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## Corrective Justice in Contract Law: Is There a Case for Punitive Damages?

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# NOTES

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### I. INTRODUCTION

Twentieth-century American legal theory has been dominated by utilitarian and economic approaches. As a result, scholarly analyses of contract and tort law have focused on the public effects of the resolution of private disputes. But in the last twenty years or so justice has undergone a renaissance as so-called corrective-justice theorists have tried to shift the discussion in private law back to the relationships between individual parties. Tort law has been a particularly fertile ground for corrective-justice theorists, and a lively debate has developed about what the best corrective-justice account of tort law would look like.

By contrast, comparatively little has been written about corrective justice and contract law. In fact, Jules Coleman, one of the most influential corrective-justice theorists, argues that contract law is best explained by economic considerations that make bargaining

easier and more reliable, whereas tort law requires corrective justice because the bargaining costs are simply too high among tortfeasors and victims.<sup>1</sup> Coleman is the exception: Most corrective-justice theorists assume, or argue briefly in passing, that corrective justice will apply equally well to contract law.<sup>2</sup> However, few attempts have been made at anything like a comprehensive corrective-justice account of contract.<sup>3</sup>

This lacuna is surprising. While most major doctrines of contract law are well entrenched and accepted, the theories meant to explain those doctrines are not so well accepted, and many scholars believe that there is no “generally recognized” theory of contract.<sup>4</sup> Economic and utilitarian analyses aside, twentieth-century theories of contract generally fell into one of two broad categories. The first claimed that what little distinct law of contract exists was simply manufactured by Christopher Columbus Langdell and Oliver Wendell Holmes, among others.<sup>5</sup> Contract law is a subset of tort law, according to these theorists, and we should realize that and treat it as such.<sup>6</sup> The courts were already doing so, it was claimed, leading these theorists to talk of the “death of contract,” and to speak hopefully of the future when law schools would teach contract and torts together, perhaps even calling them “contorts.”<sup>7</sup> In fact, Grant Gilmore was so convinced that he began his 1974 book, *The Death of Contract*, with the claim that not only was contract dead, but that “the point is hardly worth arguing anymore,” and proceeded to apologize for even writing on such an uncontroversial subject.<sup>8</sup> For death-of-contract theorists, the fallacy of the Langdell-Holmes view lay in the link of contract to promises.<sup>9</sup> Contracts are binding, these theorists argued, not because of promises, but rather because the promisee generally relies on the promise to her detriment.<sup>10</sup> As Charles Fried, an opponent of the

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1. JULES L. COLEMAN, RISKS AND WRONGS 197 (1992).

2. See, e.g., ERNEST J. WEINRIE, THE IDEA OF PRIVATE LAW 50-53, 136-40 (1995).

3. Peter Benson has made the most comprehensive attempt. See Peter Benson, *Contract*, in A COMPANION TO PHILOSOPHY OF LAW AND LEGAL THEORY 24 (Dennis Patterson ed., 1996) [hereinafter Benson, *Contract*]; Peter Benson, *The Unity of Contract Law*, in THE THEORY OF CONTRACT LAW 118 (Peter Benson ed., 2001) [hereinafter Benson, *The Unity of Contract Law*]; Peter Benson, *The Basis of Corrective Justice and Its Relation to Distributive Justice*, 77 IOWA L. REV. 515 (1992) [hereinafter Benson, *The Basis of Corrective Justice*].

4. Benson, *Contract*, *supra* note 3, at 24.

5. GRANT GILMORE, THE DEATH OF CONTRACT 6 (Ronald K.L. Collins ed., 1974).

6. For two of the most famous and comprehensive accounts of this kind, see generally P.S. ATIYAH, THE RISE AND FALL OF FREEDOM OF CONTRACT (1979); GILMORE, *supra* note 5.

7. GILMORE, *supra* note 5, at 98.

8. *Id.* at 1.

9. Benson, *Contract*, *supra* note 3, at 29-30.

10. *Id.*

contract-as-tort theories, put it, "My statement is like a pit I have dug in the road, into which you fall. I have harmed you and should make you whole."<sup>11</sup> P. S. Atiyah went so far as to give a comprehensive historical argument claiming that only the Victorian morality of the nineteenth century had led to the focus on promising and to a willingness of courts to enforce executory contracts.<sup>12</sup>

The other main category of contract theories, though often referred to as "classical," was a response to the death-of-contract theories.<sup>13</sup> These "autonomy-based" theories tried to reestablish the central position of the promise in contract law.<sup>14</sup> Contracts are binding, they argued, for reasons very similar to the reasons promises—or at least promises of a certain sort—are binding.<sup>15</sup> Following Kant, contemporary autonomy theorists like Charles Fried argued that a promise is a paradigmatic case of a moral act and constitutes the grounds for our status as moral agents and, indeed, as humans.<sup>16</sup> Thus, executory contracts should be enforced even without reliance, since the basis for enforcing contracts in the first place is the promise, irrespective of whether the nonbreaching party has relied on it to his detriment.

Neither category of theories adequately explained contract law as a whole. Contract remains alive and well today, and contract-as-tort theories have never been able to explain why damages should be measured by the nonbreaching party's expectation interest, the standard contract remedy, rather than by her reliance interest, as the tort view would suggest. Nor could they explain why wholly executory contracts which the nonbreaching party had not relied upon should be actionable, as they continue to be today.<sup>17</sup> Although contract flourishes as a distinct body, autonomy theories of contract have not provided adequate explanatory accounts of its doctrine. While autonomy theories did adequately explain the enforcement of executory contracts, they provided a poor explanation for both the expectancy measure of damages and for the doctrine of consideration.<sup>18</sup> Since the

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11. CHARLES FRIED, *CONTRACT AS PROMISE: A THEORY OF CONTRACTUAL OBLIGATION* 10 (1981).

12. ATIYAH, *supra* note 6.

13. Benson, *The Unity of Contract Law*, *supra* note 3, at 121.

14. For perhaps the most well-known example of the classical model, see FRIED, *supra* note 11, *passim*.

15. For historical background on the autonomy, or "will" theorists, as well as some standard objections, see P. S. ATIYAH, *PROMISES, MORALS AND LAW* 17-22 (1981).

16. FRIED, *supra* note 11, at 19-21.

17. See, e.g., *id.* at 21-27.

18. See, e.g., Richard Craswell, *Contract Law, Default Rules, and the Philosophy of Promising*, 88 MICH. L. REV. 489, 494-95, 511-16 (1989).

enforcement of executory contracts, the expectancy measure of damages, and the doctrine of consideration are all so deeply entrenched in contract doctrine, a theory that fails to explain any one of them must of necessity be considered incomplete.

