**Introduction**

1. **Con-Tort Problem**
   1. Business torts often arise at the boundary between contract and tort
   2. **Contract vs. Tort**
      1. Differences
         1. Statute of limitations
         2. Different elements need to be proven
         3. Statutory considerations
            1. Statute might make one claim superior over the other claim
         4. Intentional/Unintentional
            1. Contract law has nothing to do with fault or punishment
         5. Consequential damages
            1. Contract

Consequential damages available if injury foreseeable *at the time of contract*

Consequential damages available if injury was foreseeable *at the time of wrong doing*

* + 1. **Tort Actions**🡪 Out of Pocket/Reliance Damages
       1. Allow for
          1. Punitive damages
          2. Mental anguish/emotional damages
    2. **Contract actions**- Benefit of the Bargain/Expectation
       1. DO NOT ALLOW
          1. Generally no recovery for punitive damages

Purpose of K damages is to make you whole again (compensate)- not punish

No moral censure

No fault component

No distinction between intentional and unintentional breach

However

Punitive damages may be available if conduct constituting breach is also a tort for which punitive damages are available

Generally no recovery for mental anguish/emotional harm

Unless

Breach causes bodily harm; or serious emotional disturbance was particularly likely consequence of breach

* + - 1. Statute of Frauds
         1. Classic concern of K law with no application to tort action
    1. **Advantages of tort action over Breach of K action**
       1. No statute of frauds
       2. No worries about parol evidence rule
       3. No concerns about existence of consideration
       4. No worries about contract being illegal per se
       5. Potentially longer statute of limitations due to tolling only upon discovery of the injury (depending on tort)
       6. Avoid limited liability language in a contract
       7. Avoid contract defenses
       8. May avoid necessity of joining parties to a joint contract in one action
       9. Punitive damages may be available
    2. Recipient may have a cause of action in both tort and contract

**Negligent Conduct Causing Pure Economic Loss**

1. **Pure Economic Loss**
   1. Only “money harm”
      1. Tort does not cause any personal injury or property damage
      2. No duty owed to you
   2. Courts are more likely to restrict liability in cases of only pure economic loss
2. **Limitations on Recovering for Pure Economic Loss**
   1. **Testbank Rule**
      1. **In the absence of bodily injury or property damage, party cannot sue for pure economic loss under theory of negligence (Majority Rule)**
         1. More restrictive than normal tort law which extends liability to foreseeable harms
         2. Exceptions
            1. Certain torts have been carved out of the Testbank rule as exceptions

Example

Negligent Misrepresentation, Fraud

* + 1. Virtue of Testbank rule is that it shifts all responsibility on the victims- by requiring them to get first party insurance if they want to protect against negligently caused economic harm
  1. **Policy for limiting pure economic loss**
     1. Predictability
        1. Pure economic loss is difficult to quantity/anticipate🡪 the indirect economic repercussions of negligence are virtually open-ended
           1. Even if foreseeable, not recoverable
           2. Frustrates business’ expectations
        2. Indeterminate liability
     2. Slippery Slope (disproportionate liability/where does liability end?)
        1. Open-ended scope of liability
           1. Small negligent act potentially causes a chain of economic losses
           2. Need for line-drawing
     3. Lack of insurability (third party insurance)
        1. Difficult for an insurer to measure the scope of open-ended liability
           1. Easier for potentially harmed individual parties to insure b/c those parties can more easily quantify potential losses (first party insurance)

Those losses are not open-ended

Business interruption insurance

* + - * 1. Third party insurance-your negligence harms other people
        2. First party insurance- covers your stuff, your apt burns down
        3. Ridiculous premiums or unavailability of policies
    1. Fostering Economic activity
       1. Protection of businesses, otherwise open-ended liability will deter companies from offering the risky service
          1. Consider property damages ensuing from power outage
       2. Motivates victims to get insurance to protect themselves
       3. If businesses cant get insurance, businesses go out of business
  1. Criticism for limiting recovery of pure economic loss
     1. Rule favors tortfeasors over victims
        1. No deterring effect
     2. Lots of uninsured innocent parties will suffer pure economic damages from a foreseeable negligent event, without any relief
        1. Victims will not be made whole
        2. Departs from traditional tort principles of foreseeability and proximate cause

**Fraud and Negligent Misrepresentation**

1. **Misrepresentation**
   1. Technically encompasses (3) torts of misrepresentation
      1. Fraud or fraudulent misrepresentation (intentional tort)
         1. Also known as “deceit”
         2. Tort you can bring in almost every context b/c we expect people not to lie
      2. Negligent Misrepresentation (negligence in tort)
         1. Only shows up in certain cases where we believe you should use reasonable care- generally in advice giving role
      3. Innocent Misrepresentation- functional equivalent to breach of contract, strict liability
         1. Minority recognize this
         2. Very few permissible situations
   2. All misrepresentations are based on false statements
      1. Statement = written, oral, or conduct
2. **Fraudulent Misrepresentation vs. Negligent Misrepresentation**

|  |  |  |
| --- | --- | --- |
|  | Fraudulent | Negligent |
| Statement | False statement of material fact OR failure to disclose a material fact (Omission) | False statement of material fact |
| Culpability | Scienter: intent to deceive | Negligence- duty, breach, causation, harm |
| Liability (Who can be π) | Intended for π to rely or had reason to expect (highly foreseeable)- ***constructive knowledge***; more potential liability | Intended to supply information to π or limited group- ***actual knowledge*** required (other approaches exist R2T §552) |
| Reliance | Justifiable reliance (subjective reliance only required) (1) don’t have to investigate even if reasonable P would (2) if ∆ preyed on your vulnerability, still justifiable even if not reasonable  🡪 Contributory Negligence not defense, but can still challenge the π’s reasonableness as part of their claim for a prima facie case | Reasonable reliance (subjective and objective reliance)  -Must act as reasonable π would  🡪 Contributory Negligence is available as a defense |
| Damages | Benefit of the bargain (expectation) + punitive damages | Out of pocket damages (reliance) |
| Defendant | Fraud applies to anyone | Courts USUALLY only apply negligent misrepresentation to professionals, but 552 is not explicitly limited to professionals |

1. **Fraud**
   1. **Five Prima facie elements of fraud**
      1. **False statement of material fact or failure to disclose a material fact based on a duty to disclose**
         1. **Anyone can be a ∆ in fraud action (no privity requirement)**
      2. **Scienter or intent to deceive, mental state**
      3. **Intent that the π rely on the statement**
      4. **Π Justifiably relies on the ∆’s statement**
      5. **Π is damaged by his justifiable reliance**
   2. ***False Statement of material fact***
      1. Generally
         1. False statement of material fact
            1. ***Oral or written*** statement
            2. ***Physical act that conveys words***

(covering whole in wall with picture)

* + - * 1. ***Silence is not actionable unless there is a positive duty to disclose***
    1. ***False Statements***
       1. Misleading Statements (Half-truths)
          1. Half truth: When statement only reveals part of the truth

The unsaid portion misleads

Not necessarily a false statement R2T §529

Stating that half truth, which the maker knows or believes to be materially misleading b/c of its incompletion is a fraudulent misrepresentation

* + - * 1. Defense against this may be to sell “as is”
      1. Concealment
         1. R2T §550 Liability for fraudulent concealment

Actively concealing material info from the other party is equivalent to a fraudulent misrepresentation

* + - * 1. Two common instances of concealment

Active concealment of a defect, facts, or knowledge

Preventing another party from making an investigation

* + - * 1. Example of conduct which constitutes a statement
        2. Lying that you don’t know about something, when in fact you do, is also fraudulent
    1. **Materiality**
       1. Materiality of Fact
          1. Whether the fact would affect the recipient’s conduct in the transaction at hand
       2. R2T § 538
          1. Material if

Reasonable man would attach importance to existence or nonexistence in determining his choice of action in a transaction; or

Maker of representation knows or has reason to know that the particular recipient of the information would regard the information as important in determining his course of action

* + - 1. Immateriality an liability
         1. Lying about immaterial maters is not actionable
    1. Nondisclosure- **silence is not actionable unless there is a positive duty to disclose**
       1. ***In an arm’s length transaction, a person has no duty to disclose even material facts (Majority Rule)***
          1. Arm’s length transaction- one negotiated between unrelated parties
          2. No liability for failing to disclose material info to opposing party
          3. Swinton rule- is essentially Caveat Emptor
       2. Duty to disclose may be difficult to prove, so better to identify an affirmative fraudulent action
       3. Courts unlikely to find a buyer has a duty to disclose
       4. ***Policy***
          1. For majority rule

Places onus on individual parties to do proper research and ask the right questions

Rewards the effort to research and ask the right questions

Superior information is a legitimate advantage without liability

Allowing people to profit from info they have produced (incentive to produce)

Incentive to develop info and investigate further

Questions may lead to statements which would be actionable as fraud

Buyer must ask broad questions

Reflects societal judgment regarding difference between nondisclosure and affirmative fraud (lying)

* + - * 1. Against majority rule

Seller has more information and should therefore be disclosing that info

Buyer protection- opposite of caveat emptor

If unequal bargaining power or sophistication of parties, buyer may not know which questions to ask

* + - 1. Texas Real Estate Statute Exception
         1. Texas common law has been preempted by statute regarding what must be disclosed in a real estate transaction
    1. R2T §551 Liability for Nondisclosure: **When is there a duty to disclose** and silence becomes fraudulent
       1. “One who fails to disclose to another a fact that he knows may justifiably induce the other to act or refrain from acting in a business transaction, is subject to the same liability to the other as though he had represented the nonexistence of the matter that he has failed to disclose, IF BUT ONLY IF, he is ***under a duty to the other*** to exercise reasonable care to disclose the matter in question”
       2. **One Party to a business transaction is under a duty to exercise reasonable care to disclose to the other before the transaction is consummated, in order to:**

**When is there a Duty to Disclose?**

* + - * 1. **Satisfy a fiduciary duty**

Fiduciary duty is the highest duty that the law can impose

Must act solely for beneficiary’s interest

May include contractual duty and other types of confidential relationships

Insurer-Insured

Doctor-Patient

Priest-Parishioner

Partners

* + - * 1. **Prevent a (half-truth) partial statement from being misleading**

May be actionable as a half truth action instead of a non-disclosure action

* + - * 1. **Subsequently acquired info that makes previously disclosed information untrue**

When statement is true at time made, but no longer true, prior to the formation of the contract

* + - * 1. **Falsity of a previous representation** if one learns the other party is acting on the previous false representation
        2. **Facts basic to the transaction**- if he knows that the other party is about to enter into it under a mistake as to them, and that the other party, b/c of relationship btwn them, the customs of the trade, or other objective circumstances, would reasonably expect disclosure of those facts

*What are “Basic facts to the transaction”*

**Facts Basic to**

**the Transaction**

Facts that are assumed by the parties as a basis/purpose for the transaction

Not simply something which affects the value of the transaction

“a fact that goes to the basis or essence of the transaction, and is an important part of the substance of what is bargained for or dealt with” (comments definition)

***Extrinsic factors are not basic to transaction***

definition is expanding

Variables as to when a court might find a “basic fact”

Is it a defect to the subject matter of the contract?

Certain vs. speculative information

More certain = basic fact🡪 more likely to require disclosure

Speculative information cuts more toward non-liability for nondisclosure

Who has easier access to the information

Is this the seller pushing something or the buyer purchasing something unsolicited

Cts more inclined to require disclosure if seller approaches buyer

“Basic facts” element is the restatement attempts to lead the common law by charting new territory

Applied in instances of extreme unfairness tantamount to a swindle

POLICY: may show an interest in ensuring that both parties understand the purpose of the transaction (weak argument for efficiency)

* + - 1. Texas has not explicitly adopted §551
    1. Compare false statement vs. silence case
       1. If false statement, don’t have to worry about whether duty was present
       2. Don’t have to worry about whether it is a basic fact to the case
  1. **Scienter- Intent to Deceive**
     1. Scienter is hallmark of fraud
        1. Fraud requires a showing that the false representation was made either
           1. Knowingly;
           2. Without belief in its truth; or
           3. Recklessly with regard to its truth or falsity
     2. ∆ is liable if there is an intention to mislead (deceive) regardless of whether there is an intention to do harm
     3. Scienter and motive are different
        1. Scienter is the intent to deceive or reckless action constituting deception
        2. Motive is concerned with an intent to cause harm
           1. Motive is relevant with regard to punitive damages

Not relevant with regard to liability inquiry

* + 1. Knowledge of falsity is not essential
       1. It is enough if ∆ believes the representation to be false
    2. Testing one’s belief in Truth/Falsity of a statement
       1. Whether a reasonable man in the same situation as ∆ with ∆’s knowledge and means to knowledge might well believe what the ∆ claims to have believed and consider that representation as substantially true
          1. Unreasonableness of a ∆’s belief may signal that the ∆ probably didn’t not possess such a belief

Still subjective test

* + 1. Not Fraud
       1. Making a false statement that the actor believes is true
          1. No scienter exists
       2. Negligently making a false statement
          1. Must be at least reckless
  1. **Reliance: Intent that π rely on statement of material fact**
     1. Reliance generally
        1. Usually must show subjective reliance and objective reliance
           1. Subjective reliance

Actual in-fact reliance by the π on the misrepresentation

* + - * 1. Objective reliance

Whether reasonable person would have so relied

* + - 1. Materiality
         1. Best to think of materiality as separate element of the tort

*Cannot rely on something that is not material*

* + 1. Liability for fraudulent misrepresentation
       1. R2T §531
          1. One who makes a fraudulent misrepresentation ***is subject to liability to the persons or class of persons*** (does not have to be specific person) whom he ***intends*** or has ***reason to expect to*** act or refrain from action in reliance upon the misrepresentation, for pecuniary loss suffered…***in the type of transaction*** in which he intends or has reason to expect their conduct to be influenced
          2. Intend- Actor has purpose or desire to bring about a certain result
          3. Reason to expect = ***Highly foreseeable***

Reasonably foreseeable is insufficient, has to be more

Maker of misrepresentation must have information that would lead a reasonable man to conclude that there is an especial likelihood that it will reach those persons and will influence their conduct

* + - * 1. Who can be a plaintiff?

