AUTONOMY AND ACCOUNTABILITY IN THE LAW OF CONTRACTS: A RESPONSE TO PROFESSOR SHIFFRIN

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I. INTRODUCTION

Professor Seana Valentine Shiffrin's recent influential article in the *Harvard Law Review*, *The Divergence of Contract and Promise*,[1] has generated a lively discussion in six full-length articles[2] and continues to be frequently cited by other commentators[3] and the courts.[4] Notwithstanding

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1. Seana Valentine Shiffrin, *The Divergence of Contract and Promise*, 120 HARV. L. REV. 708 (2007). Professor Shiffrin is Professor of Philosophy and Law, University of California, Los Angeles.

2. *See* Barbara H. Fried, *What's Morality Got to Do with It?*, 120 HARV. L. REV. FORUM 53, 53 (2007) (calling Professor Shiffrin's article "exacting and provocative"); Charles Fried, *The Convergence of Contract and Promise*, 120 HARV. L. REV. FORUM 1, 1 (2007) (finding Professor Shiffrin's article to be "lucid and closely reasoned"); Jody S. Kraus, *The Correspondence of Contract and Promise*, 109 COLUM. L. REV. 1603 (2009); Jeffrey M. Lipshaw, *Objectivity and Subjectivity in Contract Law: A Copernican Response to Professor Shiffrin*, 21 CAN. J.L. & JURISPRUDENCE 399, 399 (2008) (noting that Shriffrin's article is "undoubtedly an important contribution"); Liam Murphy, *Contract and Promise*, 120 HARV. L. REV. FORUM 10, 11–12, 18 (2006) (finding that Professor Shiffrin's "argument is subtle and complex," "original and important," and "a significant impact on legal theory in general"); Michael G. Pratt, *Contract: Not Promise*, 35 FLA. ST. U. L. REV. 801, 802 (2008) (calling Professor Shiffrin's article "one of the most important recent contributions to contract theory [in] an elegantly wrought paper").

3. *See* HOWARD O. HUNTER, MODERN LAW OF CONTRACTS § 1:3 (2009); 1

the prominence of Professor Shiffrin's article, however, I respectfully suggest it has some fundamental flaws that have not been addressed in the existing commentaries. I will summarize Professor Shiffrin's thesis, identify my concerns, and propose an alternative formulation.

Professor Shiffrin's central argument is that contract law undercuts the moral requirement that breach should be impermissible, as opposed to being merely subject to a price through damages.[5] Citing Oliver Wendell Holmes, Professor Shiffrin argues that breach of contract is "not a legal wrong" because the law has reinterpreted every contract as an agreement in the alternative—to perform or to pay an amount of money equal to the value of performance.[6] Thus, "contract diverges from promise" in that the "contents of the legal obligations and the legal significance of their breach do not correspond to the moral obligations and the moral significance of their breach."[7]

In supporting her argument, Professor Shiffrin criticizes at length the law's treatment of morality and breach. Contract law, she says, will neither

B.E. WITKIN, SUMMARY OF CALIFORNIA LAW § 10 (2005 & Supp. 2008) (finding that Professor Shiffrin's article represents an "innovation in theory and doctrine"); *see also* Shyamkrishna Balganesh, *Demystifying the Right to Exclude: Of Property, Inviolability, and Automatic Injunctions*, 31 HARV. J. L. & PUB. POL'Y 593, 631 n.130 (2008); Curtis Bridgeman, *Contracts as Plans*, U. ILL. L. REV. 341, 357 (2009); Curtis Bridgeman, *Why Contracts Scholars Should Read Legal Philosophy: Positivism, Formalism, and the Specification of Rules in Contract Law*, 29 CARDOZO L. REV. 1443, 1462 n.116 (2008) (calling Professor Shiffrin's article "particularly thoughtful"); George S. Geis, *Automating Contract Law*, 83 N.Y.U. L. REV. 450, 485 n.143 (2008); Robin Bradley Kar, *Contract Law and the Second-Person Standpoint: Why Efficiency-Maximization Principles Can Neither Explain Nor Justify the Expectation Damages Remedy*, 40 LOY. L.A. L. REV. 977, 983 n.18 (2007) (finding Professor Shiffrin's article an "illuminating discussion of the many distinctions between contract law and the ordinary morality of promise-keeping"); Gregory Klass, *Contracting for Cooperation in Recovery*, 117 YALE L.J. 2, 7 n.10 (2007); Gregory Klass, *Three Pictures of Contract: Duty, Power and Compound Rule*, 83 N.Y.U. L. REV. 1726, 1781 (2008); Ethan J. Leib, *Friends as Fiduciaries*, 86 WASH. U. L. REV. 665, 692, n.118 (2009).

4. Ortiz v. Lyon Mgmt. Group, Inc., 69 Cal. Rptr. 3d 66, 75 n.11 (Cal. Ct. App. 2007).

5. *See* Shiffrin, *supra* note 1, at 709, 722, 724. Professor Shiffrin properly equates "moral concepts" with notions of fairness and reasonableness. *Id.* at 710 n.1. *See also* Seana Shiffrin, *Could a Breach of Contract Be Immoral?*, 107 MICH. L. REV. 1551, 1551 n.2 (2009) (referencing morality as "those nonlegal, objectively grounded normative principles that regulate our motives, reasons, and conduct (and perhaps our attitudes)").

6. *See* Shiffrin, *supra* note 1, at 710, 727–28, 737.

7. *Id.* at 709.

"place pressure on the promisor to behave morally" nor "directly proscribe moral behavior by promisors."[8] Concentrating on intentional breach,[9] Professor Shiffrin claims: (1) the law "reflects an underlying view that promissory breach is not a wrong, or at least not a serious one," (2) the law, unlike morality, does not offer "proportionate expressions" of reproach to contract breakers, and (3) "[c]ontract law's stance on the wrongfulness of promissory breach is equivocal at best, manifested most clearly by its general prohibition of punitive damages."[10] Professor Shiffrin also accepts the legal validity of the "efficient breach" doctrine.[11] This doctrine holds that breaches of contract which are efficient and wealth-enhancing should be encouraged when the promisor will still profit after compensating the other party for its expectation interest.[12] Professor Shiffrin does not, however, analyze the role of morality under the implied covenant of good faith and fair dealing.

Professor Shiffrin further addresses the law's perspective on morality and the key topics within her chief legal subject: contract remedies.[13] She asserts that contract law diverges from morality by favoring damages over specific performance.[14] She says the principle in *Hadley v. Baxendale* on consequential damages departs from morality by determining foreseeability of damages from the time of contract formation, rather than the time of breach.[15] Professor Shiffrin criticizes the rule on mitigation of damages because she says it inappropriately "places the burden on the promisee to make positive efforts to find alternative providers" instead of placing that burden on the breaching promisor.[16] In Professor Shiffrin's view, promise inappropriately diverges from contract in all these respects

8. *Id.* at 729–30.

9. "Contract breaches are in some sense always intentional . . . ." Ennen v. Pub. Serv. Mut. Ins. Co., 774 F.2d 321, 326 (8th Cir. 1985). Nevertheless, both Professor Shiffrin's article and this Article concentrate on willful and opportunistic breaches, as opposed to non-willful, inadvertent, or well-intended breaches.

10. Shiffrin, *supra* note 1, at 710, 724.

11. *Id.* at 731.

12. *See id.* at 730–33. *See also* Thyssen, Inc. v. S.S. Fortune Star, 777 F.2d 57, 63 (2d Cir. 1985) (defining the efficient breach doctrine).

13. Shiffrin, *supra* note 1, at 719 ("Chiefly, I examine the treatment of remedies in contract and promise . . . .").

14. *Id.* at 722–23.

15. *Id.* at 724 (citing Hadley v. Baxendale, 156 Eng. Rep. 145 (Exch. 1854)) (arguing additionally that "a case could be made that the promisor should be liable for all consequential damages").

16. *Id.* at 710, 724–26.

by expecting "less of the promisor and more of the promisee"[17] and by tending to "make it harder for the morally decent person to behave decently."[18]

Apart from scattered references to the *Restatement (Second) of Contracts*, the Uniform Commercial Code (UCC), and a very few cases, Professor Shiffrin focuses almost exclusively on philosophical issues and sources.[19] Even though her thesis strongly contends that contract law undermines moral requirements, she does not analyze in any depth whether the asserted divergence of contract and promise actually exists in statutory and case law. When Professor Shiffrin does perform a legal analysis of the relationship between contract and promise, it is incorrect or incomplete on important issues. In contrast, I will perform that crucial legal analysis, and I will establish that contract does not diverge from promise in the sense Professor Shiffrin has argued.[20]

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17. *Id.* at 710, 719, 738 n.58 (discussing the law's asserted "current promisor-favoring approach").

18. *Id.* at 710.

19. Professor Shiffrin notes two philosophical views of contract and morality. First, the reflective position holds that "[i]f contract law's business is to enforce promises, its structure, as a whole, should reflect the moral structure of promises." *Id.* at 710, 713. Second, the separatist position holds that "the law, especially private law, should not directly enforce morality . . . because promise and contract occupy different realms with independent purposes." *Id.* at 711, 713. She proposes an intermediate "accommodationist approach" between these positions, in which the law is to be made compatible with the conditions for moral agency to flourish but does not enforce morality as such. *Id.* at 713–14. This Article will demonstrate that the relevant statutes and case law greatly tend toward the reflective position.

In a follow-up to and confirmation of her *Harvard Law Review* article, Professor Shiffrin has contributed a paper to the June, 2009 issue of the *Michigan Law Review*, which contained a symposium on the role of fault in contract law. *See* Shiffrin, *supra* note 5, at 1551. Her methodology in the 2009 article is the same as in the 2007 article—an extensive discussion of philosophical issues and very limited analysis of the primary legal materials. *See generally id.*

20. A handful of authors have analyzed the role of morality in the law of contract remedies, but none examines the relevant statutes and case law in the systematic way presented in this Article. Professor Patricia H. Marschall advocates greater recognition of the important role of willfulness in selecting remedies for breach of contract but limits her case law commentary to contracts by building, grading, and mining contractors. *See generally* Patricia H. Marschall, *Willfulness: A Crucial Factor in Choosing Remedies for Breach of Contract*, 24 ARIZ. L. REV. 733 (1982). She does not discuss several of the important subjects in this Article, such as foreseeability under *Hadley v. Baxendale* and the mitigation of damages. *See id.* Professor George Cohen examines the role of fault in contract damages and examines a limited number of cases, primarily through the lens of economic theory. *See generally* George M. Cohen, *The*

Part II of this Article will cover the legality and morality of intentional breach. This Part will document the long common law tradition expressing moral and legal disapproval of intentional breach of contract, as supplemented by the more modern doctrine of promissory estoppel. This Part will further show how the minority judicial position—denying the moral basis of contract—has inherent contradictions. Part III will address the implied covenant of good faith and fair dealing, which is the most powerful tool courts use to voice their moral and legal disapproval of intentional breach of promise. Part IV will consider Oliver Wendell Holmes's "pay or perform" theory of contract and will further demonstrate that it is usually quoted out of context and contrary to Holmes's later clarification of its effect. Part V will analyze the efficient breach doctrine, which is the minority position in the United States and does not detract from the moral basis of contract obligations from the standpoint of general doctrine. Part VI will cover judicial attitudes toward specific performance versus expectation damages and will demonstrate the increasing importance of specific performance as a form of equitable relief. Part VII considers contractual punitive damages and will contrast the traditional view with the modern view that favors using this relief to punish the faithless promisor or to deter the abuse of economic power. Part VIII covers foreseeability and consequential damages under *Hadley v. Baxendale* and will demonstrate how *Hadley* achieves moral goals along with its qualifications and savings doctrines. Lastly, Part IX analyzes the mitigation of damages and how the law favors the superior moral position of the promisee as the injured party over the promisor as the wrongdoer.

In covering all these subjects, I will further address two fundamental questions of contract law: Is intentional breach of contract morally and legally permissible? Does the structure of contract law reflect the moral structure of promises? I will add to the discussion in the literature by specifically showing with respect to each topic how the law enforces moral norms regarding intentional breach in two complementary ways: first, by respecting the autonomy of the parties, consistent with public policy, in forming their bargain under the freedom of contract; and second, by holding the promisor accountable to the promisee for the promisor's wrongdoing.

Fault Lines in Contract Damages, 80 VA. L. REV. 1225 (1994). Professor Peter Linzer focuses on specific performance in his article. *See generally* Peter Linzer, *On the Amorality of Contract Remedies—Efficiency, Equity, and the Second* Restatement, 81 COLUM. L. REV. 111 (1981).

II. THE LEGALITY AND MORALITY OF INTENTIONAL BREACH OF CONTRACT

A. *The Convergence of Law and Morality on Intentional Breach*

Professor Shiffrin fails to consider that long-standing precedents from the great majority of state and federal jurisdictions—including the United States Supreme Court—specifically express strong legal *and* moral disapproval of unexcused, intentional breach of promise:[21]

- "Commercial law should reflect commercial morality. . . . Repudiators of fair and solemn and binding promises are commercial sinners. If they are unrepentant, courts should hold them to the full consequences of their sins."[22]

- It is "indisputable" that the party breaching a private or public contract is a "repudiator" who bears all the "wrong and reproach that term implies."[23]

- Every breach of contract reflects, in some sense, an "injustice"[24] or "unfairness"[25] and can be a "species of fraud"

21. Undoubtedly, the law cannot and does not claim to enforce all contractual promises. Numerous reasons, including mistake, frustration, impossibility, duress, lack of capacity, and unconscionability may excuse contractual noncompliance. *See* CHARLES FRIED, CONTRACT AS PROMISE 57–58, 92–93 (1981); Linzer, *supra* note 20, at 111.

22. Lagerloef Trading Co. v. Am. Paper Prods. Co. of Ind., 291 F. 947, 956 (7th Cir. 1923); *see also In re* G Survivor Corp., 171 B.R. 755, 759 (Bankr. S.D.N.Y. 1994) (calling a promisor's breach of contract a "dishonorable deed"); Brock v. Brock, 8 So. 11, 13 (Ala. 1890) (noting that breach of contract is "often a moral wrong"); Walker & Co. v. Harrison, 81 N.W.2d 352, 355 (Mich. 1957) (finding that an unwarranted contract "repudiator" was an "aggressor"); Ward v. Coleman, 39 P.2d 113, 118–19 (Okla. 1934) (reproaching the defaulter by saying that contracts are "solemn agreements" and that "[m]oral obligations, fairness, and integrity seem to have had no place in [his] code of ethics").

23. Lynch v. United States, 292 U.S. 571, 580 (1943) (quoting Sinking Fund Cases, 99 U.S. 700, 719 (1878)); Perry v. United States, 294 U.S. 330, 353–54 (1935) (quoting *Sinking Fund Cases*, 99 U.S. at 719); *see also* Studio Frames v. Standard Fire Ins. Co., 369 F.3d 376, 382 (4th Cir. 2004); Franconia v. United States, 61 Fed. Cl. 718, 742 (2004); State *ex rel.* Lane v. Dashiell, 75 A.2d 348, 355 (Md. 1950); City of Phila. v. Fidelity Phila. Trust Co., 56 A.2d 99, 104 (Pa. 1947).

24. Se. Tex. Inns, Inc. v. Prime Hospitality Corp., 462 F.3d 666, 674 (6th Cir. 2006) (quoting Mobil Oil Corp. v. Linear Films, Inc., 718 F. Supp. 260, 268–69 (D. Del. 1989)).

25. United Roasters, Inc. v. Colgate-Palmolive Co., 649 F.2d 985, 992 (4th Cir.

where the party breaches a contract for its own monetary advantage.[26]

- The defaulting promisor is a "wrongdoer"[27] and courts sympathetically call the promisee a "victim"[28] and an "injured party."[29]

- A party has no legal right to breach a contract;[30] the breach is

1981).

26. Foss v. Heineman, 128 N.W. 881, 884–85 (Wis. 1910).

27. *E.g.*, Guardian Trust & Deposit Co. v. Fisher, 200 U.S. 57, 68 (1906) (citations omitted); Boyce v. Soundview Tech. Group, Inc., 464 F.3d 376, 391–92 (2d Cir. 2006); Bituminous Cas. Corp. v. Commercial Union Ins. Co., 652 N.E.2d 1192, 1196 (Ill. 1995); Aetna Cas. & Sur. Co. v. Commonwealth, 179 S.W.3d 830, 859 (Ky. 2005); *see also* Waste Corp. of Am. v. Genesis Ins. Co., 382 F. Supp. 2d 1349, 1356 (S.D. Fla. 2005) (finding that the "primary purpose of imposing liability for breach of contract is to deter wrongdoers"); *accord* RESTATEMENT (SECOND) OF TORTS § 766 cmt. v (1979) (calling breaching promisor a "wrongdoer" in discussing tortious interference with contract). A Westlaw search performed by the author on July 30, 2009 revealed that forty-six states, ten federal circuits, and the United States Supreme Court have used the term "wrongdoer" to describe the breaching party.

28. *See, e.g.*, Domino's Pizza, Inc. v. McDonald, 546 U.S. 470, 479 (2006); Emerald Inv. Ltd. P'ship v. Allmerica Fin. Life Ins. & Annuity Co., 516 F.3d 612, 616 (7th Cir. 2008); LaRocca v. Borden, Inc., 276 F.3d 22, 30 (1st Cir. 2002); Basiliko v. Pargo Corp., 532 A.2d 1346, 1348 (D.C. 1987); Royal Extrusions Ltd. v. Cont'l Window & Glass Corp., 812 N.E.2d 554, 562 (Ill. App. Ct. 2004). A Westlaw search performed by the author on July 30, 2009 revealed that twenty states, seven federal circuits, and the United States Supreme Court have used the term "victim" to describe the injured promisee.

29. *E.g.*, Franconia Assocs. v. United States, 536 U.S. 129, 144 (2002); Contempo Design, Inc. v. Chi. & N.E. Ill. Dist. Council of Carpenters, 226 F.3d 535, 553 (7th Cir. 2000) (citing RESTATEMENT (SECOND) OF CONTRACTS § 347 (1981)).

30. *See* Rousey v. Jacoway, 544 U.S. 320, 328 (2005) (stating that a party has no "unrestricted right to breach a contract"); Smith v. Jones, 497 N.E.2d 738, 741 (Ill. 1986) ("We do not . . . suggest that the State has a right to breach a contract or otherwise to act improperly."); *see also* Joseph M. Perillo, Essay, *Misreading Oliver Wendell Holmes on Efficient Breach and Tortious Interference*, 68 FORDHAM L. REV. 1085, 1086–89 (2000) (calling right to breach "preposterous"); Willard T. Barbour, Note, *The "Right" to Break a Contract*, 16 MICH. L. REV. 106, 109 (1917) ("[N]either the history of the common law nor logic sustains the proposition that there is no legal obligation to perform a contract or, conversely, that there is a right to break a contract.").

The few states purporting to give a party the right to breach a contract have conflicting case law on the point. *Compar*e Epperly v. Johnson, 734 N.E.2d 1066, 1073 (Ind. Ct. App. 2000) ("[e]ach party to a contract has 'common law rights to breach a contract'" (quoting Miller Brewing Co. v. Best Beers of Bloomington, Inc., 608

"unlawful"[31] and a "legal wrong"[32] even when the promisee obtains only nominal damages.[33]

- Justice Benjamin Cardozo denounced the willful breacher as a "transgressor [who] must accept the penalty of his transgression."[34]

- The exalted and "civilizing concept" of the "sanctity of contract,"[35] which is closely aligned with freedom of

N.E.2d 975, 984 (Ind. 1993)) *with* Masonic Temple Ass'n of Crawfordsville v. Ind. Farmers Mut. Ins. Co., 837 N.E.2d 1032, 1039 (Ind. Ct. App. 2005) (quoting Sorenson v. Fio Rito, 431 N.E.2d 47, 52 (Ill. App. Ct. 1980) (calling breaching promisor a "wrongdoer")).

31. Sw. Publ'g Co. v. Ney, 302 S.W.2d 538, 543 n.4 (Ark. 1957) (citing Lion Oil Co. v. Marsh, 249 S.W.2d 569 (Ark. 1952)); Edison Realty Co. v. Bauernschub, 62 A.2d 354, 358 (Md. 1948); Den Norske Ameriekalinje Actiesselskabet v. Sun Printing and Publ'g Ass'n, 122 N.E. 463, 465 (N.Y. 1919).

32. *E.g.*, Ford Motor Co. v. EEOC, 458 U.S. 219, 231 n.15 (1982) (quoting C. MCCORMICK, LAW OF DAMAGES 127–58 (1935)); RLI Ins. Co. v. MLK Ave. Redevelopment Corp., 925 So. 2d 914, 918 (Ala. 2005) (quoting Avis Rent A Car Sys. v. Heilman, 876 So. 2d 1111, 1120 (Ala. 2003)); Seabed Harvesting, Inc. v. Dep't of Natural Res., 60 P.3d 658, 662 n.12 (Wash. Ct. App. 2002); *see also* Park Prop. Assocs. v. United States, 82 Fed. Cl. 162, 163 (2008) (quoting Glus v. Brooklyn E. Terminal, 359 U.S. 231, 232–33 (1959) ("[N]o man may take advantage of his own wrong.")); W.U. Tel. Co. v. Green, 281 S.W. 778, 782 (Tenn. 1926) (quoting JOHN W. SALMOND, LAW OF TORTS 3 (6th ed. 1924) ("Breach of contract is a species of wrong which stands apart from . . . other forms of civil liability.")).

33. *E.g.*, Sweet v. Johnson, 337 P.2d 499, 500 (Cal. Dist. Ct. App. 1959).

34. Jacob & Youngs, Inc. v. Kent, 129 N.E. 889, 891 (N.Y. 1921); *accord* United States v. Canova, 412 F.3d 331, 352 (2d Cir. 2005); Antonoff v. Basso, 78 N.W.2d 604, 611 (Mich. 1956); Material Movers, Inc. v. Hill, 316 N.W.2d 13, 18 (Minn. 1982). Courts and commentators acknowledge Cardozo's major contributions to the law in general and to contract law in particular. *See, e.g.*, Spoon-Shackett Co. v. County of Oakland, 97 N.W.2d 25, 32 (Mich. 1959) (calling Cardozo "the great juristic teacher" of the twentieth century); Lawrence A. Cunningham, *Cardozo and Posner: A Study in Contracts*, 36 WM. & MARY L. REV. 1379, 1379 (1995) (noting that "[f]or over seventy years, [Cardozo's] opinions have formed the basis for many discussions of doctrine, method, and policy").

35. Morta v. Korea Ins. Corp., 840 F.2d 1452, 1460 (9th Cir. 1988); *accord* Blount v. Smith, 231 N.E.2d 301, 305 (Ohio 1967) ("The right to contract freely with the expectation that the contract shall endure according to its terms is as fundamental to our society as the right to write and to speak without restraint."). "In the overwhelming majority of circumstances, contractual promises are to be performed, not avoided: *pacta sunt servanda*, or, as . . . loosely translated . . . 'a deal's a deal.'" Specialty Tires of Am., Inc. v. CIT Group/Equip. Fin., Inc., 82 F. Supp. 2d 434, 437 (W.D. Pa. 2000) (quoting Waukesha Foundry, Inc. v. Indus. Eng'g, Inc., 91 F.3d 1002,

contract,[36] rests upon a "solid foundation of reason and justice"[37] and is the "most fundamental underpinning of commerce."[38]

1010 (7th Cir. 1996)).

In keeping with notions of sanctity of contract, the traditional viewpoint is that willful breach is deserving of greater sanction than inadvertent breach because it "undermines more than just the expectation of the promisee." Oren Bar-Gill & Omri Ben-Shahar, *An Information Theory of Willful Breach*, 107 MICH. L. REV. 1479, 1482 (2009). Willful breach demonstrates indifference and disregard toward the institutions of contractual commitment and of trustworthiness. *See id.* at 1499.