The renewed interest in corrective-justice theory as a noneconomic theory of tort law naturally leads to the question of whether corrective justice might provide the unifying theory that is lacking in contract law. This Note will explore that question in a small way. Since little has been written about the role of corrective justice in contract law, I shall begin in Part II by briefly discussing two of the leading corrective-justice tort theorists, Jules Coleman and Ernest Weinrib. After pointing out an important difference between Weinrib's and Coleman's views, in Part III I shall turn to contract law and briefly speculate about the prospects for a Weinribian account of contract law. Drawing on the work of Weinrib and Peter Benson, I shall argue that the relational features of private law highlighted by corrective justice show great promise as possible explanations for much of contract law. In particular, I shall focus on the question of damages and, drawing again from Weinrib and Benson, argue that despite Fuller and Purdue's famous assertion that by embracing the expectation measure of damages, contract law leaves the realm of corrective justice and enters that of distributive justice, expectation damages when properly understood are, in fact, compensatory. I will then enter new territory by arguing that one surprising consequence of Weinrib's view is that under a corrective-justice account of contract law punitive damages may be appropriate. That is, if corrective justice does the best job of explaining and justifying contract law, minor adjustments may still be necessary for the sake of coherence in contract's underlying principles. If those underlying principles are the corrective-justice principles advocated by Weinrib, I argue that we should reconsider contract's per se ban on punitive damages. With the conceptual possibility of punitive damages in place, in Part IV I shall provide a positive argument for why punitive damages would be warranted in some cases. This argument appeals to Kantian moral theory, but in a way that differs from the usual appeals to Kant in classical theories of contract. In Part V, I shall try to differentiate between the kind of willful breaches that warrant punitive damages and those that do not. To do so I examine the so-called tort of bad-faith breach of contract, which is now good law only in insurance contexts, and argue that the norms implicit in those contexts cohere well with more general values in contract law as well as the specific Kantian values for which I argue in Part IV.

## II. CORRECTIVE JUSTICE IN TORT LAW

This part begins, in Section A, with a brief discussion of corrective-justice theory for the sake of background. In Section B, I focus on a dispute between Coleman and Weinrib. That dispute is important because it leads Weinrib to make a crucial distinction between normative gains and losses and factual gains and losses, a distinction that I discuss in Section C. The implications of that distinction for a corrective-justice account of contract law are discussed in Part III.

### *A. Corrective Justice: Broad Outlines*

While it is not easy to find a single description of corrective justice that all corrective-justice theorists will support, a few common features can be identified. First and foremost, corrective justice seeks to correct previous wrongdoings by examining the relationship between wrongdoer and victim. This view of private law is most easily distinguished from distributive justice. While distributive justice concerns the distribution of wealth and other goods across the general population, corrective justice operates on private relationships among individuals.<sup>19</sup>

To illustrate the difference between distributive and corrective justice, Coleman proposes a thought experiment.<sup>20</sup> He asks that you imagine yourself to be extremely wealthy, more so than the Rockefellers, in fact, so wealthy that your wealth cannot be justified by any principle of distributive justice. Imagine, on the other hand, that Coleman is the opposite: so desperately poor despite his best efforts that no theory of distributive justice would tolerate his poverty. One day Coleman commits a tort that costs you money and results in a gain for him. Since you are now somewhat less rich and he is now slightly less poor, you are both closer to satisfying the demands of any plausible theory of distributive justice. But our tort law would demand that he reimburse your loss nonetheless. The reason, he claims, is because tort law is not concerned with distributive justice, but rather with corrective justice. Most corrective-justice theorists would agree

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19. Even this statement may assume too much agreement among corrective-justice theorists. For a broader discussion of the background of current corrective-justice theory, see Ken Kress, *Introduction to Formalism, Corrective Justice, and Tort Law*, 77 IOWA L. REV. i (1992).

20. COLEMAN, *supra* note 1, at 304.

with this simple intuition.<sup>21</sup> Furthermore, for the same reason, they would argue that tort law does not purport to satisfy some other instrumental goals, like deterring certain behavior, spreading loss over many members of society, or providing risk-of-loss insurance. Such goals may be worthwhile, but they are more appropriately pursued in the political realm than in individual private litigation over whether a given actor is liable for a victim's damages.

Second, most corrective-justice theorists agree that the private relations that corrective justice governs are in some sense bipolar.<sup>22</sup> In other words, while distributive justice is concerned with the justness of one's holdings in relation to society at large, corrective justice involves the correlative rights that we hold in relation to one another.<sup>23</sup> Tort law's methods of correction reflect this bipolarity:

Unjust gains and losses are not independent but coincidental changes in the value of the parties' holdings. If the gains and losses were independent, the losses and gains could be restored by two independent operations. However, because the plaintiff has lost what the defendant has gained, a single liability links the particular person who gained to the particular person who lost.<sup>24</sup>

Thus, tort law does not pertain to individual losses that have nothing to do with other people, as for example, when a hurricane destroys uninsured property. Rather, tort law, and private law generally, is concerned with losses that need to be corrected by others.<sup>25</sup> When someone drives her car carelessly and as a result strikes and injures a pedestrian, justice demands that the driver repair that loss and make the victim whole again, or at least as whole as monetary damages can make her.

Finally, many corrective-justice theorists trace their roots to Aristotle.<sup>26</sup> In fact, it was Aristotle who first paired private law with corrective justice and contrasted this pairing with the pairing of public

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21. As would most non-corrective-justice theorists as well. For an example of an argument criticizing corrective-justice theories on these grounds, see generally Gregory C. Keating, *Distributive and Corrective Justice in the Tort Law of Accidents*, 74 S. CAL. L. REV. 193 (2000).

22. Ernest J. Weinrib, *Corrective Justice*, 77 IOWA L. REV. 403, 409-11 (1992). For a similar view, but with a different conception of bipolarity, see COLEMAN, *supra* note 1, at 311-18.

23. See, e.g., Benson, *The Basis of Corrective Justice*, *supra* note 3, at 536.

24. WEINRIB, *supra* note 22, at 409.

25. The precise way in which corrective justice is bipolar is a matter of some controversy among corrective-justice theorists; this Note will explore part of that controversy. The basic idea that corrective justice concerns relations that are correlative in some way, however, is uncontroversial.

26. See, e.g., WEINRIB, *supra* note 2, ch. 3; Weinrib, *supra* note 22, at 404-09; Benson, *The Basis of Corrective Justice*, *supra* note 3, at 529-49; Stephen R. Perry, *The Moral Foundation of Tort Law*, 77 IOWA L. REV. 449, 452-56 (1992). But for a largely nonhistorical account, see generally COLEMAN, *supra* note 1.

law and distributive justice.<sup>27</sup> He also saw corrective justice as a bipolar relationship between two individuals.<sup>28</sup> While justice is a virtue, unlike other virtues, justice is directed towards another.<sup>29</sup> The most distinctive feature of Aristotle's account, however, is the fact that he saw justice as a mathematical operation.<sup>30</sup> The pursuit of justice is the pursuit of *to ison*, which in Greek means both "fairness" and "equality."<sup>31</sup> "In Aristotle's account, fairness as a norm is inseparable from equality as a mathematical function."<sup>32</sup> For him, corrective justice and distributive justice are simply different mathematical operations.<sup>33</sup> Particularly, corrective justice involved Aristotle's notion of balance, or equipoise, between two individuals.<sup>34</sup> Torts are transactions that upset this balance and result in one person having too much at the expense of another; corrective justice is about righting the scales.<sup>35</sup> While the idea of seeing law as a form of mathematics is jarring to us, and in the end Aristotle's account will be too simplistic for our purposes, his basic intuition is still quite compelling and has motivated many current thinkers.

*B. Coleman's "Mixed Conception" of Corrective Justice Versus  
Weinrib's Fully Relational Account*

Coleman was one of the pioneers of the rebirth of corrective justice in tort law. His early work in corrective justice centered on his "annulment thesis," according to which the purpose of tort law was to annul wrongful losses suffered by individuals.<sup>36</sup> He distinguished corrective justice from distributive justice, according to which tort law is a vehicle for preventing future losses, and saw the purpose of tort law instead as being about making victims of wrongful losses whole again.<sup>37</sup> He was heavily criticized, however, by Ernest Weinrib and

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27. ARISTOTLE, NICOMACHEAN ETHICS 120-23, 1131b25-1132b20 (Martin Ostwald trans., Macmillan Publ'g Co. 1962).