Class of persons- actual identity not required

Someone who ∆ intended to rely, or someone that the ∆ had reason to expect to rely (highly foreseeable)

* + - * 1. Type of transaction limitation

Loss must occur with respect to type of transaction contemplated

Small differences in transaction details are allowed

* + 1. Justifiable Reliance- particular to fraudulent misrepresentation
       1. Justifiable reliance is determined in relation to a particular π, not by a community standard
          1. Subjective reliance
       2. ***Justifiable reliance is a lesser standard than reasonable reliance, only because it allows for two exceptions***

**Justifiable**

**Reliance**

* + - * 1. π does not have a to investigate, even if reasonable P would
        2. If ∆ preyed on π’s vulnerability or gullibility, π may still be justified in his reliance EVEN though it was NOT reasonable

Standard is justifiable so that even a gullible person may recover in the event of a fraud

Client can act a little dumber

* + - 1. **Contributory Negligence**
         1. R2T §545A No affirmative defense of Contributory negligence

Contributory negligence does not bar recovery for reliance upon a fraudulent misrepresentation

Contributory negligence means you did not act as a reasonable person

even if you don’t act as reasonable person, you are not barred from bringing claim and can still satisfy justifiable reliance

* + - * 1. You CAN contest the prima facie elements of π’s case and assert that his justifiable reliance was unreasonable,

you are challenging an element of his claim,

***Not asserting it as a defense***

* + 1. False statement & Duty to Investigate
       1. ***False statement***
          1. R2T 541 Representation known to be false

No justifiable reliance if one knows that the statement is false or its falsity is obvious to him

**Cannot recover if cursory investigation or examination would make representation patently false**

**Cursory examination = using your senses**

**Ex- ordinary observation**

Where is line between using your senses and conducting an investigation

* + - * 1. Obviousness of a statement’s falsity is a question of fact

Determined in light of intelligence and experience of misled individual

* + - 1. ***Investigations-*** 
         1. R2T §540 Duty to Investigate

No duty to investigate even though one might have ascertained falsity of the representation if the investigation had been made

Even if investigation is possible without considerable trouble OR if reasonable people would have made an investigation, there is still NO duty to investigate

HOWEVER, If cursory glance would reveal falsity, falsity is considered obvious and may not be relied upon

* + - * 1. RULE- no duty to conduct investigation, but MUST make cursory examination using senses
        2. **Effect of investigation**

Majority Rule

*Commencing your own investigation is only evidence of non-reliance on ∆’s representation*

Respects concept of “partial reliance”

It is one of many factors and is not conclusive

Minority rule

*Investigation precludes reliance*

Moll does not like this rule b/c it ignores possibility of partial reliance

* 1. **Damages for Fraudulent Misrepresentation** 
     1. **Benefit of the Bargain Damages** (***Majority Rule) (Expectation damages)***

🡪***(traditional Contract damages)***

* + - 1. Damage Calculation
         1. Difference between what was promised and what was actually received

**Same Formula used to assess damages in Contract Cases**

* + - 1. Seek to compensate π as if transaction had been carried out as represented
         1. A bit unusual for tort damages
      2. Benefit of the bargain damages usually result in greater damages
         1. Go beyond making you whole
         2. Π normally prefers benefit of the bargain damages

EXCEPTION

A bad deal which was not going to be fruitful

* + - 1. Some Jurisdictions allow πs to choose between benefit-of-the bargain damages or out-of-pocket damages (***Texas***)
         1. Why would you ever want reliance rather than expectation/benefit of the bargain

If you struck a bad bargain, you don’t want to handle it using expectation damages and you would prefer reliance damages

* + 1. **Out of Pocket Damages** ***(Minority Rule)(Reliance Damages)***

**🡪*(traditional TORT damages)***

* + - 1. Damage calculation
         1. Price you paid- value of what you got
         2. Recoupment of actual losses

***More consistent with tort law***

* + - 1. Situations when bad bargain took place, OOP damages could be preferred🡪 most of the time BOB will be better
         1. If you pay $62,500 for a piece of land

The value actually ends up being $27,500

The value as represented was $50,000

Benefit of the Bargain: 50,000- 27,500 = $22,500

Reliance Damages: 62,500-27,500 = $35,000

* + 1. **Consequential damages**- damages that were foreseeable at the time of the tortuous conduct
    2. **Punitive**- wanton callous disregard- even if you meet prima facie elements of fraud does not mean you can get punitive damages
       1. In fraud cases- punitive given if you intended to HURT

1. **Misrepresentations of Opinion, Law & Intention 🡪 applicable to both fraud and negligent misrepresentation** 
   1. Opinion
      1. Universally Incorrect Rule
         1. An opinion cannot be the basis for fraud (WRONG)
            1. Notion that opinions are subjective or conjecture and people should recognize an opinion as someone’s view and not fact
            2. HOWEVER, every opinion contains at least one statement of fact:

That the maker of the opinion holds that opinion

You are stating the fact that it is your opinion

* + 1. Opinion deals with reliance element
       1. Courts will allow an opinion to be basis of misrepresentation action if court considers the π’s reliance to be justifiable
       2. Courts acknowledge some types of opinions on which π may rely
    2. **R2T 539 Representation of Opinion Implying Justifying Facts**
       1. A statement of opinion as to facts not disclosed and not otherwise known to the recipient may, if reasonable, be interpreted as an implied statement
          1. That the facts known are not incompatible with his opinion
          2. That the knows facts sufficient to justify him forming the statement
       2. **Example**: statement that a bond is a good investment, even though made by a person attempting to sell it, is a fraudulent misstatement of the actual character of the bond if the vendor knows that the interest on the bond has for years been in default and the corporation that issued it is in the hands of a receiver.
          1. Although some allowance must be made for puffing or depreciation by an adverse party, such a statement is so far removed from the truth as to make it a fraudulent misrepresentation of the character of the bond.
    3. **Opinion of Adverse Party**
       1. *Generally no justification for relying on opinion of an adverse party,* ***UNLESS****:*
          1. Person purports to have special knowledge that recipient does not have

This cannot be read literally

* + - * 1. Person owes a fiduciary duty to the recipient
        2. Person has successfully gained someone’s trust or confidence; or
        3. Person has some other special reason to expect that recipient will rely on his opinion
      1. Policy
         1. In adverse situation, recipient’s guard should be up
         2. Unreasonable to rely on an opinion when the speaker has an adverse interest
    1. **Opinion of Disinterested Party** (apparently disinterested)
       1. Reliance is justifiable if opinion is from person whom the recipient reasonably believes to be disinterested and the fact that such a person holds the opinion is material
       2. Circumstances under which and manner in which opinion is expressed are important
       3. Policy
          1. No interest in the transaction = no reason to be pushing one interest over the other
          2. No reason for person to offer a dishonest opinion

Disinterested party has no reason to mislead

* + 1. **Puffery**
       1. an exaggerated statement of high value occurs so frequently that we all recognize that is not meant for reliance
          1. Everyone understands such talk is designed simply to push the product
       2. Puffery is generally not actionable🡪 no justifiable reliance
       3. Puffing vs. Actionable Opinion
          1. Specificity of statement🡪 more specific, more likely to be actionable
          2. Whether or not opinion is objectively verifiable, more actionable
          3. Context
          4. Whether its written or oral 🡪 written puffery more likely to be actionable b/c writing appears to be more reliable

oral statements are more difficult to verify and involve greater recall, speculation, interpretation errors, potential fabrication

* + 1. **Misrepresentation of Law**
       1. Opinion of law is actionable just as an opinion about anything else might be actionable
       2. Statement of fact regarding law is actionable just as actionable just as an other statement of fact might be actionable
    2. **Misrepresentation of Intention**
       1. A misrepresentation of intention is almost universally regarded as a statement of fact
       2. R2T § 530
          1. Representation of maker’s own intention to do or not to do a particular thing is fraudulent if he does not have that intention
          2. To be actionable, maker of representation must in fact NOT have the stated intention
       3. Proof of Intention not to Perform
          1. May be established solely by proof of nonperformance

May be a case where contract is breached so rapidly that a jury could infer an intention not to perform

* + - * 1. Additional evidence is necessary to establish misrepresentation of intention

Scienter problem

When entering into a contract there is an implicit representation of an intent to perform

Regardless of how stupid rationale for intending to perform is, there is no misrepresentation if that person honestly possess that intention

* + 1. **Statement of Intention** 
       1. When reliance on Intention is justifiable- recipient of fraudulent misrepresentation of intention is justified in relying upon it if the existence of the intention is material and the recipient has reason to believe that it will be carried out
       2. Your intent is a factual material representation-
          1. It is a fact that you intend to do something and therefore others are supposed to be able to rely on it
       3. Recipient must believe that intention is “firmly entertained” and will be carried out
          1. Reasonableness depends on circumstances
       4. **Negligence-** unreasonable for you to sign contract when you knew there was a lawsuit against you which could take half of your company out
          1. Consider capacity and circumstantial evidence
    2. **Prediction**
       1. Prediction is just an opinion about some future event
          1. No difference between prediction and opinion

Both usually are not actionable

* + - * 1. Prediction by an apparently disinterested party, like an opinion by an apparently disinterested party, may be actionable
    1. **ConTort Problem**
       1. If a party to a contract simply changes his mind down the road and does not perform, it is not a tort-
          1. Breach of contract
       2. Blurs the Contort line b/c certain breaches of contract can be tortuous

1. **Negligent Misrepresentation**
   1. **Generally**
      1. The distinguishing feature between fraud and Negligent Misrepresentation is scienter
      2. Negligent Misrepresentation is an exception to the Testbank rule that there can be no recover in a negligence based action for pure economic loss
      3. Negligent misrepresentation is most always associated with professionals (accountants, auditors, attorneys, etc)
         1. Every jurisdiction will allow a suit against an expert/professional for NM
         2. Expectation that professionals will speak with care
         3. Professionals usually have measurable standard of performance
            1. Published standards of conduct exist
      4. Many jurisdictions do NOT recognize NM action against laypersons in arm’s-length transactions
         1. For arm’s-length transaction there is no baseline standard of conduct
            1. Justification for limiting NM to professionals
         2. Texas likely would allow NM action against laypersons
   2. **Elements of Negligent Misrepresentation** 
      1. Prima facie elements of NM
         1. False statement of material fact
         2. Negligence (lower level of culpability)
         3. Intent to supply information to π or limited group of which the π is a member (who can be a π)
         4. Π reasonably relies on the information
         5. Π is harmed
         6. Generally limited to ∆ professionals (who can be a defendant)
   3. **Negligent Misrepresentation involving Physical Harm**
      1. **R2T §311** Negligent Misrepresentation involving Physical Harm
         1. **One who negligently gives false information to another is subject to liability for physical harm caused to the other in reasonable reliance upon such information, where such harm results**
            1. **To the other, or to such third persons as the actor should expect to be put in peril by the action taken.**

**R2T §311**

**Negligent Misrepresentation Involving Physical Harm**

* + - 1. Such negligence may consist of failure to exercise reasonable care in ascertaining the accuracy of the information, or in the manner in which it is communicated.
      2. Broader liability than liability for a strictly pecuniary loss
         1. Physical harm will have a broader range of liability
      3. Liability may attach even if the representation is given gratuitously
         1. Distinguished from 552 where only economic harm results, ∆ may avoid liability for gratuitous services
      4. Not an exception to Testbank
    1. Publishing Company Context- ***physical injury occurs*** after readers eat mushrooms which were supposedly safe according to encyclopedia🡪 ***Publishers and Author Not liable***
       1. Ct held publishers did not have duty to verify accuracy of information in the interest of public policy
          1. Hinders first amendment
          2. Secondary liability
          3. Will impede publishers from publishing more books
       2. What about liability of authors?
          1. Indeterminate scope of liability
          2. Hindering publication of new texts
       3. Most cts will not extend R2T 311 liability to authors
          1. Under R2T these suits would clearly be permitted, but policy considerations prevail in this instance
       4. If the incident occurred via verbal advice, you could probably sue, but if you read it in a book then cant sue b/c of first amendment implications
          1. Probably constrained to manuscripts
          2. Where is the line between R2T illustrations and public policy exceptions
  1. **Liability to Third Parties for Economic Loss**
     1. Four Approaches: *Ultramares*, Near Privity Rule (*Credit Alliance*), *Citizens*, §552
        1. **Ultramares (Cardozo)**
           1. Most strict, most favored by accountants/auditors/etc
           2. **Third party must be in privity with negligent actor in order to impose liability**
           3. Policy

Without privity limitation, accountants would be exposed to liability “in an indeterminate amount for an indeterminate time to an indeterminate class”

Liability would be much too wide-ranging (Testbank problem)

* + - 1. **Near-Privity Rule (Credit Alliance) (popular, not Majority)**
         1. Bond between the accountant and interested 3rd party is so close as to approach that of privity
         2. **Near Privity Test**

**To hold accountants liable to non-parties, π must show:**

**Known Purpose- Accountant was aware that his product was to be used for a particular purpose or purposes**

**Known Party- a known party was intended to rely on the product**

**Approach #1**

**Approach #2**

**Link- accountant exhibited some conduct which links them to the party that evinces the accountant’s understanding of that party’s reliance**

**Requires some sort of interaction between accountant/professional and non-privity 3rd party**

**Favors actual knowledge of the party over constructive knowledge**

**Direct communication, meetings, personal representations, specific arrangements, giving a copy to 3rd party**

Last element seems to be superfluous boot-strapping

Less strict than Ultramares, but still restrictive

Most likely this case overrules Ultramares

* + - * 1. Rationale for near privity

Assumption of risk- auditors possess some degree of knowledge that there is reliance associated with their audit and possible exposure

As long as there is no linkage, you can know about them and the purpose and be fine