36. *See, e.g.*, Andrews v. Blake, 69 P.3d 7, 18 (Ariz. 2003) (quoting SDG Macerik Prop., L.P. v. Stanek, 648 N.W.2d 581, 589 (Iowa 2002)). "[Because] the right of private contract is no small part of the liberty of the citizen . . . the usual and most important function of courts of justice is rather to maintain and enforce contracts, than to enable parties thereto to escape from their obligation . . . ." Balt. & Ohio Sw. Ry. v. Voigt, 176 U.S. 498, 505 (1899); *see also* Fox v. I-10, Ltd., 957 P.2d 1018, 1022 (Colo. 1998); Calhoun v. WHA Med. Clinic, PLLC, 632 S.E.2d 563, 573 (N.C. 2006).

Professor Charles Fried correctly explains that "[t]he moral force behind contract as promise is autonomy: the parties are bound to their contract because they have chosen to be." *See* FRIED, *supra* note 21, at 57. Undoubtedly, Professor Fried has his critics. For example, Professor Richard Craswell charges that Fried's analysis has "little or no relevance to those parts of contract law that govern the proper remedies for breach, the conditions under which the promisor is excused from her duty to perform, or the additional obligations (such as implied warranties) imputed to the promisor as an implicit part of her promise." Richard Craswell, *Contract Law, Default Rules, and the Philosophy of Promising*, 88 MICH. L. REV. 489, 489 (1989). The critics' objections about the relevance of Professor Fried's analysis to contract law are misplaced, because the cases have endorsed Professor Fried's thesis. *See, e.g.*, Kern v. Levolor Lorentzen, Inc., 899 F.2d 772, 784 n.4 (9th Cir. 1990); *Morta*, 840 F.2d at 1460.

37. Opera Co. of Boston v. Wolf Trap Found. for the Performing Arts, 817 F.2d 1094, 1097 (4th Cir. 1987) (quoting Dermott v. Jones, 69 U.S. (2 Wall.) 1, 8 (1864)).

38. N.Y. State Elec. & Gas Corp. v. Saranac Power Partners, 117 F. Supp. 2d 211, 253 (N.D.N.Y. 2000) (citing *In re* Schenck Tours, Inc., 69 B.R. 906, 910–11 (Bankr. E.D.N.Y. 1987)); *accord* Chambers Dev. Co. v. Passaic County Utils. Auth., 62 F.3d 582, 589 (3d Cir. 1995) ("The sanctity of a contract is a fundamental concept of our entire legal structure."); Iffland v. Iffland, 589 N.Y.S.2d 249, 251 (N.Y. Sup. Ct. 1992) (noting that in the five years following the Supreme Court's first contract clause decision, twenty-two state constitutions were changed to protect sanctity of contracts); Abernathy v. Black, 42 Tenn. 314, 318 (1865) (noting that the obligation of a contract is a "solemn engagement, and the welfare of society demands its faithful observance"); *see also* Comment, *Remedies for Total Breach of Contract Under the Uniform Revised Sales Act*, 57 YALE L.J. 1360, 1361 n.4 (1948) ("'[T]he basis of commercial life is the sanctity of contract. If either party to a written obligation felt it possible to withdraw without the consent of the other from his obligations, then no one could ever make future commitments with any degree of certainty that they would be carried out.'")

This promise-keeping obligation, a corollary of the law's general concern that contracts comport with "good morals,"[39] is a moral duty[40] with deep roots in ecclesiastical and other philosophical influences.[41] It is

(quoting 683 TEXTILE DISTRIBUTORS INSTITUTE BULLETIN 1 (Sept. 30, 1946)).

The corollary to the sanctity of contract is that the courts will not second guess the parties on the value of their bargain absent invalid assent such as with fraud, duress, undue influence, or mistake. Shoenfelt v. Donna Belle Loan & Inv. Co., 45 P.2d 507, 509 (Okla. 1935). Courts are often only interested in the legality of a contract because "'[t]he fairness or unfairness, folly or wisdom, or inequality of contracts are questions exclusively within the rights of the parties to adjust at the time the contract is made.'" Bilbrey v. Cingular Wireless, L.L.C., 164 P.3d 131, 134 (Okla. 2007) (quoting Barnes v. Helfenbein, 548 P.2d 1014, 1021 (Okla. 1976)); *see also* Groberg v. Hous. Opportunities, Inc., 68 P.3d 1015, 1019 (Utah Ct. App. 2003) (stating that a trial court will not examine alleged errors in a contract absent specific objections).

39. *See, e.g.*, Griffin v. McCoach, 313 U.S. 498, 506 (1941); Dacotah Mktg. & Research, L.L.C. v. Versatility, Inc., 21 F. Supp. 2d 570, 579 n.24 (E.D. Va. 1998) (describing contracts against good morals as against public policy); Montgomery v. Montgomery, 127 S.W. 118, 120 (Mo. Ct. App. 1910) (stating that "it is universally agreed that the promotion of public and private morals is one of the chief purposes of [contract] law"); *see also* Melvin Aron Eisenberg, *The Role of Fault in Contract Law: Unconscionability, Unexpected Circumstances, Interpretation, Mistake, and Nonperformance*, 107 MICH. L. REV. 1413, 1430 (2009) (noting that efficiency of the contract system rests in important part on the "moral norm of promise keeping").

40. *See* Citizens Light, Heat & Power Co. v. Montgomery Light & Water Power Co., 171 F. 553, 561 (5th Cir. 1909) (asserting that "public and private morality" are "insecure" when the law encourages the non-observance of contracts); Stark v. Parker, 19 Mass. 267, 279 (1824) (stating that intentional breach of contract is "repugnant . . . to the dictates of moral sense").

In some departures from her main theme, Professor Shiffrin appears to acknowledge this moral premise of contract law. For example, she concedes: (1) "The language of promises, promisees, and promisors saturates contract law," Shiffrin, *supra* note 1, at 721; (2) "it is not clear . . . that the aims of contract do intrinsically rely on relaxing or abandoning moral behavior," *id.* at 744; and (3) "[t]he majority of the aims of contract law are surely compatible with moral constraints," *id.* at 744 n.69. *But see* Shiffrin, *supra* note 5, at 1552 (stating that contract law "embraces and encourages immoral action").

41. *See, e.g.*, Ogden v. Saunders, 25 U.S. (12 Wheat.) 213, 222 n.(a) (1827) (noting that philosophers such as Grotius, Burlamaqui, Pothier, and others have based contractual obligations on the sanctity of promise making). *See also* Larry A. DiMatteo, *The Counterpoise of Contracts: The Reasonable Person Standard and the Subjectivity of Judgment*, 48 S.C. L. REV. 293, 305–09 (1997); Charles Donahue, Jr., Ius Commune*, Canon Law, and Common Law in England*, 66 TUL. L. REV. 1745, 1766 (1992); Roscoe Pound, *Promise or Bargain?*, 33 TUL. L. REV. 455, 455 (1959) ("From antiquity the moral obligation to keep a promise had been a cardinal tenet of ethical philosophers, publicists, and philosophical jurists.").

binding in conscience and rests upon principles of "natural justice."[42] Thus, the law incorporates a promisor-based conception of contract law, emphasizing the enforcement of the promisor's honesty and fair dealing.[43] These numerous judicial statements further reflect the belief of the general public that "breaking a promise is a serious wrong,"[44] which brings us back to the viewpoint cited above that commercial law should reflect

42. Camp v. Bates, 11 Conn. 487, 497 (1836); *see also* Doe v. Robertson, 24 U.S. (11 Wheat.) 332, 344 (1826) ("Every political society or government is bound by the ties of justice and morality, and to the observance of good faith in its contracts with individuals."); Driggs v. Utah State Teachers Ret. Bd., 142 P.2d 657, 661 (Utah 1942) (stating that both "justice and morality" require parties to comply with their contractual obligations).

43. Professor Shiffrin does not squarely take a position on whether contract law takes an overall promisor- or promisee-based theory of obligation. Professor E. Allan Farnsworth famously advocated the promisee-based theory. In his 1970 article, he observed that "[o]ur system, then, is not directed at *compulsion of promisors* to *prevent* breach; rather, it is aimed at *relief* to *promisees to redress* breach." E. Allan Farnsworth, *Legal Remedies for Breach of Contract*, 70 COLUM. L. REV. 1145, 1147 (1970). Professor Eisenberg also tends toward the promisee-based orientation. He has stated that "it is fair to say that American contract law, although in some measure influenced by both conceptions, tends to be promisee-based, that is, tends to focus on compensating injured promisees and facilitating commerce rather than on promise-keeping as an end in itself." Melvin Aron Eisenberg, *The World of Contract and the World of Gift*, 85 CAL. L. REV. 821, 839 (1997).

Other research shows that the case law strongly favors the promisor-based orientation; indeed, the promisee-based interpretation is inconsistent with the promise-based nature of contract itself. *See* Nance v. L.J. Dolloff Assocs., 126 P.3d 1215, 1220 (N.M. Ct. App. 2005) ("A contract is a legally enforceable promise."); FRIED, *supra* note 21, at 19 (observing that "a person is bound by his promise and not by the harm the promisee may have suffered in reliance on it"). The promisee-based view contradicts the promise-oriented theory of expectation damages, which is to place the injured party "[i]n as good a position as he would have been in had performance been rendered *as promised*." Linan-Faye Constr. Co. v. Hous. Auth. of City of Camden, 49 F.3d 915, 921 (3d Cir. 1995) (emphasis added); *accord* Agredano v. United States, 82 Fed. Cl. 416, 447 (2008) (citing 11-55 ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 55.3 (rev. ed. 2008)). Further, the theory of expectation damages is promisor-based because it generally uses the promisor's profits as the measure of relief when those profits tend to define the plaintiff's losses. *See, e.g.*, Cincinnati Siemens-Lungren Gas Illuminating Co. v. W. Siemens-Lungren Co., 152 U.S. 200, 204–07 (1894); U.S. Naval Inst. v. Charter Commc'ns, Inc., 936 F.2d 692, 696 (2d Cir. 1991); Murphy v. Lifschitz, 49 N.Y.S.2d 439, 441 (Sup. Ct. 1944), *aff'd*, 52 N.Y.S.2d 943 (App. Div. 1945), *aff'd*, 63 N.E.2d 26 (N.Y. 1945). I agree with Professor Charles Fried that "to the extent that contract is grounded in promise, it seems natural to measure relief by the expectation, that is, by the promise itself." FRIED, *supra* note 21, at 18.

44. Mark Pennington, *Punitive Damages for Breach of Contract: A Core Sample from the Decisions of the Last Ten Years*, 42 ARK. L. REV. 31, 45 (1989).

commercial morality.

The law goes well beyond Professor Shiffrin's restrictive statement about contract that "[s]ome cases and doctrines involve appeal to moral concepts of fairness or reasonableness" but that "[n]ot all of these cases and doctrines can be recast more narrowly as judgments about what *justice* requires."[45] To the contrary, "[t]he incorporation of justice, fairness, and equity principles into contract law can be traced to the very beginnings of contractual exchange."[46] The law's emphasis on justice and the promisor's accountability for breach is even more prominent under evolving case law. After an in-depth analysis of the decisions, one scholar has stated that "[t]here has been a slow but steady trend . . . towards an application of higher standards of good faith, fair dealing and morality to all contracts and transactions."[47] Another commentator takes the same position, stating that conventional, relational, critical, and law and economics scholars all agree that "contract law is undergoing a 'transformation' as a result of an infusion of 'communitarian values', such as fairness, trust, paternalism, and cooperation."[48] More than ever, it remains a truism that "[t]he moral

45. Shiffrin, *supra* note 1, at 710 n.1.

46. Larry A. DiMatteo, *The History of Natural Law Theory: Transforming Embedded Influences into a Fuller Understanding of Modern Contract Law*, 60 U. PITT. L. REV. 839, 918–19 (1999); *see also* Brian A. Blum & Juliana B. Wellman, *Participation, Assent and Liberty in Contract Formation*, 1982 ARIZ. ST. L.J. 901, 906 n.22 (recognizing that "moral precepts of individual accountability and individual rights [have] strongly influenced the formation of contract rules"); George M. Cohen, *The Fault that Lies Within Our Contract Law*, 107 MICH. L. REV. 1445, 1446 (2009) (noting that "fault plays an inherent, invaluable, and ineluctable role in contract law"); Robert E. Scott, *In (Partial) Defense of Strict Liability in Contract*, 107 MICH. L. REV. 1381, 1381 (2009) ("Numerous scholars have pointed out that, in fact, there are many notions of fault that infuse contract law, ranging from prescriptions against intentional 'bad behavior,' to assessments of the reasonableness of an actor's behavior in assessing both liability and damages.").

47. Nicola W. Palmieri, *Good Faith Disclosures Required During Precontractual Negotiations*, 24 SETON HALL L. REV. 70, 120 (1993).

48. G. Richard Shell, *Substituting Ethical Standards for Common Law Rules in Commercial Cases: An Emerging Statutory Trend*, 82 NW. U. L. REV. 1198, 1205 (1988). "Courts have increasingly relied on generalized, ethical standards to decide disputes between businesses." *Id.* at 1198.

The *Restatement (Second) of Contracts* cites the general principle that the rules of contract remedies "are based on fundamental principles of fairness and justice." RESTATEMENT (SECOND) OF CONTRACTS ch. 10, introductory n. (1981). Covering numerous aspects of contract interpretation, performance, and enforcement, the *Restatement* has nineteen sections enforcing the norm of meeting the requirements of "justice" or avoiding the imposition of "injustice." *See* Peter A. Alces, *On*

standard that requires individuals to keep their promises certainly has had an important effect on the development of contract law."[49]

B. *Promissory Estoppel and the Morality of Fair Dealing*

Courts further express their moral and legal disapproval of a breach of promise even when the parties do not have a contract. In this respect, Professor Shiffrin has failed to analyze in any significant way the widely accepted remedial theory of promissory estoppel.[50] This principle holds that "a promise made without consideration may nonetheless be enforced to prevent injustice if the promisor should have reasonably expected the promisee to rely on the promise and if the promisee did actually rely on the promise to his or her detriment."[51] Many courts give weight to Section 90

Discovering Doctrine: "Justice" in Contract Agreement, 83 WASH. U. L.Q. 471, 476 n.23 (2005) (providing an extensive analysis of the *Restatement*); DiMatteo, *supra* note 46, at 894–95 (1999) (observing that the *Restatement* "confirms the profound influence of equitable principles upon modern contract law").

Frequently, courts award different levels of damages consistent with their moral disapproval of intentional breach. *See infra* Parts VII–VIII. Therefore, the courts' moral condemnation of the intentional defaulter is not just empty rhetoric.

49. HUNTER, *supra* note 3, § 1:2; *see also* Steven Shavell, *Is Breach of Contract Immoral?*, 56 EMORY L.J. 439, 455 (2006) (acknowledging that most sources on contract law and prominent commentators consider or describe breach as "having a generally unethical dimension"). *But see* Barry E. Adler, *Efficient Breach Theory Through the Looking Glass*, 83 N.Y.U. L. REV. 1679, 1685–86 & n.20 (2008) (concluding erroneously that the law views breach of contract as "morally neutral").

Undoubtedly, the moral justifications against intentional contract breach cited in the case law also may be understood as being based on economic principles of efficiency, reduction of transaction costs, and the facilitation of beneficial commercial activity. Nevertheless, as commentators point out, no clear division exists between economic and moral justifications for contract law principles. *See, e.g.*, Charles L. Knapp, *The Promise of the Future—And Vice Versa: Some Reflections on the Metamorphosis of Contract Law*, 82 MICH. L. REV. 932, 949 n.43 (1984) (reviewing E. ALLAN FARNSWORTH, CONTRACTS (1982) ("It is obviously possible to take the position that 'morality' is also 'efficient,' or that 'efficiency' is also 'moral' (or, perhaps, both?), so the characterization of particular commentators according to the dichotomy . . . is, at best, arguable.")); Linzer, *supra* note 20, at 112 ("In many cases the alleged necessary connection between efficiency and amorality is mythical.").

50. *See* RESTATEMENT (SECOND) OF CONTRACTS § 90 (1981) (promise reasonably inducing action or forbearance); 4 SAMUEL WILLISTON, WILLISTON ON CONTRACTS § 8:4 (Richard A. Lord ed., 4th ed. 1992) (promises made enforceable by promissory estoppel); Eric Mills Holmes, *Restatement of Promissory Estoppel*, 32 WILLAMETTE L. REV. 263, 300–514 (1996) (providing a state-by-state survey of the pervasive use of promissory estoppel).

51. BLACK'S LAW DICTIONARY 591 (8th ed. 2004); *see also* Bd. of County

of the *Restatement (Second) of Contracts* when employing this doctrine.[52]

The promissory estoppel principle is the *Restatement*'s "most notable and influential rule"[53] and is "perhaps the most radical and expansive development of [the twentieth] century in the law of promissory liability."[54] Section 90 has had a "profound influence" on contract law because it gives a remedy when a binding contract is absent.[55] The "routine remedy" in Section 90 cases is enforcement of the promise, either by expectation damages or by specific performance.[56]

Comm'rs of Summit County v. DeLozier, 917 P.2d 714, 716 (Colo. 1996) (citing Vigoda v. Denver Urban Renewal Auth., 646 P.2d 900, 905 (Colo. 1982)) (explaining the purpose of promissory estoppel); Seater Constr. Co. v. Rawson Plumbing, Inc., 619 N.W.2d 293, 297 (Wis. Ct. App. 2000) (citing Hoffman v. Red Owl Stores, Inc., 133 N.W.2d 267, 273 (Wis. 1965)) (adopting *Restatement* view of promissory estoppel). *Compare* Shiffrin, *supra* note 1, at 709–10 n.1 (acknowledging that some parts of contract law depend upon moral concepts).

52. *E.g.*, Flying J Inc. v. Comdata Network, Inc., 405 F.3d 821, 834 n.6 (10th Cir. 2005); Bechtel Corp. v. CITGO Prods. Pipeline Co., 271 S.W.3d 898, 926 (Tex. App. 2008).

53. Edward Yorio & Steve Thel, *The Promissory Basis of Section 90*, 101 YALE L.J. 111 (1991) (quoting ALLAN FARNSWORTH, CONTRACTS § 2.19 (1982)).

54. *Id.* (quoting Charles L. Knapp, *Reliance in the Revised* Restatement*: The Proliferation of Promissory Estoppel*, 81 COLUM. L. REV. 52, 53 (1981)).

55. *Id.* at 111; *see also* Grouse v. Group Health Plan, Inc., 306 N.W.2d 114, 116 (Minn. 1981) (noting that promissory estoppel is a creature of equity and implies a "contract in law when none exists in fact").

56. *See* Yorio & Thel, *supra* note 53, at 151; *see also* Goldstick v. ICM Realty, 788 F.2d 456, 464 (7th Cir. 1986) ("[T]he value of the promise is the presumptive measure of damages for promissory estoppel, to be rejected only if awarding so much would be inequitable.").

Some courts advocate tort-based reliance damages as the preferred remedy for promissory estoppel. *See, e.g.*, Rosnick v. Dinsmore, 457 N.W.2d 793, 800 (Neb. 1990) (providing that the "usual measure of damages" under promissory estoppel is "loss incurred by the promisee in reasonable reliance on the promise"). If the facts of a case so merit, however, precedent is now clear that a plaintiff asserting promissory estoppel may regularly recover its contract-based expectation interest—including consequential harms such as lost profits—through a damages award, even when the damages exceed readily calculable reliance damages. *See* Garwood Packaging, Inc. v. Allen & Co., 378 F.3d 698, 703 (7th Cir. 2004) ("[I]f the promise giving rise to an estoppel is clear, the plaintiff will usually be awarded its value, which would be the equivalent of the expectation measure of damages in an ordinary breach of contract case."); 3 ERIC MILLS HOLMES, CORBIN ON CONTRACTS § 8.8, at 21 (Joseph M. Perillo ed., rev. ed. 1996); *id.* § 8.12, at 101–03 ("[In promissory estoppel cases,] the court can give judgment for expectation damages measured by the value of the promised performance."); Yorio & Thel, *supra* note 53, at 130–31 (citing cases from 1891 to 1985 showing that the vast majority of courts ordered expectation damages as

Although based on a unilateral and not a bilateral commitment, the theory of promissory estoppel "[keeps] remedies abreast of increased moral consciousness of honesty and fair representations in all business dealings."[57] The underlying conceptions of this doctrine appear to be "moral indignation at [the] breaking [of] seriously made promises" and the affirmation of "a personal autonomy notion that people should be free to bind themselves by promise and others should be able to take them at their word."[58] As the Colorado Court of Appeals has observed, "[p]romissory estoppel is an extension of the basic contract principle that one who makes [a] promise[ ] must be required to keep [it]."[59] Once again, the law has expressed its dominant view of the immorality of intentional breach of promise—even when the promise is made unilaterally.

C. *The Minority Position on Morality and Breach*

A handful of jurisdictions deny the moral basis of contract, but they also take contrary positions. For example, the Washington Supreme Court has opined broadly that "a breach of contract is neither immoral nor wrongful; it is simply a broken promise."[60] At the same time, Washington decisions consistently call the promisee a "victim" and the breaching promisor a "wrongdoer."[61] The Washington Supreme Court also strongly adheres to the implied covenant of good faith and fair dealing,[62] which according to many decisions imposes a moral code of conduct on the parties.[63] In addition, Washington decisions accept the tort of intentional

relief in promissory estoppel claims). This prevailing judicial willingness in promissory estoppel cases to go beyond the reliance standard by awarding the plaintiff its expectation interest—a form of quasi-punitive damages in this setting—proves once more the great importance courts place on promise-keeping.

57. Goff-Hamel v. Obstetricians & Gynecologists, P.C., 588 N.W.2d 798, 801 (Neb. 1999) (quoting *Rosnick*, 457 N.W.2d at 801).

58. *See* Yorio & Thel, *supra* note 53, at 166 n.363 (positing two possible underlying rationales for promissory estoppel).

59. Patzer v. City of Loveland, 80 P.3d 908, 912 (Colo. App. 2003) (citing Bd. of County Comm'rs v. DeLozier, 917 P.2d 714 (Colo. 1996)); *see also* Yorio & Thel, *supra* note 53, at 166 ("Courts enforce promises under Section 90 when they view the promises as serious and deserving of enforcement *qua* promise . . . .").

60. Ford v. Trendwest Resorts, Inc., 43 P.3d 1223, 1227 (Wash. 2002).

61. *See* Jet Boats, Inc. v. Puget Sound Nat'l Bank, 721 P.2d 18, 25 (Wash. Ct. App. 1986) (citing Ward v. Painter's Local Union 300, 276 P.2d 576 (Wash. 1954)).

62. *See* Badgett v. Sec. State Bank, 807 P.2d 356, 360 (Wash. 1991) (citing decisions in which the Washington Supreme Court has recognized and relied on the duty of good faith and fair dealing).

63. *See supra* Part III.

interference with contract, which deems the tortfeasor and breaching party both wrongdoers.[64] Therefore, notwithstanding the broad statement quoted above about the amorality of breach, Washington courts in practice follow the prevailing doctrine that breach of contract is a form of wrongdoing and is both morally and legally unacceptable.

Other courts seeming to deny the moral values of contractual promise-keeping employ the same contradictions. California and Hawaii have characterized intentional breach of contract as "morally neutral,"[65] Utah has called contract law "amoral,"[66] and the United States Court of Appeals for the Federal Circuit has opined that contract law is not concerned with the "notion of wrong-doing."[67] In other decisions, however, these same jurisdictions call the breaching promisor a "wrongdoer,"[68] recognize the doctrine of tortious interference with contract,[69] and endorse the implied covenant of good faith and fair dealing.[70] Therefore, these jurisdictions' actual adherence to the morally

64. *See, e.g.*, Leingang v. Pierce County Med. Bureau, Inc., 930 P.2d 288, 300 (1997).

65. *See* Ortiz v. Lyon Mgmt. Group, Inc., 69 Cal. Rptr. 3d 66, 75 (Ct. App. 2007); Francis v. Lee Enters., 971 P.2d 707, 716 (Haw. 1999).

66. *See* TruGreen Cos. v. Mower Bros., 199 P.3d 929, 933 (Utah 2008).