28. *Id.*

29. Aristotle's term is *pros allon*. See, e.g., *id.* at 114, 1129b25; WEINRIB, *supra* note 2, at 58-59; Benson, *The Basis of Corrective Justice*, *supra* note 3, at 533.

30. WEINRIB, *supra* note 2, at 57-63.

31. *Id.* at 58.

32. *Id.* It is important to note, however, that "equality" in this context does not suggest distributive justice. It does not mean, for example, that justice demands that everyone have equal holdings. Rather, it means that one does not have anything at the expense of another.

33. *Id.* at 57.

34. *Id.* at 62-63.

35. *Id.* at 61-63.

36. See, e.g., Jules L. Coleman, *Tort Law and the Demands of Corrective Justice*, 67 *IND. L.J.* 349 (1992).

37. COLEMAN, *supra* note 1, at 304-06.



Stephen Perry, among others, for his failure to link the wrongdoer with the wrongful loss, and thus for his inability to account for why we make injurers pay for the victim's losses rather than holding society at large responsible.<sup>38</sup> Under the annulment thesis, wrongdoers have no more duty or reason to act to repair an injustice than anyone else does.<sup>39</sup> In light of these criticisms, Coleman developed what he refers to as a "mixed conception of corrective justice," in which he argues that corrective justice also "imposes the duty to repair the wrongs that one does."<sup>40</sup> According to this view, the wrongful loss is related to the injurer because the injurer caused the loss.<sup>41</sup>

Even after modifying his theory, Coleman still had his critics. Perhaps the most prominent of them has been Ernest Weinrib. For Weinrib, the causal connection between injurer and victim is not strong enough for corrective justice.<sup>42</sup> Coleman's view focuses heavily on the victim and on annulling the victim's wrongful loss. Weinrib countered that under Coleman's view, wrongdoing by the injurer is not necessary for tort liability;<sup>43</sup> all that is required is that the loss be wrongful and that it be caused by the injurer.<sup>44</sup> A loss is wrongful for Coleman if it involves a violation of an individual's rights.<sup>45</sup> And for Coleman such violations can sometimes be caused by justifiable actions—in particular in what he calls "infringement" cases.<sup>46</sup> In such cases, an injurer takes a morally justifiable action that in fact violates the rights of another. The most famous example of such a case is *Vincent v. Lake Erie Transportation Co.*<sup>47</sup> Since the rights of another were violated, the loss is wrongful; since the wrongful loss was caused

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38. Stephen R. Perry, *Comment on Coleman: Corrective Justice*, 67 IND. L.J. 381 (1992); Ernest J. Weinrib, *Non-Relational Relationships: A Note on Coleman's New Theory*, 77 IOWA L. REV. 445 (1992).

39. *See, e.g.*, COLEMAN, *supra* note 1, at 312.

40. *Id.* at 320.

41. *Id.*

42. Weinrib, *supra* note 38, *passim*.

43. *Id.* at 445.

44. *Id.* at 445-48.

45. COLEMAN, *supra* note 1, at 335.

46. *Id.* at 344-49.

47. 124 N.W. 221 (Minn. 1910). In *Vincent*, the crew of a steamship moored to a dock during a violent storm decided not to cast off from the dock during the storm for fear of losing the vessel. *Id.* The dock was destroyed by the steamship during the storm as the wind and waves pounded the ship against it. *Id.* The dock's owners sued for the resulting damage to the dock, and the court held the steamship owners liable. *Id.* However, the court went out of its way to stress that the conduct by the steamship's owners was morally justified under the circumstances. *Id.* at 221-22. "Theologians hold that a starving man may, without moral guilt, take what is necessary to sustain life; but it could hardly be said that the obligation would not be upon such a person to pay the value of the property so taken when he became able to do so." *Id.* at 222.

by the injurer, the injurer is responsible, even though the injurer's actions were morally justifiable.<sup>48</sup>

According to Weinrib, corrective justice requires not only a wrongful loss but also wrongdoing on the part of the injurer.<sup>49</sup> Coleman's "mixed conception," on the other hand, is open to certain kinds of counterexamples.<sup>50</sup> For instance, in some cases the doctrine of superseding cause will allow the injurer to not be held responsible for the entirety of the loss.<sup>51</sup> For example, if a negligent driver strikes a pedestrian, he will be liable for her injuries. But if the pedestrian is taken to a hospital where she is subjected to gross negligence, the injurer is generally not responsible for the further injuries even though his actions caused them.<sup>52</sup> The additional injuries are wrongful losses that were in a sense caused by the injurer (but for his striking the pedestrian she would not have been in the hospital in the first place), but the injurer is not responsible for the medical malpractice.<sup>53</sup> Therefore, Weinrib argues, wrongful loss (as defined by Coleman) plus causation is not sufficient for tort liability.<sup>54</sup> According to Weinrib, even under his mixed conception Coleman is merely shifting loss around without an adequate account of why the injurer in particular should bear the burden of that loss. What is required is a thicker conception of the connection between injurer and victim. For Weinrib, this thicker conception must be fully relational in the Aristotelian sense where a bipolar relation exists between the wrongfulness of the loss and the wrongdoing by the injurer.<sup>55</sup>

Weinrib's account is fully relational in another way that Coleman's account is not. We saw above how for Aristotle corrective justice involves two individuals who are linked because one has gained at the expense of the other.<sup>56</sup> As we shall see below, Weinrib preserves

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48. Weinrib, on the other hand, agrees with the judgment in *Vincent*, but for different reasons. Rather than calling the loss a wrongful loss that was not the result of wrongdoing, Weinrib characterizes the transaction as a gain made by the defendant at the expense of the plaintiff that must be disgorged through restitution. See WEINRIB, *supra* note 2, at 196-203. Therefore, according to Weinrib, *Vincent* is not best explained by tort law at all. *Id.*

49. Weinrib, *supra* note 38, at 445-48.

50. *Id.*

51. *Id.* at 447.

52. Weinrib is probably incorrect in referring to "wrongful medical treatment" as an intervening cause. The injurer is generally liable for "all ordinary forms of professional negligence." W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 44, at 309 (5th ed. 1984). Weinrib's point still holds, however, for "highly unusual varieties of medical misconduct." *Id.*

53. *Id.*

54. Weinrib, *supra* note 38, at 445-48.

55. *Id.* at 448.

56. See *supra* note 27.

the idea that the injurer has gained something by injuring the defendant. While Coleman once entertained this idea,<sup>57</sup> he now claims that "corrective justice has [nothing] at all to do with wrongful gains."<sup>58</sup> Thus Weinrib's view of corrective justice links the injurer to the victim in two ways that Coleman's does not: it requires wrongdoing instead of just wrongful loss, and it requires wrongful gain on the part of the injurer.

Settling this dispute, or even giving a fully adequate explanation of it, is beyond the scope of this Note. Instead, I have noted the dispute as a way of highlighting the nature of Weinrib's fully relational view of corrective justice. Understanding the motivation for his view is important, because the fully relational view has certain surprising consequences if we try to apply corrective-justice theory to contract law—as Weinrib, unlike Coleman, wants to do. First it is important to examine more closely the specifics of Weinrib's "fully relational" view.