Accountant should efficiently address potential risk/liability

Didn’t want to overtly overrule Cardozo

* + - * 1. Criticism- Not fair to expose auditor to untold amounts of liability

Clients are generally more culpable than auditor

Clients provide the faulty financials- either intentionally or negligently

* + - 1. **Citizens Approach (Reformist Approach) (Minority)**

**Approach #3**

* + - * 1. No privity requirement- as long as foreseeable, auditor can be liable
        2. **To hold accounts liable to non-parties, π non party must show:**

**Non-party π suffered reasonable, foreseeable injury resulting from accountant’s negligent action**

* + - * 1. ***UNLESS***, court decides that recovery should be denied as a matter of public policy:

Injury too remote from negligent act;

Injury is wholly out of proportion to the culpability;

In retrospect, it appears too highly extraordinary that the negligence should have brought about the harm

Allowing recovery would place too unreasonable a burden on the negligent tort-feasor;

Allowance of recovery would be too likely to open the way for fraudulent claims;

Allowance of recovery would enter a field that has no sensible or just stopping point

Indeterminate liability language similar to Testbank

* + - * 1. Policy

Protection for innocent 3rd parties relying on the accuracy of the financial statements

Deterring accountants from negligent practices

Other reasons exist for accountants to act prudently

Without imposition of liability, cost of credit will go up as banks pass cost to consumer

Banks spend more on more credit reports

Accountants can spread the risk through liability insurance

b/c risk is not quantifiable and often speculative, it is difficult to ascertain a premium

how to you write a policy to cover reasonably foreseeable damage

Costs will get passed down to the creditors seeking the audits

* + - * 1. Problems with Citizen’s Bank

Increased auditor liability might lead to a decrease in availability of audits🡪 *decrease in lending*

Different costs to creditors

Liability out of proportion to fault

Client retains primary control of financial reporting and may be true fraudulent actors

Difficult to quantify liabilitys

Massive Liability imposed for a negligence tort

Obstacles to attaining Insurance

* + - 1. **R2T § 552 (Texas) (Majority)- intermediate approach**

**Approach #3**

**Approach #4**

* + - * 1. **Rule: liability attaches to one who, in the course of his business, profession, employment, or in any other transaction in which he has a pecuniary interest, fails to exercise reasonable care and supplies false information to another for guidance in a business transaction**
        2. Liability attaches when:

Loss is suffered by the person or one of a limited group of persons for whose benefit and guidance he intends to supply the information or knows that the recipient intends to supply it; and

He intends that information to influence such persons in a certain transaction or a substantially similar transaction

Basically- *unintentionally supplying false information in a transaction in which they have pecuniary interest*

* + - * 1. **Limitations to qualify as π or ∆**

**∆ must *intend* to supply info to π, or ∆ knew client was going to give it to π**

Transactions you intended to influence or knew the client intended to influences

Compare with Credit Alliance (near privity) don’t care about what ∆’s intention is, just what he knew (party or person)

**∆ must have Pecuniary Interest-** “Course of business, profession, employment, or in any other transaction, in which he has a *pecuniary interest*”

Pecuniary interest usually found if information is given in context one one’s business, employment, or profession

Restatement comment suggest “pecuniary interest” modifies the first part “business, profession, employment”

Not everything done in course of profession or employment is actionable, bc possibly no pecuniary gain

***BUT, ct says giving business advice is sufficient indication he has a pecuniary interest, even without consideration, but not conclusive***

Pecuniary interest may be ***indirect***-

Giving info in the course of your business is good evidence of pecuniary interest, but its not conclusive

Easily blurred line which may be argued both ways

It is unclear how attenuated the interest can be

Ex- give advice + business card

***Under 552, No duty of care when information is given only gratuitously (no pecuniary interest)***

**Negligent misrepresentation must be part of Substantially Similar transaction**

Whether departure from contemplated transaction is so major and so significant that if cannot be regarded as essentially the same transaction

Difference in the loan size or amount;

Different purpose than initially represented to the accountant

Ordinary business practices and attitude taken into account

Whether the departure from the contemplated transaction is so major and so significant that it cannot be regarded as essentially the same transaction

“Notice requirement” to the auditor

**π must be a “person or one of a limited group of persons”**

Does not have to be a specific party, no exact identity required

***Limited group***

Comment suggests “banks” is a limited group

Potential Investors is NOT a limited group (5th Cir.)

Illustration 4: 1000 prospective purchasers = limited group and auditor subject to liability

Illustration 9: uses bidders

***Compare with Credit Alliance near privity rule, which requires you know the exact identity of π***

**∆ must have actual knowledge of π (group/individual) and transaction**

Actual knowledge of group and transaction (or substantially similar transaction)

Constructive knowledge insufficient

Customary use insufficient

Ever-present possibility of repetition is insufficient

Not liable to every foreseeable consumer of financial information

When does professional have actual knowledge?

*Actual knowledge is measured at point of inception of the arrangement between accountant and client; OR*

Risk assessed at time of contract

**Clause:** if material changes occur, then accountants reserve the right for different time of delivery with different costs

*Liability attaches when content of audit is published, not by the foreseeable path of harm envisioned by jurists years after an unforunate business decision;*

Molls does not like this rule b/c of changing conditions that do not let auditors assess risk

* + - * 1. **Nothing in §552 limits negligent misrepresentation to professionals**
        2. More expansive than Credit Alliance near privity rule

b/c broader class of potential πs

* + - * 1. Policy

Confront the risk- Allows auditors/professionals to address risks and imposes liability commensurate with those risks

Makes auditor aware of potential exposure (notice) and then can decide based on magnitude of exposure if he wants to conduct the audit

Extends liability without the harsh effects of the Citizens Bank Rule (no privity, should be foreseeable)

Limits liability to specific persons or limited groups

Does not promote exclusive reliance on auditors

Reasonable investors should be encouraged to conduct some investigation deeper tan just auditor report

Investor may commission its own audit or establish direct communication with the auditors

Auditor is not an insurer for bad investments

Company/client is actually responsible and engages in fraudulent activity

Books can be cooked very well- fraud tough to detect

Client is real wrongdoer- possesses primary responsibility for scandal

At best accountant is secondary watch dog

Easy for 3rd party to lie and say they relied solely on the audit report in decision making process, when actually it was one of many factors

Burdening auditors will effect economic development- they will avoid businesses with high risk of failure like start ups, need protection so they can go in and conduct audits

* + - * 1. **§552 and Attorneys**

No reason that §552 should not apply to attorneys

Courts generally acknowledge that representation is not reliable when it occurs in adversarial context

Inevitably this affects atty’s advocacy for their clients

Rule imposes a duty to non-clients

There will be instances where duty to non-client and fiduciary duty come into conflict

Some argue lawyers are different b/c supposed to zealously advocate for client

Communications to non-clients will affect representation of client

Lawyers can limit liability through disclaimers

* + 1. ***Non-professionals & Negligent Misrepresentation*** - NM extends to lawyers and other professionals b/c they have standards of care which you can use to measure their actions by and determine if their conduct was negligent
       1. Only Professionals- Weisman argues- failure to exercise due care only creates economic loss, and you need more to impose tort liability
       2. Everyone- §552 does not limit to scope to professionals
          1. Available in arms-length transactions

Facially 552 applies anywhere the requirements are met, but whether court will actually accept its application is unclear

* + - * 1. Moll thinks it should be limited to professionals for policy reasons b/c there are clear standards we can hold them to
    1. **Negligent Misrepresentation & Public Policy**
       1. Tort law is essentially state common law
          1. Always policy reasons to limit or restrict common law torts
       2. First Amendment
          1. Concerns about holding publishers/authors liable for negligent misrepresentations
          2. Chilling Effect

Restricting dissemination of ideas for fear of broad liability

* + - 1. No duty for publishers to investigate content of publications
    1. **Reliance**
       1. Generally
          1. Reasonable reliance includes

Subjective reliance- actual, in-fact based on the misrepresentation

Objective reliance- whether reasonable person would have so relied

* + - * 1. **If π acts unreasonably, then π loses b/c prima facie elements of case are not met🡪 Tort fails**
      1. Materiality-
         1. Best to think of materiality as separate element of the tort

Cannot rely on something that is not material

* + - 1. **Contributory negligence R2T 552A**
         1. A recipient of negligent misrepresentation is barred from recovery for pecuniary loss in reliance upon the misrepresentation if he is negligent in so relying
         2. **Contributory negligence is a complete defense**

**Negligent = unreasonable**

* + - 1. Contrast with fraud, where CN is not a defense!
    1. **Damages for Negligent Misrepresentation (reliance/out of pocket)**
       1. Out-of-Pocket Damages
          1. Damages for negligent misrepresentation are measured as out-of-pocket damages

Difference between value of what is received and value of what is exchanged

* + - * 1. Usually results in less damages than benefit of the bargain damages

Reflects less culpable mental state for negligent misrepresentation

* + - * 1. R2T § 552B. Damages for Negligent Misrepresentation
        2. Texas has adopted out-of-pocket damages as measure of damages for negligent misrepresentation
      1. Consequential Damages
         1. Consequential damages may also be available but may be harder to get than in fraud case
      2. No mental anguish, emotional damages available
      3. Punitive damages *may* be available for “gross negligence
  1. **innocent misrepresentation**
     1. Generally
        1. **Elements**
           1. **Misrepresentation of material fact or failure to disclose a material fact;**
           2. **Intent for π to rely (on disclosure or non-disclosure)**
           3. **Justifiable reliance**
           4. **Damages**
        2. Innocent misrepresentation may be actionable if declarant has some means of knowing, ought to know, or has the duty of knowing the truth
           1. No scienter or negligence requirement

Innocent misrepresentation is equivalent to strict liability

* + - * 1. Simply must make a misrepresentation that turns out to be false
      1. Minority Rule: VERY Few cts allow actions under this cause
         1. Not recognized in Texas
         2. No general expectation for people to be 100% accurate, 100% of the time
      2. Codified at R2T §552C- “one who in a sale, rental, or exchange transaction with another, makes a misrepresentation of a material fact for the purpose of inducing the other to act or refrain from acting in reliance upon it, is subject to liability to the other for pecuniary loss caused to him by his justifiable reliance on the misrepresentation, even though it is not made fraudulently or negligently
         1. Super broad- includes almost any arm’s length transaction
         2. Most jurisdictions have not adopted this provision and if they have, they have common law principles limiting it
      3. Negligent vs. Innocent misrepresentation-
         1. Innocent is analogous to strict liability
         2. Negligence requires some showing of culpability- must prove that someone did not act as reasonable person would
    1. **Con-Tort Problem- erosion of the line between contract and tort law**
       1. Every breach of Contract would also be an Innocent misrepresentation
          1. Functional equivalent
       2. Contract law has certain advantages
          1. Don’t have to prove culpability, basically strict liability for breaches
          2. BUT, ancillary rules- parol evidence rule, statute of frauds, don’t apply in tort law

So you get the same recovery with a lot less requirements and hurdles

* + - 1. The strict liability framework is analogous to breach of warranty claim under contracts???
    1. Damages
       1. **Restatement Formula: Reliance Damages: TORT (out-of-pocket)**
          1. ***Difference between value of what is parted with and value of what is received (value of what ∆ parted with – value of what π got)***

Generally applies to tort context for measuring damages

* + - * 1. Restatement attempts to limit damages to reliance damages only in order to keep tort damages separate from contract damages🡪 justify the existence of innocent misrepresentation tort

They want to claim that this is a different cause of action, so they assign different damages

Trying to preserve some of the differences between contract and tort law

Both tort and K law may be no liability frameworks, BUT under K law you will receive the greater expectation damages vs. the lesser reliance/restitution damages under tort law

ALI argues this is distinct tort

***reliance damages are consistent with tort, but expectation damages are not consistent with tort b/c they go beyond making you whole***

The restatement acknowledged the criticism to Waldman case where ct gave the same damages in the tort claim as it would have for a contract claim

* + - 1. **Waldman Formula: Expectation Damages: CONTRACT (Benefit-of-Bargain)**
         1. ***Value of property as represented – value of the actual property that π got***

Goal of contract law is to put you in the same place as you would have been if the contract had been performed

Cost of repair is also a good way to estimate expectation damages

* + - * 1. Allowed benefit of the bargain damages or expectation damages

Same as contract damages

Such damages may open door to contract defenses or further blur the line between tort and K

* + - * 1. Moll thinks Waldman court blew damages analysis

1. **Interference with Existing and Prospective Contractual Relations**
   1. Generally
      1. Umbrella policy is protection against interference with economic relationships
         1. Protects against interference with
            1. Contract
            2. Prospective business relationships/economy expectancy
         2. It is more culpable to interfere with an existing contract
         3. Interference with prospective K is less culpable and less likely to be tortuous since it has not come to fruition
      2. Many Jurisdictions treated Interference with Existing Contract in the same manner as Interference with Prospective Contract; however, modern view requires a showing of impropriety for Interference with Prospective Contract
         1. Reflects a common law reluctance to make legitimate, competitive activities actionable
            1. Do not want to hinder market activity
         2. Π has higher burden with IEC
            1. Requires some proof of wrongful conduct
      3. **Relation to Breach of contract** 
         1. One can imagine situations in which a breach of K action will not lie and therefore IEC is the only available means to recovery
            1. Example- impossibility defense to breach of K
         2. **Efficient breach of K**
            1. Breach of K is not a culpable act

At times it may be economically efficient for parties to breach a K when it helps resources get to the parties who value those resources most

Economist have been influential in the development of this social perception

* + - * 1. Nobody is made worse off and resources allocated to the person who values them the most

Only efficient if gain from breach occurs, notwithstanding the compensation to the injured party

* + - * 1. Tort may dissuade parties from finding an efficient distribution of resources

Potential ∆s may not approach a contracting party due to fear of tort liability

* + - 1. However
         1. Damages for IEC are often very difficult to quantify, b/c highly speculative

Much more difficult to quantify damages in a service contract than a commodities contract

Parties generally bring up IEC claims regarding services contracts

Commodities contracts more naturally lend themselves to an efficient breach analysis

Also, breach of K for commodities generally compensates the π for his loss anyways, so no need to look to tort law for damages

* + - * 1. Difficult to determine who would be better off upon a breach of services contract

Efficient breach concern with regard to services K is therefore probably overblown

