees, or where requisite aggravating circumstances are present, punitive damages, for frivolous action, bad faith, or delay); *id.* § 386.6 (West Supp. 1996) (interpleader); *id.* § 396 (West Supp. 1996) (change of venue); *id.* § 411.35 (West Supp. 1996) (failure to supply statutorily-required certificate of statement of merit of actions for professional negligence against architects, engineers, and land surveyors); *id.* § 411.36 (West Supp. 1996) (same for actions of occupational negligence by common interest development association against contractor); *id.* § 527.6(i) (West Supp. 1996) (injunctions to prevent harassment); *id.* § 527.7(c) (West Supp. 1996) (action to enjoin concerted acts of violence); *id.* § 580(c) (West Supp. 1996) (mortgagor or trustor liability); *id.* § 585.5(e) (West Supp. 1996) (default judgment upon failure to answer); *id.* § 697.410(d) (West 1987) (release of erroneous judgment lien on real property); *id.* § 697.660(d) (West 1987) (same for personal property); *id.* § 724.260 (West Supp. 1996) (acknowledgment of satisfaction of matured installments under installment judgment); *id.* § 1021.1 (West Supp. 1996) (meritless rejection of settlement offer under § 998 of the Civil Procedure Code); *id.* §§ 1021.4-1021.7 (West Supp. 1996) (damage actions based on commission of felony offense, cases resulting in public benefit, claim for implied indemnity, and actions against peace officers in bad faith and without reasonable cause); *id.* § 1021.9 (West Supp. 1996) (trespass actions); *id.* § 1028.5 (West Supp. 1996) (action between small business and regulatory agency); *id.* § 1029.8(a) (West Supp. 1996) (personal injury action against unlicensed person); *id.* § 1031 (West Supp. 1996) (action for recovery of wages for labor performed); *id.* § 1036 (West Supp. 1996) (costs in inverse condemnation proceedings); *id.* § 1038(b) (West Supp. 1996) (defense costs on granting of summary judgment or nonsuit); *id.* § 1987.2 (West 1983) (expenses in making or opposing order to quash, modify, or limit subpoena); *id.* § 2023(a)(9) (West Supp. 1996) (sanctions for discovery misuse); *id.* § 2033(o) (West Supp. 1996) (failure to respond properly to a request for admission); *id.* § 2034(k) (West Supp. 1996) (unsuccessful motion to augment or amend, or unsuccessful opposition to motion to augment or amend, expert witness information). However, the default rule, the so-called "American Rule," is that attorney's fees are generally not recoverable unless provided for by statute or the parties' agreement. *Id.* § 1021 (West Supp. 1996). There are numerous exceptions developed by the cases. *See, e.g.*, *Prentice v. North Am. Title Guar. Corp.*, 59 Cal. 2d 618, 620, 381 P.2d 645, 647, 30 Cal. Rptr. 821, 823 (1963) (holding that "[a] person[,] who through the tort of another has been required to act in the protection of his

palatable than punitive damages since attorney's fees are not subject to tremendous discretion in their appraisal, as are punitive damages.²⁷⁷ Established factors guide courts and juries in determining an amount to award as attorney's fees.²⁷⁸ In *Freeman & Mills*, for instance, the court upheld the plaintiff's attorney's fees award for the litigation tactics of the defendant's counsel.²⁷⁹ *Freeman & Mills* is a good example then of other current mechanisms of compensation designed to punish a contracting party's bad faith litigation conduct.

interests by bringing or defending an action against a third person[,] is entitled to recover compensation for the reasonably necessary loss of time, attorney's fees, and other expenditures thereby suffered or incurred"); *Nelson v. Kellogg*, 162 Cal. 621, 623, 123 P. 1115, 1118 (1912) (awarding attorney's fees for false arrest or imprisonment); *Estate of Legeas*, 208 Cal. App. 3d 1516, 1526, 256 Cal. Rptr. 117, 123 (1989) (allowing attorney's fees in a probate proceeding involving fraudulent destruction of a will); *Glendale Fed. Sav. and Loan Ass'n v. Marina View Heights Dev., Inc.*, 66 Cal. App. 3d 101, 149-50, 135 Cal. Rptr. 802, 831 (1977) (holding award of attorney's fees proper in a fraud action that required resisting a bankruptcy petition that formed an aspect of the fraudulent scheme).