67. Glendale Fed. Bank v. United States, 239 F.3d 1374, 1379 (Fed. Cir. 2001); *see also* Benderson Dev. Co. v. U.S. Postal Serv., 998 F.2d 959, 962 (Fed. Cir. 1993) (breach of contract is "not unlawful").

68. *See* LaSalle Talman Bank v. United States, 317 F.3d 1363, 1371–72 (Fed. Cir. 2003); Buell-Wilson v. Ford Motor Co., 46 Cal. Rptr. 3d 147, 173 (Ct. App. 2006) (quoting Speegle v. Bd. of Fire Underwriters, 172 P.2d 867 (1946)); Fought & Co. v. Steel Eng'g & Erection, Inc., 951 P.2d 487, 501 (Haw. 1998); Hector, Inc. v. United Sav. & Loan Ass'n, 741 P.2d 542, 546 (Utah 1987) (quoting 22 AM. JUR. 2D *Damages* § 32 (1965)); *see also* Driggs v. Utah State Teachers Ret. Bd., 142 P.2d 657, 661 (Utah 1943) (observing that concepts of "justice and morality" require all parties to adhere to their contracts and that contract "repudiators" bear "all the wrong and reproach that term implies").

69. *See, e.g.*, Citizens of Humanity, LLC v. Costco Wholesale Corp., 89 Cal. Rptr. 3d 455, 464 (Ct. App. 2009); Buscher v. Boning, 159 P.3d 814, 828 (Haw. 2007); Kemp v. Murray, 680 P.2d 758, 760 (Utah 1984). Although tortious interference with contract is not, strictly speaking, a cause of action in contract, this remedy recognizes that both the tortfeasor and the breaching party are equally wrongdoers. *See* RESTATEMENT (SECOND) OF TORTS § 766 cmt. v (1979) (stating that the parties "are both wrongdoers, and each is liable to the plaintiff for the harm caused to him by the loss of the benefits of the contract").

70. *See, e.g.*, First Nationwide Bank v. United States, 431 F.3d 1342, 1349 (Fed. Cir. 2005); Foley v. Interactive Data Corp., 765 P.2d 373, 389 (Cal. 1988); Young v. Allstate Ins., 198 P.3d 666, 690 (Haw. 2008); Asael Farr & Sons Co. v. Truck Ins. Exch., 193 P.3d 650, 662 (Utah Ct. App. 2008).

and legally neutral nature of breach of contract is not supported.

III. INDEPENDENT ENFORCEMENT OF MORALITY: THE IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALING

Perhaps the most powerful doctrine courts use to voice their legal and moral disapproval of intentional promissory default is the implied covenant of good faith and fair dealing, which differs from specific contract obligations and is a basis for breach-of-contract liability.[71] Applicable to contract formation, performance, and enforcement,[72] and non-waivable,[73] the covenant reflects society's "normative values,"[74] and protects against conduct that violates "community standards of decency, fairness, or reasonableness."[75] The implied promise is "a pledge that 'neither party

71. *See* Engstrom v. John Nuveen & Co., 668 F. Supp. 953, 958 (E.D. Pa. 1987); *Foley*, 765 P.2d at 389; Allworth v. Howard Univ., 890 A.2d 194, 201–02 (D.C. 2006). A very small minority of jurisdictions does not accept this implied covenant as a general duty, but will give it partial recognition. *See, e.g.*, Bradley v. Phillips Petroleum Co., 527 F. Supp. 2d 661, 686–87 (S.D. Tex. 2007) (stating that Texas does not recognize the duty of good faith and fair dealing unless intentionally created by express language in the contract or a special relationship of trust and confidence exists between the parties); Allison v. Union Hosp., Inc., 883 N.E.2d 113, 123 (Ind. Ct. App. 2008) (stating that an implied covenant generally applies only in limited circumstances involving employment contracts and insurance contracts).

72. *E.g.*, Mkt. St. Assocs. Ltd. P'ship. v. Frey, 941 F.2d 588, 595 (7th Cir. 1991); De La Concha of Hartford, Inc. v. Aetna Life Ins. Co., 849 A.2d 382, 388 (Conn. 2004); Joy A. McElroy, M.D., Inc. v. Maryl Group, 114 P.3d 929, 942 (Haw. Ct. App. 2005).

Denigrating the moral basis of the duty of good faith and fair dealing, Judge Richard Posner of the United States Court of Appeals for the Seventh Circuit has propounded an economic justification for the implied term. *See Mkt. St. Assocs.*, 941 F.2d at 595 ("The concept of the duty of good faith like the concept of fiduciary duty is a stab at approximating the terms the parties would have negotiated had they foreseen the circumstances that have given rise to their dispute."). In other decisions, however, Judge Posner correctly trends to the moral protections of the implied duty of good faith and fair dealing. *See In re* Ocwen Loan Servicing, LLC Mortgage Servicing Litig., 491 F.3d 638, 644 (7th Cir. 2007) (stating that the provision protects the plaintiff against opportunistic behavior such that the defendant has a duty to "avoid taking advantage of the plaintiff's vulnerabilities"). The cases relying on the moral view of good faith and fair dealing, cited in this Part, are the majority view.

73. *See* U.C.C. § 1-102(3) (2004); *see also* Stark v. Circle K Corp., 751 P.2d 162, 166 (Mont. 1988); PDQ Lube Ctr., Inc. v. Huber, 949 P.2d 792, 797 n.7 (Utah Ct. App. 1997) (citing Olympus Hills Shopping Ctr., Ltd. v. Smith's Food & Drug Ctrs., Inc., 889 P.2d 445, 450 n.4 (Utah Ct. App. 1994)).

74. *Foley*, 765 P.2d at 413 (citing several cases supporting that proposition).

75. Brunswick Hills Racquet Club, Inc. v. Route 18 Shopping Ctr. Assocs.,

shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract.'"[76] Some common examples of such a violation are the willful rendering of imperfect performance, abuse by one party in specifying terms, and interference or failure to cooperate with the other party's performance.[77] Although violations of the covenant typically accompany a clear contract breach, a party can infringe upon the duty of good faith—even when that party has literally fulfilled all the terms of the contract[78]—because the doctrine focuses on "'what the parties likely would have done if they had considered the issue'" initially.[79]

In sum, good faith "is of a piece with explicit requirements of 'contractual morality'"[80] because courts focus on "'conscious doing of a wrong'" that reflects "'dishonest purpose or moral obliquity.'"[81] The

864 A.2d 387, 395 (N.J. 2005) (quoting Wilson v. Arrerada Hess Corp., 773 A.2d 1121 (N.J. 2001)).

76. Dalton v. Educ. Testing Serv., 663 N.E.2d 289, 291 (N.Y. 1995). Consumer protection statutes liberally enforce the same standard. *See, e.g.*, TENN. CODE ANN. § 47-18-102(4) (2001) (mandating "ethical" and "good faith" dealing at "all levels of commerce").

77. *See* N. Star Ala. Hous. Corp. v. United States, 76 Fed. Cl. 158, 188–89 & n.36 (2007); Tang v. C.A.R.S. Prot. Plus, Inc., 734 N.W.2d 169, 183 (Wis. Ct. App. 2007).

78. *See* Fields v. Thompson Printing Co., 363 F.3d 259, 271 (3d Cir. 2004) (finding that a party can breach the implied covenant without violating an express contract term).

79. *See* Horizon Holdings, L.L.C. v. Genmar Holdings, Inc., 244 F. Supp. 2d 1250, 1257 (D. Kan. 2003) (quoting Cincinnati SMSA Ltd. P'Ship v. Cincinnati Bell Cellular Sys. Co., 708 A.2d 989, 992 (Del. 1998)).

80. Robert S. Summers, *The General Duty of Good Faith—Its Recognition and Conceptualization*, 67 CORNELL L. REV. 810, 811 (1992) (quoting J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE ch. 4 (2d ed. 1980)); *see also* Reed v. State Farm Mut. Auto Ins. Co., 857 So. 2d 1012, 1022 n.9 (La. 2003) (noting that the concept of good faith and fair dealing represents "a requirement for moral and ethical conduct"); *Brunswick Hills Racquet Club, Inc.*, 864 A.2d at 399 (finding that the covenant enforces "ethical norms").

81. *See* Bailey v. Bailey, 724 So. 2d 335, 338 (Miss. 1998) (quoting BLACK'S LAW DICTIONARY 139 (6th ed. 1990)); *see also In re* Ocwen Loan Servicing, LLC Mortgage Servicing Litig., 491 F.3d 638, 645 (7th Cir. 2007) (holding that the duty of good faith performance means "that a party to a contract cannot engage in opportunistic behavior" (citing Lockwood Int'l, B.V. v. Volm Bag Co., 273 F.3d 741, 745 (7th Cir. 2001); Original Great Am. Chocolate Chip Cookie Co. v. River Valley Cookies, Ltd., 970 F.2d 273, 280 (7th Cir. 1992); Martindell v. Lake Nat'l Bank, 154 N.E.2d 683, 690 (Ill. 1958); Hentze v. Unverfehrt, 605 N.E.2d 536, 539–40 (Ill. App. Ct. 1992))); Equip. & Sys. for Indus., Inc. v. Northmeadows Constr. Co., 798 N.E.2d 571,

covenant incorporates, in the traditional sense, "a moral quality . . . equated with honesty of purpose, freedom from fraudulent intent and faithfulness to duty or obligation."[82] This contractual overlay of good faith and fair dealing is a wide-ranging code of moral conduct that spans the full spectrum of formation, performance, and enforcement. Accordingly, the implied covenant makes the promisor fully accountable to the promisee for breach and contradicts Professor Shiffrin's opinion that contract law neither places pressure on the promisor to behave morally nor proscribes immoral behavior by promisors.[83]

IV. "PAY OR PERFORM" AND HOLMES'S THEORY OF CONTRACT

A. *The Impact of "Pay or Perform" on the Courts*

In saying that breach is "not a legal wrong," Professor Shiffrin relies on Oliver Wendell Holmes's observation that a party signing a contract has the option to break it.[84] In 1897, Holmes observed that "'[t]he 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.'"[85] Professor Shiffrin overstates, however, the impact of Holmes's "pay or perform" theory upon the courts.

Historically, most cases deny the promisor any option to perform or to answer in damages,[86] as does the UCC.[87] The only jurisdictions found expressly accepting the Holmes observation or its equivalent are the Federal, Second, Seventh, and Eleventh Circuits; federal district courts in Arizona, Florida, and Missouri; and state courts in Arkansas, Delaware, Hawaii, Maryland, Montana, New York, Ohio, and Oregon.[88] Notably,

575 (Mass. 2003) (citing Nagel v. Provident Mut. Life Ins. Co. of Phila., 749 N.E.2d 710, 715 (Mass. App. Ct. 2001)) (noting that a breach of the implied covenant implicates a "dishonest purpose, consciousness of wrong, or ill will in the nature of fraud").

82. Raab v. Casper, 124 Cal. Rptr. 590, 593 (Ct. App. 1975) (citing People v. Nunn, 296 P.2d 813, 818 (Cal. 1956); 18A WORDS AND PHRASES 83 (perm. ed. 1956)).

83. *See* Shiffrin, *supra* note 1, at 719–20.

84. *Id.* at 727, 737.

85. *Id.* at 727 (quoting Oliver Wendell Holmes, Jr., *The Path of the Law*, 10 HARV. L. REV. 457, 462 (1897)).

86. *Remedies for Total Breach of Contract Under the Uniform Revised Sales Act*, *supra* note 38, at 1361 n.3.

87. U.C.C. § 2-609 cmt. 1 (2003) ("[T]he essential purpose of a contract . . . is actual performance and [parties] do not bargain merely for a promise, or for a promise plus the right to win a lawsuit.").

88. Moran Foods, Inc. v. Mid-Atl. Mkt. Dev. Co., 476 F.3d 436, 439 (7th Cir. 2007); United States v. Blankenship, 382 F.3d 1110, 1133–34 (11th Cir. 2004); Glendale

these same tribunals ignore the contrary UCC standard in those jurisdictions, as well as their own law labeling the breaching party as a "wrongdoer" or a breach of contract as "wrongdoing."[89] Furthermore, the Holmes aphorism fails to reflect the view that no party has an enforceable right to breach a contract.[90]

Prominent commentators correctly observe that the Holmes observation is legally "wrong"[91] and even "heresy."[92] To put the "pay or perform" doctrine in Hohfeldian terms, the breaching promisor has the

Fed. Bank v. United States, 239 F.3d 1374, 1379–80 (Fed. Cir. 2001); TM Park Ave. Assocs. v. Pataki, 214 F.3d 344, 349 (2d Cir. 2000); Norcia v. Equitable Life Assurance Soc'y of the U.S., 80 F. Supp. 2d 1047, 1047 (D. Ariz. 2000); Allapattah Servs., Inc. v. Exxon Corp., 61 F. Supp. 2d 1326, 1329 (S.D. Fla. 1999); Wells v. Holiday Inns, Inc., 522 F. Supp. 1023, 1028 n. 4 (W.D. Mo. 1981); L.L. Cole & Son, Inc. v. Hickman, 665 S.W.2d 278, 280 (Ark. 1984); E.I. DuPont de Nemours & Co. v. Pressman, 679 A.2d 436, 445 n.18 (Del. 1996); Francis v. Lee Enters., 971 P.2d 707, 716 (Haw. 1999); Willard Packaging Co. v. Javier, 899 A.2d 940, 947 (Md. 2006); Hostetter v. Donlan, 719 P.2d 1243, 1244 (Mont. 1986); Banc of Am. Sec. LLC v. Solow Bldg. Co. II, 847 N.Y.S.2d 49, 56 (App. Div. 2007); Van Cantfort v. Colmar Realty Co., 13 Ohio Law Abs. 499, 501 (Ct. App. 1932); Eckles v. State, 760 P.2d 846, 859 n.20 (Or. 1988).

89. *E.g.*, Gallagher v. Lambert, 549 N.E.2d 136, 140 (N.Y. 1989) (labeling breach of contract "wrongdoing"); Depouw v. Bichette, 833 N.E.2d 744, 746 (Ohio Ct. App. 2005) (calling the breaching promisor a "wrongdoer"); *see also supra* notes 27, 32 and accompanying text. While accepting the Holmesian paradox, Delaware courts hold that the promisor has a mere "pseudo right" to breach a contract and that his conduct is "high-handed" and "faithless." *See* Phila. Storage Battery Co. v. R.C.A., 194 A. 414, 429 (Del. Ch. 1937). Several of these jurisdictions are even more conflicted on this issue. Thus, in Maryland, the intermediate appellate court (the Maryland Court of Special Appeals) has overlooked contrary direction from the highest appellate court (the Maryland Court of Appeals). *Compare* Armstrong v. Stiffler, 56 A.2d 808, 810 (Md. 1948) ("Normally contracts are made to be performed, not to give an option to perform or pay damages."), *with Willard Packaging Co.*, 899 A.2d at 947 (accepting Holmes's observation); *see also* State *ex rel.* Lane v. Dashiell, 75 A.2d 348, 355 (Md. 1950) (terming the breaching party a "repudiator" who bears "all the wrong and reproach that term implies").

90. *See, e.g.*, *In re* Marino, 115 B.R. 863, 870 (Bankr. D. Md. 1990).

91. Melvin A. Eisenberg, *Actual and Virtual Specific Performance, the Theory of Efficient Breach, and the Indifference Principle in Contract Law*, 93 CAL. L. REV. 975, 1018 n.86 (2005); *see also* Kevin M. Teeven, *A Legal History of Binding Gratuitous Promises at Common Law: Justifiable Reliance and Moral Obligation*, 43 DUQ. L. REV. 11, 54 n.228 (2004) (noting that the Holmesian paradox has been "roundly criticized by other commentators").

92. Karl N. Llewellyn, *A Realistic Jurisprudence—The Next Step*, 30 COLUM. L. REV. 431, 437 (1930); *see generally* Perillo, *supra* note 30, at 1085 (devoting an entire law review article to Holmes's "pay or perform" language, and demonstrating that many courts and commentators have construed Holmes's observation out of context).

actual or physical *power*, but not the *right* or the legal authority, to effect a change in the parties' legal relations.[93]

B. *Holmes on "Pay or Perform"—In His Own Words*

Although she relies heavily on the Holmes dictum in claiming that breach of contract is "not a legal wrong,"[94] Professor Shiffrin overlooks Holmes's other statements concerning "pay or perform." While on the bench, Holmes did mention in a one-sentence dictum that a promisor has the option to pay or perform, but he also commented that this rule is a technicality of "the old law."[95] In other cases, he said breach of contract could be punishable as a "crime"[96] and "[b]reach of a legal contract without excuse is wrong conduct."[97] Off the bench, Holmes said the law "always . . . measure[s] legal liability by moral standards"[98] and that the pay

93. Richard R.W. Brooks, *The Efficient Performance Hypothesis*, 116 YALE L.J. 568, 593 (2006) (citing Wesley Newcomb Hohfeld, *Some Fundamental Legal Conceptions as Applied in Judicial Reasoning*, 23 YALE L.J. 16, 44, 52 (1913)). Professor Hohfeld explained his classification of legal rights, duties, privileges, liabilities, powers and immunities as follows:

> Accordingly, the most promising line of procedure seems to consist in exhibiting all of the various relations in a scheme of "opposites" and "correlatives," and then proceeding to exemplify their individual scope and application in concrete cases. . . . :
>
> | | | | | |
> |---|---|---|---|---|
> | {Jural Opposites | rights no-rights | privilege duty | power disability | immunity liability |
> | {Jural Correlatives | right duty | privilege no-right | power liability | immunity disability |

Hohfeld, *supra*, at 30 (corresponding columns).

94. *See* Shiffrin, *supra* note 1, at 727, 737.

95. Globe Ref. Co. v. Landa Cotton Oil Co., 190 U.S. 540, 543 (1903) (stating that "[t]he old law seems to have regarded it as technically in the election of the promisor to perform or to pay damages").

96. United States v. Reynolds, 235 U.S. 133, 150 (1914) (Holmes, J., concurring) (explaining that neither the United States Code nor the Thirteenth Amendment prevents a state from making breach of contract a crime).

97. Bailey v. Alabama, 219 U.S. 219, 246 (1911) (Holmes, J., dissenting).

98. OLIVER WENDELL HOLMES, JR., THE COMMON LAW 25 (American Bar Association ed. 2009) (1881), *cited in* DiMatteo, *supra* note 41, at 329 n.166. Holmes also observed that "[a] legal duty cannot be said to exist if the law intends to allow the person supposed to be subject to it an option at a certain price." Oliver Wendell Holmes, Jr., *The Law Magazine and Review*, 6 AM. L. REV. 723, 724 (1872) (reviewing Frederick Pollock, *Law and Command*, 1 LAW MAG. & REV. 189 (1872)), *reprinted in*

or perform doctrine reflects the viewpoint of the "bad man, who cares only for the material consequences."[99] He never specifically stated that breach was an ethically neutral act.[100] Indeed, Holmes later clarified his "pay or perform" commentary when he wrote, in 1911, "I stick to my paradox as to what a contract was at common law: *not* a promise to pay damages or, etc., but an act imposing a liability to damages *nisi*."[101] Holmes reiterated these thoughts in 1928 when he said, "I don't think a man promises to pay damages in contract any more than in tort. He commits an act that makes him liable for them if a certain event does not come to pass, just as his act in tort makes him liable *simpliciter*."[102]

Holmes's other statements and clarifications prove that his "pay or perform" dictum is "frequently misunderstood"[103] and taken out of context. Breach of contract is a legal wrong because the law will supply damages or equitable relief in a meritorious case. As commentators correctly conclude, "Holmes viewed nonperformance of contract as a legal wrong that compelled compensation," and "[p]aying compensation was not in his view an alternative form of performance or a legal right to which promisors were entitled."[104] The Holmes dictum, properly understood, does not detract from the law's stance on the promisor's accountability to the promisee for breach.

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1 THE COLLECTED WORKS OF JUSTICE HOLMES 294, 296 (Sheldon M. Novick ed. 1995), *cited in* Brooks, *supra* note 93, at 572 n.13.

99. Holmes, *supra* note 85, at 459.

100. *See* Shavell, *supra* note 49, at 457.

101. 1 HOLMES–POLLOCK LETTERS: THE CORRESPONDENCE OF MR. JUSTICE HOLMES AND SIR FREDERICK POLLOCK 1874–1932, at 177 (Mark DeWolfe Howe ed., 1941) [hereinafter HOLMES–POLLOCK LETTERS] (letter of Mar. 12, 1911) (first emphasis added), *cited in* Perillo, *supra* note 30, at 1086 n.4.

102. 2 HOLMES–POLLOCK LETTERS, *supra* note 101, at 233 (letter of Dec. 11, 1928), *cited in* Perillo, *supra* note 30, at 1086 n.6. Along the lines of the UCC viewpoint on pay or perform, see *supra* note 87, Holmes admitted that "when people make contracts, they usually contemplate the performance rather than the breach." HOLMES, *supra* note 98, at 203.

103. Perillo, *supra* note 30, at 1106. In a recent example of the continuing confusion on Holmes's pay or perform theory, Judge Richard Posner incorrectly has asserted that "[Holmes] thought of contracts as options—when you sign a contract in which you promise a specified performance (supplying a product, or providing a service) you buy an option to perform or pay damages." Richard A. Posner, *Let Us Never Blame a Contract Breaker*, 107 MICH. L. REV. 1349, 1350 (2009).

104. Brooks, *supra* note 93, at 572 n.13 (citing Perillo, *supra* note 30, at 1086–89).

V. EFFICIENT BREACH AS A REMEDIAL THEORY

While she does not endorse it on moral grounds,[105] Professor Shiffrin accepts the legal premise of the efficient breach doctrine and asserts that the rule is a "common justification" for the scheme of contract remedies.[106] Much discussed in the legal and economic literature,[107] the theory of efficient breach posits:

> "If a party breaches, and is still better off after paying damages to compensate the victim of the breach, the result is *pareto superior*, that is, considered as a unit, the parties are better off because of the breach and the breach makes no party worse off. Consequently, according to the theory, the party who will benefit from the breach should breach."[108]

Although some decisions do favorably mention this case-law doctrine,[109] as do some commentators,[110] Professor Shiffrin does not

105. Shiffrin, *supra* note 1, at 733 n.47 ("The efficient breach justification is not rejected because it is morally wrong but because it cannot be endorsed by a moral agent and is therefore inconsistent with the imperative to accommodate."). Other commentators state more directly that "[i]f . . . we wish to take seriously the moral force of contracts as promises, then we must conclude that efficient breach is wrong and, as such, should not be encouraged." Frank Menetrez, Comment, *Consequentialism, Promissory Obligation, and the Theory of Efficient Breach*, 47 UCLA L. REV. 859, 879 (2000); *see also id.* at 880 (criticizing efficient breach theory as "schizophrenic," "incoherent," and "find[ing] no support in the ordinary understanding of the morality of promises" because it both acknowledges the binding force of the promise and encourages its unexcused breach).

In her follow-up 2009 *Michigan Law Review* article, Professor Shiffrin modified her 2007 position by observing that the efficient breach doctrine "embraces and encourages immoral action." *See* Shiffrin, *supra* note 5, at 1552.

106. Shiffrin, *supra* note 1, at 730–33.

107. *See, e.g.*, Brooks, *supra* note 93; Amy B. Cohen, *Reviving* Jacob & Youngs, Inc. v. Kent*: Material Breach Doctrine Reconsidered*, 42 VILL. L. REV. 65, 93 n.104 (1997); Eisenberg, *supra* note 91, at 1018 n.86; Dawinder S. Sidhu, *The Immorality and Inefficiency of an Efficient Breach*, 8 TENN. J. BUS. L. 61 (2006).

108. *In re* Grace, No. 7-04-14547 SA, 2008 WL 1766752, at *7 (Bankr. D.N.M. Apr. 14, 2008) (quoting 11 CORBIN ON CONTRACTS § 55.15, at 78 (2005)). The Kaldor–Hicks principle, another economic theory related to efficient breach, has no concerns for whether the non-breaching party is compensated. When the net gain to the breacher exceeds the non-breaching party's loss, the "result is efficient because the world is wealthier." *See* Perillo, *supra* note 30, at 1091 n.40 (citing RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 14–17 (5th ed. 1998)).