* 1. **Intentional Interference with Existing contracts (tort)**
     1. **Prima Facie elements**
        1. **Intentional**
           1. Must have knowledge of contract’s existence

Actual knowledge concerning

Existence of the contract, AND

Fact that he is interfering with the performance of the contract

* + - * 1. Acting with purpose or desire of causing prohibited conduct

**Existing Contract**

* + - * 1. You know with substantial certainty that the result will occur

Ill-will not required

* + - 1. **Interference with existing contract**
         1. Method of interference can be lawful, does not have to be independently tortuous

Mere persuasion may suffice as interference in some situations

Need only induce or otherwise cause

* + - 1. **Injury to π**
         1. Breach; or
         2. Non-performance of contract

although this is usually a breach, it is not necessarily one

* + 1. Tort is generally thought of as a party or person, not involved with the K, interfering what a party to the K
       1. Prima facie elements for IEC easier to meet than IPBC
       2. Reflects societal judgment on importance due to contractual relationship
    2. **R2T § 766- Intentional Interference with Performance of Contract by Third Person 🡪** allows the 3rd party to sue when the interferee (person interfered with ) doesn't perform the K
       1. One who intentionally and improperly interferes with the performance of a contract (except a contract to marry) between another and a third person not to perform the contract, is subject to liability to the other for the pecuniary loss resulting to the other from the failure of the third person to perform the contract.
          1. Restatements add “improper” element to interference with existing contract tort
          2. Knowing interference with a valid, enforceable contract is usually deemed “improper”

This notion meshes the interference/improper element under the Restatement

* + 1. **R2T § 766A Intentional Interference with Another’s Performance of His Own Contract. {*When the Plaintiff is the person directly interfered with}.-->*** allows interferee to sue if he can no longer perform the K, or if they can, it makes performance more expensive or burdensome
       1. One who interferes with a party to a contract by causing that party’s performance of the contract to be more expensive or burdensome
          1. Causing plaintiff not to perform by preventing his performance by some means other than simply influencing his mental choice
       2. If you interfere with a contract, both parties to the contract should be able to sue you
       3. Actionable if interference merely causes plaintiff’s performance to be more expensive or burdensome
          1. NOTE—This is different from § 766 which requires *non*-performance or actual breach
    2. Example of 766 and 766A
       1. **HYPO**: A (an employer) & B (an employee) have an employment contract. C keeps B from going to work by locking him out of the building. B (the interferee)
          1. A--------B (fails to perform & Breaches K) <---C (interferor)
          2. A sues C under 766 for intentional interference with existing K

A also sues B for breach of K

* + - * 1. B sues C under 766A for intentional interference with existing K
    1. **Damages**
       1. Damages must be foreseeable at the time of interference
       2. Pecuniary loss resulting from interference
          1. Lost profits to the person with the contract
       3. Consequential damages may also be available if interference was the legal cause of failure to perform other contracts
       4. Punitive damages
          1. Punitive damages are the big wild card
    2. **Efficient Breach problem- does this group of torts deter efficient breach?**
       1. Torts discourage efficient breach
       2. Should it matter if it is a contract for services that are harder to quantify or a commodity like apples
          1. BUT, efficient breach doesn’t quite make as much sense when you are seeking services

Efficient breach assumes nobody is made worse off and that you can quantify damages and totally compensate them to make them whole again

But with contracts for unique services, there is no efficient breach of that contract

No equivalent opera singer- there will be damages that you can’t measure or compensate for

* + - * 1. **Relational Contract-**

characterized by long-duration relationships,

personal involvement or cooperation between the parties

exchange of things that are difficult to monetize

unique singer, etc

Examples-

Marriage

Employment

Damages are those which are tough to quantify and compensate for

Efficient breach is IMPOSSIBLE- b/c efficient breach requires you to quantify damages and fully compensate them for it

* + - * 1. **Discrete contract**

Contract with someone that you are never going to see again

Buying gas at a gas station on cross country trip, which you will never return to again

No desire to keep relationship in tact

Apple contract is discrete contract

One time deal

Easy to monetize

Damages were just

* 1. **Defenses for Intentional Interference with Existing Contracts**
     1. Burden Shift to defendant to prove affirmative defense justifying the interference with the existing contract
     2. **Affirmative Defenses to Intentional Interference with Existing Contracts:** 
        1. **Does the π meet the Elements for Intentional Interference with existing contract**
           1. **Intentional**
           2. **Interference with existing Contract**
           3. **Injury to π**
        2. **If π satisfies all the prima facie elements for the tort, the burden shifts to ∆**
        3. **∆ Must prove that he was privileged to interfere with the contract**
           1. **Texas Justification Defense**

**Legal Right (motivation does not matter)**

**Colorable Legal Right (Good faith claim= Good Motive)**

* + - * 1. **Public Policy: Public health, constitutionally protected right (free speech)**
        2. **Legal Rights Defense R2T § 773**

**Asserting bona fide claim**

* + 1. **Texas Justification Defense (Texas Beef Cattle)** 
       1. *Justification defense* is based either on exercise of either (1) one’s own existing legal right; or (2) a good faith claim to a colorable legal right even though such claim ultimately proves mistaken
          1. **Exercise of One’s Own Legal Right**

**Texas**

Court must first find existence of legal right (matter of law)

If defendant had a legal right to interfere, motivation for interference does not matter

Good faith does not enter into the equation

“Improper motive cannot transform a lawful action into an actionable tort”

Legal right itself conclusively establishes a justification defense

Question of law- the court makes this determination through judge

***California***, you must make sure that you exert the legal right in good faith.

But, in Texas, you just have to make sure that you have the legal right clause in your contract.

* + - * 1. **Good Faith Claim to Colorable Legal Right, even though that claim ultimately appears to be mistaken**

“Colorable Legal Right”

A right that appears without further inquiry (appears on its face) to be genuine, truthful, valid, or existing

***What you subjectively believed in your head***

**Second element: Something other than sincerity and honest conviction- your reason for asserting your right should be good motive**

***Good motive***

Court first must determine existence of “colorable legal right”

Jury then determines whether defendant acted with good faith

**the trial court (judge) determines the ∆ interfered while exercising a colorable right (one that it appeared you had) AND**

**the jury finds that, although mistaken, the ∆ exercised that colorable legal right in good faith**

**only here does jury inquire into good faith of the ∆**

“**Exercise/assert** right in good faith”🡪 means how did you carry out & is a **motive inquiry**

**Good faith and possibly motive *do enter***the equation

Open question as to whether court applies good faith to:

Belief in right’s existence (subjective inquiry); or

Exercise of the claimed right (objective inquiry—was it reasonable?)

* + - * 1. More consistent application of rule is to apply “*good faith” to existence of colorable right (subjective)*

After finding good faith belief, motive should not matter

This allows for the reality that people have mixed motives

Good faith belief in existence of legal right → bad motive in exercising such right

Consistent with “Type I” defense of exercise of one’s own legal right where there is not motive inquiry

Removing motive from the picture provides more certainty in business settings

* + - * 1. **Good faith could be interpreted as “A GOOD MOTIVE” is sufficient🡪 mixed motives are possible-** Leigh furniture addresses this concept by stating that the majority of your motive needs to be improper motive before finding absence of good faith

**Malice or bad faith is not irrelevant to the type two defense, it is just nullified, essentially, if a good faith motive is also found.**

Restatement § 768- as long as you have A good motive, then you are fine

* + - 1. **Texas Public Policy Defense**
         1. **Public policy and social welfare- yes**

**A reasonable and disinterested motive for the protection of other individuals, or the public, will justify intentional interference**

free speech

Safe to assume that Texas courts have not made “legal right” the exclusive means for a justification defense [Moll]

* + - * 1. A major public policy reason would likely prevail
      1. **Analysis in Texas**
         1. Burden is on Defendant to prove the legal right.

**Justification Defense Analysis for Texas**

Type-one defense: motive is irrelevant if legal right to act.

Type-two defense: did you have a colorable legal right? Court decides. Next, it goes to the jury. But should you ask the jury:

Do you believe that the defendant exercised a colorable legal right in good faith? –OR-

Did the defendant believe in good faith that he had a colorable-legal right?

* + 1. **Legal Rights Defense (Most Jurisdictions)**
       1. R2T § 773. Asserting Bona Fide Claim.
          1. “One who, by asserting *in good faith* a legally protected interest of his own or threatening in good faith to protect the interest by appropriate means, intentionally causes a third person not to perform an existing contract or enter into a prospective contractual relation with another does not interfere improperly…”
          2. Operates only when actor

Has a legally protected interest;

In good faith asserts or threatens to protect it; and

The threat is to protect it by appropriate means

* + - 1. *Rancherita* (California) court imposes good faith requirement on exercise of legal right
         1. To assert a contractual right in good faith, one must assert the right for the reason that the right is inserted into the contract in the first place
         2. Essentially this is a motive inquiry [Moll]
    1. Public Policy Defenses
       1. Interference may be justified/privileged for public policy concerns
          1. Public health (*Brimelow*)
          2. First Amendment

Boycotts

* + - * 1. Consumer protection
  1. **Interference with Prospective Contract** 
     1. Generally- must offer proof that ∆ intentionally and IMPROPERLY interfered with prospective contract, causing injury to π
        1. Prima Facie Elements: **Four I’s**
           1. **Intentional**

Purpose or desire to bring about the interference OR know with substantial certainty (necessary consequence) that the prohibited act will occur as a result of conduct

Must have knowledge of the prospective contract

* + - * 1. **Improper**

Improper means- the way in which you interfere, measurable

Tortuous

**Prospective Contract**

Criminal

Unethical

Improper motive- subjective

hard to prove

in someone’s head

not always illegal

* + - * 1. **Interference with prospective Contract**

Inducing or otherwise causing a third person not to enter into or continue the prospective relation; or

Preventing the other from acquiring or continuing the prospective relation

* + - * 1. **Injury to π**

Π must establish that more likely than not (reasonable probability, likelihood) that prospective business relation would become an actual contract

* + - 1. ***At Will Employment Relationships***- under Restatement are treated as prospective contracts
         1. At will employment is the default employment relationship in majority of US jurisdictions

At will employee can be fired for no reason or any reason at all subject to narrow public policy considerations

Restatement suggests at will employment is not worthy of the protection which is given to existing contracts

* + 1. **Restatement § 766B** – Intentional Interference with Prospective Contractual Relations
       1. One who intentionally and improperly interferes with another’s prospective contractual relation (except a contract to marry) is subject to liability to the other for the pecuniary harm resulting from loss of the benefits of the relation, whether the interferences consists of
          1. Inducing or otherwise causing a third person not to enter or continue the prospective relation or
          2. Preventing the other from acquiring or continuing the prospective relation.
    2. **Improper (How to Determine if Interference is Improper)**
       1. Without this element, ordinary competition would become a prima facie tort
       2. Courts have found that either an improper motive or improper means may be sufficient to find improper interference
       3. **Improper Means**
          1. Improper means provides a clearer benchmark for improper interference

**Improper Means**

Violation of common law/statute

Independently tortious means

Conduct that falls below established, objective standard of conduct

EXAMPLE

Published rules of conduct for a profession

* + - * 1. Texas- **Improper means inquiry only🡪To establish liability for interference with a prospective contractual or business relation the plaintiff must prove that it was harmed by the defendant’s conduct that was either independently tortious or unlawful**

Improper conduct is unlawful conduct (means inquiry)

That conduct which is already recognized as wrongful under common law or statute—

conduct that would violate some other recognized tort duty.

Open question as to whether unlawful conduct includes a violation of code of ethics or some other industry standard

Bad motive has nothing to do with improper conduct

No “mean breach”

***Plaintiff must prove that defendant’s conduct would be actionable as a recognized tort*** (or violation of law)

Does not have to actually prove up the tort

So, now, the plaintiff must prove that the defendant’s act was improper. *Instead of the Defendant having the burden of showing that the action was justified (proving propriety), the plaintiff has to prove that he defendant’s act was improper.*

Independently tortious, or

Unlawful

* + - 1. **Restatement Approach: Restatement § 767**. Factors in Determining Whether Interference is Improper.
         1. Factors for Consideration

**Restatement Factors**

Nature of the actor’s conduct;

Actor’s motive (to injure [Moll]);

Interests of the other with which the actor’s conduct interferes;

Interests sought to be advanced by the actor;

Social interests in protecting the freedom of the action of the actor and the contractual interests of the other;

Proximity or remoteness of the actor’s conduct to the interference; and

Relations between the parties

* + - * 1. Restatement provides a balancing test

Real question: Whether the actor’s conduct was fair and reasonable under the circumstances

Unpredictable balancing test

Much more difficult to get summary judgment due to fact questions involved

* + - * 1. **Should Improper Motive be a basis for an interference claim by itself?**

**The Restatement §767 doesn’t give us much direction.**

**It says that if your sole motive, then that is enough.**

**If it is your primary motive, then that might be enough.**

**If it is something less, then that will be something to consider**

* + - 1. **Improper Motive**
         1. Improper motive = motive to hurt/injure the other party
         2. Improper motive is difficult to prove—subjective inquiry

**Improper Motive**

Improper motive is even more difficult to prove when dealing with a business entity instead of a person

* + - * 1. **Competition as Proper motive**

One who intentionally causes a third person not to enter into a prospective contractual relation with another who is his competitor or not to continue an existing contract terminable at will does not interfere improperly w/ the other’s relation if

The relation concerns a matter involve in the competition between the actor and the other and

The actor does not employ wrongful means and

His action does not create or continue an unlawful restraint of trade and

His purpose is at least in part to advance his interest in competing with the other

The fact that one is a competitor of another for the business of a third person does not prevent his causing a breach of an existing contract with the other from being an improper interference if the contract not terminable at will.