277. See *supra* note 13 and accompanying text (discussing the problem of jury discretion in assessing punitive damages).

278. See, e.g., *City of L.A. v. Los Angeles-Inyo Farms Co.*, 134 Cal. App. 268, 276, 25 P.2d 224, 227-28 (1933) (holding that in deciding what represents reasonable compensation for an attorney rendering services with reference to a legal proceeding, the following factors should be considered: (1) The nature of the litigation; (2) the litigation's level of difficulty; (3) the skill required to handle the litigation; (4) the skill actually rendered to handle the litigation; (5) the attention given the matter by the attorney; (6) the success or failure of the attorney's efforts; and (7) the attorney's skill and learning, including his age and experience in the particular field of law to which the litigation belongs); CAL. RULES OF PROFESSIONAL CONDUCT Rule 4-200(B) (1989) (promulgating the following factors to be considered in determining whether attorney's fees are excessive to the point of unconscionability: (1) The fee amount in proportion to the value of the services rendered; (2) the level of sophistication of both the attorney and the client; (3) the novelty and the difficulty of the issues involved in the matter, and the level of skill required to perform the legal services adequately; (4) the likelihood, if apparent to the client, that acceptance of the client's case by the attorney would preclude the attorney from handling other matters; (5) the amount of litigation involved and its results obtained by the attorney; (6) time limitations imposed by either the client or the circumstances; (7) the nature and length of the professional relationship between the attorney and client; (8) the experience, reputation, and ability of the attorney performing the services; (9) whether the attorney's fee is fixed or contingent; (10) the time and labor required of the attorney; and (11) whether the client gave informed consent to the attorney's fees).

279. *Freeman & Mills*, 11 Cal. 4th at 89, 900 P.2d at 671, 44 Cal. Rptr. 2d at 422. The trial court awarded *Freeman & Mills* \$212,891 in attorney's fees. *Id.* at 117, 900 P.2d at 689, 44 Cal. Rptr. 2d at 440 (Mosk, J., concurring and dissenting); see CAL. CIV. PROC. CODE § 128.5(a) (West Supp. 1996) (permitting a trial court to award attorney's fees as sanctions for bad faith conduct or tactics that are frivolous or intended solely to cause unnecessary delay); *id.* § 2033(o) (West Supp. 1996) (authorizing the award of reasonable expenses, including reasonable attorney's fees, for failing to make an admission after the adverse party proves the truth of the admission).

4. Legislative Versus Judicial Action

Another legal principle underlying the California Supreme Court's opinion in *Freeman & Mills* is judicial restraint.²⁸⁰ As Chief Justice Lucas noted in *Freeman & Mills*, the high court prefers legislative rather than judicial action when it comes to expanding tort liability.²⁸¹ Decisions of courts addressing the propriety of expanding tort remedies for breach of the implied covenant of good faith and fair dealing have also expressed the Chief Justice's sentiments on this point.²⁸²

Although this Casenote has argued that punitive damages should be unavailable as a remedy for the denial of an ordinary commercial contract's existence, the legislature can review the subject as it sees fit. If the state legislature finds, after a thorough evaluation of the subject, that plaintiffs are undercompensated for defendants' intentional or bad faith denial of contractual existence, it could always enact a statute that permits tort recovery in situations it deems appropriate.²⁸³ Legislative action was effective, for example, during the

280. The legal dictionary defines "judicial self-restraint" as the "[s]elf-imposed discipline by judges in deciding cases without permitting themselves to indulge in their own personal views or ideas which may be inconsistent with existing decisional or statutory law." BLACK'S LAW DICTIONARY 849 (6th ed. 1990). Conversely, the dictionary defines "judicial activism" as the "judicial philosophy which motivates judges to depart from strict adherence to judicial precedent in favor of progressive and new social policies which are not always consistent with the restraint expected of appellate judges. It is commonly marked by decisions calling for social engineering and occasionally these decisions represent intrusions into legislative and executive matters." *Id.* at 847. The judicial restraint versus judicial activism debate is an old one, and there are obviously valid strengths and criticisms of both doctrines. In any event, the merits of the debate are beyond the scope of this Casenote and have been fully treated elsewhere. See generally Mark V. Tushnet, *The Role of the Supreme Court: Judicial Activism or Self-Restraint?*, 47 MD. L. REV. 147 (1987) (exploring thoroughly the meanings of judicial activism and restraint and discussing their respective merits, consequences, and significance).