### *C. Weinrib and the Distinction Between Normative and Factual Loss*

For Aristotle, corrective justice concerns equipoise or balance between the injurer and the victim. The ideal, easy case is where the injurer gains by his unjust action the same amount that the victim loses. For example, if someone steals a taxicab and converts it to her use, then it makes sense for the law to force her to return not only the cab, but also any profits she may have made from its use. Her wrongful action has not only caused the owner a loss but has also resulted in a gain for the wrongdoer. Corrective justice seeks to restore the balance by taking from the wrongdoer what she unjustly gained and making good the victim's loss.

This account as it stands is too simplistic to explain modern tort law for the simple reason that very often wrongful losses by the victim do not result in any gain to the injurer. If instead of converting the taxi-cab the wrongdoer drives recklessly and crashes her own car into it, the victim suffers a loss, but so does the wrongdoer. In such cases, the measure of damages is generally determined just by the amount it takes to make the victim whole, even if the wrongdoer is also worse off for his behavior. Aristotelian mathematics does not seem to explain such situations. It is therefore easy to see why Coleman decided to abandon the idea of gain to the wrongdoer as a

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57. See, e.g., Jules Coleman, *Corrective Justice and Wrongful Gain*, 11 J. LEGAL STUD. 421, 424 (1982).

58. COLEMAN, *supra* note 1, at 369.

critical feature of corrective justice.<sup>59</sup> Under his “mixed conception” of corrective justice, Coleman still requires a violation of the victim’s rights by the injurer and therefore still stakes a claim to bipolarity for his view, but he does not go so far as to require Aristotelian equipoise.

Ernest Weinrib addresses this difficulty in a different way by drawing a distinction between factual gain or loss and normative gain or loss.<sup>60</sup> Factual losses are those decreases in the amounts of one’s holdings—the diminution in monetary value of the car, for example, and the owner’s loss of profits. Normative losses, on the other hand, derive from the justificatory structure of corrective justice. A person suffers a normative loss when “there is justification for the law’s augmenting his or her holdings.”<sup>61</sup> Factual gain and normative gain are similarly distinguished. Therefore, according to the correlativity of corrective justice, even though a tortfeasor may not enjoy a factual gain from negligently smashing another’s car, she does achieve a normative gain. It consists in “the excess in the defendant’s holdings, given the defendant’s violation of the norm that the duty signifies.”<sup>62</sup> In short, we all have certain rights of noninterference. When a tortfeasor violates the rights of a victim, the result is a normative gain for the tortfeasor—he has taken more, on some normative measure, than he is allowed to take—and a normative loss for the victim. We impose liability to rectify both wrongs.

Weinrib’s description of conduct violating norms of responsible behavior as conferring a normative gain on the actor is controversial.<sup>63</sup> For present purposes, however, I will treat it as intelligible and defensible. The point on which I wish to focus is whether it helps us to understand measures of damages in private law. Typically the goal in tort law is to compensate the victim for his losses. For Weinrib, that means the injurer owes the victim the amount of her factual loss.<sup>64</sup> But once we distinguish normative loss from factual loss the way Weinrib does, the question becomes: Why should the victim be

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59. *Id.*

60. WEINRIB, *supra* note 2, at 116.

61. *Id.*

62. *Id.* at 136.

63. For example, Weinrib’s description of normative gain is arguably circular. What is more, it is hard to imagine what a noncircular account of normative gain would be. George Fletcher developed a Rawlsian account based on risk taking and used it to argue for a tort regime of strict liability. George P. Fletcher, *Fairness and Utility in Tort Theory*, 85 HARV. L. REV. 537 (1972). Gregory Keating further developed Fletcher’s account. Gregory C. Keating, *Reasonableness and Rationality in Negligence Theory*, 48 STAN. L. REV. 311, 313-18 (1996). But these theories have their critics, too. See, e.g., John C.P. Goldberg, *Twentieth Century Tort Theory*, 70 GEO. L.J. (forthcoming 2003) (manuscript at 61, on file with author).

64. WEINRIB, *supra* note 2, at 135.

compensated for her *factual* loss? If the basis for liability is *normative* gain or loss, should not the goal be to make the victim *normatively* whole again? And if that is our goal, how do we know that the proper measure for what counts as being made normatively whole is factual loss? Perhaps a sincere apology should be required, or a public beating administered by the victim, or a sign worn by the tortfeasor that "I violated the rights of John Doe." Of course, I do not mean to suggest that any of these alternatives are better than the compensatory damages scheme now in place. Rather, the point is that if we are to take the distinction between factual loss and normative loss seriously, then it is not at all obvious that rectifying one would rectify the other.<sup>65</sup>

Even if we admit that rectifying factual losses by means of monetary awards is somehow the key to rectifying normative gains and losses, it is not clear that there would be a one-to-one mapping of the one to the other. If tort law is about making victims whole again and we take the distinction between normative and factual losses seriously, then we have to ask whether we mean making them factually whole again or normatively whole. Perhaps, for example, some violations of rights are particularly vile, normatively speaking, whether or not they result in much factual loss. Such an idea is almost certainly behind the concept of dignitary harm. One argument for allowing punitive or exemplary damages in tort law is to compensate the victim for the amount by which her normative losses exceeded her factual losses.

Weinrib himself rejects punitive damages as an appropriate remedy even under tort law.<sup>66</sup> Liability for Weinrib is completely determined by the injurer's violation of the victim's right and his subsequent duty to restore the victim to her previous position (her previous *factual* position).<sup>67</sup> Since we are merely trying to return the victim to her previous position, only compensatory damages should be allowed.<sup>68</sup> That is fine as far as it goes, but we should ask why the distinction between factual and normative loss for which Weinrib argued so strenuously in establishing the *basis* for liability should not be transferred to the *measure* of liability as well. Presumably, when he

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65. Both Coleman and Stephen Perry have made a related objection to Weinrib. "If I was wrong in my earlier work to focus entirely on the wrongfulness of the loss as the point of corrective justice, then I would commit a greater error by accepting the pure relational view that treats the loss as only coincidentally connected to the duty to repair." COLEMAN, *supra* note 1, at 323-24; Perry, *supra* note 26 at 478-88.

66. WEINRIB, *supra* note 2, at 135 n.25.

67. *Id.*

68. *Id.*

speaks of making the victim whole, he means to make her factually whole—i.e., reimburse her for her lost holdings. But perhaps we should strive to make her normatively whole instead, or additionally. Weinrib speaks as though the mere assignment of liability settles the normative score “in a single bipolar operation.”<sup>69</sup> However, merely holding the tortfeasor liable may not rectify the normative loss. If it did, then there would be no reason to go further and award damages. On the other hand, given that the tortfeasor does have a duty of repair based on his commission of the tort, it is reasonable to conjecture that in some cases his duty may go beyond merely compensating his victim for her factual loss.

Exceeding factual loss does not necessitate conceptualizing this increment as “punitive.” With Weinrib’s distinction in force, recognizing a normative loss above and beyond the factual one and ordering damages based on that additional loss is in some sense compensatory, though not for the victim’s out-of-pocket expenses and her other factual losses. It would be compensation for more than just losses in holdings, since we would be forcing an injurer to pay above and beyond factual loss based solely on the degree of his own misconduct (in Weinrib’s terms, the amount of normative gain by him and normative loss by the victim). The term “punitive” suggests a debt owed to society and brings to mind attempts by courts to influence future behavior of similar would-be injurers not party to the current litigation. Thus conceived, it would be difficult to justify punitive damages as a form of corrective justice, and Weinrib’s rejection of them is therefore understandable. But to the degree the term “punitive”—or the older term “exemplary”—refers to attempts to make one party right a wrong she has done to another party, a wrong which may not be rectified by mere repair of factual loss, then such damages are at home in a corrective-justice account like that provided by Weinrib. Traditionally, punitive damages in tort law have been paid to individuals, not to the government. Just as corrective justice is distinguishable from distributive justice in that it involves relations among individuals instead of the relationship between individuals and society at large, the punitive damages in private law are distinguishable from more conventional notions of punishment, since they are owed to individuals rather than to society.