* + - * 1. Mixed Motive

People often operate with mixed motives

R2T § 768 Approach

One does not improperly interfere if his purpose “is at least in part to advance his” competitive interest

*Any* competitive motive makes “entire motive” proper

Primary Motive Approach (*Leigh Furniture*)

If predominate or primary motive is improper, “entire motive” is improper

If long-term motive is economic, a short-term motive to harm a competitor is not necessarily improper

* + - * 1. Bad Motive – Good Results

It is possible to have a terrible motive with beneficial consequences

Is there a true correlation between bad motive and bad results/bad conduct? [Moll]

Motive is a complicated benchmark

Arbitrary outcomes

* + - 1. **Mean Breach: Breach of Contract with an intent to injure (does not have to be predominant intent) = Improper Means** (*Leigh Furniture*)
         1. Generally, deliberate breach of contract ≠ improper interference
         2. HOWEVER

Deliberate breach of contract + purpose to inflict injury = improper means/improper interference

In such a case, improper motive need not be predominate

Contract remedies are not enough to compensate for mean breach

* + - * 1. Intentional Interference is not “interference” as btwn Party A and Party B

Intentional Interference is means of interfering with *another* existing contract or prospective business relationship between Party A and a third party

***For Both of the interference torts, the Breacher and interferor CANNOT be the same person***

***Parties to the K are liable for breach of K if they break the contract, but not tort damages***

***We hold 3rd party liable under principle of tort for intentionally interfering with the contract***

* + - * 1. Example of a court judging the “why” of a contract breach

Policy Consideration

Plaintiff (interfered with business) might go out of business as result of breach and interference

Difficult to quantify potential lost profits

Punitive damages might be only damages available to compensate if company is driven out of business

* + 1. **Damages**
       1. Difficult to Quantify
          1. Damages for interference with prospective business relations is difficult to calculate

No guarantee that prospective contract would have occurred

Lost good will

Lost commercial relations

“Loss of Chance”

Total value of prospective relationship discounted by some % of likelihood

* + - 1. Punitive damages are generally thought to be available
  1. **Challenging allegations to Interference with Prospective Contract**
     1. ***TEXAS***: There is **NO affirmative defense of justification** in intentional interference with prospective contract
        1. π need not prove that the ∆’s conduct was not justified or privileged, nor can ∆ assert such defenses
           1. BUT- You can bring in evidence that it is proper as part of “π’s impropriety evidence”

You raise your evidence earlier in the case, b/c no affirmative defense permitted later

* + - * 1. ***No burden shifting, if π establishes 4 I’s, then claim is satisfied🡪 must bring evidence and challenges earlier as part of π’s prima facie case***

**Instead, you are arguing π has not met its burden of impropriety b/c of your conduct/evidence**

* + 1. Other Jurisdictions
       1. See affirmative defenses under interference with an existing contract, *supra*
  1. **Corporate Agent Problem**
     1. Corporate Agent Issue:
        1. The act of a corporate agent is an act of the corporation
        2. By definition, the person who induces the breach (under intentional interference with existing contract) cannot be a party to that contract
           1. Cannot be sued for intentional interference with your own contract
           2. To hold otherwise would convert every breach of contract into a tort action
        3. *When can you sue a corporate officer for causing a corporation to breach a contract with the plaintiff?*
           1. Must separate the act of the officer from the corporation
     2. **RULE: for both of the interference torts, the interferer cannot be the same person as the breacher. However, that creates tension within a case in which an agent of a corporation persuades the corporation to breach a contract.**

**Corporate Agent Problem**

* + - 1. **How did Texas get around this problem?** 
         1. **They said that you can sue the agent for interference if the agent was acting solely for his own personal gain. (Holloway v. Skinner).**
      2. **If a principal does not complain about its agent’s actions, then an agent cannot be held to have only acted for its own interest. (Powell Indus. v. Allen).** 
         1. **If the principal does complain, that complaint is not conclusive**
      3. **Personal Gain**: Must show that the ∆ acted in a fashion so contrary to the corporation’s best interest that his actions could only have been motivated by personal interests (*Holloway*)
         1. **∆ is liable if when serving as an agent his interference was solely in the furtherance of his own personal interests.**
         2. and Must show that defendant’s actions could only have been motivated by personal interests

A mixed motive is NOT sufficient to create “sole personal motive”

Still a motive inquiry

Motive must be shown to be so contrary that the motive could only be defendant’s personal interest

* + - 1. **Complaint:** If principal does not complain about agent’s actions, agents cannot be held to have acted contrary to principal’s interests (*Powell Industries*)
         1. Corporate board silence = no complaint about corporate officer

Negates the motive inquiry somewhat

* + - * 1. No complaint about corporate officer = agent/corporation as *one* entity

One entity = no interference claim

* + - * 1. Even if principal does complain, the complaint is not conclusive—only evidence (*Powell*)
      1. How Does Plaintiff’s Attorney Overcome this Rule?
         1. Near impossible situation—has to find a complaint!
         2. Board meeting minutes unlikely to help

Boards will be disposed toward their CEOs and officers

Easy, though unnecessary, for CEO to get board approval

* + - * 1. Impossible situation probably leads to few of these complaints being filed
    1. Justice Hecht’s Preferred Rule (NOT THE LAW)
       1. Corporate agent is separate from corporation if agent acts outside his scope of authority
       2. Not a motive inquiry
          1. Motive is a fact question but scope of authority is generally a legal question

Hecht’s Test more favorable to summary judgment

* + - 1. Hecht’s Test is actually less favorable for an agent
         1. ***Agent who is acting in good faith for the corporation but outside the scope of his authority might still be liable***

Agent would not be liable under the Majority Test

Moll thinks this test is even less protective in some circumstances

1. **Insurance Torts**
   1. **Introduction**
      1. Liability Insurance & Tort
         1. Intersection between insurance and tort is critical
         2. Affects who to sue; why to sue; how to try a case; how to plead
      2. Types of Insurance
         1. Liability Insurance (Third Party Insurance)
            1. Insurer promises to indemnify insured for damages against a third party if the insured causes an injury of the sort covered under the policy
            2. ***Two Promises of Third Party Insurer***

Duty to defend- if you get sued for something that could/potentially within the coverage of the policy

Even if frivolous

This is NOT capped by policy limits

Duty to pay- duty to pay for any damages you are legally responsible for up to limits enumerated in policy, sometimes worded like a duty to indemnify

Capped by policy limits

* + - 1. First Party Insurance
         1. Promise by insurer to pay insured when insured himself sustains a loss

EXAMPLES: healthcare, property, disability insurance

* + - 1. Combined Insurance
         1. Many policies cover both first and third party insurance

EXAMPLE: homeowners insurance

* + 1. ***Scope of Policy***
       1. Claims made policy- provides coverage for any legal claim that is made against the insured within the policy period
          1. Even if that claim is based on underlying events or injuries that occurred outside the policy period
       2. Occurrence Policy- provides coverage for injuries that occurred during the policy period, even if a claim is not made during the policy period
       3. ***Π’s Incentive to underplead***
          1. There is incentive to underplead b/c if establish intentional, then insurance company likely won’t fork up money

So π will make everything sound like negligence and avoid intentional tort allegations

Π underpleads b/c fears triggering an exclusion of insurance policy or not falling within the scope of coverage

* + 1. Insurance Suit Procedures
       1. Underlying Suit (Tort plaintiff v. insured) 🡪 declaratory judgment on duty to defend (insurer v. insured) 🡪 duty to indemnify suit (insurer v. insured)
    2. Insurance Policy Exclusions
       1. Intentional injury
          1. Most policies exclude injuries which are expected or intended by the insured
       2. Often insurer has burden to establish that insured’s act is subject to an exclusion
       3. Existence of insurance might cause plaintiffs to underlitigate—plead a negligence action instead of an intentional action
          1. Incentive to stay away from intentional torts
          2. Emphasizes the less “morally wrong” tort
       4. Some intentional acts may be covered
          1. EXAMPLE: sexual harassment; wrongful termination; etc.
    3. Conflicts of Interest Between Insurer & Insured
       1. Insurer would rather see plaintiff prevail on an intentional tort theory
          1. b/c then insurer would be relieved of compensating the π
       2. Insured would rather see plaintiff prevail on a negligence theory in order to fall within insurance coverage
    4. Subrogation
       1. Subrogation
          1. Insurance company’s right to step into the shoes of the insured and make a claim for the insured’s loss

Your homeowner’s policy pays for a fire your neighbor started

Ins. Co then in its right of subrogation is allowed to sue Neighbor on your behalf and all proceeds go to reimbursing Ins. Co for payment it made to the insured

* + - * 1. Insurance company can either

Take over litigation in the underlying action and keep recovery; or

Stay out of lawsuit and ask court to direct any judgment to the insurance company

* + - 1. Goal of Subrogation
         1. Prevention of double recovery
         2. Many jurisdictions will not allow subrogation if the insured is not made whole

Certainly no danger of double recovery in such a situation

* + - 1. Forms of Subrogation- If not contractual, ct will generally impose equitable
         1. Contractual—right of subrogation contained in insurance policy

Policies *will always* include a subrogation clause

Is this a good policy or is this now an adhesion contract?

* + - * 1. Equitable Subrogation

Court-imposed subrogation

Court wants to avoid double recovery (windfall) to plaintiff

Makes sense when there is a finite damages number (i.e., property damages)

Makes less sense when damages cannot be easily quantified (i.e., health insurance to cover lingering health problems)

No double recovery because insured is in constant need of resources

Make Whole Doctrine

If plaintiff has not been made whole, no *equitable* subrogation

TX Supreme Court has not applied “Make Whole Doctrine” to contractual subrogation

* + 1. Do We Overconsume Liability Insurance?
       1. Idea that having a large policy puts a target on the insured
          1. Many professionals (physicians) might therefore choose to have less insurance coverage

Rationale is less insurance equals less lawsuits

But a wealthy ∆ seems to negate that reasoning

* 1. **Duty to Defend (contract claim)**
     1. Duty to Defend
        1. Duty to provide defense to the insured when insured is sued on a claim *potentially* within the scope of policy coverage
        2. Duty to defend is a contract claim
     2. Duty to Defend Test
        1. **If any part of the claim is arguably (or potentially) within the scope of the policy’s coverage, the insurer has a duty to defend**
           1. **Any doubt should be resolved in favor of the insured**

**Not “any doubt”—pleading cannot be totally inconclusive and come within ambit of insurance policy [Moll]**

**Must exhibit some causal connection between injury and subject of insurance, i.e. operation of a vehicle (*Merchants Fast Motor Lines*)**

* + - * 1. Duty is triggered by factual allegations in plaintiff’s petition

Concerned with *factual allegations*, not legal theories such as negligence

If a suit gets tossed during summary judgment, it’s generally the lawyer’s fault for poor pleading [Moll]

* + - * 1. Insured has to establish that claim is covered; burden is on π to prove claim is within the scope of coverage

Insurer has the burden to establish the exclusion

* + - 1. **Courts apply “eight corners” test**
         1. **Court looks at policy**
         2. **Court looks at pleadings (factual allegations in the petition)**

**Assume it’s true**

* + - 1. Test is perhaps broad (liberal) because insured needs the duty to defend immediately at the outset of the lawsuit
         1. As compared to duty to indemnify
    1. Duty to Defend & Declaratory Judgments
       1. Insurance companies often bring declaratory judgment actions seeking declaration of no duty to defend or duty to indemnify
          1. Courts may stay duty to indemnify until underlying action is completed
       2. Purpose of Declaratory Judgments
          1. Early answer on duty to defend may keep costs down by managing it from beginning of incident
          2. Insurance companies have to “set reserves”

Early knowledge lets them set reserves early on in the process

* + - * 1. Choice of Venue

If insurer knows that insured is going to sue, might as well pursue a declaratory action with insurer as plaintiff, choosing the venue

* + - 1. Burden on Insured
         1. Insurance company not only wants to deny defense in underlying action but has also subjected insured to declaratory judgment lawsuit
    1. Damages
       1. Breach of contract action
       2. Expectation or benefit of the bargain damages
       3. Typically no mental anguish or punitive damages
       4. Attorney’s fees available
          1. Attorney’s fees in underlying action (plaintiff v. insured)
          2. Attorney’s fees in duty to defend action (insured v. insurer)
  1. **Duty to Indemnify**
     1. Duty to Indemnify
        1. Insurer’s duty to pay—up to policy limits—the injured party (indemnify the insured against the injured party) for any tort judgment obtained against insured that is within the scope of the policy’s coverage
           1. Insurer’s duty to pay when insured is found legally liable

Based on *proven* facts (and not merely allegations like duty to defend)

* + - * 1. Damages limited by policy limitations
      1. Contractual obligation (contract claim)
      2. Insured has burden of establishing that insuring language (policy) covers the claim
      3. Insurer has burden of proving that exceptions apply
  1. **Duty to Settle (tort claim)**
     1. Duty to Settle
        1. Settlement of claim is one usual method by which an insured receives protection under an insurance policy
        2. Tort action
           1. Odd that action sounds in tort when in some jurisdictions the COA arises out of breach of an implied covenant

Contrast to duty to defend which sounds in contract

* + - 1. Arises only in third party context
    1. Origins of Duty to Settle
       1. Why Duty to Settle is Necessary
          1. Conflict Between Insurer & Insured

Insurer

Only concerned with policy limits—when is settling actually better than going to trial?