109. *E.g.*, Windsor Sec., Inc. v. Hartford Life Ins. Co., 986 F.2d 655, 664 (3d Cir. 1993); Patton v. Mid-Continent Sys., Inc., 841 F.2d 742, 750 (7th Cir. 1988); E.I. DuPont de Nemours & Co. v. Pressman, 679 A.2d 436, 445 (Del. 1996); ConAgra, Inc.

acknowledge that a great majority of jurisdictions have yet to accept it in theory, and still fewer use it to decide cases. As one authority has stated, "[t]he law has not gone as far as the commentators in recognizing the virtues of an efficient breach."[111]

The reasons for that general lack of judicial approval are practical *and* moral. One decision comments, "'[h]ealthy business relationships help the market function efficiently and encourage market activity. Such relationships are almost always disrupted by a breach, whether it is efficient or otherwise.'"[112] Another case observes, "thankfully, there remain a large number of people who live up to contractual obligations as a matter of honor and integrity, even if they could reap greater rewards by breaking their promises."[113] Furthermore, these adverse judicial views on efficient breach are consistent with commercial practices. Commentators have shown how the business world deems efficient breach immoral and unacceptable. One empirical study shows that the overwhelming majority of respondents (105 out of 119) believe that "if a trading partner

v. Nierenberg, 7 P.3d 369, 384–85 (Mont. 2000).

110. *E.g.*, 3 E. ALLAN FARNSWORTH, FARNSWORTH ON CONTRACTS § 12.3 (3d ed. 2004); Fred S. McChesney, *Tortious Interference with Contract Versus "Efficient Breach": Theory and Empirical Evidence*, 28 J. LEGAL STUD. 131, 135–36 (1999).

111. HUNTER, *supra* note 3, § 1:3; *accord* JOSEPH M. PERILLO, CALAMARI AND PERILLO ON CONTRACTS § 14.36 (5th ed. 2003); Craig S. Warkol, Note, *Resolving the Paradox Between Legal Theory and Legal Fact: The Judicial Rejection of the Theory of Efficient Breach*, 20 CARDOZO L. REV. 321, 322 (1998) ("While the theory of efficient breach is widely embraced by law professors, it is widely rejected by the courts.").

Among the many jurisdictions and courts that have yet to approve or mention the efficient breach doctrine are: the United States Supreme Court, the First Circuit, the Federal Circuit, and state courts in Alabama, Alaska, Arizona, Florida, Georgia, Illinois, Maine, Maryland, Pennsylvania, Tennessee, Texas, Utah, Vermont, Virginia, West Virginia, and Wyoming. The relatively few jurisdictions approving the efficient breach theory are actually more equivocal in their endorsement of the doctrine than they acknowledge. Thus, the Seventh Circuit, which is the leading proponent of efficient breach, *see, e.g.*, *Patton*, 841 F.2d at 750, also unqualifiedly calls the breaching promisor a "wrongdoer" and the promisee an "injured party" or a "victim." *See* Emerald Invs. Ltd. P'ship v. Allmerica Fin. Life Ins. & Annuity Co., 516 F.3d 612, 616 (7th Cir. 2008) (using the term "victim"); Morgan v. Inter-Continental Trading Corp., 360 F.2d 853, 855 (7th Cir. 1966) (using the term "wrongdoer"). Further, the Seventh Circuit has consistently endorsed the implied covenant of good faith and fair dealing, which is antithetical to any doctrine that encourages intentional contract-breaking. *See, e.g.*, E.B. Harper & Co. v. Nortek, Inc., 104 F.3d 913, 919 (7th Cir. 1997); Jordan v. Duff & Phelps, Inc., 815 F.2d 429, 435 (7th Cir. 1987).

112. *In re Grace*, 2008 WL 1766752, at *7 n.16 (quoting 11 JOSEPH M. PERILLO, CORBIN ON CONTRACTS § 55.15 (Rev. ed. 2005)).

113. Chesapeake Corp. v. Shore, 771 A.2d 293, 353 n.146 (Del. Ch. 2000).

deliberately breaches a contract" because it can obtain a better deal elsewhere, such behavior is unethical.[114] In the same survey, a strong majority (96 out of 119) said that they would always or almost always withhold future business from a party that had willfully breached, and further said that such conduct would increase the likelihood of litigation with that party.[115]

Prominent scholars provide additional criticism of the doctrine. After an extensive analysis, Professor Joseph Perillo asserts that efficient breach theory "is not, and should not be, the basis of normative determinations in the legal system."[116] His major observation is that the cause of action for tortious interference with contract "severely conflicts with the notion that willful efficient breaches are desired by the legal system."[117] Here, he reasons that the law cannot both encourage willful, efficient breach and penalize the third-party promisor in tort when the tortfeasor induces the promisor to violate the contract.[118] Professor Melvin Eisenberg points out that the efficient breach theory conflicts with the rule of consequential damages under *Hadley v. Baxendale* because it encourages promisor opportunism in the decision to breach.[119] He first notes that under efficient breach, "the decision to perform or to breach a contract should depend on the costs and benefits of breach to parties" when the breach occurs.[120] Under *Hadley*, however, "the seller, in determining whether to breach, can disregard all reasonably foreseeable costs except those he has reason to know are probable at the time the contract is made."[121] Lastly, Professor Lawrence Cunningham notes that the efficient breach doctrine does not lend itself to distinguishing between efficient and inefficient breaches because it unrealistically "assumes judges and contracting parties can easily and objectively determine the amount or value of damages incurred and

114. David Baumer & Patricia Marschall, *Willful Breach of Contract for the Sale of Goods: Can the Bane of Business be an Economic Bonanza?*, 65 TEMP. L. REV. 159, 165 (1992).

115. *Id.* at 166.

116. Perillo, *supra* note 30, at 1106.

117. *Id.* at 1100.

118. *Id.*; *see also* Wolnak v. Cardiovascular & Thoracic Surgeons of Cent. Wis., 706 N.W.2d 667, 677 n.5 (Wis. Ct. App. 2005) ("To say there is nothing wrong with urging someone to break a valid contract so as to join someone else in a business venture would seem to eviscerate tortious interference as a cause of action.").

119. Melvin A. Eisenberg, *The Principle of* Hadley v. Baxendale, 80 CAL. L. REV. 563, 587 (1992).

120. *Id.*

121. *Id.*

the amount or value of profits saved."[122] He further asserts that the theory gives little or no weight to potentially significant transaction costs, including the costs of negotiation, search, and dispute resolution.[123]

The courts and commentators make a strong legal and moral case against the efficient breach doctrine. Efficient breach is not a contractually express or implied escape hatch for parties seeking to overturn their agreements. The rule cannot stand with the precept that "[t]he parties to the contract in essence create a mini-universe for themselves, in which each voluntarily chooses his contracting partner, each trusts the other's willingness to keep his word and honor his commitments, and in which they define their respective obligations, rewards and risks."[124] For all the above reasons, and contrary to Professor Shiffrin's position, efficient breach theory has not become a "common justification" for the scheme of contract remedies and does not, in most jurisdictions, undermine the promisor's accountability to the promisee for breach.

VI. SPECIFIC PERFORMANCE VERSUS EXPECTATION DAMAGES

A. *Shiffrin on Specific Performance*

Professor Shiffrin argues that the law diverges from morality because she claims that a party cannot obtain an order of specific performance when it successfully alleges the promisee's anticipatory repudiation.[125] She

122. Cunningham, *supra* note 34, at 1450.

123. *Id.* On the same basis, the *Restatement (Second) of Contracts* gives a lukewarm endorsement to efficient breach, noting concerns about the valuation of damages and the problems of transaction costs. *See* RESTATEMENT (SECOND) OF CONTRACTS ch. 16, introductory n. (1981); *see also* Frank J. Cavico, Jr., *Punitive Damages for Breach of Contract: A Principled Approach*, 22 ST. MARY'S L.J. 357, 372–75 (1990) (providing an excellent summary of the problems with efficient breach theory); Cohen, *supra* note 107, at 93–94 n.104 (citing several articles discussing the efficient breach theory).

124. Erlich v. Menezes, 981 P.2d 978, 987 (Cal. 1999) (quoting Applied Equip. Corp. v. Litton Saudi Arabia Ltd., 869 P.2d 454, 461 (Cal. 1994)).

125. *See* Shiffrin, *supra* note 1, at 723 ("[O]ne cannot obtain an order of specific performance even when one successfully alleges anticipatory repudiation."); *see also id.* ("The difference between the moral and legal reaction to breach does not appear [until] only after the specified time for performance elapses.").

"Anticipatory repudiation" exists when a party to an executory contract manifests an unambiguous and unequivocal intent, before the time fixed in the contract, that it will not render timely performance. *See* Leazzo v. Dunham, 420 N.E.2d 851, 854 (Ill. App. Ct. 1981) (citing Keep Prods., Inc. v. Arlington Park Towers Hotel Corp., 364 N.E.2d 939 (Ill. App. Ct. 1977); Hull v. Croft, 132 Ill. App. 509, 510

also contends that the law generally diverges from morality on the choice between specific performance and damages for breach because, except in special circumstances, damages will be the rule and actual performance is not judicially required, even when it is possible.[126] In making these criticisms, she observes that "[o]n the contrary, moral observers would direct that the performance should occur as promised, unless the promisee waives."[127] Further, she asserts that the law, in considering specific performance, gives secondary importance to morality by taking refuge in the "distinctive features associated with law and legal mechanisms."[128] These distinctive features include "the difficulty and expense of ordering and supervising performance by a reluctant party and, in some cases, the unseemly and disproportionately domineering nature of such state enforced orders on individuals."[129]

(Ill. App. Ct. 1907); Engesette v. McGilvray, 63 Ill. App. 461, 464 (Ill. App. Ct. 1896); 17 AM. JUR. 2D *Contracts* § 450 (1964); 4 ARTHUR CORBIN, CORBIN ON CONTRACTS § 973 (1951); 11 SAMUEL WILLISTON, A TREATISE ON THE LAW OF CONTRACTS § 1323 (3d ed. 1968)). It also encompasses instances when "reasonable grounds support the obligee's belief that the obligor will breach the contract" and when the obligee demands adequate assurance of performance, but the obligor does not give such assurance. Danzig v. AEC Corp., 224 F.3d 1333, 1337–38 (Fed. Cir. 2000).

126. Shiffrin, *supra* note 1, at 723. As an example of a special circumstance, Professor Shiffrin cites the rule from UCC § 2-716 "that specific performance may be available when goods are unique, the buyer cannot find cover, and under other 'proper circumstances.'" *Id.* at n.26.

127. *Id.* at 723. Professor Shiffrin asserts that the doctrine of efficient breach is the reason the law disfavors specific performance. *See id.* at 731. Case law refutes her argument. *See* Mass. Mut. Life Ins. Co. v. Associated Dry Goods Corp., 786 F. Supp. 1403, 1424 n.31 (N.D. Ind. 1992) (noting that the efficient breach doctrine "is of little assistance to a court in equity determining whether to order specific performance of a contract").

128. *See* Shiffrin, *supra* note 1, at 733. Professor Shiffrin explains:

> Whether or not these grounds are persuasive, they are distinctively legal. They do not question the general proposition that specific performance is the appropriate moral response to breach or anticipatory repudiation; rather, they resist the idea that specific performance should be implemented through legal means because of distinctive features associated with law and legal mechanisms.

Id.

129. *Id.*; *see also* 3 D. DOBBS, LAW OF REMEDIES § 12.8(3)–(4) (2d ed. 1993) (noting that "[c]ourts will not specifically enforce contracts if they regard enforcement as futile, impractical, . . . too demanding upon judicial resources," or unfair).

B. *The Modern View of Specific Performance Versus Damages*

Professor Shiffrin's first criticism regarding the supposed unavailability of specific performance after an anticipatory repudiation is readily addressed, because she has erroneously stated the law.[130] Longstanding precedent establishes that a court may indeed grant specific performance instead of damages in the face of anticipatory repudiation, provided the injunctive remedy meets equitable requirements:

> [B]y analogy to the general rule that a renunciation of a contract before time for performance gives the adverse party an option to treat the entire contract as breached and sue immediately for damages as for total breach, when a contract is of that general class of contracts that equity will specifically enforce, upon such a repudiation of the contract by one party, the adverse party may at his or her election sue for specific performance notwithstanding the time has not arrived for complete performance of the contract.[131]

Her second objection—that the law, in denying specific performance, will evade moral questions by relying excessively on the distinct normative features associated with the law and legal mechanisms—warrants more extensive examination.[132]

First, a brief summary will show Professor Shiffrin's incomplete analysis of the legal issues, particularly regarding the difference between the rules the courts commonly cite and the standards they actually employ. "Specific performance is an equitable remedy which compels the performance of a contract on the precise terms agreed upon or such a substantial performance as will do justice between the parties under the circumstances."[133] Although specific performance is a matter of sound

130. *See* Shiffrin, *supra* note 1, at 722–23.

131. 71 AM. JUR. 2D *Specific Performance* § 206 (2001); *accord* RESTATEMENT (SECOND) OF CONTRACTS § 357 (1)–(2), cmt. a (1981) (providing for specific performance against a threatened breach of contract); 5A ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 1141 (1964) (noting the availability of specific performance against breach of contract); *see also* Far W. Fed. Bank, S.B. v. Office of Thrift Supervision, 119 F.3d 1358, 1365–66 (9th Cir. 1997) (stating that the aggrieved party in reacting to the repudiation has the option of damages, restitution, or specific performance); Dixon v. Anderson, 252 F. 694, 695–96 (4th Cir. 1918); Saliba v. Brackin, 69 So. 2d 267, 269 (Ala. 1953); Bonde v. Weber, 128 N.E.2d 883, 891 (Ill. 1955); Cavanagh v. Cavanagh, 598 N.E.2d 677, 679 (Mass. App. Ct. 1992); Miller v. Jones, 71 S.E. 248, 249 (W. Va. 1911).

132. *See* Shiffrin, *supra* note 1, at 733.

133. McCoy Farms, Inc. v. J & M McKee, 563 S.W.2d 409, 415 (Ark. 1978).

judicial discretion,[134] a traditional case law prerequisite, as Professor Shiffrin points out, is the inadequacy of damages to protect the promisee's expectation interest.[135] A number of courts still cite this common law factor in considering the two remedies. For example, the United States Court of Appeals for the Seventh Circuit has said that the "normal remedy" for breach of contract is the award of damages, and that specific performance is an "exceptional" remedy that "comes into play when damages are inadequate, whether because of the defendant's lack of solvency or because of the difficulty of quantifying the injury to the victim."[136] The common law also had some fairly hard and fast rules categorizing particular contracts as suitable (or not suitable) for specific performance. To illustrate, the traditional adequacy test usually denies specific performance of most contracts for building, construction, or repair projects[137] and for personal services contracts involving skill, labor, and judgment,[138] but the opposite is true for most land transfer contracts.[139]

Although various courts continue to give "lip service"[140] to the traditional adequacy rule described above, prominent commentators have noted that in practice, specific performance has become widely available.[141] In contrast with the more rigid common law standard, the modern approach is that the remedy generally is not as limited to special categories of contracts,[142] and the trend is to relax the damages prerequisite.[143] "Courts have been increasingly willing to order performance in a wide variety of cases involving output and requirements contracts, contracts for the sale of a business or of an interest in a business represented by shares

134. All Star Constr. Co. v. Koehn, 741 N.W.2d 736, 740–41 (S.D. 2007); Cangiano v. LSH Bldg. Co., 623 S.E.2d 889, 894 (Va. 2006); *see also* 3 DOBBS, *supra* note 129, § 12.8(4) (noting that the scope of equitable discretion in granting or denying specific performance is broad and case-specific).

135. *See* Shiffrin, *supra* note 1, at 723, 723 n.26 (citing RESTATEMENT (SECOND) OF CONTRACTS § 359(1)).

136. Miller v. LeSea Broad., Inc., 87 F.3d 224, 230 (7th Cir. 1996).

137. 3 DOBBS, *supra* note 129, § 12.19(3).

138. *Id.* § 12.21(4). *But see id.* § 12.22(2) (noting that not every contract with an element of service in it qualifies as a "personal service" contract).

139. *Id.* §§ 12.8(2), 12.10, 12.11(3), 12.12(3).

140. Osborne v. Bullins, 549 So. 2d 1337, 1340 (Miss. 1989).

141. *See* 5A CORBIN, *supra* note 43, §§ 1142–1155; Linzer, *supra* note 20, at 126–30.

142. 3 DOBBS, *supra* note 129, § 12.8(2); Linzer, *supra* note 20, at 126–30.

143. Gudenau v. Bierria, 868 P.2d 907, 912 n.5 (Alaska 1994).

of stock, and covenants not to compete."[144] To the same end, the UCC has liberalized the standards for granting specific performance in contracts for the sale of goods.[145] Some states follow even more expansive rules. For example, Louisiana holds that specific performance is the preferred, albeit not the automatic, remedy for breach of contract.[146]

The formalistic requirement that specific performance is available only with no adequate remedy at law is a vestige of the ancient common law division between law and equity and the policy that equity courts would not interfere with the business of the law courts.[147] The trend over the past thirty years is to compare damages versus specific performance to determine which remedy would be more effective and to resolve any doubts in favor of granting specific performance.[148] This comparison, which has been called a moral approach, "often appears in the cases."[149]

144. RESTATEMENT (SECOND) OF CONTRACTS ch. 16, topic 3 introductory n. (1981).

145. U.C.C. § 2-716, cmt. 1 (1977). Professor Shiffrin correctly notes the UCC view in a footnote. *See* Shiffrin, *supra* note 1, at 723 n.26.

146. Concise Oil & Gas P'ship v. La. Intrastate Gas Corp., 986 F.2d 1463, 1471 (5th Cir. 1993) (citing J. Weingarten, Inc. v. Northgate Mall, Inc., 404 So. 2d 896, 897, 899 (La. 1981)), *reh'g. denied*, 990 F.2d 1254 (5th Cir. 1993). Prominent commentators have taken a similar position. *See* Alan Schwartz, *The Case for Specific Performance*, 89 YALE L.J. 271, 271 (1979) (arguing "that the remedy of specific performance should be as routinely available as the damages remedy"); Thomas S. Ulen, *The Efficiency of Specific Performance: Toward a Unified Theory of Contract Remedies*, 83 MICH. L. REV. 341, 401 (1984) (concluding that "economic efficiency considerations urge specific performance as the routine remedy"). For an extensive discussion of specific performance versus damages, see Edward Yorio, *In Defense of Money Damages for Breach of Contract*, 82 COLUM. L. REV. 1365 (1982).

147. 3 DOBBS, *supra* note 129, § 12.8(2). Indeed, one commentator persuasively has concluded in an exhaustive study that the adequate-remedy-at-law test no longer has any real impact in the decided cases. *See* Douglas Laycock, *The Death of the Irreparable Injury Rule*, 103 HARV. L. REV. 687, 771 (1990), approved in *In re* Ward, 194 B.R. 703, 711 n.30 (Bankr. D. Mass. 1998).

148. RESTATEMENT (SECOND) OF CONTRACTS § 359 cmt. a (stating "[s]uch a comparison will often lead to the granting of equitable relief"); FARNSWORTH, *supra* note 110, § 12.6 (indicating that the adequacy test "has tended to become relative"); *accord* Nemer Jeep-Eagle, Inc. v. Jeep-Eagle Sales Corp., 992 F.2d 430, 436 (2d Cir. 1993); Trans Pac. Leasing Corp. v. Aero Micr., Inc., 26 F. Supp. 2d 698, 710 (S.D.N.Y. 1998) (quoting RESTATEMENT (SECOND) OF CONTRACTS § 359 cmt. a); Mid-Continent Tel. Corp. v. Home Tel. Co., 319 F. Supp. 1176, 1197 (N.D. Miss. 1970) (finding that under modern practice, courts "will examine both remedies to determine which is more likely to do substantial justice in th[e] case"); 81A C.J.S. *Specific Performance* § 6 (2008).

149. Linzer, *supra* note 20, at 127.

As the Mississippi Supreme Court observed, "[w]here a contracting party can feasibly be given what he bargained for, where is the justice in decreeing a substitute?"[150] A court also may award specific performance because the defendant has violated the implied covenant—and moral imperative—of good faith and fair dealing.[151] Accordingly, when courts decide between damages and specific performance, "there is often at least a hint of the view that people should be held to their promises and that the only effective way to do this is to grant specific performance."[152]

Instead of evading moral issues and relying on administrative objections, modern courts note that "the 'difficulty of enforcement' idea is exaggerated."[153] The trend regarding the weight of institutional concerns is to favor specific performance "if the claimant's need is great or a substantial public interest is involved."[154] These decisions forthrightly give high importance to justice and morality on a sliding scale with administrative issues to determine if specific performance is the appropriate response to a breach of contract. When the claimant has a greater need for relief or when the public interest favors specific performance, institutional or practical concerns become less important, and vice versa.[155] Even beyond this weighing of legal and normative concerns, moreover, it can be argued that specific performance will be a matter of right and not just of judicial discretion. When (1) a court has jurisdiction over the case, (2) the granting of relief would conform with equitable principles, and (3) no valid objection exists, such as to the enforceability of the contract or with the superior intervening rights of innocent third parties, then (4) it will be as much a matter of course—and even a matter of right—for a court to decree specific performance as compared with damages.[156]

150. Osborne v. Bullins, 549 So. 2d 1337, 1340 (Miss. 1989).

151. *E.g.*, *In re* Edgewater Med. Ctr., 373 B.R. 845, 860 (Bankr. N.D. Ill. 2007) (in context of contract for land); Chariot Holdings, Ltd. v. Eastmet Corp., 505 N.E.2d 1078, 1085–86 (Ill. App. Ct. 1987) (deceptive actions in contract for land).

152. N.J. Indus. Props., Inc. v. Y.C. & V.L., Inc., 495 A.2d 1320, 1329 (N.J. 1985) (quoting Linzer, *supra* note 20, at 130).

153. 3 FARNSWORTH, *supra* note 110, § 12.7 (citing Grayson-Robinson Stores v. Iris Constr. Corp., 168 N.E.2d 377, 379 (N.Y. 1960)).

154. *Id.*

155. RESTATEMENT (SECOND) OF CONTRACTS § 366 cmt. a (1981).

156. *See In re* Stokes, 198 B.R. 168, 179 (Bankr. E.D. Va. 1996) (citing Haythe v. May, 288 S.E.2d 487, 488 (Va. 1982)) (decreeing specific performance as the remedy for breach of a settlement agreement); Radiophone Broad. Station v. Imboden, 191 S.W.2d 535, 537 (Tenn. 1946) (applying specific performance to a contract to sell land).

Professor Shiffrin cites almost none of the above precepts and developments. She is incorrect that specific performance is not available for anticipatory repudiation.[157] She is incorrect that specific performance is not "commonly invoked."[158] She also implicitly relies on the fading view of specific performance as a disfavored remedy available only in special circumstances under rigid classifications.[159] Contrary to Professor Shiffrin's view, the courts, in considering this equitable relief, characteristically do not subvert the moral issues to administrative ones. With respect to the availability of specific performance, no divergence exists between promise and contract as courts hold the promisor accountable to the promisee for breach.

VII. CONTRACT LAW AND PUNITIVE DAMAGES: AN ASCENDING DOCTRINE

A. *Punitive Damages: The Conventional View*

The issue of punitive damages most commonly arises in tort cases when courts punish and deter the wrongdoer for his invasion of the victim's property or personal interests. As Professor Shiffrin correctly indicates, many authorities hold that punitive damages cannot be obtained for a mere breach of contract, no matter how egregious the default.[160]

The cases have advanced various rationales for this viewpoint. One reason is that the use of punitive damages as a legal compulsion to perform contracts "would tend to substitute the coercive power of the courts for the freedom of the marketplace."[161] A second justification is that contract injuries are easier to value than tortious ones.[162] A third is that breach of

157. *See, e.g.*, Yitzhaki v. Sztaberek, 831 N.Y.S.2d 267, 269 (App. Div. 2007) (allowing specific performance as a remedy in an anticipatory repudiation case); *supra* note 131 and accompanying text.