281. *Freeman & Mills*, 11 Cal. 4th at 102, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431 (stressing the preference for legislative rather than judicial action as a factor favoring abrogation of *Seaman's*); cf. *Harris v. Capital Growth Investors XIV*, 52 Cal. 3d, 1142, 1168 & n.15, 805 P.2d 873, 888 & n.15, 278 Cal. Rptr. 614, 629 & n.15 (stating that "[i]n the absence of clear legislative direction . . . we are unwilling to engage in complex economic regulation under the guise of judicial decision-making").

282. See, e.g., *Tameny v. Atlantic Richfield Co.*, 27 Cal. 3d 167, 179-83, 610 P.2d 1330, 1337-39, 164 Cal. Rptr. 839, 846-48 (1980) (Clark, J., dissenting) (admonishing the majority for usurping the legislature's responsibility to determine when employees should be allowed to proceed in tort against their employers for wrongful termination of the employment contract); *Harris v. Atlantic Richfield Co.*, 14 Cal. App. 4th 70, 82, 17 Cal. Rptr. 2d 649, 656-57 (1993) (declining to extend tort remedies for breach of contract in violation of public policy outside of the employment contract context on policy grounds that where important policy principles involving commercial contractual relationships are implicated, the legislature is better suited to address the appropriate relief in such instances). Even the *Seaman's* court expressed caution against activism in extending tort remedies for bad faith commercial contractual conduct: "[This] is not to say that tort remedies have no place in such a commercial context, but . . . it is wise to proceed with caution in determining their scope and application." *Seaman's Direct Buying Serv. v. Standard Oil Co.*, 36 Cal. 3d 752, 769, 686 P.2d 1158, 1167, 206 Cal. Rptr. 354, 363 (1984).

283. Of course, Chief Justice Lucas noted in *Freeman & Mills* that thus far, the state legislature has not expressed an interest in expanding tort remedies in the context of breach of commercial contracts. *Freeman & Mills*, 11 Cal. 4th at 103, 900 P.2d at 680, 44 Cal. Rptr. 2d at 431.

medical malpractice insurance crisis in 1975 as a response to the effects of costly and expansive litigation of medical malpractice claims.²⁸⁴ In the court's view, however, the matter of determining the availability and scope of punitive damages remedies for bad faith denial of contract is better left to the legislature rather than the courts.

B. *Economic Ramifications*

Economically efficient breaches of contract, which are often intentional and in bad faith, are recognized as "a judicially accepted staple of our system of commercial law."²⁸⁵ The Restatement of Contracts, Second, seems to approve of the "efficient breach" of contract theory,²⁸⁶ which owes much of its acceptance in the legal community to Judge Richard Posner and his influential economic analysis of the law.²⁸⁷

Parties, especially in commercial settings such as that in which *Seaman's* and its progeny made punitive damages available, voluntarily enter into contracts for economically beneficial reasons, mostly to maximize their allocation of resources.²⁸⁸ For this reason, the law has generally recognized the validity of the

284. See Ann-Marie Davidow, Note, *Borrowing Foley v. Interactive Data Corp. to Finance Lender Liability Claims*, 41 HASTINGS L.J. 1383, 1413-14 (1990) (suggesting that a legislative response similar to that of the California Legislature's enactment of Civil Code § 3333.2 in 1975, which capped noneconomic damages in medical malpractice suits to \$250,000 in response to then-skyrocketing malpractice premium insurance costs, would be an appropriate answer to the increased number of lender liability suits for tortious breach in recent years).

285. Thomas A. Diamond, *The Tort of Bad Faith Breach of Contract: When, If At All, Should It Be Extended Beyond Insurance Transactions?*, 64 MARQ. L. REV. 425, 433 (1981). Professor Diamond defined bad faith in this context as any intentional breach motivated by crass economic self-interest. *Id.*

286. See RESTATEMENT (SECOND) OF CONTRACTS ch. 16 introductory note at 100 (1979) (recognizing that the law of contracts has generally not distinguished between willful and non-willful breaches of contract, and noting that a contracting party may find it "advantageous" to breach the contract if the breaching party will still retain an overall net gain of resources after compensation of the injured party for its loss).