May have locked in flat attorney’s fees so is not concerned about trial expenses

Insured

Concerned about an excess judgment (judgment which is in excess of policy limits)

Does not want judgment against him on public record

Does not want the hassle of a trial

* + - * 1. Duty to settle forces insurer to subordinate its own economic interests
      1. **Texas**
         1. ***Duty to settle comes from*** ***agency law***

Insurance company is agent of the insured

* + - 1. **California**
         1. ***Duty to settle comes from implied covenant of good faith and fair dealing that is found in every contract***
         2. NOTE—No implied duty of good faith and fair dealing in Texas contracts (except UCC)

Texas is never eager to wade into a good faith situation

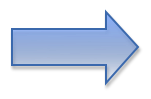
Too unpredictable

* + 1. **Duty to Settle Test**
       1. **Texas** (*Stowers*)
          1. *Stowers* Duty to Settle Requirements

Claim against insured is within scope of coverage;

Demand is within policy limits;

Demand policy above policy limits, even if reasonable, does not trigger *Stowers* duties

**TEXAS**

Terms of demand are such that an ordinarily prudent insurer would accept it, considering the insured’s potential exposure to excess judgment

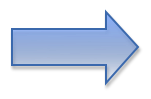
* + - * 1. ***Expected value analysis***

Expected Claim Value =

(Probability of Judgment x Judgment Amount) + Attorney’s Fees

If settlement offer comes in lower than Expected Claim Value, a reasonably prudent insurer would accept the settlement

* + - 1. California (and many other jurisdictions) (*Crisci*)

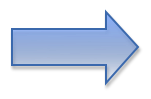
**California**

* + - * 1. **Whether a prudent insurer, without policy limits, would have accepted the settlement offer**

**Question of fact**

**Does not take into consideration whether demand is within policy limits** *(unlike Texas*)

* + - 1. Strict Liability (MINORITY RULE)

**Strict Liability**

* + - * 1. If original settlement demand was within policy limits and judgment exceeds policy limits (excess judgment), insurer is liable for entire judgment (policy limit + excess)
    1. Settlement Outcomes and Expected Value analysis
       1. Example of Outcomes for Ins. Company:
          1. Settlement offer = 99,000 / policy limit is $100,000 / 80% chance of judgment.

Scenario 1 = Judgment and plaintiff wins $40,000 + $20,000 defense costs

Insurance has to pay $60,000

Scenario 2 = Judgment for plaintiff = $79,000 + $20,000 defense costs

Insurance reaches break even

Scenario 3 = Plaintiff judgment >$100K + $20,000 defense costs

120,000 total, but Insurance only out 100,000 policy limit.

Scenario 4 = Defendant wins

Insurance co is only out $20,000 in defense costs.

* + - 1. Expected Value Analysis
         1. Plaintiff’s probability of winning = 90%
         2. Plaintiff’s damages = 200,000
         3. Defense Costs = 20,000
         4. Settlement Offer = 99,000
         5. Policy Limits = 100,000
      2. (.9 x 200,000) + (.1 x 0 [if P loses]) = 180,000 + 20,000 Def costs = $200,000.
         1. A prudent insurer without policy limits would accept any settlement offer that is below $200,000.
    1. **Damages**
       1. Compensatory damages
          1. Liable for difference between judgment and settlement offer
       2. Punitive damages and mental anguish damages (California)
          1. Texas courts have yet to award mental anguish damages or punitive damages though the action does sound in tort in Texas
  1. **Covenant Not to Execute & Covenant Not to Pursue Settlement**
     1. Covenant Not to Execute
        1. Tort Plaintiff agrees not to (never) execute a judgment against the insured in return for an assignment of part or all of insured’s claims against the insurer for failure to settle or failure to defend
     2. Covenant Not to Pursue Settlement (No Longer in Practice)
        1. Tort plaintiff and defendant insured “collude” and agree on a huge settlement
           1. Insurance company balks at settling
        2. Similar to Covenant Not to Execute but *no* trial occurs between plaintiff and insured
        3. Insured still assigns failure to settle/defend action to tort plaintiff
        4. Texas eventually invalidated this process and required an adversarial trial between tort plaintiff and defendant insured
  2. **Duty of Good Faith & Fair Dealing (tort)**
     1. **Texas**—Special Relationship
        1. ***Texas law does not impose duty of good faith and fair dealing on every contract***
           1. ***EXCEPTION—contracts covered by UCC***
        2. **BUT Texas *will* impose duty of good faith and fair dealing where “special relationship” exists: Insurer and Insured = example of special relationship🡪 TORT DUTY OF GOOD GIATH AND FAIR DEALING EXISTS**
        3. Texas courts have found “special relationship” between insurer and insured
           1. Characteristics of Insurer-Insured Relationship

Unequal bargaining power

Insurer has exclusive domain over evaluation, processing, and denial of claims

Insurance company can advance a little of the requested money and then get a release from liability

Insurance company can twist arms to force settlement by paying pennies on the dollar

Insurance companies only subject to cost of claims + interest in damages

“Special trust” (*Aranda*)

Insurance is a quasi-public service

* + - * 1. Courts want to impose a tort duty to keep insurance companies in check

Consequence of “liberal” justices of 1980s [Moll]

Liberal justices trust in courts and juries to do what is fair [Moll]

Conservative justices favor more predictability in the law (disfavor juries) [Moll]

Conservative justices will eschew common law rules when statutes address the situation (*Aranda* dissent)

Statutory causes of action against insurers do exist in Texas:

Texas Insurance Code

TX DTPA

Statutory causes of action level the playing field somewhat

* + - 1. Plaintiff lawyers seek a “special relationship” in many different contexts
         1. ***Special relationship = duty of good faith and fair dealing tort claim***
      2. Worker’s Compensation Claims (*Aranda*)
         1. *Court has found Worker’s compensation insurance carrier owes duty of good faith and fair dealing to insured employee*
         2. For breach of duty, employee must establish

An absence of a reasonable basis for denying or delaying payment; and

That carrier knew or should have known that there was not a reasonable basis for denying or delaying payment

* + - * 1. Special relationship despite statutory protections
      1. No special relationship between franchisor-franchisee (*Crim Truck*)
    1. California—Employer-Employee Relationship (*Foley*)
       1. ***Special relationship does not exist between employer-employee***
          1. Unlike insured, employee has more options, more potential self-help remedies

Employee can find a new job

Employer is not providing a quasi-public service

Interest between employer and employee are usually aligned (as contrasted to interest between insurer and insured)

* + - 1. There are arguments that a “special relationship” does exist between employer and employee
         1. There is trust between the parties
         2. There is one-sided bargaining power
      2. Better argument that employer-employee relationship just is not equivalent to insurer-insured relationship
    1. Damages
       1. Out-of-pocket damages
       2. Punitive damages and mental anguish damages
       3. Other penalties
          1. Attorney’s fees
          2. Reputational issues
          3. State penalties
          4. Other penalties may actually negate argument that tort liability is necessary [Moll]

1. **TEXAS DECEPTIVE TRADE PRACTICES ACT**
   1. **Key Points**
      1. **Treble and Mental Anguish Damages permitted if acted “knowingly”**
         1. Damages
            1. Producing cause
            2. Economic damages- pecuniary loss
            3. If knowingly- then damages for mental anguish also
         2. Additional damages-
            1. civil practice and remedies code does not apply
            2. if knowingly, up to 3x economic damages
            3. if intentionally, up to 3 times economic damages and damages for mental anguish
         3. Consumer’s attys’ fees
            1. Each consumer who prevails shall be awarded court costs and reasonable and necessary attys’ fees
      2. **Notice & Settlement**
         1. Must send pre-suit notice (60 days)
            1. Must include amount of damages and
            2. amount of attorney’s fees
         2. Defendant gets two shots to pay settlement
            1. First—within 60 days after getting notice
            2. Second—90 days after lawsuit is filed
         3. If defendant agrees to settle in full, plaintiff *must* accept it
            1. Settlements may be in-kind (i.e., fixing what is broke)
         4. Consumer’s damages and attorney’s fees are limited if the plaintiff rejects a reasonable settlement offer
      3. **Provisions to deter frivolous suits**:
         1. ∆’s atty fees
            1. This statute uses “or” instead of “And”-
            2. ∆ may recover attys fees if suit was

groundless in law or fact, or

brought in bad faith, or

brought for the purpose of harassment

* 1. **Introduction**
     1. Goal of DTPA
        1. Main goal was to eliminate litigation by encouraging settlement
           1. Settlement is the single-most significant aspect of the DTPA [Alderman]
        2. Places risk allocation on businesses
           1. Businesses in a better opportunity to spread risk premium
     2. General Applicability of DTPA
        1. Always better for plaintiffs when DTPA applies
           1. Conversely always worse for defendants when DTPA applies
        2. DTPA often applies
        3. Do not put in all causes of action
           1. A good DTPA claim trumps any excessive tort claims
           2. Do not want multiple claims to yield an inconsistent jury verdict
     3. Court Interpretation of DTPA
        1. DTPA instructs courts to interpret the DTPA *liberally in favor of consumers* (§ 17.44)
           1. One of the few statutes that actually tells courts how to interpret
  2. **Benefits of DTPA**
     1. Benefits to Potential Plaintiffs
        1. Broad Applicability
           1. DTPA gives broad definition of “consumer” (§ 17.45(4))
           2. Businesses are included as “consumers”

Any business with less than $25 million in assets

This is the vast majority of businesses

TX DTPA is one of few consumer fraud statutes in the nation which includes businesses as consumers

* + - 1. No-Fault Liability (Strict Liability)
         1. Does not require a culpable mental state
         2. Strict liability for

A misrepresentation

An unconscionable act

* + - 1. Lowest Causation Standard
         1. Need only be “producing cause”

Much lower standard than “proximate cause”

Closer to causation in fact

* + - 1. Essentially all tort damages *and* contract damages available
         1. Economic damages and mental anguish damages available
         2. Lowest standard for awarding punitive damages

Knowingly

Knowingly = knew or should have known

Objective or subjective

Treble damages

* + - * 1. Mandatory award of attorney’s fees

DTPA mandates attorney’s fees (“shall”)

Texas Supreme Court has determined that attorney’s fees are to be calculated on an hourly basis

Significant benefit as attorney’s fees will usually outstrip the amount in controversy

* 1. **Application of DTPA**
     1. Waiver
        1. Generally DTPA duties may not be waived
           1. In theory, duties can be waived but exceptions are almost impossible to meet
        2. Waiver considered contrary to public policy and unenforceable
     2. Consumer Status
        1. Only a “consumer” can bring a claim under the DTPA
           1. Consumer status is one of the most frequently litigated aspects of DTPA

Affirmative defense

Defendant seeks to prove that plaintiff is not a “consumer”

* + - 1. Consumer is one who “seeks or acquires by purchase or lease any goods or services”
         1. Seek or Acquire

“Seek” makes consumer definition extremely broad and liberal

Includes an “intended beneficiary”

Intended beneficiary “acquires” and is therefore a consumer

* + - * 1. Purchase or Lease

Who Pays?

It does not matter who pays

Only matters that services are acquired via purchase or lease

Any *free* goods or services ≠ consumer

* + - * 1. Goods or Services

Real estate is included as a good (“goods means tangible chattels or real property purchased or leased for use”)

Intangible property is seemingly excluded

Pure loan transaction does not fall under DTPA

Services include: work, labor, services furnished in connection with the sale or repair of goods

* + - 1. Good Faith
         1. Must be seeking or acquiring in good faith

DTPA will not apply to one hunting for a lawsuit

Instills some reasonableness limitations

* + - 1. Business as Consumer
         1. Consumer includes a business with less than $25 million in net assets
         2. When are assets measured?

At point in time when business could have protected itself with relation to the transaction [Alderman]

Reasonable time period within date of misrepresentation

* + - * 1. Affirmative defense to prove that business had *more* than $25 million in assets
      1. NOT consumers
         1. States
         2. Federal government
         3. Unincorporated associations
    1. “In Connection With” Requirement
       1. Misrepresentation must occur “in connection with” the transaction
       2. Cannot sue a remote seller for an immediate misrepresentation
          1. EXAMPLE

Cannot sue manufacturers in a home-builder context because manufacturers do not make representations directly to the consumer

* + 1. Exemptions
       1. Professionals
          1. DTPA does not apply to “rendering of a professional service, the essence of which is the providing of advice, judgment, opinion, or similar professional skill”
          2. EXCEPTIONS—Exemption Does Not Apply

Professional may be sued for

Misrepresentation of material fact that cannot be characterized as advice, judgment, or opinion;

A failure to disclose a violation;

An unconscionable action or course of action which cannot be characterized as advice, judgment, or opinion;

Breach of an express warranty

* + - * 1. These exceptions make this exemption virtually toothless
      1. Personal Injury
         1. Not a real exemption [Alderman]
         2. Basically cannot sue under the DTPA on the sole basis of an injury

Still must be some DTPA violation

* + - 1. Large Transaction Exemption
         1. Transactions over $500,000 are exempt

Includes single transaction, project, or set of transactions relating to the same project

SOLUTION

Restructure your transactions so they do not exceed $500,000

Divide up projects if possible

* + - * 1. EXCEPTION

Exemption does not apply to a consumer’s residence

* + 1. DTPA Causes of Action
       1. Laundry List
          1. 27 examples that are per se deceptive and misleading (§ 17.46(b))

No culpable mental state necessary

Includes pretty much *any* misrepresentation

* + - 1. Failure to disclose
         1. Actually requires element of “intent”
      2. Unconscionability
         1. When someone is taken advantage of and result is “grossly unfair”
         2. “Grossly unfair”

Objective standard

* + - 1. Breach of Warranty
         1. Express
         2. Implied
         3. In breach of warranty, DTPA acts as a vehicle to bring other causes of action but with the ability to get DTPA remedies
    1. Notice & Settlement
       1. Plaintiff must send “pre-suit notice” of 60 days
       2. Defendant gets two shots to pay settlement
          1. First—within 60 days after getting notice
          2. Second—90 days after lawsuit is filed
       3. If defendant agrees to settle in full, plaintiff *must* accept it
          1. Settlements may be in-kind (i.e., fixing what is broke)
       4. Consumer’s damages and attorney’s fees are limited if the plaintiff rejects a reasonable settlement offer
       5. Either side may request mediation and mediate within 90 days of the request
    2. Damages
       1. Standard is “producing cause”
       2. Economic Damages
          1. Pecuniary loss
       3. Mental Anguish Damages
          1. If defendant acted “knowingly,” mental anguish damages available
          2. Available even if no economic loss
       4. Punitive Damages
          1. If “knowingly,” punitive damages in amount of treble economic damages
          2. If “intentionally,” punitive damages in amount of treble economic damages *and* mental anguish damages
       5. Attorney’s Fees
          1. If consumer prevails, attorney’s fees are mandatory

Fees calculated on hourly basis

* + - * 1. Defendant can recover attorney’s fees if suit is

Groundless;