In a somewhat different context, Stephen Perry has raised a similar objection to Weinrib’s theory,<sup>70</sup> to which Weinrib has

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69. *Id.* at 136.

70. See Perry, *supra* note 26, at 478-88.

responded.<sup>71</sup> Perry argues that if anything, Weinrib's Kantian theory of tort law establishes a "primary duty" not to injure others, but fails to establish the "secondary" duty to repair injuries that one (even wrongfully) causes.<sup>72</sup> Another way of putting the same point is that what Weinrib establishes is that the wrong itself, the normative gain and loss, is to be rectified, but he does not establish that the wrongful loss, meaning the factual loss, is to be reversed: "Even if we suppose that the notion of wrong which is said to derive from the normativity inherent in agency carries with it some requirement that the *wrong itself* be reversed or annulled, Weinrib nowhere demonstrates that any loss which results from the wrongful conduct must also be reversed."<sup>73</sup> Perry then goes on to argue for the stronger claim that not only does Weinrib not establish the secondary duty to repair, but that his theory of agency in fact makes it impossible for him to do so.<sup>74</sup>

Perry's argument, grossly oversimplified, is that Weinrib's Kantian theory of agency, which requires abstraction for the particular factual circumstances at hand, cannot possibly bridge the gap between the normative gain or loss and the factual gain or loss.<sup>75</sup> Weinrib's response, again grossly oversimplified, is that this objection ignores the fact that the Kantian conception of agency requires not only an abstraction from particular circumstances, but also an actualization under particular conditions in order to be a case of purposive, willful action.<sup>76</sup> The details of this debate are beyond the scope of this project, especially since Weinrib handles Perry's stronger objection quite nicely. What Weinrib does not do, however, is quite relevant: He does not answer Perry's weaker objection. That is, while he answers Perry's argument that Weinrib's Kantian theory of agency can never bridge the gap between primary and secondary duties, he does not answer the implicit weaker objection raised here. Weinrib does not explain why the amount of factual loss exactly quantifies the duty to repair normative loss.

By looking briefly at Weinrib's response to Perry, we can imagine how he might go about answering this objection. Weinrib claims that normative losses are tied to factual losses because in tort law one generally infringes the rights of another by causing a factual

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71. See WEINRIB, *supra* note 2, at 126-33.

72. See Perry, *supra* note 26, at 479.

73. *Id.* at 480 (emphasis in original).

74. "Not only does he not show us how to get from the primary duty to the secondary duty, but the conception of normativity that he says is inherent in agency turns out to preclude that very move." *Id.*

75. See *id.* at 481-88.

76. WEINRIB, *supra* note 2, at 127-33.

loss to the other.<sup>77</sup> That is so because Kantian rights are based on bodily integrity—whereby we are not to be treated as objects but rather as free, purposive beings—and on the embodiment of our rights in external objects of the will (things in which we have property rights).<sup>78</sup> Kantian rights deal with constraints on action.<sup>79</sup> We judge transactions to determine whether or not a constraint on action has been violated. If it has, then the violator of that constraint has a duty to “undo the consequences of the wrongful act by making good the factual loss.”<sup>80</sup> Thus, Weinrib sees the duty to compensate as the “natural remedial response to the infliction of wrongful loss.”<sup>81</sup>

And so it is. That is why—or at least one reason why—private law generally requires compensation rather than apologies, imprisonment, or public humiliation. Any theory that did not at least allow for this duty would be so at odds with our practices as to be seriously flawed if it purported to be at all explanatory.

The fact still remains that tort law is *not* just about annulling wrongful losses. As explained above, Weinrib himself has gone to great pains (along with Perry) to impress this point upon Jules Coleman.<sup>82</sup> Weinrib in particular wants to emphasize not only the wrongfulness of the loss suffered by the victim, but also the wronging of the victim by the injurer.<sup>83</sup> Unless the distinction between normative and factual loss is only a theoretical device for tenaciously clinging to an Aristotelian conception of corrective justice as mathematical equality, in some cases the two will not line up. And while it makes sense that rectifying factual loss will usually suffice to rectify normative loss, Weinrib has said nothing to establish that this must always be the case. Particularly bad acts may require more than just an undoing of factual loss or gain, since they may cause normative harm beyond the amount of factual harm. At the very least, the conceptual possibility remains open. Contrary to Weinrib’s own conclusion, the awarding of punitive damages in particularly egregious tort cases fits well into this conceptual gap.

So far, I have discussed corrective justice in the context of tort law, which is where most of the discussion of corrective justice in the academic literature has taken place. I shall now turn to an examination of how corrective justice might be applied to contract law,

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77. *Id.* at 129.

78. *See id.* at 128.

79. *Id.* at 130.

80. *Id.* at 129.

81. Perry, *supra* note 26, at 480.

82. *See supra* Part II.C.

83. Weinrib, *supra* note 38, *passim*.



where remedies are different from those of tort law because of contract law's default rule of expectation damages and its per se ban on punitive damages. Part III briefly looks at contract law through the lens of corrective justice. When we do we shall see how undoing normative losses will require more than merely undoing factual losses. In fact, the standard remedy of expectation damages requires going beyond factual loss to correct normative loss as a matter of course.

### III. CORRECTIVE JUSTICE AND CONTRACT LAW

Most of the work currently being done in corrective-justice theory lies in the realm of tort law. In fact, Jules Coleman, who, along with Weinrib, currently dominates the corrective-justice literature, simply surrenders all of contract law to economic theory.<sup>84</sup> Weinrib has, however, sketched the broad outlines of a possible corrective-justice theory of contract law,<sup>85</sup> and Peter Benson has also developed a fairly thorough account.<sup>86</sup> Through their efforts, we can begin to see how a corrective-justice theory might offer an even more coherent explanation of contract law than it does of tort law. Most obviously, contract law lends itself to the principles of correlativity common to corrective-justice theory even more than does tort law, since contracts generally involve two or more parties who freely obligate themselves to each other. Contract law seems especially well suited to a "fully relational" view of corrective justice such as that of Weinrib.

First, one central doctrine of contract law maintains that there is no enforceable contract unless there is both offer and acceptance. This requirement of mutual assent suggests that contracting is bipolar: action by both parties is required.<sup>87</sup> An offer without an acceptance is not enforceable, and vice versa. Without action by both parties nothing changes; with the right kind of action by both parties the rights and duties of both parties change. Transactions in tort law are bipolar in that the rights and duties of both parties can change, but generally the change is involuntary for at least one of the parties. Contract law is bipolar in an additional way, in that the rights and duties change only as a result of voluntary action by both parties.<sup>88</sup>

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84. See COLEMAN *supra* note 1, Part II.

85. See WEINRIB *supra* note 2, at 136-50.

86. See Benson, *The Unity of Contract Law*, *supra* note 3.

87. WEINRIB, *supra* note 2, at 137. For a much more detailed account, see Benson, *The Unity of Contract Law*, *supra* note 3, at 138-51.