158. Shiffrin, *supra* note 1, at 724. For examples of the many cases invoking specific performance, see *Stokes*, 198 B.R. at 179–80 (Virginia case), and *Radiophone*, 191 S.W.2d at 537 (Tennessee case).

159. *See, e.g.*, Asbury v. Crawford Elec. Coop., 51 S.W.3d 152, 158 (Mo. Ct. App. 2001) (allowing specific performance to be granted when needed to ensure complete justice between two parties).

160. *See* Shiffrin, *supra* note 1, at 723 (citing RESTATEMENT (SECOND) OF CONTRACTS § 355); *see also* Oliver v. Mustafa, 929 A.2d 873, 879 n.3 (D.C. 2007); Drinkwater v. Patten Realty Corp., 563 A.2d 772, 776 (Me. 1989).

161. Ennen v. Pub. Serv. Mut. Ins. Co., 774 F.2d 321, 326 (8th Cir. 1985) (citing Pogge v. Fullerton Lumber Co., 277 N.W.2d 916, 919 (Iowa 1979)).

162. Thyssen, Inc. v. S.S. Fortune Star, 777 F.2d 57, 63 (2d Cir. 1985).

contract does not ordinarily engender as much resentment or mental or physical discomfort as a tort, and no valid retributive purpose would be served thereby.[163] The most frequent justification, however, is that punitive damages for breach of contract would inappropriately punish the promisor and unfairly give the promisee a windfall, as opposed to his expectation interest.[164] Undoubtedly, these policies have some weight, which accounts for the traditional reluctance to award punitive damages for a breach of contract.

B. *The Evolution of Contractual Punitive Damages*

The conventional view disfavoring punitive damages in contract cases is now in decline. What Professor Shiffrin omits is that over the last twenty years, courts have increasingly allowed punitive damages for breach of contract as they have "broken down the doctrinal barriers between contracts and torts."[165] The distinction was always weak, as courts have commented frequently upon the "'borderland [between contract and tort actions], where the lines of distinction are shadowy and obscure. . . ."[166] Along similar lines, courts observe that no clear distinction exists between compensatory and punitive damages because an expectation damages

163. *Id.* (quoting 5 CORBIN, *supra* note 125, § 1077) (internal quotations omitted)). *Compare* Epperly v. Johnson, 734 N.E.2d 1066, 1073 (Ind. Ct. App. 2000) ("Breaches of contract will almost invariably be regarded by the complaining party as oppressive, if not outright fraudulent . . . ."). *See generally* Cavico, *supra* note 123, at 366–69 (discussing traditional policies for denying punitive damages in contract cases).

164. *See* Platinum Tech., Inc. v. Fed. Ins. Co., 282 F.3d 927, 932–33 (7th Cir. 2002); Rosener v. Sears, Roebuck & Co., 168 Cal. Rptr. 237, 242 (Ct. App. 1980); Perroncello v. Donahue, 859 N.E.2d 827, 832 (Mass. 2007) (citing Situation Mgt. Sys., Inc. v. Malouf, Inc., 724 N.E.2d 699 (Mass. 2000)); Madden v. Hanson, No. 98-2401, 1999 WL 33479, at *2 (Wis. Ct. App. Jan. 28, 1999); 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, 1571 (1986) ("The fear of overcompensating contract plaintiffs is undoubtedly the most important single basis for the traditional rules against recovery of punitive and nonpecuniary damages in contract.").

165. 1 LINDA L. SCHLUETER, PUNITIVE DAMAGES § 7.0 (5th ed. 2005).

166. Carvel Corp. v. Noonan, 350 F.3d 6, 16 (2d Cir. 2003) (quoting Rich v. N.Y. Cent. & Hudson River R.R. Co., 87 N.Y. 382, 390 (1882)); *accord* Sommer v. Fed. Signal Corp., 593 N.E.2d 1365, 1368 (N.Y. 1992); CLL Assocs. v. Arrowhead Pac. Corp., 497 N.W.2d 115, 120–21 (Wis. 1993) (Abrahamson, J., dissenting) (stating that "[c]ourts and commentators have recognized that a single set of facts may give rise to actions both in contract and in tort, making it difficult to draw a clear distinction between the two actions"); Timothy J. Sullivan, *Punitive Damages in the Law of Contract: The Reality and Illusion of Legal Change*, 61 MINN. L. REV. 207, 225 (1977).

remedy for breach of contract "possess[es] a deterrent and punitive aspect as well."[167] Based on the foregoing, courts accurately conclude that the supposed general prohibition of punitive damages in contract cases "'has never really been the impenetrable barrier it has appeared to be.'"[168]

The moral and policy arguments favoring punitive damages in contract cases for willful breach are gaining judicial traction. The emerging policy for contractual punitive damages is that a valid desire can exist to punish a faithless promisor or to deter against the abuse of economic power.[169] Such opportunistic breaches "do not increase societal wealth,"[170] and "[t]hey have 'no economic justification and ought simply to be deterred.'"[171] In a contractual punitive damages case, the New Mexico Supreme Court observed along these lines: "Overreaching, malicious, or wanton conduct such as targeted by [punitive damages] is inconsistent with legitimate business interests, violates community standards of decency, and tends to undermine the stability of expectations essential to contractual relationships."[172] Indeed, a sharp upsurge has occurred in the number and

167. TVT Records v. Island Def Jam Music Group, 279 F. Supp. 2d 413, 424 (S.D.N.Y. 2003), *rev'd on other grounds*, 412 F.3d 82 (2d Cir. 2005); Romero v. Mervyn's, 784 P.2d 992, 1001 n.6 (N.M. 1989) (citing CORBIN, *supra* note 125, § 1077) ("[P]unitive damages long have been recognized as an appropriate remedy in situations in which exposure merely to compensatory damages is an inadequate deterrent to prevent . . . oppressive conduct."); *see also* 5 CORBIN, *supra* note 125, § 1002 (noting that expectation damages have multiple purposes including compensation for loss, substitution for personal vengeance, and deterrence of other breaches).

168. *See* Linscott v. Rainier Nat'l Life Ins. Co., 606 P.2d 958, 963 (Idaho 1980) (quoting Sullivan, *supra* note 166, at 246–47).

169. *See* RESTATEMENT (SECOND) OF CONTRACTS § 355 (1979) (noting an exception allowing punitive damages in cases in which "the conduct constituting the breach is also a tort for which punitive damages are recoverable"); SCHLUETER, *supra* note 165, §§ 7.2–7.3 (discussing general rules of contract damages and exceptions to such rules); *see also* Sullivan, *supra* note 166; Randy L. Sassaman, Note, *Punitive Damages in Contract Actions—Are the Exceptions Swallowing the Rule?*, 20 WASHBURN L.J. 86 (1980).

170. William S. Dodge, *The Case for Punitive Damages in Contracts*, 48 DUKE L.J. 629, 698 (1999).

171. *See id.* (citing POSNER, *supra* note 108, at 130); *see also* Forty Exch. Co. v. Cohen, 479 N.Y.S.2d 628, 639 (Civ. Ct. 1984) (quoting 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, 434, 440 (1981) ("A promisor often finds breach attractive . . . because he expects never to pay for that liability.")).

172. *Romero*, 784 P.2d at 1001; *see also* Jackson v. Johns-Manville Sales Corp., 781 F.2d 394, 403 (5th Cir. 1986) (stating that "punitive damages reward individuals who serve as 'private attorneys general' in bringing wrongdoers to account" (citing

amount of punitive damage awards in contract cases, which further shows the law's receptiveness to this remedy in the interests of justice.[173]

The law's increasing acceptance of punitive damages in contract cases is best understood by examining the numerous qualifications of the general rule. The most widely used punitive damages exception, as Professor Shiffrin acknowledges, is for a breach of contract that also constitutes an independent tort for which punitive damages would be appropriate.[174] In many jurisdictions, a wide variety of independent torts committed under aggravated circumstances can justify a contractual punitive damages claim, including "conversion, forgery, breach of a fiduciary duty, tortious interference with business relationships, [and] intentional breaches of contract when accompanied by 'willful acts of violence, malicious, or oppressive conduct'" or fraudulent misrepresentation (the most frequently used exception).[175] Notably, eighteen jurisdictions allow punitive damages for a willful or malicious breach of the implied covenant of good faith and fair dealing with proof of a special relationship between the parties, such as insurer–insured, bank–depositor, employer–employee, franchisor–franchisee, lawyer–client, public utility–customer, and security broker–customer.[176] Even the independent-tort exception is not always strictly enforced; sometimes, the "tort" is little more than one party's refusal to perform after accepting the other party's performance.[177]

Indiana v. Veal, 354 So. 2d 239, 247 (Miss. 1977)); Quigley v. Pet, Inc., 208 Cal. Rptr. 394, 402 (Ct. App. 1984) (noting that the "threat of retribution [through punitive damages] may discourage unethical business practices"); Employers Mut. Cas. Co. v. Tompkins, 490 So. 2d 897, 906 (Miss. 1986) ("[T]he right to seek punitive damages serves a valid and justiciable place in our system of jurisprudence.").

173. *See* ERIK MOLLER, TRENDS IN CIVIL JURY VERDICTS SINCE 1985, at 34 (1996) (noting that approximately 47% of punitive damage awards are in business contract cases); Russell J. Weintraub, *A Survey of Contract Practice and Policy*, 1992 WIS. L. REV. 1, 8 n.28 (1992) (citing MARK PETERSON ET AL., PUNITIVE DAMAGES: EMPIRICAL FINDINGS viii, 23–24 (1987)). Professor Shiffrin acknowledges that this trend has been reported, but she believes that "[i]t is difficult to know what to make of" such reports "without further details of the cases involved and the nature of the successful claims." Shiffrin, *supra* note 1, at 724 n.32.

174. Shiffrin, *supra* note 1, at 723 n.27. *See also, e.g.*, Strum v. Exxon Co., 15 F.3d 327, 330 (4th Cir. 1994); Grynberg v. Citation Oil & Gas Corp., 573 N.W.2d 493, 500 (S.D. 1997); Hayseeds, Inc. v. State Farm Fire & Cas., 352 S.E.2d 73, 80 (W. Va. 1986). Professor Shiffrin correctly points out some states allow these damages for bad faith breach of contract. Shiffrin, *supra* note 1, at 723 n.27.

175. SCHLUETER, *supra* note 165, § 7.3.

176. *Id.*

177. *See* Excel Handbag Co. v. Edison Bros. Stores, 630 F.2d 379, 385 (5th Cir. 1980) (discussing the defendant's conscious decision to take goods wrongfully and to

In still other qualifications, some states have dispensed with the independent tort prerequisite altogether and hold that punitive damages can be available for breach of contract with willful, fraudulent, or malicious conduct.[178] Next, the collateral source rule—the tort doctrine that a wrongdoer may not receive a credit for monies the victim receives from independent sources—has a punitive damages element and has been approved in contract cases with a tortious breach or where the equities favor the plaintiff.[179] Parties may stipulate that a breach will result in punitive damages even when the contract action alone will not support a punitive damages award.[180] Many consumer protection statutes allow supra-compensatory damages for an immoral, abusive, or malicious breach of contract.[181] The United States Supreme Court has held that an

withhold payment therefor for the purpose of forcing the plaintiff to relinquish some of its legal rights), *analyzed in* Clark A. Remington, *Intentional Interference with Contract and the Doctrine of Efficient Breach: Fine Tuning the Notion of the Contract Breacher as Wrongdoer*, 47 BUFF. L. REV. 645, 696 n.162 (1999).

178. *E.g.*, Boise Dodge, Inc. v. Clark, 453 P.2d 551, 556 (Idaho 1969); Hood v. Fulkerson, 699 P.2d 608, 611–12 (N.M. 1985); *see also* Dodge, *supra* note 170, at 645 (finding twelve states that "either expressly allow or appear to allow punitive damages" without an independent tort). Disagreeing with the independent-tort prerequisite for the award of contractual punitive damages, an Illinois Supreme Court Justice cogently observed:

> Absent the assessment of punitive damages, a wilful violator of a contract incurs no sanction and bears only the costs of performance under the terms and conditions of his agreement. In many instances, the sum awarded is not subject to prejudgment interest, and absent a specific provision, the wronged party cannot recover his attorney fees. *No rational basis presents itself for holding that wilful misconduct arising out of a breach of contract should not be discouraged in the same manner as wilful misconduct resulting in a tort.*

Morrow v. L.A. Goldschmidt Assoc., 492 N.E.2d 181, 186 (Ill. 1986) (Goldenhersh, J., dissenting) (emphasis added).

179. *See* LaSalle Talman Bank, F.S.B. v. United States, 317 F.3d 1363, 1372 (Fed. Cir. 2003); Metoyer v. Auto Club Family Ins. Co., 536 F. Supp. 2d 664, 667–70 (E.D. La. 2008). *But see* Corl v. Huron Castings, Inc., 544 N.W.2d 278, 286 (Mich. 1996) (finding the collateral source rule inapplicable in contract cases).

180. Gold Rush Invs., Inc. v. G.E. Johnson Constr. Co., 807 P.2d 1169, 1176–77 (Colo. Ct. App. 1990).

181. *See, e.g.*, Fair Debt Collection Practices Act, 15 U.S.C. § 1692k (2006) (allowing enhanced damages against debt collectors based on the nature, intent, frequency, and persistence of their noncompliance with the statutory procedures); Utzler v. Braca, 972 A.2d 743, 756 (Conn. App. Ct. 2009) ("'A court may exercise its discretion to award punitive damages'" for a violation of the Connecticut Unfair Trade Practices Act when evidence "'reveal[s] a reckless indifference to the rights of others or

arbitration contract may authorize the arbitrator to impose punitive damages.[182] What one commentator terms "covert" punitive damages[183] exist under doctrines which provide that the willfulness of the breach justifies a lesser degree of certainty in the proof of the amount of damages[184] or of the foreseeability of consequential damages.[185] Similarly, under some decisions, an intentional breach of a building or construction contract justifies compensation for the higher cost of repair or replacement versus the lower diminished value of the work.[186] Another de facto punitive damages rule still followed in some states is that when a party inexcusably stops short of complete performance, it may not obtain restitution for the value of part performance.[187]

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an intentional and wanton violation of those rights'" (quoting Votto v. Am. Car Rental, Inc., 871 A.2d 981 (Conn. 2005))); *see also* Mont. Code Ann. § 27-1-220(2)(a) (2007) (providing that punitive damages are awardable in contract cases only when allowed by statute).

182. Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52, 61–62 (1995) (quoting Mastrobuono v. Shearson Lehman Hutton, Inc., 20 F.3d 717, 717 (7th Cir. 1994)) (observing that punitive damage claims arise with "great frequency" in arbitration matters).

183. Sebert, *supra* note 164, at 1642–47; *see also* Steve Thel & Peter Siegelman, *Willfulness Versus Expectation: A Promisor-Based Defense of Willful Breach Doctrine*, 107 MICH. L. REV. 1517, 1518 (2009) ("[I]n reality, courts frequently award promisees more than their expectation when they find that a breach is willful, and thus act to deprive willful breachers of any gains from breach.").

184. *See* Bell BCI Co. v. United States, 81 Fed. Cl. 617, 637 (2008) (citing Locke v. United States, 283 F.2d 521, 524 (Ct. Cl. 1960)) ("The defendant who has wrongfully broken a contract should not be permitted to reap advantage from his own wrong by insisting on proof which by reason of his breach is unobtainable."); *see also* Boyce v. Soundview Tech. Group, 464 F.3d 376, 391–92 (2d Cir. 2006) (noting that a breaching party should not escape liability due to uncertainty of amount of damages).

185. *See* CHARLES T. MCCORMICK, HANDBOOK ON THE LAW OF DAMAGES §§ 140–141 (1935).

186. *E.g.*, Groves v. John Wunder Co., 286 N.W. 235, 236–37 (Minn. 1939); Roudis v. Hubbard, 574 N.Y.S.2d 95, 96 (App. Div. 1991). *But see* Peevyhouse v. Garland Coal & Mining Co., 382 P.2d 109, 114 (Okla. 1962), *cert. denied*, 375 U.S. 906 (1963) (awarding as damages the difference in market value). A similar focus on promisor good faith guides courts on whether to apply the "substantial performance" doctrine in allowing breaching promisors compensation in construction cases. Nepstad Custom Homes Co. v. Krull, 527 N.W.2d 402, 406 (Iowa Ct. App. 1994). The substantial performance doctrine pertains to whether a contractor has substantially complied with a contract in good faith and the party seeks recovery of the contract price with deductions for any defects or incompleteness. *Id.*

187. *See* Le Bel v. McCoy, 49 N.E.2d 888, 889 (Mass. 1943); Richard H. Lee, *The Plaintiff in Default*, 19 VAND. L. REV. 1023, 1023 (1965) (explaining that this rule has been adopted by many jurisdictions); *see also* Freedman v. Rector, Wardens &

These multifarious qualifications to the so-called general rule demonstrate that contract law has significantly eroded the barriers to punitive damages claims. The law increasingly recognizes that opportunistic breaches should be deterred, and that awarding the victim punitive damages coincides with contract law principles. Contrary to Professor Shiffrin's assertion about the existence of a "general prohibition" against this recovery,[188] the law in appropriate circumstances is not "equivocal" about holding promisors accountable with the award of punitive damages.[189]

VIII. MORALITY, FORESEEABILITY, AND *HADLEY V. BAXENDALE*

A. *Shiffrin's Moral Objection to* Hadley *and the Foreseeability of Consequential Damages*

Professor Shiffrin objects on moral grounds to the rule first established in the English case of *Hadley v. Baxendale*[190] (which is followed in all American jurisdictions)[191] that promisors are liable only for those consequential damages the parties reasonably could have foreseen at the time of contract formation, versus comparing what the parties could have anticipated at the time of breach.[192] She states:

Vestrymen of St. Mathias Parish, 230 P.2d 629, 632 (Cal. 1951) (calling traditional view a form of punitive damages).

188. Shiffrin, *supra* note 1, at 710 (arguing that "[c]ontract law's stance on wrongfulness of promissory breach is equivocal at best, manifested most clearly by its general prohibition of punitive damages"). In her follow-up *Michigan Law Review* article, Professor Shiffrin inaccurately observes that, except where gratuitous breaches are also torts, the law does not subject these breaches "to the distinctive punitive measures endorsed and administered by law." Shiffrin, *supra* note 5, at 1552.

189. Shiffrin, *supra* note 1, at 710.

190. Hadley v. Baxendale, (1854) 156 Eng. Rep. 145 (Exch.).

191. *See* Wells Fargo Bank v. United States, 33 Fed. Cl. 233, 242 (1995), *rev'd on other grounds*, 88 F.3d 1012 (Fed. Cir. 1996) (describing the rule as "universally accepted"); *see also* U.C.C. § 2-715(2)(a) (2003) (establishing that the seller shall be liable to the buyer for "any loss resulting from general or particular requirements and needs of which the seller at the time of contracting had reason to know").

192. *See, e.g.*, Giampapa v. Am. Family Mut. Ins. Co., 64 P.3d 230, 240 (Colo. 2003) (finding that the critical time to measure foreseeability is at the time of contract formation); Ferrer v. Trs. of Univ. of Pa., 825 A.2d 591, 610 (Pa. 2002) (allowing recovery for damages "reasonably foreseeable" by the parties at the time contract was made).

In *Hadley v. Baxendale*, Hadley's mill shut down because of a broken crankshaft, and he entered a contract to have a new one built. *Hadley*, 156 Eng. Rep. at 146. When the builder asked Hadley to send him the broken shaft to use as a model,

> From a moral perspective, this is quite strange. If one is bound to perform but without excuse voluntarily elects to breach one's duty, a case could be made that the promisor should be liable for all consequential damages. If foreseeability should limit this liability at all, what would matter morally is what was foreseeable at the time of breach rather than at the time of formation. Whereas the former reflects the idea that breach is a wrong for which the promisor must take responsibility, the latter fits better with the idea that the contract merely sets a price for potential promissory breach.[193]

As will be shown below—and contrary to Professor Shiffrin's argument—a strong moral basis exists to justify the *Hadley* rule of measuring foreseeability at the time of contract formation.

B. *The Forseeability Rule and the Moral Vision of* Hadley

To summarize the *Hadley* rule, the first category of contract damages is "general damages"—those which may fairly and reasonably be considered as arising naturally from the breach according to "the usual course of things."[194] General damages are foreseeable as a matter of law without reference to the particular contemplation of the parties.[195] The second category of damages is "consequential damages"—"those damages that 'result naturally, but not necessarily, from the defendant's wrongful

Hadley took it to Baxendale, a common carrier, for delivery to the builder. *Id.* Baxendale did not deliver the shaft until seven days later. *Id.* Hadley sued Baxendale for the lost profits during that period. *Id.* at 146–47. The carrier did know that the mill was stopped and that the shaft needed to be sent immediately, but he did not know that the stoppage of the mill was solely because of the broken shaft. *Id.* at 149, 151. Because Hadley did not communicate to Baxendale this special circumstance—the mill's inoperability without a crankshaft—the court that held Baxendale did not assume the risk of compensating Hadley for lost operating profits resulting from the late delivery. *Id.* at 151–52; *see also Wells Fargo Bank*, 33 Fed. Cl. at 241 (summarizing facts of *Hadley*); Lewis Jorge Constr. Mgmt., Inc. v. Pomona Unified Sch. Dist., 102 P.3d 257, 262 (Cal. 2004).

193. Shiffrin, s*upra* note 1, at 724.

194. *E.g.*, Anchor Sav. Bank v. United States, 81 Fed. Cl. 1, 75 (2008) (citing DOBBS, *supra* note 129, at § 12.1(1)); Hoang v. Hewitt Ave. Assocs., 936 A.2d 915, 934 (Md. Ct. Spec. App. 2007).

195. *See* Birmingham Waterworks Co. v. Ferguson, 51 So. 150, 152 (Ala. 1909) (noting the conclusive presumption that a breaching party contemplates the damages that directly result from the breach); Long v. Abbruzzetti, 487 S.E.2d 217, 219 (Va. 1997) ("If damages are direct, they are compensable."); 22 AM. JUR. 2D *Damages* § 306 (2008).

acts.'"[196] These damages will be compensable when they are reasonably supposed to have been within the contemplation of the parties as a probable result of breach when the parties entered into the contract.[197] Thus, to illustrate the difference between compensable general and consequential damages, a seller of a machine to a manufacturer usually has reason to foresee that a delay in delivering the machine as agreed will probably cause the manufacturer to lose a reasonable profit from its use. These damages are general damages. By contrast, a seller who delays in delivering a machine to a manufacturer is not liable for the manufacturer's loss of profit to the extent that it results from an intended use that was beyond the usual range of damages for such a breach, such as lost profits on other, unrelated contracts, unless the seller had reason to know of this special circumstance.

Professor Shiffrin's complaint against the consequential damage doctrine centers on the point in time from which the damages should be measured. The prevailing test for these damages depends on those facts existing and known to the parties at the time of contract formation and not at the time of the breach.[198] The test is an objective one.[199] Foreseeability is based not on what the defendant actually foresaw but is measured by what the hypothetical reasonable person in the position of the defendant, coupled with the defendant's knowledge of the surrounding circumstances,

196. Stuart v. Bayless, 964 S.W.2d 920, 921 (Tex. 1998) (quoting Arthur Andersen & Co. v. Perry Equip. Corp., 945 S.W.2d 812, 816 (Tex. 1997)).