287. Judge Posner, in turn, acknowledges two early 1960s articles as the first modern attempts to apply economic theories in law. RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 21-22 (4th ed. 1992) (citing Guido Calabresi, *Some Thoughts on Risk Distribution and the Law of Torts*, 70 YALE L.J. 499 (1961); Ronald H. Coase, *The Problem of Social Cost*, 3 J.L. & ECON. 1 (1960)). Of course, some disagree with Judge Posner and do not accept wholeheartedly the efficient breach of contract theory. See, e.g., Daniel L. Farber, *Reassessing the Economic Efficiency of Compensatory Damages for Breach of Contract*, 66 VA. L. REV. 1443 (1980) (finding that the efficient breach theory overlooks the costs of recovering damages for breach of contract (transaction costs, such as attorney's fees and filing fees, etc.) and that it also compensates inadequately the nonbreaching party for its subjective and idiosyncratic values in performance of the contract); Ian R. Macneil, *Efficient Breach of Contract: Circles in the Sky*, 68 VA. L. REV. 947 (1982) (arguing that the Posner model relies on unrealistic price differentials and that it fails to take into account nonrecoverable expenses that should be part of the equation, like attorney's fees and other costs of litigation, many of which are intangible and thus incapable of economic classification, such as lost confidence in business dealings).

288. See I FARNSWORTH, *supra* note 10, § 1.2, at 8 (reporting that parties voluntarily arrive at bilateral exchanges through the process of bargaining, each party ultimately hoping to "maximize its own economic advantage on terms tolerable to the other party"); POSNER, *supra* note 287, at 91 (stating that the fundamental role of contract is to deter parties from acting opportunistically toward one another to facilitate the optimal

“efficient breach” theory of contract damages.²⁸⁹ That theory holds that the law should encourage intentional breach of contracts when the promisor fully compensates the promisee by awarding as damages an amount equal to that which the promisee would have received had the promisor fully performed the contract.²⁹⁰ The promisor is better off because that party shifts its resources to a more valuable use, despite compensating the promisee for expectation damages.²⁹¹ Economists recognize that society benefits from this efficient redistribution of the resources of all involved parties.

Remedies for contractual breach in the form of punitive damages discourage and deter this efficient reallocation of society’s resources.²⁹² When fashioning damages for breach of contract, the law must be careful to avoid the waste of resources.²⁹³ Professor Farnsworth notes further that compelling performance in the event of an inefficient breach distributes wealth improperly, “since the party in breach would lose more than the injured party would gain.”²⁹⁴ That is, the nonbreaching party will receive performance under the contract; thus, the nonbreaching party finds itself in at least as good a position as that in which it found itself before the contract, while the breaching party will have lost the opportunity to enter into a more profitable enterprise by performing the immediate contract. Therefore, the breaching party finds itself in a less favorable position than that in which it found itself prior to the contract.

timing of economic activity and to lessen costly measures of self-protection); John H. Barton, *The Economic Basis of Damages for Breach of Contract*, 1 J. LEGAL STUD. 277, 278 (1972) (asserting that each party contracts hoping that the party guesses the market more accurately than the other, or, if the parties differ in their willingness to bear risk, that the party’s judgment concerning the agreed-upon price relieves it of the risk in purchasing at the market price).

289. See Diamond, *supra* note 285, at 433 (highlighting that this idea is one of the most poorly kept secrets in legal history); see also *Freeman & Mills*, 11 Cal. 4th at 106, 900 P.2d at 682, 44 Cal. Rptr. 2d at 433 (Mosk, J., concurring and dissenting) (stating that the intentional breach of contract is viewed as a morally neutral act, and “the economic insight that an intentional breach of contract may create a net benefit to society” by permitting the optimal movement of resources supports this theory); RESTATEMENT (SECOND) OF CONTRACTS ch. 16 introductory note at 100 (1979) (recognizing that the law of contracts has generally not distinguished between willful and non-willful breaches of contract, and noting that a contracting party may find it “advantageous” to breach the contract if the breaching party will still retain an overall net gain of resources after compensation of the injured party for its loss); 3 FARNSWORTH, *supra* note 10, § 12.3, at 155 (noting that the efficient breach notion “accords remarkably with the traditional assumptions of the law of contract remedies”).