88. Benson also points out that the same "logic of a transfer of ownership" is at work in gifts of property, and gifts also must be accepted in order for a legally recognized transfer of ownership to take place. Benson, *The Unity of Contract Law*, *supra* note 3, at 127-38.

Second, contract law requires that promises be given in exchange for valuable consideration in order to be enforceable. The doctrine of consideration also reveals the bipolarity of contract law “by affirming the promisee’s participation in creating the right to the promisor’s performance.”<sup>89</sup> The doctrine of consideration helps to ensure that the parties are treated as equals by requiring that parties become bound only in exchange for something for which they bargain, “thus participat[ing] as equal agents in the creation of the contract.”<sup>90</sup>

Third, contract law demonstrates the bipolarity of corrective justice in its treatment of unconscionable contracts.<sup>91</sup> Courts will rarely enforce contracts deriving from the exploitation of a vulnerability of one of the parties.<sup>92</sup> By protecting against agreements obtained through exploitation, the law of contract treats bargaining parties as equals and protects their rights as such. These fairness constraints reflect the bipolar requirement of corrective justice that the two bargaining parties stand in equal relation to one another.

The focus of this Note, however, is on damages, particularly punitive damages. Before addressing punitive damages, it is necessary to say a word about expectation damages. Despite the best efforts of the contract-as-tort theorists, expectation damages remain the standard remedy for breach of contract, and there is no indication that this will soon change.<sup>93</sup> Any adequate theory of contract must be able to explain why this is so. As Benson observes,<sup>94</sup> for decades discussions of contract law have generally begun by referring to Fuller and Perdue’s (really, Fuller’s<sup>95</sup>) famous essay on contract damages.<sup>96</sup> In that essay, Fuller criticized the expectation damages remedy, claiming, among other things, that it went beyond the realm of corrective justice into distributive justice.<sup>97</sup> Therefore, anyone who posits a corrective-justice account of contract law must explain not only why expectation damages are the standard remedy, but also how

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89. WEINRIB, *supra* note 2, at 138. For a much more detailed account, see Benson, *The Unity of Contract Law*, *supra* note 3, at 151-63.

90. WEINRIB, *supra* note 2, at 138.

91. *Id.* For a much more detailed account, see Benson, *The Unity of Contract Law*, *supra* note 3, at 184-95.

92. E. ALLAN FARNSWORTH, *CONTRACTS* § 4.28 (3d ed. 1999).

93. *Id.* § 12.8.

94. Benson, *Contract*, *supra* note 3, at 25.

95. Fuller is “universally regarded as the main author of the article and, in particular, its theoretical discussions.” *Id.*

96. L. L. Fuller & William R. Perdue, Jr., *The Reliance Interest in Contract Damages: 1*, 46 *YALE L.J.* 52 (1936); L. L. Fuller & William R. Perdue, Jr., *The Reliance Interest in Contract Damages: 2*, 46 *YALE L.J.* 373 (1937).

97. Fuller & Perdue, *The Reliance Interest in Contract Damages: 1*, *supra* note 96, at 56.

expectation damages are a remedy in *corrective* justice. As it turns out, Weinrib's theory can provide an answer to Fuller and explain expectation damages. Like Weinrib's explanation of the Aristotelian equipoise of tort law, it turns on the distinction between normative and factual loss. This explanation comes at a cost, however, as it did in tort law, by opening the door for punitive damages.

Fuller's argument that expectation damages are properly considered as grounded in distributive and not corrective justice is really quite simple. Corrective justice is concerned with compensating a victim for the loss inflicted upon him by the wrongdoing of another. In the case of breach of contract, a victim suffers a loss only to the extent of the detriment caused by the promisor's breach. To that extent, he should be compensated. But contract law goes further. Rather than simply restoring the nonbreaching party to the place he would have been had he never contracted with the breaching party, contract law "no longer seeks merely to heal a disturbed status quo, but to bring into being a new situation."<sup>98</sup> It is unlikely that this additional amount can be explained by reference to the value of the nonbreaching party's psychological expectation.<sup>99</sup> Thus, according to Fuller, contract law actually performs distributive justice rather than merely restorative or corrective justice. The challenge for corrective-justice theories of contract is to explain how it is that expectation damages are really compensatory.

Peter Benson has offered a thoughtful response. According to Benson, corrective justice is the justice of transactions, both voluntary and involuntary.<sup>100</sup> Contract law effectuates a transfer of ownership. To satisfy Fuller's demand and establish that the expectation damage remedy is compensatory, it must be the case that "prior to the breach and therefore before the time of performance, the promisee has an entitlement to the thing promised, including its value, whether or not the latter also figures as a reliance loss."<sup>101</sup> This transfer takes place not at the time of performance, but rather at the formation of the contract.

To begin, it is clear where we must locate the source of this entitlement: It must be in the contract itself, effected by contract formation. Contract formation, therefore, must itself constitute a mode of acquisition; it must give the promisee the requisite entitlement. More specifically, at and through formation, the promisee must acquire this entitlement from the promisor with his or her consent. Unless this is so, the expectation

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98. *Id.*

99. *Id.* at 57-58.

100. Benson, *The Basis of Corrective Justice*, *supra* note 3, at 538.

101. Benson, *The Unity of Contract Law*, *supra* note 3, at 127.

principle cannot qualify as a principle of compensation. Contract, then, must be intelligible as a transfer of ownership from one party to the other.<sup>102</sup>

Benson goes on to develop more fully the “logic of a transfer of ownership” and to explain how this logic supports much of contract law.<sup>103</sup> Expectation damages are compensatory, then, because they merely give the nonbreaching party exactly what he already owned—or at least the value of it.

The logical structure of this argument no doubt provides the framework for an answer to Fuller. One feature of the argument, however, is quite problematic: It seems strange, if not outright false, to say that ownership is transferred at the time of contracting rather than at the time of performance. Certainly the rights of possession that normally accompany ownership are generally only transferred at performance. For example, in the context of the sale of goods, “[t]he essential element that determines the location of the risk of loss is the identity of the party who has control over the goods.”<sup>104</sup> Even Blackstone, who saw contractual rights as a species of property rights, distinguished rights of possession from rights to performance.<sup>105</sup> According to Blackstone, executory contracts create only a chose in action and not a chose in possession.<sup>106</sup> It is only after a contract has been performed that the buyer has a possessory right against the world. What is more, the very idea that the promisee’s right is a property right at all is certainly debatable in the case of contracts for services.<sup>107</sup>

Benson does acknowledge that the rights a buyer gains at the time of contracting but before performance are in personam rather than in rem.<sup>108</sup> He argues that although the right that the promisee

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102. *Id.* at 128.

103. *Id.* at 127-38.

104. U.C.C. § 2-509(4) (1991).

105. “As soon as the bargain is struck, the property of the goods is transferred to the vendee, and that of the price to the vendor; but the vendee cannot take the goods, until he renders the price agreed on. But if he tenders the money to the vendor, and he refuses it, the vendee may seize [sic] the goods, or have an action against the vendor for detaining them.” 2 WILLIAM BLACKSTONE, COMMENTARIES ON THE LAWS OF ENGLAND \*448 (1766) (citations omitted). On the other hand, according to Blackstone, once the buyer had performed, he incurred the risk of loss even if the seller had not delivered the goods. *Id.* at \*448-49.