197. *Anchor Sav. Bank*, 81 Fed. Cl. at 75; Brandon & Tibbs v. George Kevorkian Accountancy Corp., 277 Cal. Rptr. 40, 48 (Ct. App. 1990); 22 AM. JUR. 2D *Damages* §§ 305, 308; *see also* Eisenberg, *supra* note 119, at 565 (noting that lost profits of a business are the most frequent example of consequential damages). "Contemplation" includes "both circumstances that are actually foreseen and those that are reasonably foreseeable." *Long*, 487 S.E.2d at 219 (citing Richmond Med. Supply Co. v. Clifton, 369 S.E.2d 407, 409 (Va. 1988)). Courts disagree on whether both parties or only the promisor must foresee the consequential damages. *See* Coastal Power Int'l, Ltd. v. Transcon. Capital Corp., 10 F. Supp. 2d 345, 368 n.166 (S.D.N.Y. 1998); 22 AM. JUR. 2D *Damages* § 309. This variation does not affect the analysis in this Article.

198. *E.g.*, Precision Pine & Timber, Inc. v. United States, 72 Fed. Cl. 460, 477 (2006) (citing cases supporting the "general rule . . . that foreseeability should be assessed at the time of contracting"); Ind. & Mich. Elec. Co. v. Terre Haute Indus., 507 N.E.2d 588, 601 (Ind. Ct. App. 1987); George H. Swatek, Inc. v. N. Star Graphics, Inc., 587 A.2d 629, 631 (N.J. Super. Ct. App. Div. 1991).

199. *Anchor Sav. Bank*, 81 Fed. Cl. at 79; *Ind. & Mich. Elec. Co.*, 507 N.E.2d at 601.

would be expected to foresee.[200] The rule thereby accords with the general theory of expectation damages, which is to place the plaintiff in the position he would have occupied had the defendant performed as promised, a commitment that, by definition, takes place at contract formation and not at the breach.[201]

Contrary to Professor Shiffrin's first criticism of *Hadley*, cited above, that "a case could be made that the promisor should be liable for all consequential damages,"[202] reason and justice dictate otherwise. As stated in many decisions, "a party does not and cannot assume limitless responsibility for all consequences of a breach."[203] An award of full compensation for a plaintiff's full losses stemming from the breach "would simply be unfair to the defendant as well as possibly paralyzing to commerce."[204] The *Hadley* rule thereby advances the public interest by "'diminish[ing] the risk of business enterprise' by avoiding a 'crushing burden' from an unforeseen liability."[205] Accordingly, the *Hadley* rule helps to maintain the distinction between damages for tort, which allow recovery for all proximate losses, and those for breach of contract, which limit damages to the bounds of the agreement.[206]

200. Wells Fargo Bank v. United States, 33 Fed. Cl. 233, 242 (1995), *rev'd on other grounds*, 88 F.3d 1012 (Fed. Cir. 1996); Kewin v. Mass. Mut. Life Ins. Co., 295 N.W.2d 50, 60 (Mich. 1980); Coyle v. Englander's, 488 A.2d 1083, 1087 (N.J. 1985); *see also* Native Alaskan Reclamation & Pest Control v. United Bank Alaska, 685 P.2d 1211, 1219–20 (Alaska 1984) (stating party in breach need not have made a tacit agreement to be liable for the loss); Alces, *supra* note 48, at 485.

201. *See* Duncan v. Theratx, Inc., 775 A.2d 1019, 1022 (Del. 2001) ("[T]he standard remedy for breach of contract is based upon the reasonable expectations of the parties *ex ante*."); Timberline Equip. Co. v. St. Paul Fire & Marine Ins. Co., 576 P.2d 1244, 1248 (Or. 1978).

202. Shiffrin, *supra* note 1, at 724.

203. *E.g.*, Brandon & Tibbs v. George Kevorkian Accountancy Corp., 277 Cal. Rptr. 40, 48 (Ct. App. 1990).

204. Hector Martinez & Co. v. S. Pac. Transp. Co., 606 F.2d 106, 109 (5th Cir. 1979).

205. Robert M. Lloyd, *Contract Damages in Tennessee*, 69 TENN. L. REV. 837, 866 (2002) (quoting Farnsworth, *supra* note 43, at 1199). The argument that *Hadley* diminishes business risk and avoids unfair burdens to the promisor is a good example of when moral and economic policies coincide for a contract principle. *See supra* notes 48–49.

206. *See* Birmingham Waterworks Co. v. Ferguson, 51 So. 150, 152 (Ala. 1909); Hunt Bros. v. San Lorenzo Water Co., 87 P. 1093, 1095 (Cal. 1906); W. Union Tel. Co. v. Green, 281 S.W. 778, 781–82 (Tenn. 1926); *see also* 24 RICHARD A. LORD, WILLISTON ON CONTRACTS § 64:13 (4th ed. 2002) ("The law of torts and of contracts differ in this respect. For a tort, the defendant becomes liable for all proximate

Regarding Professor Shiffrin's second criticism of *Hadley*, cited above, that the law and morality should measure foreseeability at the time of breach, the policy against undue promisee liability also explains why the law generally assesses the foreseeability of consequential damages at the time of contract formation. In this vein, the Colorado Supreme Court has explained *Hadley* in moral terms as aligning with the consensual nature of contract and holding parties only to their freely entered bargain:

> The *Hadley* rule is designed to further a fundamental principle of contract law: parties must be able to confidently allocate risks and costs during bargaining without fear that unanticipated liability may arise in the future, effectively negating the parties' efforts to build these cost considerations into the contract. Under *Hadley*, a party to a contract is only responsible for those damages he should reasonably have contemplated as the probable result of a breach at the time the contract was entered into. Because the party is aware, or should be aware, that these damages are a potential consequence of the breach, he presumably will take into account the risk that these contingencies will occur while negotiating the contract. Thus, by limiting contractual liability to those damages foreseen by the parties at the time the contract was formed, *Hadley* ensures that the bargain struck reflects a mutually agreeable allocation of the risks and costs of breach. In other words, *Hadley* guarantees the fairness of a bilateral agreement by protecting the parties from unanticipated liability arising in the future.[207]

Professor Dan Dobbs agrees with this perspective, commenting that

consequences, while for breach of contract the defendant is liable only for consequences that were reasonably foreseeable, at the time the contract was made, as likely to result if the contract were broken.").

In contrast, the law has significantly broken down the distinction between contract and tort on the question of the awardability of punitive damages in contract cases. *Compare supra* notes 163–66 and accompanying text.

207. Vanderbeek v. Vernon Corp., 50 P.3d 866, 871 (Colo. 2002); *accord* Ill. Cent. R.R. Co. v. Bros., 67 So. 628, 629 (Ala. Ct. App. 1914) (noting that "simple fairness" requires that every person entering a contract should know the extent of the assumed risks). "The very notion of contract is the consensual formation of relationships with bargained-for duties." Isler v. Tex. Oil & Gas Corp., 749 F.2d 22, 23 (10th Cir. 1984); *see also* Giampapa v. Am. Family Mut. Ins. Co., 64 P.3d 230, 249 (Colo. 2003) (quoting Sebert, *supra* note 164, at 1567) ("'[D]amage rules recognize the consensual basis of contract liability . . . .'"); Smith v. Boyd, 553 A.2d 131, 133 (R.I. 1989) ("A contract is a consensual endeavor.").

"[t]he moral understanding of *Hadley* is that it attempts to respect those understandings of the parties."[208] On the same point, Professor Peter Alces concludes that "*Hadley*, then, is about 'agreement' and ascertaining agreement by reference to justice."[209]

Further reflection supports the fairness of the Colorado court's approach to the appropriateness of measuring consequential damages from the time of contract formation. When the promisor is at risk for a large award of damages, and has no independent notice or knowledge of such, he should be notified in advance of contracting so that he can adjust his risk exposure accordingly, such as by charging a higher price, obtaining insurance, adding appropriate terms, or refusing to enter into the agreement.[210] If the promisor can instead be held liable for events not foreseeable at the time of formation, he will lack a fair and reasonable opportunity for self-protection.[211]

Another moral element of the *Hadley* rule is the protection of party autonomy in contracting decisions. All damage rules, including *Hadley*, protect the parties' freedom of contract[212] and thereby maximize the welfare of individuals and the good of society.[213] Freedom of contract is a "'paramount public policy'"[214] that takes individual autonomy "'seriously

208. 3 DOBBS, *supra* note 129, § 12.4(5).

209. Alces, *supra* note 48, at 486.

210. *See* Martin v. U-Haul Co. of Fresno, 251 Cal. Rptr. 17, 24 (Ct. App. 1988) (stating that a party does not have unlimited liability for all consequences of a breach and must be advised of any special harm which may result from the breach to determine whether to contract or not); 5 CORBIN, *supra* note 125, § 1008; Farnsworth, *supra* note 43, at 1207–08; Lloyd, *supra* note 205, at 866.

211. Patterson v. Ill. Cent. R.R. Co., 97 S.W. 426, 427 (Ky. Ct. App. 1906).

212. *See* Doe v. SexSearch.com, 502 F. Supp. 2d 719, 734 (N.D. Ohio 2007) (stating that "a limitation on damages clause is commercially reasonable to avoid the specter of potential liability which far exceeds the meager price paid"); *Ill. Cent. R.R. Co.*, 67 So. at 629 (observing that without the *Hadley* rule, "the burden upon freedom of contract might become intolerable"); Stop Loss Ins. Brokers, Inc. v. Brown & Toland Med. Group, 49 Cal. Rptr. 3d 609, 626 (Ct. App. 2006) (stating that limiting contract damages to those contemplated by the parties when the contract was formed "serves to encourage contractual relations and commercial activity by enabling parties to estimate in advance the financial risks of their enterprise").

213. Compuware Corp. v. Moody's Investors Servs., Inc., 499 F.3d 520, 535 n.1, (6th Cir. 2007) (Rogers, J., concurring in part and dissenting in part) (citing FARNSWORTH, *supra* note 110, § 1.7); Benavides v. State Farm Gen. Ins. Co., 39 Cal. Rptr. 3d 650, 657 (Ct. App. 2006) (quoting Freeman & Mills, Inc. v. Belcher Oil Co., 900 P.2d 669 (Cal. 1995)); Rory v. Cont'l Ins. Co., 703 N.W.2d 23, 30–31 (Mich. 2005).

214. *E.g.*, Fairfield Ins. Co. v. Stephens Martins Paving, LP, 246 S.W.3d 653,

as a principle for ordering human affairs.'"[215] It is the "founding principle"[216] of the American economy, a "cherished" value of the legal system,[217] and a "vital part"[218] of contractual obligation. Perhaps even more importantly, it is a fundamental individual right, consistent with law

664 (Tex. 2008) (quoting Wood Motor Co. v. Nebel, 238 S.W.2d 181, 185 (Tex. 1951)).

215. Morta v. Korea Ins. Corp., 840 F.2d 1452, 1460 (9th Cir. 1988) (quoting FRIED, *supra* note 21, at 113). In recent years, commentators have noted the increasing importance and continuing vitality of freedom of contract as "a fundamental principle of American contract law." *See* Mark L. Movsesian, *Two Cheers for Freedom of Contract*, 23 CARDOZO L. REV. 1529, 1532 (2002) (reviewing THE FALL AND RISE OF FREEDOM OF CONTRACT (F.H. Buckley ed., 1999)). The courts' desire to protect party autonomy—the prevailing view in American jurisdictions—finds additional support in the "will theory" of contract formation. *See* TKO Equip. Co. v. C & G Coal Co., 863 F.2d 541, 545 (7th Cir. 1988). This long-standing theory, which goes unmentioned by Professor Shiffrin, bases contractual liability upon the freely willed consent of the parties to the agreement. *See* Coleman v. Crescent Insulated Wire & Cable Co., 168 S.W.2d 1060, 1066–67 (Mo. 1943) (noting that duress diminishes free exercise of willpower). The will theory is evidenced in numerous principles of contract law, such as the traditional statement that courts may not and will not make a contract for the parties. Chad McCracken, Note, *Hegel and the Autonomy of Contract Law*, 77 TEX. L. REV. 719, 732 (1999); *see also* Imperial Fire Ins. Co. v. Coos County, 151 U.S. 452, 462 (1894); *Morta*, 840 F.2d at 1460 (quoting Sanger v. Yellow Cab Co., 486 S.W.2d 477, 482 (Mo. 1972)) ("'[T]he general rule of freedom of contract includes the freedom to make a bad bargain'"); Weitzman v. Steinberg, 638 S.W.2d 171, 176 (Tex. App. 1982).

A commentator has analyzed the link between the will theory, party autonomy, and the emphasis on freedom of contract:

> Such a theory seems a natural corollary to classical liberal views about the nature and importance of individual autonomy, and about the proper limits to public interference with private decision-making power. Indeed, if contract law is thought to be an outgrowth (or a guardian) of liberal notions of personal autonomy, it would seem that the will theory is very nearly a requirement, because it is the actual, subjective choice of the individual that liberalism takes to be crucial for autonomy and thus deserving of protection. As Fried writes: "The regime of contract law, which respects the dispositions individuals make of their rights, carries to its natural conclusion the liberal premise that individuals have rights. And the will theory of contract, which sees contractual obligations as essentially self-imposed, is a fair implication of liberal individualism."

McCracken, *supra*, at 730 (quoting FRIED, *supra* note 21, at 2); *see also Morta*, 840 F.2d at 1460 (endorsing Professor Fried's will theory formulation).

216. Allen v. Mich. Bell Tel. Co., 171 N.W.2d 689, 693 (Mich. Ct. App. 1969).

217. Sutton v. Epperson, 631 So. 2d 832, 835 (Ala. 1993).

218. Randy E. Barnett, *Some Problems with Contract as Promise*, 77 CORNELL L. REV. 1022, 1025 n.16 (1992) (analyzing Lon L. Fuller, *Consideration and Form*, 41 COLUM. L. REV. 799 (1941)).

and public policy, protected by the federal and many state constitutions,[219] as well as by federal and state civil rights legislation[220] and the UCC.[221] When the law holds the promisor accountable solely for the risks foreseeable at the time of contract formation, as opposed to the time of breach, the law respects the rights of the parties to prescribe their liabilities upon entering the agreement, consistent with the freedom of contract.[222]

The *Hadley* rule enhances the normative goals of contract in still other ways. One of the main purposes of contract damages "is the prevention of similar harms in the future."[223] If the law held the promisor liable for future events not reasonably predictable at the time of contract formation, he would not be able to alter his potentially breaching behavior to avoid this risk. Lastly, the *Hadley* rule tends to prevent opportunistic

219. *See* Bd. of Regents of State Colls. v. Roth, 408 U.S. 564, 572 (1972) (quoting Meyer v. Nebraska, 262 U.S. 390, 399 (1923)) (construing the Due Process Clause of the Fifth and Fourteenth Amendments to the Constitution); I.C.C. Protective Coatings, Inc. v. A.E. Staley Mfg. Co., 695 N.E.2d 1030, 1036 (Ind. Ct. App. 1998) (construing federal and Indiana constitutions); Am. Tours, Inc. v. Liberty Mut. Ins. Co., 338 S.E.2d 92, 98 (N.C. 1986) (construing N.C. CONST. art. I, § 17); 16B AM. JUR. 2D *Constitutional Law* §§ 594, 595 (1998 & Supp. 2009); Blum & Wellman, *supra* note 46, at 901. Courts emphasize that it "has long been an established principle of law that the freedom of contract is not unlimited and that parties may not enter into a contract that is in violation of established law or public policy." J.F. v. D.B., 879 N.E.2d 740, 742 (Ohio 2007) (Cupp, J., dissenting) (citations omitted); *see also* Marshall v. Kan. Med. Mut. Ins. Co., 73 P.3d 120, 128 (Kan. 2003).

220. *See* 42 U.S.C. § 1981(a) ("All persons within the jurisdiction of the United States shall have the same right in every State and Territory to make and enforce contracts . . . as is enjoyed by white citizens"), *construed in* Ofori-Tenkorang v. Am. Int'l Group, Inc., 460 F.3d 296, 300–01 (2d Cir. 2006); *see also* MASS. GEN. LAWS ANN. ch. 93, § 103(a) (West 2006); R.I. GEN. LAWS § 42-112-1(a) (2006). Statutes also may restrict freedom of contract. For example, no party has a legal right to discriminate against other persons in the provision of public accommodations on the basis of race, color, religion, or national origin. *See* Civil Rights Act of 1964 § 201, 42 U.S.C. § 2000a (2006).

221. *See* U.C.C. § 1-302 cmt. 1 (2004) ("Subsection (a) states affirmatively at the outset that freedom of contract is a principle of the Uniform Commercial Code . . . ."); *see also* McKee Constr. Co. v. Stanley Plumbing & Heating Co., 828 S.W.2d 700, 705 (Mo. Ct. App. 1992) ("[T]he U.C.C. should not be construed to impair the freedom of contract.").

222. *See* Am. Airlines, Inc. v. Wolens, 513 U.S. 219, 230 (1995) ("'The stability and efficiency of the market depend fundamentally on the enforcement of agreements freely made, *based on needs perceived by the contracting parties at the time*.'" (quoting Brief for United States as Amicus Curiae Supporting Respondents at 23, Am. Airlines, Inc. v. Wolens, 513 U.S. 219) (1995) (No. 93-1286))) (emphasis added).

223. 5 CORBIN, *supra* note 125, § 1002.

tactics by promisees: "[w]ithout such a rule, the injured party has an incentive to withhold disclosure of the unusual consequences of nonperformance until after the contract price is negotiated."[224] The courts and commentators have correctly assessed the moral nature of the foreseeability rule under *Hadley* and its respect for party autonomy under the freedom of contract.

C. *Qualifications and Savings Doctrines:* Hadley *and Foreseeability*

As explained in the prior section, the *Hadley* rule as commonly understood gauges foreseeability from the time of formation and not at some later time. Nevertheless, various qualifications exist in the UCC and case law that accept the time of breach as the point of departure. A number of savings doctrines also remedy any unfairness that may result from the conventional rule. These qualifications and savings doctrines show that the law of breach of contract damages is sufficiently flexible to meet the moral necessities of a particular case.[225]

1. *Qualifications*

A few cases hold that foreseeability at the time of formation is just the "general rule."[226] For these jurisdictions, there can be a "valid reason," when the consequences of the breach may be more apparent and assessable, and the deterrent effect greater, to make foreseeability more appropriately measured at the time of the breach. [227] Thus, when the

224. Charles J. Goetz & Robert E. Scott, *The Mitigation Principle: Toward a General Theory of Contractual Obligation*, 69 VA. L. REV. 967, 987 n.48 (1983); *see also* Evra Corp. v. Swiss Bank Corp., 673 F.2d 951, 957 (7th Cir. 1982) (stating that the "animating principle" of *Hadley* is the party that was able to avert the untoward consequence of a course of dealing at the least cost, but failed to do so, should bear the burden of such costs).

225. 5 CORBIN, *supra* note 125, § 1002 (stating that rules of law on breach of contract damages "are very flexible" and act "merely as guides to the court" where the court may take into account "the special circumstances of the particular case").

Notwithstanding the common law rule of *Hadley*, parties are free to apportion damages in the event of breach. *See, e.g.*, *In re* Graham Square, Inc., 126 F.3d 823, 828–29 (6th Cir. 1997). Thus, under the UCC, a term that limits or excludes consequential damages will be enforceable where conscionable, with a qualification for consumer goods. U.C.C. § 2-719(3) (2003).

226. Sys. Fuels, Inc. v. United States, 78 Fed. Cl. 769, 788 n.18 (2007); *accord* Precision Pine & Timber, Inc. v. United States, 72 Fed. Cl. 460, 477, 480 (2006).

227. Gardner Displays Co. v. United States, 346 F.2d 585, 589 (1965); *see also Sys. Fuels, Inc.*, 78 Fed. Cl. at 788 n.18 (discussing Tenn. Valley Auth. v. United States, 69 Fed. Cl. 515 (2006), and noting the significance of that court's ability to calculate

breaching party at the time of default should be on notice of the ramifications of its actions or failure to act, a court may select this later point in time to determine foreseeability.[228] A good example of this situation occurred in a Texas case, in which the injured party's notice to a carrier of the urgency for prompt provision of cattle feed at the time of arrival was sufficient to hold the carrier liable for consequential losses for harm to the plaintiff's cattle following its delayed delivery.[229] Professor Shiffrin appears unaware of this line of authority that selects the time of breach in special cases when the need exists to deter a serious breach and to avoid special unfairness to the promisee. These decisions partially answer her objection that the law departs from morality in mechanically assessing foreseeability at the time of contract formation.[230]

A second *Hadley* qualification depends on the moral gravity of the promisor's breach.[231] When the proof shows "a willful and malicious breach of contract . . . 'the law will not nicely attempt to limit the amount of reparation, but will extend the line of relief so as to embrace all the consequences of the wrongdoer's act, although quite remote from the original transaction.'"[232] This doctrine amounts to punitive damages for

damages with certainty because the damages were readily foreseeable)); S. Nuclear Operating Co. v. United States, 77 Fed. Cl. 396, 404 (2007) ("[T]here may be situations where foreseeability is more appropriately measured at the time of the breach because that is when the breaching party should be on notice of the ramifications of its actions or failures."); *Precision Pine & Timber, Inc.*, 72 Fed. Cl. at 477–80 (considering whether "circumstances" presented a "compelling need" for measuring foreseeability from the time of breach).

228. *Gardner Displays Co.*, 346 F.2d at 589 ("[I]t is at the breach time that the consequences of wrongdoing are more apparent and assessable, and the deterrent accordingly greater.").

229. Bourland v. Choctaw, O. & G. Ry., 90 S.W. 483, 484 (Tex. 1906) (deeming *Hadley* inapplicable and stating that the doctrine does not embrace all breach of contract cases where justice requires otherwise). For similar instances of undue delay in inspection and approval of goods in which the court held out the possibility of measuring foreseeability at the time of breach, see *Stanish v. Polish Catholic Union*, 484 F.2d 713, 725 (7th Cir. 1973) (noting that the promisor "well knew" when it breached a contract to lend money that the injured party would not be able to construct an apartment building and to repay the loan); *Turner's Farms, Inc. v. Maine Central Railroad*, 486 F. Supp. 694, 699–700 (D. Me. 1980) ("well-established" exception to *Hadley*); and *Gardner Displays Co.*, 346 F.2d at 589.

230. *See* Shiffrin, *supra* note 1, at 724.

231. *See* Dow v. Winnipesaukee Gas & Elec. Co., 41 A. 288, 289 (N.H. 1898).

232. Salinger v. Salinger, 45 A. 558, 559 (N.H. 1899) (quoting *Dow*, 41 A. at 288); *see also* Overstreet v. Merritt, 200 P. 11, 16 (Cal. 1921) (holding that a party breaching in bad faith will be liable for all consequential damages regardless of

promisor bad faith and essentially makes *Hadley* a tort rule for consequential damages. [233] Although few jurisdictions follow this specific doctrine, commentators do agree that a strong line of cases implicitly or explicitly gives a liberal reading of foreseeability in favoring relief against the aggravated breacher.[234]

2. *Savings Doctrines*

Even if it could be argued that morality always should prohibit courts from determining foreseeability at the time of contract formation, established savings doctrines ameliorate any resulting unfairness to or undercompensation of the plaintiff.

The most prominent principle is that, from an evidentiary standpoint, the foreseeability requirement poses little difficulty for many injured parties. Professor Farnsworth notes that if the injured party is a seller, supplier, or builder, "the requirement of foreseeability is rarely a problem."[235] Here, courts have not questioned that the injured party's loss followed from the breach in the ordinary course if he resold—or could have resold without a loss of volume—insofar as the loss results from "a decline in the market, together with any expenses incurred in arranging a second sale."[236] Conversely, Professor Farnsworth notes that foreseeability "ordinarily poses no problem" when the injured party is the buyer and the buyer has or could have covered on the market.[237] Here, courts have not

foreseeability). Louisiana follows the rule that an obligor breaching in bad faith is liable for all damages, foreseeable or not, that are a direct consequence of the failure to perform. LA. CIV. CODE ANN. art. 1997 (1985). "Bad faith" under this statute "generally implies actual or constructive fraud or a refusal to fulfill contractual obligations." Delaney v. Whitney Nat'l Bank, 703 So. 2d 709, 718 (La. Ct. App. 1997). Otherwise, Louisiana follows the standard *Hadley* rules. *See* LA. CIV. CODE ANN. art. 1996; Schienuk the Florist, Inc. v. S. Bell Tel. & Tel. Co., 128 So. 2d 683, 685 n.5 (La. Ct. App. 1961).