Brought in bad faith; or

Brought for the purposes of harassment

1. **Fiduciary Duty and Shareholder Oppression**
   1. **Fiduciary Duty (Breach of Fiduciary Duty= Tort)**
      1. Fiduciary Duty Defined [Moll]
         1. Fiduciary must put the interests of the beneficiary ahead of his own
         2. Highest duty that the law imposes
         3. Breach of fiduciary duty sounds in tort
            1. Tort damages available
      2. Fiduciary Duty Jury Instruction
         1. Sample Jury Instruction
            1. ***To show that one has complied with his fiduciary duty, one must show:***

Transactions in question were fair and equitable to the beneficiary;

Fiduciary made reasonable use of confidence placed in him;

Fiduciary acted in utmost good faith and exercised scrupulous honesty;

Fiduciary placed interests of beneficiary before his own interests, did not use his position as fiduciary to gain any advantage for himself, and did not place himself in any position where his self-interest conflicted with his obligations as a fiduciary; and

Fiduciary fully and fairly disclosed all important information to the beneficiary

* + - 1. Most loaded, plaintiff-friendly jury instruction ever [Moll]
         1. Imposes onerous obligations on the fiduciary

One reason why courts will not impose fiduciary duties lightly

* + - * 1. Plaintiff’s lawyers love fiduciary duty

Breach of fiduciary duty is an amorphous legal doctrine

Allows plaintiff to tell his story about being treated unfairly

Plaintiff’s lawyers will often throw in an informal fiduciary duty in business tort context

Biggest hurdle is actually establishing the fiduciary duty

* 1. **Creating a Fiduciary Duty**
     1. Two Ways Law Recognizes Fiduciary Duty
        1. Formal Fiduciary Relationships
        2. Informal Relationships that Give Rise to Fiduciary Duty
           1. *B/c it is such a high duty, the standard is difficult to satisfy*
           2. Formal and informal fiduciary relationships are legally equivalent and treated the same under the law
     2. **Formal Fiduciary Relationships**
        1. Certain relationships that give rise to a fiduciary duty as a matter of law
        2. Law has historically considered such relationships to be fiduciary relationships
           1. Plaintiff only need establish the existence of such relationship
           2. EXAMPLES

Principal-agent

Partners

Trustee-beneficiary

Attorney-client

Corporate directors-corporation

* + - * 1. In Texas, shareholders do NOT owe each other a fiduciary duty as a matter of law
        2. In Texas franchisor-franchisee relationship does not automatically give rise to a fiduciary relationship (*Crim Truck*)
    1. **Informal Fiduciary Relationships**
       1. Existence of an informal relationship is generally a ***question of fact***
       2. Texas law had made it virtually impossible to establish an informal fiduciary relationship [Moll]
       3. Relationships of Trust & Confidence
          1. Based on relationships of “trust and confidence” or “confidential relationships”
          2. Informal relationship must be established via proof of trust and confidence
       4. **Characteristics of Relationship of Trust & Confidence which support the imposition of an informal fiduciary duty in a business transaction**
          1. Duration of the relationship

TX Supreme Court gives this factor little to no weight (*Crim Truck*)

Cordial relationship of long duration is NOT evidence of trust and confidence

* + - * 1. Prior history of transactions between the parties

Earlier arm’s-length transactions (***mutually beneficial***) cannot serve as basis for special relationship

Not indicative of trust

A partnership might serve as a prior relationship

Fiduciary relationship as matter of law

Not dispositive

***Relationship/agreement which is subject of lawsuit cannot itself be basis for relationship of trust and confidence***

* + - * 1. Disproportionate power/unequal bargaining power

TX Supreme Court has found that in a regulated environment (covered by statute), there is little to no concern about unequal bargaining power/positions

Statutory remedies might lessen impact of power imbalances

* + - * 1. Voluntary relinquishment of control/rights/power
        2. Parties’ own subjective beliefs

***Subjective trust alone does not transform an arm’s-length transaction into a fiduciary relationship***

Court does not give much weight to *one* party’s testimony about trust

Even where parties have memorialized understanding of mutual trust and confidence, Court may not give much weight (*Crim Truck*)

Non-assignment clause is usually treated as boilerplate language

* + - * 1. Familial relationship (*Flannery*) (not a TX Sup Ct case)

This is *the only* characteristic the TX ct suggests influences the imposition of an informal fiduciary duty

If there is no familial relationship, no way TX court will find an informal fiduciary duty [Moll]

Family relationship may open doors to more strict analysis of other factors such as subjective beliefs, unequal bargaining power

* 1. **Close Corporations**
     1. Definition & Characteristics of Close Corporations
        1. Definition
           1. “A business organization typified by a small number of stockholders, the absence of a market for the corporation’s stock, and substantial shareholder participation in the management of the corporation.”
        2. Characteristics
           1. Small number of shareholders;

Often shareholders have personal or familial relationships

* + - * 1. Substantial shareholder participation in management; and
        2. No publicly traded market for corporation stock
    1. Problems for Minority Shareholders
       1. Majority owners can “abuse” the minority shareholders
          1. Refuse to declare dividends
          2. Terminate minority shareholder employment in corporation

Most harmful

Distribution of close corporation profits most often distributed through salaries rather than dividends (de facto or disguised dividend)

Terminating minority shareholder strips them of share in profits

* + - * 1. Awarding high compensation to majority shareholders
      1. Freezeouts
         1. Controlling group attempts to eliminate minority financial rights and participatory rights in the close corporation
         2. Majority then attempts to buy out minority shareholder at an unfairly low price
  1. **Shareholder Oppression**
     1. Oppression Cause of Action
        1. Shareholder oppression only exists in the realm of close corporations
        2. “Oppression” may be grounds for involuntary dissolution of a close corporation
        3. Other jurisdictions have imposed an enhanced fiduciary duty between close corporation shareholders
           1. Similar to duties owed between partners
           2. Allows for breach of fiduciary duty claim
        4. Oppression claim much more preferable than breach of fiduciary duty claim in most jurisdictions
           1. Any *shareholder* has standing to bring an oppression claim as a matter of law
        5. TX statutes allow shareholder to bring dissolution action when “acts of directors or those in control of corporation are illegal, oppressive, or fraudulent”
           1. Also provides for receivership
        6. Tort action
           1. Punitive damages presumably available
     2. Measuring Oppression
        1. **Court must determine when oppressive conduct has occurred**
           1. *Three ways*

**Burdensome, harsh, and wrongful conduct** (TX courts have used this);

**Three Ways to**

**Identify Oppression**

A visible departure from the standards of fair dealing and fair play upon which every shareholder is entitled to rely

Good plaintiff’s definition (vague standard)

**Breach of the enhanced fiduciary duty**; or

**Frustration of the reasonable expectation of shareholders** (TX courts also use this)

* + - 1. **Frustration of Reasonable Expectations**
         1. MAJORITY, most-approved approach to defining oppressive conduct
         2. Occurs when majority substantially defeats expectations that, objectively viewed, were both reasonable under the circumstances and central to the petitioner’s decision to join the venture

EXAMPLES

No management participation

Termination of employment

No access to records

No ability to receive dividends

Refusal to recognize the shareholder as a shareholder

Disappointment alone does not equal oppression

* + 1. Remedies
       1. Dissolution
          1. Court orders sale of all assets
          2. Proceeds used to pay off creditors first
          3. Remainder of proceeds disbursed on pro rata ownership basis
       2. Remedies generally include everything up to actual dissolution
          1. Courts have fashioned many less harsh remedies
          2. Tremendous remedial flexibility [Moll]

*The* reason that plaintiffs try to get a shareholder oppression claim in their lawsuit

More remedial flexibility than breach of fiduciary duty action (generally)

* + - 1. ***Most dissolution actions lead to court-ordered buyout or elected buyout***
         1. Court-Ordered Buyout (TEXAS)

Most common remedy under a dissolution action

Technically not in the Texas statute but court has interpreted statute as allowing for less harsh remedies short of dissolution

Court or jury may value shares

Better price than what shareholder would receive through dissolution share of corporate assets

Dissolution sale is equivalent of fire sale with correspondingly low valuation

Oppressed shareholder gets out of corporation

Corporation still survives

This is a benefit over dissolution for the oppressing majority

* + - * 1. Elected Buyout

***NOT IN TEXAS***

Some jurisdictions permit corporation (or shareholders) to elect to buyout oppressed shareholder upon filing of a dissolution petition

Corporation or shareholder may circumvent dissolution by electing to purchase petitioner’s shares at fair value

Dissolution proceeding is converted to a valuation proceeding

Court determines valuation

Lawyers may dislike this procedure because no longer have opportunity to demonstrate how shareholder was oppressed and treated unfairly

Similar to a no-fault divorce [Moll]

Some courts have allowed minority shareholders to buyout the oppressing majority

* + - 1. Dissolution *Only*
         1. ***MINORITY Rule***
         2. Dissolution statute only gives courts authorization to dissolve the corporation

Court cannot order anything short of dissolution

* + 1. **Determining Fair Value**
       1. Valuation
          1. Buyout “at what price” is probably the most litigated aspect of shareholder oppression in Texas
          2. Texas- has not determined if FV = FMV or EV
          3. Buyout is at “fair value”

Both sides will provide experts that will provide diverging opinions

* + - * 1. Two Schools of Thought on Meaning of Fair Value

**Enterprise Value**

**Appraisers value the corporation as a whole and fair value is determined as a pro rata share of the corporation (CHC lack of liquidity can affect price)**

**Enterprise Value**

**20% shareholder gets 20% of corporation’s total value**

**100,000/20%= 20,000 enterprise value**

**NO application of minority or marketability discounts**

**Enterprise value is preferred by plaintiffs (no discounts)**

**Fair Value = Fair Market Value**

**What a willing buyer pays a willing seller (no compulsion)**

**More controversial valuation method**

**Apply minority discount to enterprise value (b/c minority shares don’t come with any control)**

**Fair Market Value**

**20,000 (EV) - 25% = 15,000**

**Then deduct an additional marketability discount (b/c CHC shares are not liquid )**

**15,000 – 25% = 11,250**

**Courts might look to Appraisal Value Statutes/Cases (NOT IN TEXAS)**

* + - 1. **Minority Discount**
         1. Minority shares by definition do not come with control of the corporation

No control, no control premium

Minority discount

* + - * 1. Minority discount is frequently at 33% [Moll]
        2. *MOST Jurisdiction’s Reject Minority Discounts in oppression context*
      1. **Marketability Discount**
         1. No market for closely held stock (no liquidity)
         2. 50% marketability discount is not uncommon [Moll]
         3. Marketability discount might not be so steep in the event that the stake is a controlling stake

More private buyers interested in buying a controlling stake

* + - 1. Apply largest discount first, apply separately
         1. Combined discount could be between 30-50%
    1. **Applying Discounts to Fair Value**
       1. Controlling (Oppressing) Shareholder Buyout
          1. Punishment Rationale

Discounts should not be applied in oppression proceeding

Purchasing (oppressing) shareholder should not be rewarded for oppressive conduct

Presupposes the ability to determine wrongdoing

Rationale should not apply at all in election context

Moll dislikes such rationale

It’s a blunt instrument and not appropriate

Obscures what is going on

Does not relate to the economic concerns which produce such discounts in the first place

* + - * 1. Minority Discount

Oppressing shareholder already has controlling interest—minority discount concerns should not apply

**MAJORITY RULE**

**No minority discount in oppression buyout**

Minority stock worth more to someone who already has control than any other purchaser

*Do not want oppressor to get benefit of oppressive conduct*

**In a dissolution context** (if court applied dissolution remedy), shareholders would have been paid pro rata without discounts

Dissolution Remedy Analogy

No minority discounts applied in dissolution

More applicable in an Elected Buyout but analogy applies in both contexts

Corporation Buyout

Shares bought back by corporation are “treasury shares” and are no longer outstanding

Minority Discount

Discount should not apply

Existing shareholder control simply increases

Corporation is not left owning a minority position—those shares disappear

* + - * 1. **Marketability Discount**

Marketability discount *may* in fact differ from controlling to minority stakes

May be used to give a smaller marketability discount

Should use the controlling marketability discount

Applying only controlling marketability discount to all shares prevents discriminating against minority versus controlling stake

Dissolution would not discriminate in such a manner and buyout should not discriminate in such a manner

All closely-held shares have a marketability discount, so it does not make sense to throw away the discount entirely

Some courts will throw out the marketability discount entirely based only on sense of equity [Moll dislikes this view]

Dissolution would have some sort of fire sale discount [Moll]

Not always the case that dissolution would produce more value than in a buyout context

Other courts apply marketability discounts even in a shareholder oppression setting

* + - * 1. Look at other Texas statutes that define fair value

Corporate statute- appraisal/dissenter’s rights statute

Every jurisdiction has it

When certain fundamental (mergers) corporation transactions occur, you as SH have statutory right to say you don’t want to participate and company is reqd to buy you out at fair value

**In appraisal context we have lots of precedent stating that fair value is enterprise value**

**Appraisal is no fault statute**

**It would be perverse to say in the fault situation we are going to apply discounts (oppression)**

* + - * 1. **What day do we use to determine fair value?**

Majority rule- date you filed your petition applying for dissolution or buyout, that’s the date you announce to the court you want out

* + 1. **Hypo*- assume your client is minority SH in a CHC and is being treated unfairly by controlling group***
       1. What is problem with breach of fiduciary duty in texas?
          1. **Standing problem**
          2. SH DO NOT OWE each other formal fiduciary duty in texas as a matter of law
          3. Too bad, b/c jury instructions for fiduciary duty are very favorable for π and it’s a tort, pun. Damages available
       2. Do not give up! Try an informal fiduciary duty claim
          1. Theoretically possible, but realisticly not very possible

Bringing this claim is a gigantic gamble these days b/c tx supreme ct has written a lot of statements that make it difficult to recover for this claim

∆ probably will bring summary judgment claim

* + - 1. What is different about oppression context?
         1. **NO STANDING ISSUE**
         2. Statute: You can bring a cause of action for oppression under statute and seek dissolution

Ct has equitable discretion to grant whatever remedies it feels appropriate

Buyout is most common remedy

Better to ask for buyout under guise of oppression, rather then breach of fiduciary duty action, which is likely to fail & probably waste of time

* + - * 1. BUT What if π is not a minority SH in corporation?