106. *Id.* at \*443.

107. I am grateful to Robert K. Rasmussen, Associate Dean for Academic Affairs and Professor of Law, Vanderbilt University Law School, for this point.

108. “Moreover, in contrast to the so-called right *in rem* which is usually thought to result from a present transfer, the right in contract is a right as against the other party only and to the other’s performance—a right *in personam*. It is only with actual performance that this personal right against the other party becomes a real right against the world.” Benson, *The Unity of Contract Law*, *supra* note 3, at 132.

has gained from the contract is against only the promisor rather than against the whole world, it is still a possessory right, a right of ownership.<sup>109</sup> If that were true, any transfer the promisor made to anyone other than the promisee would not be legally enforceable against the promisee, since it is axiomatic in the law that one cannot transfer rights that one does not have. If Seller has entered into a contract to sell his car to Buyer but instead sells it to someone else, that third party gains a right to possess the car, and Buyer has only a claim against Seller for damages. Although the transfer to the third party subjects the promisor to a breach of contract claim by the promisee, it is still a legitimate transfer to that third party, and the law is not likely to deprive the third party of the property.

Weinrib's explanation for expectation damages is more compelling. Rather than claiming that a contract instantly creates a property right, Weinrib argues that a contract entitles each party to the other's performance.<sup>110</sup> Weinrib does not elaborate on the point—he only mentions it in a footnote—but it is important for his overall view. Being entitled to performance is quite different from being entitled to a particular piece of property. When Benson argues that “the promised thing, including its value, must belong to the promisee,”<sup>111</sup> he is trying to show that at the time of contracting the promisee's belongings now include the thing promised, such that a breach of that promise would be akin to taking away property the promisee already owns. To put Benson's argument in Weinrib's language, for Benson a breach of contract entails a factual loss.

But as Weinrib points out, the promisee gains an entitlement to performance, not to the thing itself.<sup>112</sup> Such an entitlement is less tangible than an entitlement to a thing. Although Weinrib does not discuss the issue, the entitlement to performance is best understood as a normative entitlement, and the subsequent loss when the promisor fails to perform is a normative loss rather than a factual loss in holdings. Of course, the promisee may suffer a factual loss if, for example, she incurs expenditures in reliance on the promise. But contract law usually measures damages by her expectancy, not by her reliance. It would make more sense to call the loss a factual loss if, as Benson would have it, contracting actually transferred ownership

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109. *Id.* at 135-36. Interestingly, Benson notes that “[i]n reaching this conclusion, I am departing from Kant's view. According to Kant, what the promisee acquires at formation is just the promise of performance. The promise is the substance of the promisee's personal right as against the promisor.” *Id.* at 136 n.26.

110. WEINRIB, *supra* note 2, at 136 n.26.

111. Benson, *The Unity of Contract Law*, *supra* note 3, at 127.

112. WEINRIB, *supra* note 2, at 136.

prior to performance. But in fact, the promisee does not really gain ownership until performance; before performance, the promisee merely has a right to performance. This right will sometimes be assignable and thus may have a monetary value.<sup>113</sup> But the important point is that for Weinrib the contract itself does not change the promisor's position with respect to the thing promised, but rather "works a voluntarily assumed correlative change in [the] moral position" of the parties.<sup>114</sup>

Although Weinrib's view relies on the controversial distinction between normative and factual loss, if the distinction is valid his account is superior to Benson's explanation. Benson's account has the necessary logic to explain how, contra Fuller, expectation damages are compensatory and not distributive, but it relies on the strong and controversial premise that ownership is transferred at the time of contracting rather than at the time of performance. Weinrib's distinction between normative and factual losses avoids such a claim while maintaining the logic necessary for expectation damages to be compensatory. They are compensatory, but not because the promisee suffers a factual loss. In fact, aside from possible reliance, the promisee generally *does not* suffer a factual loss from the promisor's nonperformance since the promisee only really comes to ownership when the contract is performed.<sup>115</sup> But while the promisee does not yet have rights in the thing itself, such that the lack of performance would result in a factual loss, the promisee does have a right to performance: she has a normative claim against the promisor. Therefore, when the promisor fails to perform, even if the promisee suffers no factual loss, she does suffer a normative one in that "there is a justification for the law's augmenting . . . her holdings."<sup>116</sup>

We saw in Part II how Weinrib introduced the distinction between factual and normative loss to account for the fact that the injurer in tort cases is seldom any better off for having injured the

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113. Blackstone also saw contractual rights as a form of property rights, choses in action. See BLACKSTONE, *supra* note 105, at \*443. The fact that contractual rights are often assignable and therefore look in many ways like other property rights might lead one to conclude that a breach of contract results in factual loss. But this would be a mistake since the right to performance is not actually lost the way the value of one's car is lost in an accident. Therefore, even if someone's chose in action is part of her holdings, the breach of contract itself does not constitute a loss of those holdings. The loss, if any, is a normative loss.

114. WEINRIB, *supra* note 2, at 137.

115. Of course, reliance damages will sometimes be substantial, especially when they include lost opportunity costs. Indeed, Fuller speculated that expectation damages might be in part an attempt to compensate for lost opportunity costs, which are usually very speculative and difficult to calculate. Fuller & Perdue, *The Reliance Interest in Contract Damages: 1*, *supra* note 96, at 60-61.

116. *Id.* at 116.

victim. We also saw that although Weinrib is opposed to punitive damages in tort, his opposition may run afoul of his idea of normative gains and losses as providing the basis for tort liability. Now I have argued that the distinction between normative and factual loss would also be at the heart of a Weinribian account of contract law, as it is necessary to explain how it is that the expectancy measure of damages is compensatory. Expectation damages reflect the amount of normative loss suffered by the promisee even when the promisee has suffered little or no factual loss.

But while this distinction works well in that it allows Weinrib to have expectation damages be compensatory without forcing him to embrace Benson's more suspect claims regarding the transfer of ownership at the time of contracting, it again may have consequences he would not intend. As with tort law, the sort of reparation that the victim's normative loss will require is an open question. In tort law, Weinrib equated the damage remedy with factual loss. I argued that this equation may be premature and that in at least some circumstances the normative loss may be great enough that mere compensation for factual loss will not suffice. Now we see that in contract law it is, in fact, normally the case that mere compensation for factual loss will not suffice. The question naturally arises, then, whether contract damages will always be capped by the nonbreaching party's expectation interest, as current American law requires,<sup>117</sup> or whether punitive damages would sometimes be justified as a way of compensating for particularly great normative losses. Although a breach of contract will not usually result in a huge normative loss, it appears to be a consequence of Weinrib's view that particularly egregious cases could call for punitive damages.

In Part II, we saw that Stephen Perry's objection that Weinrib does not and in fact cannot derive a secondary duty to repair factual loss from a primary duty not to cause normative loss.<sup>118</sup> Perry's objection was based on the abstract nature of the Kantian rights and duties that, according to Weinrib, form the basis of tort liability. Weinrib responded that, notwithstanding the abstract nature of Kantian rights and duties, particular rights and duties are still grounded in particular, contingent circumstances. The duty to compensate for factual loss arises from the fact that the holdings that are lost in a wrongful injury are embodiments of the victim's rights. Undoing that loss is therefore the natural way to undo the normative loss the victim suffers when his rights are infringed. Just as

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117. FARNSWORTH, *supra* note 92, § 12.8.

118. See *supra* note 70 and accompanying text.

normative and factual losses are inflicted by one action, so are they corrected by one action, the restoration of the victim's holdings.