233. *But see* Vanderbeek v. Vernon Corp., 50 P.3d 866, 871–72 (Colo. 2002) (holding that *Hadley* is a rule of contract law and not tort law).

234. *See* MCCORMICK, *supra* note 185, §§ 140, 141; Farnsworth, *supra* note 43, at 1209 n.274 (citing MCCORMICK, *supra* note 185, § 141); Charles J. Goetz & Robert E. Scott, *Enforcing Promises: An Examination of the Basis of Contract*, 89 YALE L.J. 1261, 1299 n.84 (1980) (citing Ralph Bauer, *The Degree of Moral Fault as Affecting Defendant's Liability*, 81 U. PA. L. REV. 586, 592 (1933); Lon L. Fuller & William R. Perdue, Jr., *The Reliance Interest in Contract Damages: 1*, 46 YALE L.J. 52 (1936)); Sebert, *supra* note 164, at 1647 n.303.

235. *See* FARNSWORTH, *supra* note 110, § 12.14, at 263; *see also id.* at 267–68.

236. *Id.* at 263.

237. *Id.*

questioned that the injured party's loss foreseeably followed from breach when "the cause of loss will be a rise in the market, together with any expenses incurred in arranging cover."[238] Because injured parties in contracts for the sale or purchase of goods usually can obtain cover on the market in a free-enterprise economy, problems of foreseeability will arise only in the relatively rare instance when the seller or buyer cannot seek such alternative relief.[239] It can further be argued that these cover principles apply equally to contracts for commodities other than goods.

Other savings principles exist as well—some are statutory, while others come from case law. The UCC makes the time of breach determinative for assessing damages when the buyer sues the seller for breach in regard to accepted goods,[240] and when the buyer sues the seller for breach of warranty.[241] The case-law principles ameliorating the *Hadley* foreseeability test are more extensive. First, courts have been steadily eroding the level of foreseeability from one of "probability" (i.e., more than likely) to "reasonable foreseeability" (i.e., substantially likely).[242] Additionally, the test of foreseeability is only that the loss would likely result if the breach occurred and that the damages are of a type that could reasonably occur.[243] No requirement exists that the breach itself, the amount of damages, or the particular way the loss came about also must be foreseeable.[244] This standard also lowers the evidentiary bar considerably for plaintiffs because the law relieves them of proving many of the details of why the loss would have been foreseeable from the vantage point of

238. *Id.*

239. *Id.*

240. U.C.C. § 2-714(1) (2009), *analyzed in* Farnsworth, *supra* note 43, at 1203 n.240.

241. U.C.C. § 2-715(2)(b), *analyzed in* PERILLO, *supra* note 112, § 56.3.

242. Melvin Aron Eisenberg, *The Emergence of Dynamic Contract Law*, 88 CAL. L. REV. 1743, 1776–77 (2000); Eisenberg, *supra* note 119, at 610–11 n.117; Lloyd, *supra* note 205, at 868–69 (noting that the test is lower than a fifty percent chance). Professor Eisenberg sees this trend as part of a wider recognition that expectation damages tend to be undercompensatory because the promisee does not obtain recovery for items such as attorney fees. Eisenberg, *supra* note 119, at 610–11.

243. George H. Swatek, Inc. v. N. Star Graphics, Inc., 587 A.2d 629, 631–32 (N.J. Super. Ct. App. Div. 1991).

244. S. Nuclear Operating Co. v. United States, 77 Fed. Cl. 396, 405 (2007) (citing 3 FARNSWORTH, *supra* note 110, § 12.15); Harmon Cable Commc'ns of Neb. Ltd. P'ship v. Scope Cable Television, Inc., 468 N.W.2d 350, 362 (Neb. 1991); *George H. Swatek, Inc.*, 587 A.2d at 631–32; Barnard v. Compugraphic Corp., 667 P.2d 117, 120 (Wash. Ct. App. 1983); *see also* 22 AM. JUR. 2D *Damages* § 311 (2008).

contract formation.[245]

In another savings formulation, "compensation for the plaintiff's losses is to be made with reference to the conditions existing when the performance is due and the contract is broken."[246] This doctrine eases the plaintiff's evidentiary burden by situating the point of actual damages assessment at the time of breach. Here, the full injurious consequences of the breach will be manifest and concrete, as opposed to the time of formation, when the damages projections necessarily will be more speculative. Fourth, the "court[s] may consider post-breach evidence when determining [expectation] damages."[247] All these hindsight analyses are of considerable aid to plaintiffs in proving their losses.[248]

Some prominent commentators go even further and suggest that determining the time of foreseeability has minimal practical impact. Professor Corbin states that in most contracts in which a promisor assents to the terms, "he does not regard the risk of his own non-performance as great" and would not change the terms, including the price, even if his attention were drawn to the risk of consequential damages.[249] Therefore, Corbin suggests that the question of assessing foreseeability at the time of formation versus the time of breach is "not a live issue" because courts and juries characteristically determine the existence of foreseeability "without making fine distinctions as to time."[250] Another commentator draws a similar conclusion:

> While the courts routinely state that damages must be foreseeable to be recovered in a breach of contract case, it is the rare case in which the rule of foreseeability will actually determine the result. Research discloses very few cases in which the courts have held, as a matter of law, that damages were indeed proximately caused but were not

245. *See George H. Swatek, Inc.*, 587 A.2d at 632.

246. 11 ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 1005 (Interim ed. 1993) *quoted in* Ind. Mich. Power Co. v. United States, 422 F.3d 1369, 1374–75 (Fed. Cir. 2005).

247. Fifth Third Bank v. United States, 518 F.3d 1368, 1377 (Fed. Cir. 2008); *see also* Cheyenne Constr., Inc. v. Hozz, 720 P.2d 1224, 1227 (Nev. 1986).

248. *See* Wells Fargo Bank v. United States, 33 Fed. Cl. 233, 242 n.7 (1995) (stating that foreseeability analysis for the promisee's losses is "often" one of "hindsight").

249. 5 CORBIN, *supra* note 125, § 1008, at 75.

250. *See id.*

foreseeable and thus not recoverable.[251]

Although more empirical research would be helpful on this matter, if the cases they mention are any barometer, then the commentators appear to be correct.

Theoretically, the *Hadley* rule promotes fairness because it respects the consensual nature of the contract and the parties' discretion to craft their own risks and liabilities. Practically, the general test for foreseeability—along with its qualifications and savings doctrines—causes little, if any, undue burden to the plaintiffs in establishing their expectation damages entitlement.[252] By respecting the parties' autonomy under their rights of freedom of contract, along with enforcing the promisor's accountability to the promisee for damages, *Hadley* does not create any divergence between contract and promise.

IX. MITIGATION OF DAMAGES: FAIRNESS, THE BURDEN OF PROOF, AND QUALIFICATIONS

Professor Shiffrin objects to the legal doctrine of mitigation because, "unlike morality," it requires the injured promisee—and not the wrongdoing promisor—to find an alternate provider in the face of a breach and to forfeit relief for avoidable damages.[253] Although she says that "morality does not look sympathetically upon promisees who stay idle while easily avoidable damages accumulate," she argues that this rule "is a far cry from what contract expects of the promisee and what it fails to demand of the breaching promisor."[254] Under promissory norms, Professor Shiffrin asserts, the promisor should have the burden of locating and providing an acceptable substitute for his performance.[255] She suggests that it is "morally distasteful" to compel the promisee to perform the promisor's work, except when the costs of the promisee's refusal are "very steep and disproportionate to the seriousness of what is promised."[256] She

251. 1 ROBERT L. DUNN, RECOVERY OF DAMAGES FOR LOST PROFITS § 1.19 (4th ed. 1992), *quoted in* Lloyd, *supra* note 205, at 869 n.239.

252. Another mitigating doctrine holds that the foreseeability rule does not preclude restitutionary relief. *See, e.g.*, Huler v. Nasser, 33 N.W.2d 637, 640 (Mich. 1948).

253. Shiffrin, *supra* note 1, at 710, 725.

254. *Id.* at 724.

255. *Id.* at 725.

256. *Id.*

also believes the law on mitigation follows an overly "blunt" rule that incorrectly "makes the promisor's wrongdoing easier, simpler, more convenient, or less costly."[257]

Throughout her article, Professor Shiffrin correctly equates moral purposes in contract law with fairness, reasonableness, and justice.[258] Her questions on mitigation therefore can be reformulated. First, is placing the task of mitigation on the injured promisee fair, reasonable, and just? Second, does the law's allocation of this burden to the promisee sufficiently take the promisor's wrongdoing into account?[259] The answers require an explanation of the basic mitigation standard, its policy, the parties' respective burdens of proof, and the numerous qualifications to the mitigation rule.

A. *Basic Mitigation Standards*

The non-breaching party has a duty to mitigate its damages, also known as the doctrine of "avoidable consequences."[260] The rule is that one who is injured by a breach of contract "'is bound to exercise reasonable care and diligence to avoid loss or to minimize or lessen the resulting

257. *Id.* at 725 (noting that the promisor may ask "the promisee to shoulder this burden" for reasons of efficiency, but arguing it should be "unacceptable for the promisor to insist were the promisee to refuse").

258. *Id.* at 710 n.1.

259. Ironically, while making her argument, Professor Shiffrin twice refers to the promisor's "wrongdoing" in describing the breach of a contract. *Id*. at 725. This unqualified description is inconsistent with Professor Shiffrin's earlier statements that the law treats breach of contract as "not a wrong, or at least not a serious one." *Id.* at 724.

260. Tampa Pipeline Transp. Co. v. Chase Manhattan Serv. Corp., 928 F. Supp. 1568, 1578 n.10 (M.D. Fla. 1995); Barrie Sch. v. Patch, 933 A.2d 382, 391 (Md. 2007) (quoting Circuit City v. Rockville Pike, 829 A.2d 976, 990 (Md. 2003)). The avoidable consequences concept applies equivalently in tort and contract cases. *See, e.g.*, New Mexico v. Gen. Elec. Co., 335 F. Supp. 2d 1185, 1230 (D.N.M. 2004); Lynch v. Scheininger, 744 A.2d 113, 125 (N.J. 2000), which makes the precedents interchangeable to this extent.

Many courts and commentators have observed that the term "duty" in this context is misleading. The promisor here does not have a cause of action against the promisee—the failure to mitigate merely disables the injured party from recovering avoidable losses. St. George Chi., Inc. v. George J. Murges & Assocs., 695 N.E.2d 503, 509 (Ill. App. Ct. 1998) (citations omitted); Stewart v. Bd. Educ. of Ritenour Consol. Sch. Dist., R-3, 630 S.W.2d 130, 133 (Mo. Ct. App. 1982) (quoting 5 CORBIN, *supra* note125, § 1039); RESTATEMENT (SECOND) OF CONTRACTS § 350, cmt. b (1979); 5 CORBIN, *supra* note 125, § 1039; Goetz & Scott, *supra* note 224, at 967 n.1.

damage.'"[261] The injured party must execute the duty to mitigate damages based upon the following factors: (1) "[G]ood faith; (2) . . . reasonable skill, prudence, and efficiency; (3) . . . [effort] reasonably warranted by and proportioned to the injury and the consequences to be averted; and (4) . . . a reasonably justified belief . . . [the effort] will avoid or reduce damage otherwise to be expected from the wrongdoing."[262] A common instance of when a promisee fails to mitigate damages would be when, absent a contrary contractual arrangement, a tenant wrongfully abandons the premises before the term but the landlord makes no effort to secure a substitute tenant during that period.[263] Another frequent example occurs when an employer breaches an employment agreement. In that case, the injured employee must reasonably seek comparable employment.[264]

B. *Mitigation Policies*

In objecting to the promisee's general obligation to mitigate the loss, Professor Shiffrin fails to mention the sound moral and legal rationales courts have used to justify placing upon the promisee, as opposed to the promisor, the task of alleviating contract damages.[265]

An "equitable doctrine,"[266] this mitigation concept is a "fundamental principle"[267] of contract law and "a thread permeating the entire

261. Life Care Ctrs. of Am., Inc. v. Charles Town Assocs. Ltd. P'ship, 79 F.3d 496, 514 (6th Cir. 1996) (citations omitted); Memphis Light, Gas & Water Div. v. Starkey, 244 S.W.3d 344, 353 (Tenn. Ct. App. 2007) (citation omitted). Some jurisdictions make the test even more favorable to the promisee, holding that the doctrine applies only where "the damages can be avoided with only slight expense and reasonable effort." Pulaski Bank & Trust Co. v. Tex. Am. Bank/Fort Worth, 759 S.W.2d 723, 735 (Tex. App. 1988).

262. Tulsa Mun. Airport Trust v. Nat'l Gypsum Co., 551 P.2d 304, 311 (Okla. Civ. App. 1976).

263. *See, e.g.*, Austin Hill Country Realty, Inc. v. Palisades Plaza, Inc., 948 S.W.2d 293, 295 (Tex. 1997) (considering to what extent a landlord has a mitigation duty if a tenant defaults before the expiration of its lease).

264. *See, e.g.*, Salem Cmty. Sch. Corp. v. Richman, 406 N.E.2d 269, 275 (Ind. Ct. App. 1980).

265. *See* Bridgeport v. Aetna Indem. Co., 105 A. 680, 682 (Conn. 1919); Miller v. Mariner's Church, 7 Me. 51, 56 (1830); Hamilton v. McPherson, 28 N.Y. 72, 76 (1863) (citing several cases stating that the mitigation responsibility is a moral and legal duty); *see also* Gilbert v. Kennedy, 22 Mich. 117, 132–35 (1871) (noting the "duty of the plaintiff . . . to prevent, at any particular time, further injury").

266. 25 C.J.S. *Damages* § 167 (2002).

267. Citizens Fed. Bank v. United States, 66 Fed. Cl. 179, 185 (2005); Avery Wiener Katz, *The Option Element in Contracting*, 90 VA. L. REV. 2187, 2199 (2004).

jurisprudence."[268] One primary rationale is morality. Professor Eisenberg observes that if a promisor "is at risk of incurring a significant loss, and [the promisee] could prevent that loss by an action that would not require [the promisee] to forego a significant bargaining advantage, undertake a significant risk, or to incur some other cost that is significant under the circumstances," then "as a matter of morality" the promisee should take that action.[269] Concisely put, the mitigation rule draws in large measure from the implied covenant of good faith and fair dealing.[270]

The rule has other supporting policies, which have intermixed strands of morality and economic efficiency. The rule avoids rewarding the promisee for his contributory negligence in not averting avoidable damages; the underlying policy is to make the plaintiff's recovery

Compare Sylva Shops L.P. v. Hibbard, 623 S.E.2d 785, 790 (N.C. Ct. App. 2006) ("The existence of a common law duty of care does not . . . absolutely preclude parties from agreeing in a contract to relieve a party of that duty."), *with* Goetz & Scott, *supra* note 224, at 971–72 (stating that parties may contractually modify the mitigation doctrine).

268. Shiffer v. Bd. of Educ. of Gibraltar Sch. Dist., 224 N.W.2d 255, 258 (Mich. 1974).

269. Eisenberg, *supra* note 91, at 1022; *see also* FRIED, *supra* note 21, at 131 (noting that the mitigation rule is an "altruistic duty").

270. Johnson v. First Nat'l Bank of Shreveport, 792 So. 2d 33, 54 (La. Ct. App. 2001); Dupre v. Tri-Parish Flying Serv., Inc., 355 So. 2d 554, 556 (La. Ct. App. 1978); *Gilbert*, 22 Mich. at 134; *see also* Katz, *supra* note 267, at 2199 (arguing fairness dictates that the "aggrieved party owes a duty of cooperation").

Professor Shiffrin makes the puzzling suggestion that the promisor should simply overlook the promisee's unreasonable failure to mitigate. *See* Shiffrin, *supra* note 1, at 726. She opines that "[t]his wrong may fall within the category of wrongs the law should allow because interference in this particular domain might preclude recognizable realization of the virtuous thing to do—namely, to be gracious and forgiving in the face of another's wrong." *Id.* Professor Shiffrin's view of contract undermines the core notion that a party remains morally and economically free to seek contractual remedies to the party's legitimate maximum advantage. Interpreting the duty of contractual good faith, a view which readily applies to the promisee's duty of mitigation, Judge Richard Posner observed in *Wisconsin Electric Power Co. v. Union Pacific Railroad Co.*, 557 F.3d 504, 510 (7th Cir. 2009), that:

> "Parties are not prevented from protecting their respective economic interests." JOHN EDWARD MURRAY, JR., MURRAY ON CONTRACTS § 90, p. 501 (4th ed. 2001). As we explained, interpreting Wisconsin law in *Market Street Associates Ltd. Partnership v. Frey*, 941 F.2d 588, 594 (7th Cir. 1991), "even after you have signed a contract, you are not obliged to become an altruist toward the other party and relax the terms if he gets into trouble in performing his side of the bargain."

dependent upon proper and reasonable care for his own interests.[271] Third, the mitigation rule reduces social costs because it avoids economic waste.[272] In this respect, courts observe that "'recovery for the harm is denied because it is in part the result of the injured person's lack of care, and public policy requires that persons should be discouraged from wasting their resources, both physical and economic.'"[273] Fourth, the promisor is not liable for these damages because it is the promisee, and not the promisor, who is the sole proximate cause of the needless losses.[274] Fifth, the mitigation rule is consistent with the rule against contract penalties because allowing the promisee to recover more than its expectation interest under the contract has the effect of imposing an unenforceable penalty upon the promisor.[275] Sixth, the mitigation rule precludes the promisee's

Id. In any event, as argued subsequently in this Article, the promisee actually has a minimal duty to mitigate because of the moral wrong associated with the promisor's breach. *See infra* Part IX.D.

271. Williams v. Manchester, 864 N.E.2d 963, 986 (Ill. App. Ct. 2007) (quoting Clarkson v. Wright, 483 N.E.2d 268 (Ill. 1985), in turn quoting WILLIAM L. PROSSER, TORTS § 65 (4th ed. 1971)) (acknowledging the rule of avoidable consequences, but declining to apply it), *vacated in part on other grounds*, 888 N.E.2d 1 (Ill. 2008); *accord* Dillinger v. Caterpillar, Inc., 959 F.2d 430, 438 (3d Cir. 1992) (noting the similarities between contributory negligence and the avoidable consequences doctrine); Ridley v. Safety Kleen Corp., 693 So. 2d 934, 942–43 (Fla. 1996) (finding contributory negligence because plaintiff did not protect his own interests). "Although the affirmative defense of contributory negligence in a breach of contract action does not act as a complete bar to recovery, the defense is relevant when the mitigation of damages is at issue." A.G. Edwards & Sons, Inc. v. Drew, 978 S.W.2d 386, 391 (Mo. Ct. App. 1998).

272. Hygeia Dairy Co. v. Gonzalez, 994 S.W.2d 220, 224 (Tex. App. 1999).

273. Schlossberg v. Epstein, 534 A.2d 1003, 1007 (Md. Ct. Spec. App. 1988) (quoting RESTATEMENT (SECOND) OF TORTS § 918 cmt. a (1979)); *accord* Lynch v. Scheininger, 744 A.2d 113, 125 (N.J. 2000); Pulaski Bank & Trust Co. v. Tex. Am. Bank/Fort Worth, N.A., 759 S.W.2d 723, 735 (Tex. App. 1988). The mitigation rule is designed to "'prevent and repair individual loss and injustice'" as well as to "'conserve the economic welfare and prosperity of the whole community.'" Shiffer v. Bd. of Educ. of Gibraltar Sch. Dist., 224 N.W.2d 255, 258 (Mich. 1974) (quoting MCCORMICK, *supra* note 185, § 33); *see also* Katz, *supra* note 267, at 2199 (noting that the rule is based on efficiency concerns because it is "wasteful to encourage the aggrieved party to run up losses for which she is the least-cost avoider").

274. Preston v. Keith, 584 A.2d 439, 441–42 (Conn. 1991); *Williams*, 864 N.E.2d at 986 (quoting 1 DAN DOBBS, TORTS § 196 (2001)); McClelland v. Climax Hosiery Mills, 169 N.E. 605, 609 (N.Y. 1930); 22 AM. JUR. 2D *Damages* § 341 (2003) (noting that plaintiff's own negligence becomes an intervening cause); *see also* Katz, *supra* note 267, at 2199 (noting that the rule is based on corrective justice because the aggrieved party caused the losses).

275. Austin Hill Country Realty, Inc. v. Palisades Plaza, Inc., 948 S.W.2d 293, 298 (Tex. 1997); *see also* Cooney Indus. Trucks, Inc. v. Toyota Motor Sales, U.S.A., 168

unjust enrichment for losses that otherwise could have been reasonably minimized or eliminated.[276] Lastly, insofar as the injured promisee must sell his goods or services elsewhere, or fill his needs from another source, the mitigation rule is a variation on the expectancy rule of damages because the law protects the promisee "only to the extent that he has in reliance on the contract foregone other equally advantageous opportunities for accomplishing the same end."[277]

C. *Burden of Proof*

The next important issue on the morality of mitigation is how the law allocates the burden of proof, which is often outcome-determinative in civil cases. [278] Although the promisee bears the responsibility for mitigation,[279]

F.3d 545, 547 (1st Cir. 1999) (quoting Ficara v. Belleau, 117 N.E.2d 287, 289 (Mass. 1954)) (explaining that the mitigation rule requires an injured party not be placed in a better position than if the promisor had performed the contract); Frenchtown Square P'ship v. Lemstone, Inc., 791 N.E.2d 417, 419 (Ohio 2003) (noting that the mitigation rule justly helps to "place an injured party 'in as good a position had the contract not been breached at the least cost to the defaulting party'" (quoting F. Enters., Inc. v. Ky. Fried Chicken Corp., 351 N.E.2d 121 (Ohio 1976))); 5 CORBIN, *supra* note 125, § 1039 (linking concept of mitigation to expectation damages theory).

276. *See* Toledo Peoria & W. Ry. v. Metro Waste Sys., 59 F.3d 637, 640 (7th Cir. 1995) ("[A]n injured party has an obligation to take reasonable steps to minimize his damages and thus avoid heaping up additional losses for which the tortfeasor may be held liable" (citing Oddi v. Ayco Corp., 947 F.2d 257, 264 (7th Cir. 1991); Cedar Rapids & Iowa City Ry. & Light Co. v. Sprague Elec. Co., 117 N.E.461, 463 (Ill. 1917); Culligan Rock River Water Cond. Co. v. Gearhart, 443 N.E.2d 1065, 1068 (Ill. App. Ct. 1982))); Sutcliffe v. FleetBoston Fin. Corp., 950 A.2d 544, 550 (Conn. App. Ct. 2008); Ambassador Fin. Servs., Inc. v. Ind. Nat'l. Bank, 605 N.E.2d 746, 752 (Ind. 1992) (finding that the mitigation of damages defense is designed to prevent a payee's unjust enrichment when no actual damages were suffered as a result of a forged endorsement); Pamar Enters. v. Huntington Banks of Mich., 580 N.W.2d 11, 16–17 (Mich. Ct. App. 1998) (applying rationale in a conversion action); *see also* Kauffman v. Maxim Healthcare Servs., Inc., 509 F. Supp. 2d 210, 219 (E.D.N.Y. 2007) (stating that the mitigation of damages rule prevents the plaintiff's obtaining a windfall).

Several commentators note that the promisee has a conflict of interest because, except for the mitigation principle, he has an incentive to run up damages. Perillo, *supra* note 30, at 1098 n.80.

277. Fuller & Perdue, *supra* note 234, at 61. *Compare* Goetz & Scott, *supra* note 224, at 975 n.22 ("Joint minimization of costs generally requires that a mitigator credit the breacher with any new profits he obtains by virtue of the breach." (citing McAleer v. McNally Pittsburg Mfg. Co., 329 F.2d 273 (3d Cir. 1964); Bertholf v. Fisk, 166 N.W. 713 (Iowa 1918); Cole v. City of Houston, 442 S.W.2d 445 (Tex. App. 1969)).