290. This is, of course, protection of the nonbreaching party’s expectation interest, and is the traditional measure of damages for breach of a contract. See *supra* note 246 and accompanying text (describing expectation damages).

291. PETER LINZER, A CONTRACTS ANTHOLOGY 419-20 (1989); POSNER, *supra* note 287, at 119-20.

292. See 3 FARNSWORTH, *supra* note 10, § 12.3, at 155-56 (advocating that punitive damages should not be an available remedy for breach of contract because the breaching party is encouraged to perform rather than breach, and breach is more socially desirable).

293. See POSNER, *supra* note 287, at 118-19 (stressing that remedies which induce performance after breach often waste resources, such as either unused production or unnecessary time).

294. 3 FARNSWORTH, *supra* note 10, § 12.3, at 155.

Furthermore, fearing the potentially uncontrollable size of jury verdicts for punitive damages,²⁹⁵ allowance of punitive remedies in ordinary commercial contractual settings would most likely have the undesirable effect of deterring parties from entering into commercial contracts. In the context of preliminary negotiations, reasonable minds can differ concerning whether a contract exists and at what point it exists, regardless of any one party's legitimate opposition to the terms or parts of a contract. Having the bad faith denial of contract tort in mind with its potentially devastating punitive remedies,²⁹⁶ commercial parties would

295. Judge Dozier noted this phenomenon in an appendix to the court's decision in *Woolstrum v. Mailloux*, 141 Cal. App. 3d Supp. 1, 190 Cal. Rptr. 729 (1983). In reversing a jury's imposition of punitive damages, the *Woolstrum* court held that the defendant-farmer's negligent maintenance of his fence, by which his cow escaped and hit plaintiff-motorist's car on the highway, and the inferences drawn from these facts, could not amount to the requisite threshold for imposition of punitive damages: "(1) conscious disregard by defendant of (2) a known, and (3) probable likelihood of injury to others." *Woolstrum*, 141 Cal. App. 3d Supp. at 7, 190 Cal. Rptr. at 733. Among the factors militating against availability of punitive damages in negligence cases, Judge Dozier listed the following: (1) "Places before the jury inflammatory evidence affecting their dispassionate judgment as to negligence . . . and compensatory damages;" (2) "[p]laces a social policy decision in the hands of [a] jury without giving them access to the huge and broad array of facts necessary to reach an intelligent and useful decision;" (3) "[j]ury punitive damage awards of an unpredictable nature and appalling inconsistency continue to proliferate[—n]either the Legislature nor the appellate courts have been able to formulate coherent, reasonable guidelines and limitations for the remedy . . . [; i]n practice, it lacks any semblance of consistency between defendants, or even the same defendant, in cases tried by different juries . . .;" and (4) "[t]he extreme unpredictability of punitive damages and the occasional crushing amount set by a vindictive jury approaches a due process violation because, . . . the defendant lacks notice of the extent his conduct may result in loss of his entire assets." *Id.* at 12, 190 Cal. Rptr. at 736-37. Judge Dozier's list of factors for and against the propriety of punitive damages awards is pertinent because the court stated that "[f]or the convenience of future judicial reflection on the wisdom of punitive damages in negligence cases, we gather the asserted 19 demerits (and three merits) of the policy from the American judicial and law review literature." *Id.* at 9 n.3, 190 Cal. Rptr. at 734 n.3; see *supra*, note 13 (discussing the inherent uncertainties in the imposition and sizes of punitive damages awards, and noting the recent Supreme Court decision designed to assist courts in controlling the inexplicable nature of punitive damages awards). Under the economic analysis of contract law, it seems reasonable to think that punitive damages should be even less available for bad faith denial of contract than for negligence. For one view to the contrary, though, see Barry Perlstein, *Crossing the Contract-Tort Boundary: An Economic Argument for the Imposition of Extracompensatory Damages for Opportunistic Breach of Contract*, 58 BROOK. L. REV. 877 (1992) (suggesting that economic analysis of law supports extension of tort damages for "opportunistic" breach of contract, the critical inquiry being whether the breach is "opportunistic," as that term is defined by economists).