Tough luck- you then may have to try wild card breach of fiduciary duty

* + - 1. NOW, in TEXAS we have statute that says oppression statute applies to ALL business organizations
         1. LLC-

Some states like partnership, so members owe each other duty

Texas doesn’t have this, CHCs don’t owe each other duty, so LLC members don’t eiter

* + - * 1. LLP
      1. Basically two causes of action that are functionally the same- theoretically both police unfairness, but as far as practitioners are concerned🡪 doctrines rule and they result in one being very simple and the other almost impossible
         1. Treated as different causes of action
         2. And different doctrinal purposes
      2. Is oppression considered a tort? Answer should be yes, but no definite answer in Texas?
         1. If tort, then punitive damages likely
         2. Compare with breach of fiduciary duty, which is definitely tort
    1. Texas Concerns (May Apply to Other Jurisdictions)
       1. What Does Fair Value Mean?
       2. When is Fair Value Measured?
          1. No authority in Texas
          2. Other jurisdictions peg the date as the date on which lawsuit was filed

1. **The Boundary between Tort and contract**
   1. **Generally**
      1. Importance
         1. What happens when the *same set of facts* gives rise to both a breach of contract claim and a tort claim?
            1. Generally, you can always bring the contract claim

Question is: can you bring a tort claim?

* + - * 1. Under Texas law, you do not always get to bring both claims

Texas law suffers from inconsistencies [Moll]

* + - 1. Courts do not want to allow a tort claim with every instance of a breach of contract claim
         1. Converting every breach claim into a tort claim leads to unpredictability of damages

Commercial predictability

Businesses need to be able to plan for potential exposure

Contract damages allow this

Tort damages do not

Deters efficient breach

Must be able to calculate damages for efficient breach to work

Do not want punitive damages to enter picture for every breach of contract

Retards formation of contracts because of lack of predictability

* + 1. Historically: Old English law: misfeasance (tort) vs. nonfeasance (contract) [no longer good law]
       1. Active vs. passive
       2. Extremely malleable and therefore ridiculous [Moll]
    2. Purposes of Contract Law & Tort Law
       1. What is the purpose of contract?
          1. Contract law is designed to effectuate the intent of the parties
          2. Morally neutral, don’t think of it as “wrong behavior”
          3. No fault component
          4. Compensatory damages only
       2. What is purpose of tort law
          1. Vindicate social policy- conduct we as society deem undesirable
          2. To deter wrongful conduct and punish bad conduct

Punitive damages

* 1. **Modern Texas Con-Tort Law**
     1. *State of Texas Law- when the same set of facts gives rise to both a breach of contract claim and a tort claim*
        1. **Must certainly engage in a duty analysis**
           1. **Is there a TORT duty independent from the contract breach?**
        2. ***May* have to engage in nature of the injury analysis**
           1. Texas S. Ct may require a “nature of the injury” analysis on a tort-by-tort basis whenever they feel like the distance between the tort claim and the K claim is too close ***there is a great chance that every contract claim will give rise to or be converted into that certain tort, then court will evaluate the nature of the injury in determining if actionable under tort***

**Texas Con-Tort Test**

**Is there personal injury or property damage in addition to that which stems from the contract?**

**NO TORT if π only incurs Economic loss from contract breach**

**Nature of analysis may still be applicable for certain torts- negligent misrepresentation**

**Will NOT be relevant with fraud (*Formosa*)**

* + 1. *DeLanney*
       1. Duty Analysis
          1. To bring a tort claim, there must be a common law duty

Duty not to injure a person or property

This is a separate duty from the contract duty

* + - * 1. If defendant’s conduct would give rise to liability without existence of a contract, plaintiff may bring a tort claim

EXAMPLE

Person who contracts to fix a water heater and burns down a house

Burning down the house is independently negligent

* + - * 1. Contract Should Not Always Give Rise to Tort Duty (Gonzalez Concurrence in *DeLanney*)

Breach of contract is for a breach of a duty arising out of the contract

If a party must prove up the duties created by the contract and rely on those duties, the action sounds in contract

Action in tort arises out of a breach of a separate duty imposed by law not by contract

* + - * 1. This is a reformation of *Montgomery Ward*

Alleviates fear that every contract claim leaves the door open for a tort claim

* + - * 1. Test shifts from focus on the nature of the injury

*DeLanney* moves back to a duty analysis but a different analysis from *Montgomery Ward*

Duty must be independent of the contract

Duty arises out of the common law

* + - * 1. Moll thinks this realigns the law with common-sense approach to contract and tort claims
      1. Nature of Injury Analysis
         1. Court finds this instructive if not crucial
    1. *Formosa* (1998) (Fraud)
       1. **Analysis- Tort or K?**
          1. Is there a tort duty independent of the contract that was violated?

**Fraud- duty from inducing fraud, fraudulent misrepresentation; separate from K**

Recognizes importance of the *DeLanney* duty analysis

* + - * 1. Look at the nature of the injury

ONLY Economic loss stemming from contract breach

No additional property or personal injury damage

* + - * 1. **Ct says when it comes to fraud claims, nature of injury is not important**

**Tort damages are not precluded just b/c your damages are economic losses**

Pg 380: tort damages are recoverable for a fraudulent inducement claim, irrespective of whether the fraudulent representations are later

Purpose of Tort law is to deter conduct, nature of injury should not play a role

* + 1. ***DSA* (1998) (Negligent Misrepresentation)**
       1. After *DSA*, it is difficult to say what exactly is the state of the law [Moll]
       2. Claim of Note—Negligent Misrepresentation
          1. This case involved a negligent misrepresentation claim in an arm’s-length transaction

This is rare

Usually negligent misrepresentation claims brought against professionals

* + - 1. Negligent misrepresentation claim requires an independent tort injury
      2. Nature of Injury Analysis *is* applicable for negligent misrepresentation (*JWH* does apply)
         1. Why impose this on negligent misrepresentation rather than fraud (*Formosa*)?

Court has bigger fear of converting every breach of contract claim into a negligent misrepresentation claim

Negligence is easier to prove than scienter, which is necessary for fraud

Basically only requires a showing of carelessness

Far easier for a breach of contract claim to be “spun” as a negligent misrepresentation claim

* + - * 1. Injury requirement appears to still be viable at least for certain torts
      1. Alternative *DSA* Analysis
         1. Plaintiffs had asked for benefit of the bargain damages
         2. Negligent misrepresentation does not come with benefit of the bargain damages
         3. Under this analysis, *DSA* only stands for the notion that the plaintiff made a mistake by asking for expectation damages under a negligent misrepresentation🡪 ***wrong damages instruction which could only be supported by breach of K claim***

If this is the reading, then this is not even a con-tort case [Moll]

* 1. **Historical Development of Texas Con-Tort Law**
     1. Overview of Contort Problem in Texas- same facts give rise to both tort and K claims
        1. **Every K includes a tort duty to perform the K**
           1. *Montgomery Ward*
        2. **Nature of Injury- must have independent tort injury, personal or property damage in addition to those arising out of K**

**Evolution of**

**Con-Tort**

**in Texas**

* + - * 1. *Jim Walter Reed*
      1. **Tort duty- is required to recover under tort (tort duty must be indpendent of K, there is not a tort found in every contract)**
         1. Nature of injury is still instructional
         2. *Delaney*
      2. **Duty matters most, absence of special tort injury (only economic harm) does not preclude a fraud claim** 
         1. In Fraud case, nature of the injury is irrelevant

Rejects independent injury requirement from Jim Walter Homes in Fraud cases

* + - * 1. *Formosa*
      1. **If it is possible that every K claim would give rise to that specific tort issue (here NM) then the nature of the injury still matters**
         1. *DSA*
         2. *Jim walter homes analysis is still important when we fear that breach of K will become the tort of issue*
    1. *Montgomery Ward*
       1. Contract As Establishing a Tort Duty
          1. A contract may create the state of things which furnishes the occasion of a tort

Existence of duty of care may arise through an express or implied contract

Duty arises by implication

EXAMPLE

A person who contracts to make repairs can be held liable for his negligence in doing the work

“Every contract [involves] a common-law duty to perform with care, skill, reasonable expedience and faithfulness the thing agreed to be done, and a negligent failure to observe any of these conditions is a tort, as well as a breach of contract”

* + - 1. *Montgomery Ward* would turn every breach of contract claim into a concurrent tort claim
         1. Negligent failure to perform a contract is a tort *and* a breach of contract
    1. *Jim Walter Homes*
       1. Nature of the Injury (*Jim Walter Homes*)
          1. Nature of injury most often determines whether action sounds in tort or contract
          2. When loss is only the economic loss which is subject of the contract, the action sounds in contract *alone*

What Does This Mean? [Moll]

No physical injury to persons or other property

Not enough that subject of the contract itself is damaged

Brings into play “what is the subject of the contract?”

* + - * 1. Nature of the injury alone might eliminate fraud claims

Fraud claims are often concerned with economic damages under contract itself

* 1. **Breach of Contract *as* Tort**
     1. Generally
        1. Where breach of contract is so offensive that it is the equivalent of a tort
           1. Despite the fact that there is no violation of an independent tort
           2. Would allow recovery of tort damages
     2. Current California Law
        1. *Freeman* Holding
           1. No tort liability for breach of contract unless there is a special relationship where tort liability is justified
        2. *Freeman* Concurrence (Mosk)
           1. Some breaches of contract are worse then others
           2. If such offensive breaches can be identified, why not allow a tort claim?
           3. What Types of Breaches?

Breach accompanied by a traditional common law tort [Moll thinks this is obvious]

Tortious means of breach

Intentional breach knowing that breach will cause severe, unmitagatable harm in the form of mental anguish [Moll thinks this is obvious]

Remember not all consequential damages are foreseeable at time of contract and therefore contract damages would not be adequate

* + - * 1. Where might contract damages be insufficient?

Relationship-Based Contracts

Personal relationships

Unlike commodities contract, damages difficult to quantify

Lost profits

Goodwill

Efficient breach not an option in a personal services contract

Without efficient breach, why are we concerned with not allowing a plaintiff to bring a tort?

* + - * 1. Mean Breach vs. Breach

Mean breach examines motive of the actor

Mean breaches seen as undesirable by society

Mean breaches disregard predictability of contract

* + - * 1. Recognizing mean breach would lead to every breach of contract argued as a mean breach

Uncertainty would arise

* + 1. *Historic California Law* (NOT GOOD LAW) (*Seamans*)
       1. *Seamans* Holding
          1. Tort liability may attach where party to the contract denies, in bad faith, the existence of the contract

Motive inquiry

No summary judgment

These claims will go to the jury

Claims all of sudden have much settlement value

* + - 1. Consequences
         1. Legitimate contract defenses in jeopardy

Would lack of consideration, lack of mutual assent, etc. become actionable as a tortious denial of contract?

No summary judgment

Raising contract defenses would be difficult to distinguish from denial of contract

* + 1. **MEAN BREACH** *Should Breach of Contract ever be actionable as Tort?*
       1. In the Contract context we have seen it for insurance cases, arising from special relationship
       2. *CALIFORNIA- Siemens*- ct recognizes an implied covenant of good faith and fair dealing, which results in a breach of K, (analogous to breach of an implied term of the K) (overruled by *Freamon*)
          1. Tort of bad faith denial of contract- a contract may incur tort remedies when, in addition to breaching the contract, it seeks to shield itself from liability by denying, I bad faith and without probably cause, that the contract exists
       3. Consideration issue- what if ∆ claims there is no legally enforceable K b/c no consideration (or no assent etc)
          1. Worry is you cant deny the existence of K if you think its not legally enforceable
          2. Are we even allowed to contest liability?
          3. **What is the difference between bad faith denial of liability and bad faith denial of K’s existence, damages imposed are unpredictable now.**

Benefit of K was always that the damages resulting from are predictable, just compensation

All about predictability

No punitive wild card

Just fungible goods/compensation

Risk can be assessed upon entering the K

* + - 1. Freamon-
         1. What is the purpose of K law?

Purpose of K damages is to compensate the injured party, NOT to punish

Notions of punishment and fault are not key in K law

K remedies are designed to compensate, not deter or punish

K law has never distinguished btwn spite, wanton K breaches

All we ever care about in K is compensation

* + - * 1. **Policy for requiring only compensatory damages?**

Increases the formation of contracts

Fosters economic transactions and development, economic growth

Allocating risk is much easier

Estimate financial risk possible

Predictability

Breach of K should be possible🡪 efficient breach can be a good thing, nobody is made worse off and some people are made better off

This can only happen if damages are quantifiable

Siemens makes this front super challenging- b/c hard to distinguish bad faith denial of K and bad faith raising of defenses by ∆

Need to predict cost of getting in and getting out

Deters efficient breach

Ppl got nervous that they couldn’t raise defenses to contracts

And it made getting in and out of K’s unpredictable

* + - * 1. Did Freamon Court go too far? Is there a middle ground where K breach should become a tort🡪 mean breach possibility

Mean Breach by Judge Mosk- may be found when:

The breach is accompanied by traditional common law tort, such as fraud or conversion

Means used to breach the contract are tortuous, involving deceit or undue coercion; or

One party intentionally breaches the K, intending or knowing that such a breach will cause severe, unmitigable harm in the form of mental anguish, personal hardship, or substantial consequential damages

Says it wont erode line between Contract and tort🡪 only used when conduct goes beyond the lines of decency🡪 but if you allow that discretion, and make argument available, juries may be deceived and impose tort liability even when not deserved

Creating the unpredictability again

Mosk thinks Siemens facts fit into this mean breach category

* + - 1. Nota Bene
         1. “Breach of implied covenant of good faith and fair dealing” is NOT a tort

It is a tort in CA in an insurance context because of the special relationship between insurer and insured

* + 1. ***Anything that would cast doubt on the claim for a particular tort or would be inconsistent with the tort, may influence the decision***
       1. Π’s claims
       2. Damages requested
       3. ∆’s defenses