278. *See* Brock v. Dun-Par Engineered Form Co., 843 F.2d 1135, 1140 (8th Cir. 1988); *In re* Garvida, 347 B.R. 697, 706 (B.A.P. 9th Cir. 2006).

the "'overwhelming weight of authority'"[280] states that the breaching promisor must prove that the promisee inappropriately failed in avoiding or alleviating his injury.[281] The promisor employing this "affirmative defense"[282] has the very difficult requirement to plead and prove: "(1) what reasonable actions the [promisee] ought to have taken, (2) that those actions would have reduced the damages, and (3) the amount by which the damages would have been reduced."[283] In effect, the breaching party must show that the promisee knew reasonable possibilities for mitigation existed, and that the promisee ignored them.[284]

To some extent, this allocation rule is quite odd. The general rule is that the burden of proof rests on the party with peculiar knowledge of the facts; or, when the facts are much more difficult for the second party to

279. *See* Alaska Children's Servs., Inc. v. Smart, 677 P.2d 899, 902–03 (Alaska 1984) (finding that burden of proving mitigation damages rests on party claiming damages).

280. State *ex rel.* Martin v. Columbus, 389 N.E.2d 1123, 1125 (Ohio 1979) (quoting Annotation, *Presumption and Burden of Proof Regarding Mitigation of Damages*, 134 A.L.R. 242, 243 (1941)); *accord* Juvenile Diabetes Research Found. v. Rievman, 370 So. 2d 33, 36 (Fla. Dist. Ct. App. 1979); Cobb v. Osman, 433 P.2d 259, 263 (Nev. 1967). *Compare* Abrams v. Jackson County Bd. of Educ., 18 S.W.2d 1000, 1001 (Ky. 1929) (following minority rule placing burden of injured employee in breach case to make out his whole case). *See generally* 25 C.J.S. *Damages* § 261 (2008) (providing an extensive summary of promisor's burden of proof).

281. *See, e.g.*, *In re* Worldcom, Inc., 361 B.R. 675, 691–92 (Bankr. S.D.N.Y. 2007) (stating that the promisor carries the burden of showing that the promisee failed to take affirmative steps to mitigate damages); *Alaska Children's Servs., Inc.*, 677 P.2d at 902–03; Young v. Frank's Nursery & Crafts, 569 N.E.2d 1034, 1036 (Ohio 1991) (stating that the burden of proving failure to mitigate falls on the breaching party); *see also* Spalding v. Coulson, 770 N.E.2d 1060, 1066 (Ohio Ct. App. 2001) ("Where the court determines that the nonbreaching party has failed to mitigate and has placed the burden on the nonbreaching party, the court errs as a matter of law.").

282. *See* Koppers Co., v. Aetna Cas. & Sur. Co., 98 F.3d 1440, 1448 (3d Cir. 1996); Leavenworth Plaza Assocs. v. L.A.G. Enters., 16 P.3d 314, 318 (Kan. Ct. App. 2000); Roth v. Wiese, 716 N.W.2d 419, 434 (Neb. 2006). More accurately, the failure to mitigate is an "incomplete" affirmative defense because it will not entirely defeat recovery, but will reduce the plaintiff's damages. Sabine Corp. v. ONG W. Inc., 725 F. Supp. 1157, 1186 (W.D. Okla. 1989).

283. *Koppers Co.*, 98 F.3d at 1448; *see also In re* Rowland, 292 B.R. 815, 820 (Bankr. E.D. Pa. 2003) (quoting *Koppers Co.*, 98 F.3d at 1448). To reduce or eliminate mitigation damages, the defendant has the burden of proving that the plaintiff's mitigation efforts were inappropriate or unreasonable. Carolina Power & Light Co. v. United States, 82 Fed. Cl. 23, 36 (2008).

284. Koby v. United States, 53 Fed. Cl. 493, 497 (2002) (citing T.C. Bateson Constr. Co. v. United States, 319 F.2d 135, 160 (Ct. Cl. 1963)).

prove, the burden falls on the party with the lesser difficulty of proving the facts.[285] The mitigation rule, however, contradicts this burden-of-proof principle because it requires the promisor to plead and prove facts that are both much more accessible to the promisee and, quite likely, more difficult for the promisor to establish.[286] Two good examples of this difficulty for promisors are whether an injured landlord after the tenant's breach of contract exerted reasonable efforts to locate other tenants and whether an injured employee after an employer's breach of contract made appropriate inquiries to obtain a comparable position. Some judicial opinions analyzing these two scenarios have discussed these unusually difficult evidentiary problems for breaching promisors.[287]

Notwithstanding the above tensions with the ordinary evidentiary rules and the inconsistency with the legal and moral policies favoring the promisee's mitigation of the loss, proof of mitigation is not part of the promisee's case-in-chief.[288] The promisor, as a matter of policy, bears the

285. *E.g.*, Browzin v. Catholic Univ. of Am., 527 F.2d 843, 849–50 (D.C. Cir. 1975); Woerth v. City of Flagstaff, 808 P.2d 297, 304 (Ariz. Ct. App. 1990); Amaral v. Cintas Corp. No. 2, 78 Cal. Rptr. 3d 572, 597 (Ct. App. 2008); Pace v. Hymas, 726 P.2d 693, 697–98 (Idaho 1986); Iowa Comprehensive Petroleum Underground Storage Tank Fund Bd. v. Shell Oil Co., 606 N.W.2d 370, 374 (Iowa 2000); Artificial Lift, Inc. v. Prod. Specialties, Inc., 626 So. 2d 859, 862–63 (La. Ct. App. 1993); Peace v. Employment Sec. Comm'n of N.C., 507 S.E.2d 272, 281 (N.C. 1998); Acuity Mut. Ins. Co. v. Olivas, 726 N.W.2d 258, 266 (Wis. 2007); *see also* United States v. New York, New Haven & Hartford R.R., 355 U.S. 253, 256 n.5 (1957) (developing a rule based on "considerations of fairness"); Metzl v. Leininger, 57 F.3d 618, 622 (7th Cir. 1995) ("Economy in litigation also requires that burdens of presenting evidence be assigned to the parties that can produce the necessary evidence at least cost.").

286. The absence of proper mitigation efforts amounts to proof of negative facts. *See* Manor Park Apartments, L.L.C. v. Delfosse, No. 2006-L-036, 2006 WL 3772214, at *3 (Ohio Ct. App. Dec. 22, 2006); *cf.* Int'l Harvester Co. v. Ruckelshaus, 478 F.2d 615, 643 (D.C. Cir. 1973) (noting the "often-formidable task of establishing a 'negative averment'").

287. *See* Franzen v. Ellis Corp., No. 03 C 641, 2007 WL 2566237, at *8 (N.D. Ill. Aug. 30, 2007) (noting that an "[employee] is in a much better position to assess his skills and interests and to know what type of job is available and attractive to him"); Grant v. New Departure Mfg. Co., 83 A. 212, 214 (Conn. 1912) (Wheeler, J., concurring) ("The employer cannot keep track of the whereabouts of his discharged [employee] . . . ."); *Manor Park Apartments*, 2006 WL 3772214, at *3 ("[T]he tenant does not have access to the landlord's business records and has no idea what efforts were, or were not, taken to attempt to rerent the [premises]."). *But see* Broadnax v. City of New Haven, 415 F.3d 265, 268–69 (2d Cir. 2005) (collecting cases placing the burden on the employer to show the employee did not make reasonable efforts to obtain work).

288. *See* Veys v. Applequist, 155 P.3d 1044, 1052 (Wyo. 2007); 22 AM. JUR. 2D

evidentiary burden to show the promisee's failure to mitigate because the courts condemn the breaching promisor as a "wrongdoer."[289] This doctrine reflects the general insight of the law that no hard-and-fast rules govern the allocation of the burden of proof; "[t]he issue, rather, 'is merely a question of policy and fairness.'"[290] In effect, the law punishes the promisor on mitigation by making him prove facts that the law understands are essentially outside of his immediate control. Very likely, the promisor's difficult burden of proof helps to explain why courts rarely find the promisee guilty of failing to mitigate.[291]

D. *Qualifications to Mitigation Responsibilities*

Without citation to authority, Professor Shiffrin concludes that the mitigation rule "favor[s] systematically the breaching promisor and not the promisee."[292] The previous Part has amassed numerous decisions showing the opposite result, most notably concerning the promisor's difficult burden of proof.[293] Even beyond this high hurdle for promisors, and notwithstanding the promisee's legal and moral "duty" to lessen any harm, a promise will rarely be unable to avail itself of the numerous qualifications listed below that considerably dilute this mitigation responsibility.

The mitigation burden "'is not onerous'"[294] and is to be "applied with

Damages § 708 (2008); 25 C.J.S. *Damages* § 261 (2008).

289. *See Broadnax*, 415 F.3d at 269 (labeling the breaching party a "wrongdoer"); Jones v. Consol. Rail Corp., 800 F.2d 590, 593 (6th Cir. 1986) (same); 25 C.J.S. *Damages* § 261 ("The party committing the wrong ordinarily has the burden of proof as to mitigation or reduction of damages."); *see also* Preston v. Keith, 584 A.2d 439, 444 (Conn. 1991) ("'[The defendant] is the wrongdoer, and presumptions between him and the person wronged should be made in favor of the latter. For this reason, therefore, the onus must in all cases be upon the defendant.'" (quoting 1 T. SEDGWICK, DAMAGES § 227, at 448 (9th ed. 1912))); *accord* Emery v. Steckel, 17 A. 601, 602 (Pa. 1889).

290. Keyes v. Sch. Dist. No. 1, 413 U.S. 189, 209 (1973) (quoting 9 J. WIGMORE, EVIDENCE § 2486, at 275 (3d ed. 1940)); *accord In re* Methyl Tertiary Butyl Prods. Liab. Litig., 559 F. Supp. 2d 424, 434 n.59 (S.D.N.Y. 2008) (quoting *Keyes*, 413 U.S. at 209).

291. For a rare example of a court ruling that the plaintiff failed to mitigate damages, see *Seaboard Lumber Co. v. United States*, 308 F.3d 1283, 1297 (Fed. Cir. 2002) (discussing the result when a nonbreaching party resold a contract on materially different terms from the original agreement).

292. Shiffrin, *supra* note 1, at 726.

293. *See supra* Part IX.C.

294. Morris v. Clawson Tank Co., 587 N.W.2d 253, 257 (Mich. 1988) (quoting Rasheed v. Chrysler Corp., 517 N.W.2d 19 (Mich. 1994)).

extreme caution" against the injured party.[295] Case law fully supports this proposition. The promisee's "[e]fforts need not necessarily be successful when viewed in hindsight."[296] The lenient guiding principle is whether, in light of the contemporary circumstances, the injured party made efforts consistent with reasonable commercial judgment by making substitute arrangements or otherwise.[297] The contract breaker may not invoke the rule either as a basis for a hypercritical examination of the injured party's conduct, or the argument that the promisee should have taken different steps that would have been wiser or more advantageous to the defaulter.[298] The law further adjusts the promisee's damages upward—which may exceed the promisee's expectation interest—to reflect all reasonable costs he incurs in attempting to avoid the effect of a total or partial breach.[299] As listed in the footnote below, so many other qualifications exist to the rule of mitigation in so many different settings that the terms "duty" or "obligation" have minimal accuracy in describing the promisee's mitigation responsibility.[300]

295. Walton v. Cooper/T. Smith Stevedoring, 709 So. 2d 941, 950 (La. Ct. App. 1998) (citing Seagers v. Pailet, 656 So. 2d 700 (La. Ct. App. 1995)).

296. S. Nuclear Operating Co. v. United States, 77 Fed. Cl. 396, 406 (2007); *accord* Citizens Fed. Bank v. United States, 66 Fed. Cl. 179, 185 n.1 (2005).

297. *See* Robinson v. United States, 305 F.3d 1330, 1333 (Fed. Cir. 2002); *In re* Kellett Aircraft Corp., 186 F.2d 197, 198–99 (3d Cir. 1950); Carolina Power & Light Co. v. United States, 82 Fed. Cl. 23, 35 (2008); Sys. Fuels, Inc. v. United States, 78 Fed. Cl. 769, 788 (2007); *S. Nuclear Operating Co.*, 77 Fed. Cl. at 406; *see also In re* Mirant Corp., 332 B.R. 139, 149 (Bankr. N.D. Tex. 2005) (arguing that extraordinary measures and substantial expenditures are not required).

One commentator agrees that "[i]n practical application, the victim's duty to mitigate is limited." *See* Adler, *supra* note 49, at 1722.

298. *In re Kellett Aircraft*, 186 F.2d at 198–99; *Citizens Fed. Bank*, 66 Fed. Cl. at 185; Koby v. United States, 53 Fed. Cl. 493, 497 (2002); Labriola v. Pollard Group, 100 P.3d 791, 797 (Wash. 2004).

299. Ind. Mich. Power Co. v. United States, 422 F.3d 1369, 1375 (Fed. Cir. 2005); *Carolina Power & Light Co.*, 82 Fed. Cl. at 36 (stating three-part test for recovering mitigation damages). Professor Shiffrin makes the conclusory argument that the law has difficulties in measuring and fully compensating for the costs incurred in mitigation. She cites no case law or examples for her position. *See* Shiffrin, *supra* note 1, at 725. Because the losses above mitigation are simply another form of consequential damages, the better view is that mitigation of damages is no more or less difficult to prove than any other consequential loss resulting from the promisor's breach.

300. (1) An injured party is not required to mitigate when it would experience undue risk, expense, or humiliation. *See Koby*, 53 Fed. Cl. at 497 (quoting 11 WILLISTON, *supra* note 125, § 1353); *see also In re* Worldcom, Inc., 361 B.R. 675, 693 (Bankr. S.D.N.Y. 2007) (quoting RESTATEMENT (SECOND) OF CONTRACTS § 350

(1981)). (2) A plaintiff "'need not . . . make other risky contracts, incur unreasonable expense or inconvenience[,] or disrupt [his] business.'" Tenn. Valley Auth. v. United States, 69 Fed. Cl. 515, 529 n.17 (2006) (quoting RESTATEMENT (SECOND) OF CONTRACTS § 350 cmt. g.)); Sprecher v. Weston's Bar, Inc., 253 N.W.2d 493, 501 (Wis. 1977) (quoting RESTATEMENT OF CONTRACTS § 336(1), cmt. a (1932)). (3) Unless the promisor has clearly and definitively repudiated the contract, the promisee need not take steps to avoid the loss. Goetz & Scott, *supra* note 224, at 975, 989 n.50. *But see* Reliance Cooperage Corp. v. Treat, 195 F.2d 977, 982–83 (8th Cir. 1952) (citing Cont'l Grain Co. v. Simpson Feed Co., 102 F. Supp. 354, 363 (E.D. Ark. 1951)) (finding no duty to mitigate in the face of anticipatory repudiation when applying pre-UCC law). (4) When the non-breaching party cannot avoid its expenses, general damages rules do not apply and the award of gross profit, not net profit, is appropriate. DP Solutions, Inc. v. Rollins, Inc., 353 F.3d 421, 429 (5th Cir. 2003). (5) When the buyer's breach is the refusal to pay the purchase price, a seller of goods has no obligation to mitigate damages. Peoplesoft U.S.A., Inc. v. Softeck, Inc., 227 F. Supp. 2d 1116, 1121 (N.D. Cal. 2002). (6) Mitigation of damages is not relevant where the parties have an enforceable liquidated damages clause. Days Inns of Am., Inc. v. P & N Enters., 164 F. Supp. 2d 255, 263 (D. Conn. 2001); NPS, L.L.C. v. Minihane, 886 N.E.2d 670, 675 (Mass. 2008). (7) The mitigation doctrine does not require a party to accept an arrangement made conditional on the surrender of its own legal rights to contract performance. Brazos Elec. Power Coop. v. United States, 52 Fed. Cl. 121, 130 (2002); Cook Composites, Inc. v. Westlake Styrene Corp., 15 S.W.3d 124, 135 (Tex. App. 2000). (8) When the promisor and promisee have an equal knowledge and opportunity to mitigate the loss, the promisor cannot complain about the promisee's failure to do so. Travelers Indem. Co. v. Maho Mach. Tool Corp., 952 F.2d 26, 31 (2d Cir. 1991); Alexander v. Brown, 646 P.2d 692, 695 (Utah 1982). (9) The promisee is not required to accept a new and different bargain with terms less favorable than those in the existing contract. Mallek v. City of San Benito, 121 F.3d 993, 997 (5th Cir. 1997). (10) The promisee has no requirement of mitigation when he has a nonexclusive contract with the promisor. Burger King Corp. v. Barnes, 1 F. Supp. 2d 1367, 1372 (S.D. Fla. 1998). (11) Mitigation will be excused as required by law. *See* Resolution Trust Corp. v. Dismuke, 746 F. Supp. 104, 106 (N.D. Ga. 1990) (noting that the sale of foreclosed property was prohibited by a bankruptcy stay). (12) No duty of mitigation exists when the contract requires the parties to exchange performance simultaneously. Erwin v. United States, 19 Cl. Ct. 47, 57 (1989). (13) The promisee is excused from mitigation when the promisor prevents him from doing so. Toyota Indus. Trucks U.S.A., Inc. v. Citizens Nat'l Bank, 611 F.2d 465, 471 (3d Cir. 1979); 5 CORBIN, *supra* note 125, § 1039. (14) The duty to mitigate does not arise until the promisee learns of the breach. A.G. Edwards & Sons, Inc. v. Drew, 978 S.W.2d 386, 391 (Mo. Ct. App. 1998) (citing Richardson v. Collier Bldg. Corp., 793 S.W.2d 366, 375 (Mo. Ct. App. 1990)). (15) When a party has received the promisor's "repeated assurances that performance will be forthcoming, the injured party incurs no duty to mitigate . . . damages." Jet Boats, Inc. v. Puget Sound Nat'l Bank, 721 P.2d 18, 25–26 (Wash. Ct. App. 1986) (citing Sears, Roebuck & Co. v. Grant, 298 P.2d 497, 497 (Wash. 1956)). (16) Mitigation does not require the injured party to contract a second time with the breaching party, especially where the breacher's alternative terms differ substantially from the original contract. Carlisle Ventures v. Banco Español de Crédito, 176 F.3d 601, 609 (2d Cir. 1999); Citizens Fed. Bank v. United States, 66 Fed. Cl. 179, 186 (2005); *Koby*, 53 Fed. Cl. at

In holding the promisor accountable for breach, the law on mitigation of damages fully supports the superior moral position of the promisee as the injured party. Contract law condemns the promisor as the wrongdoer by imposing upon the former a relatively weak obligation rife with exclusions and by granting the promisee liberal compensation rights. When it comes to any divergence between contract and promise, and the promisor's accountability for breach, Professor Shiffrin's assertion that the promisee has a "strong responsibility to mitigate"[301] incorrectly states the law.

X. CONCLUSION

Professor Shiffrin argues that although contract law associates legal obligations with morally binding promises, contract diverges from promise because the contents of the legal obligations and the legal significance of their breach fail to correspond to the moral obligations and the moral significance of their breach.[302] Professor Shiffrin asserts that contract law undercuts the moral requirement that breach should be impermissible, as opposed to being merely subject to a price through damages.[303] Indeed, she claims that contract law may sometimes make it harder for the morally decent person to behave decently.[304]

After a comprehensive review of the relevant statutes and case law, I have reached a different conclusion. Professor Shiffrin has made incorrect or incomplete analyses of many key legal points. Long-standing precedents from the great majority of state and federal jurisdictions, including the United States Supreme Court, forthrightly express strong legal *and* moral disapproval of intentional breach. I have specifically shown that these

497. (17) A seller has no obligation under the UCC to attempt to resell or otherwise mitigate damages for goods the buyer has accepted. N.W. Airlines, Inc. v. Aeroservice, Inc., 172 F. Supp. 2d 1189, 1190 (D. Minn. 2001). (18) A lost volume seller has no requirement to mitigate damages. Gianetti v. Norwalk Hosp., 779 A.2d 847, 852–53 (Conn. App. Ct. 2001), *aff'd*, 833 A.2d 891 (Conn. 2003). Finally, (19) the promisee is excused from mitigation when the promisor inflicted intentional injury. Rice v. Cmty. Health Ass'n, 40 F. Supp. 2d 788, 798 (S.D. W. Va. 1999), *vacated in part on other grounds*, 203 F.3d 283 (4th Cir. 2000); Den Norske Ameriekalinje Actiesselskabet v. Sun Printing and Publ'g Ass'n, 122 N.E. 463, 465 (N.Y. 1919); 25 C.J.S. *Damages* § 47 (2002).

301. Shiffrin, *supra* note 1, at 725.

302. *See id.* at 709.

303. *See id.* at 722.

304. *See, e.g.*, *id.* at 732 (explaining that the efficient breach doctrine actually encourages the breach of promises).

moral values are fully embedded in numerous doctrines including promissory estoppel, the implied covenant of good faith and fair dealing, the expanding availability of specific performance and punitive damages, the minority status of efficient breach theory, the foreseeability principles of *Hadley* for consequential damages, and the promisor's difficult burden of proof for mitigation of damages.

On a deeper level, I have shown the applicable statutes and cases do not support Professor Shiffrin's claims that contract law favors the promisor over the promisee, or that the law impedes the morally decent person from acting decently. She cites no examples from any court decisions from which it can legitimately be argued that contract law inhibited a party from acting in a moral fashion toward itself or the other party. To the contrary, I have shown that the legal and moral doctrines of contract correspond in that the law's structure supports—and even insists upon—the moral virtues of promise-keeping. Indeed, contract law is undergoing a transformation toward even greater enforcement of moral values, a point similarly missed by some prominent jurists and commentators.[305]

Going beyond a critique of Professor Shiffrin's article, I have added to the discussion in the literature by establishing that courts in contract cases enforce moral norms in two complementary ways: first, by respecting the autonomy of the parties, consistent with public policy, in forming their bargain under the freedom of contract; and second, by holding the promisor accountable to the promisee for the promisor's wrongdoing. This unifying theory has direct case-law support. Courts commonly use the term "autonomy" in connection with the parties' "freedom of contract."[306] Courts further rely upon the concept of making the promisor "accountable"[307] for his breach of contract. Accordingly, the more

305. Judge Richard Posner, an advocate of the minority efficient breach theory, has opined that "[i]t is a strength rather than a weakness of contract law that it generally eschews a moral conception of transactions." Classic Cheesecake Co. v. JP Morgan Chase Bank, 546 F.3d 839, 845–46 (7th Cir. 2008). Professor Allan Farnsworth, also an advocate of the efficient breach doctrine, asserts that the law shows "a marked solicitude for men who do not keep their promises." Farnsworth, *supra* note 43, at 1216, *cited with approval in* 1 ROY RYDEN ANDERSON, DAMAGES UNDER THE UNIFORM COMMERCIAL CODE § 1:8 (2009). These claims are rebutted by the statutes and case law amassed in this Article.

306. *E.g.*, Morta v. Korea Ins. Corp., 840 F.2d 1452, 1460 (9th Cir. 1988); LeGalley v. Bronson Cmty. Schs., 339 N.W.2d 223, 226 (Mich. Ct. App. 1983); Zivich v. Mentor Soccer Club, 696 N.E.2d 201, 204 (Ohio 1998).

307. *E.g.*, Simeone v. First Bank Nat'l Ass'n, 73 F.3d 184, 190 (8th Cir. 1996);

accurate conclusion is that contract law properly supports the requirement that breach is morally and legally impermissible, as opposed to being merely subject to a price through damages.

In re Managed Care Litig., 135 F. Supp. 2d 1253, 1258 (S.D. Fla. 2001); Country Club Assocs. v. F.D.I.C., 918 F. Supp. 429, 433 (D.D.C. 1996); Westchester Decorators, Inc. v. Perazzo, 701 N.Y.S.2d 820, 821 (App. Term 1999); Saint v. Pope, 211 N.Y.S.2d 9, 13 (App. Div. 1961).