296. For instance, the *Pennzoil* court acknowledged in dicta that the jury's huge compensatory damages verdict alone, notwithstanding the punitive damages award, could have an adverse economic effect on other states and industries as well as on Texaco's financial situation. *Pennzoil Co. v. Texaco, Inc.*, 729 S.W.2d 768, 865 (Tex. Ct. App. 1987). One commentator subsequently reported that while Texaco filed bankruptcy in 1987, and its stock fell 28% to \$27 per share, two years later, after a completed settlement with Pennzoil, Texaco's stock rose to \$60 per share, an all-time high. Robert Elder, Jr., *Ten Who Made A Difference*, TEX. LAW., Apr. 3, 1995, at 1. Other businesses hit with large punitive damages awards, however, have not fared so well. See DEBORAH R. HENSLER ET AL., THE INSTITUTE FOR CIVIL JUSTICE, ASBESTOS IN THE COURTS 22 (1985) (reporting that the "most dramatic" actions that the asbestos defendants and their insurers took, as a direct result of the mounting financial impact presented by the increasing number of plaintiffs' victories, consisted of six of the major asbestos producers filing for bankruptcy protection, thus to thwart, or at least mitigate, plaintiffs' recovery of punitive damages).

probably be less likely to enter into preliminary negotiations for business deals.²⁹⁷ The law of contracts is intertwined with the dynamics of a free enterprise economy, so courts must be careful to alter provision of contractual remedies that may hamper the inherent functioning of the market.²⁹⁸ Entrepreneurs rely on advance assessments about the risk of their contractual enterprises pursuant to contract law's expectation interest remedy, which permits business to foresee the costs that a contract, or its breach, will entail.²⁹⁹ It follows that commercial parties are less likely to engage in contracting if they are unable to assess accurately the costs associated with the prospective contract, which the punitive damages remedy undoubtedly undermines since the amount of a punitive damages award is far from foreseeable.

In this sense, allowing recovery of punitive damages in ordinary commercial contractual settings has a chilling effect on the economy. The *Freeman & Mills* court served the best interests of the economy in eliminating the *Seaman's* tort.

V. CONCLUSION

Consistent with the California Supreme Court's jurisprudence limiting tort liability in recent years, much to the credit of Chief Justice Malcolm Lucas,³⁰⁰ the *Seaman's* tort of bad faith denial of existence of a contract is now dead in California. This Casenote has shown how the *Freeman & Mills* decision serves important legal and economic goals. Among them are clarification of the law concerning remedies for bad faith contract breach and promotion of the economy through restoration of predictability and certainty in contract damages. Justice Holmes would have been pleased.³⁰¹ So would the author who once asked if the *Seaman's* tort is dead.³⁰²

297. Sebert, *supra* note 168, at 1642 ("[*Seaman's*] may even discourage parties from entering into contractual arrangements that are incomplete or preliminary, such as the *Seaman's* arrangement, because the decision enhances the risk that a defendant will be subject to punitive damages for failing to perform such a contract").

298. See CHARLES T. MCCORMICK, HANDBOOK ON THE LAW OF DAMAGES § 138, at 567 (1935) (viewing the foreseeability limitation on damages for breach of contract as an expression of the law's desire to diminish the risks associated with business enterprise, which harmonizes well with the free trade economic philosophy underlying the law of contracts).

299. See Edwin W. Patterson, *The Apportionment of Business Risks Through Legal Devices*, 24 COLUM. L. REV. 335, 342 (1924) (discussing expectation damages for breach of contract and their foreseeability limitation, and noting that the policy underlying this traditional rule of damages for contract breach is that the law seeks to reduce the risk that entrepreneurs take in making contracts).

300. See *Tribute*, *supra* note 9, at 1395-97; see also *Peterson v. Superior Court*, 10 Cal. 4th 1185, 899 P.2d 905, 43 Cal. Rptr. 2d 836 (1995) (overturning *Becker v. IRM Corp.*, 38 Cal. 3d 454, 698 P.2d 116, 213 Cal. Rptr. 213 (1985), the seminal decision that extended strict products liability, for latent defects in the premises at the time they are let to the tenant, to landlords engaged in the business of leasing dwellings).

301. See *supra* note 1 and accompanying text (relating Justice Holmes's view of the scope of common law damages for breach of contract).

302. Landsdorf, *supra* note *, at 213.