I argued that while Weinrib's claim for tort law does seem to answer Perry's stronger objection (that the idea of normative loss cannot be used to impose a duty to repair factual loss at all), it fails to answer his weaker objection. Perry had objected that Weinrib had failed to demonstrate that restoring factual loss will always exactly repair normative loss. Weinrib's claim, I argued, is (like Coleman's annulment thesis) too focused on the wrongful (factual) loss of the victim while not fully accounting for the wrongdoing of the injurer. In particular, it ignores the possibility that in rare cases the wrongdoing by the injurer can be so egregious that it causes normative losses that the mere restoration of factual losses will not rectify.

Since the remedy for a breach of contract usually awards damages based on normative loss in excess of factual loss, Weinrib's response to Perry will work even less well for contract law than it does for tort law. According to that response, the measure of damages for breach of contract should be based on the promisee's reliance since that would be sufficient to restore the victim's factual holdings.<sup>119</sup> Expectation damages, on the other hand, go beyond correcting infringements in the physical embodiments of the promisee's rights. In many cases the promisee will not have suffered a loss in holdings at all, yet she is still entitled to expectation damages. The best explanation for this rule—at least, the best Weinribian explanation—is that when a promise is breached the promisee incurs a normative loss that normally cannot be corrected by simply restoring her loss in holdings. Thus, what was a mere conceptual possibility in Weinrib's theory of tort is the standard practice in contract law.

Some normative losses can be so great that even expectation damages will not suffice. Just as particularly egregious malfeasance may justify punitive damages in tort law, it now seems quite possible that egregious, bad-faith breaches may justify punitive damages in contract law as well. It seems that we need a more inclusive conception of the secondary duties of reparation than the one Weinrib suggests. Perhaps, in true Weinribian fashion, we can further specify such a duty by appealing to Kantian moral theory.

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119. As we saw, that is exactly what Lon Fuller (though not a corrective-justice theorist himself) argued that contract law ought to do.



## IV. CONTRACTS, CORRECTIVE JUSTICE, AND THE CATEGORICAL IMPERATIVE

Contemporary corrective-justice theories, Weinrib's in particular, are often understood in terms of Kant's moral philosophy. Our duty to exercise due care not to harm others is based on a duty to respect them as persons. We have a duty to exercise our own will in such a way that it does not interfere with the corresponding right of others to exercise their free will. Our own rights to act freely and to pursue our own conception of the good extend to, but do not cross, the boundaries of others' abilities to do the same. When we take excessive risks we fail to respect those rights of others. According to one formulation of Kant's famous categorical imperative, we are never to treat people as mere means to an end, but instead should always see them as ends in themselves. And according to many corrective-justice theories of tort, when we take excessive risks and thereby fail to respect the rights of others, we are treating them as objects rather than as rational agents. Of course, this is a gross oversimplification of both Kant's moral philosophy and corrective-justice theories, but it should suffice for the limited point I wish to make.

While Kantian moral theory has often been cited in contract theory, it has generally been used as an explanation for why promises ought to be binding. Autonomy theorists like Charles Fried have made much of Kant's emphasis on promising as an example of the will binding itself, and of lying or the breaking of promises as an example of a violation of Kant's categorical imperative.<sup>120</sup> But their focus has been almost entirely on the promisor against whom the contract is to be enforced. A corrective-justice account, by contrast, does not allow us to focus only on the promisor. Instead, corrective justice emphasizes the fact that private law governs relationships among individuals and focuses on the correlativity of rights and duties. Thus, a corrective-justice theory of contract law would have to account not only for the act of the promisor in making the promise, but also for the role of the promisee.

If we combine a conception of contract law underwritten by the categorical imperative not to treat others merely as means to an end with the Weinribian idea of normative gain and loss, then we have occasion to reconsider the damage remedies available for willful, bad-faith breaches. Given that contracting involves the kind of exercise of free will that is distinctively human—that is only available to rational agents and that distinguishes us from mere objects—when we take on

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120. ATIYAH, *supra* note 15, at 17-22.

contractual obligations, we are doing something that only rational agents can do. By agreeing to obligate ourselves in exchange for something else, we take risks: we risk not being able to perform and having to pay damages, we risk that the other side may be unable or unwilling to perform and perhaps unable even to pay damages should it not perform, and we risk that even if both sides perform, the benefits may not be as great as we had hoped. On the other hand, since contracting allows us to make claims on the other party that we would not otherwise be able to make, we benefit by the other party obligating itself and taking similar risks.

When we undertake such obligations, however, we also expose ourselves to various forms of predatory or opportunistic behavior. Unscrupulous people will be able to use the practice of contracting to take liberties with others that would otherwise be unavailable. In the contract formation process, one party might deceive or exploit the other. Once both parties are bound by a contract, one party may decide to completely disregard the contractual obligation and instead simply opt to pay damages, even when he knows that the other party bargained for performance and that expectation damages will be unsatisfying. Taking advantage of the other party in this way would be particularly offensive under a Kantian theory of corrective justice where the only reason the nonbreaching party would be vulnerable to such bad-faith behavior would be because she had freely entered into the contract. Given that we are to respect people as free, autonomous agents and not treat them as mere things, taking advantage of someone's agency in this way is particularly reprehensible. The normative gain and loss associated with such an exploitative transaction would exceed the terms of the contract and the expectation damages remedy.

To put the point another way, the world is made up of agents with free will and external objects without free will. In a typical tort case, an injurer comes to owe a victim money by damaging her physical property. Although this loss is merely a factual loss, it also is a normative loss because the physical property is the embodiment of the victim's agency.<sup>121</sup> By violating another's right to bodily integrity or property ownership, we treat that person as an object rather than as an agent with free will.<sup>122</sup> But in contract law the tie to Kantian moral theory is even closer, since instead of infringing on mere embodiments of another's free will, an actor who willfully and in bad

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121. "[A]gents are barred from interfering with things—the bodies and properties of other agents—that are the embodiments of someone else's free will." WEINRIB, *supra* note 2, at 129.

122. "For by such a breach one actor treats another not as a self-determining being but as the instrument of an extrinsic purpose." *Id.* at 128.

faith breaches a contract does so *by means of* another's free will. To do so is not only to fail to respect another's status as a moral agent, but is also to take advantage of that status and to use that very status to treat him as an object.

It might be objected that the argument thus far proves too much, for it seems to imply that punitive damages would be appropriate for any breach of contract, or at least for any willful breach. On the other hand, one might object that even willful breaches will never warrant punitive damages because parties enter into contracts knowing that breach by the other side is a distinct possibility. Holmes famously argued that when we enter into contracts, we are really promising either to perform or to pay damages.<sup>123</sup> If that is true, then it is difficult to see breach of contract as the kind of wrong that would warrant punitive damages.<sup>124</sup>

These two objections are best answered in conjunction. Holmes's thesis could mean two different things. On the one hand, in keeping with his separation of law and morality, it could just be an assertion of what constitutes legal obligations. According to this view, we simply think of law as "the bad man" would.<sup>125</sup> Just as the bad man is unencumbered by any moral compunction to keep promises, so too the law will not require him to keep them (although it will require him to pay damages if he does not). Whatever merits this view may have as an interpretation of what Holmes intended, it is inconsistent with any application of corrective justice. Corrective justice does not allow us just to think of law as the bad man would. Whether corrective justice is right to reject this strict separation of law and morality is beyond the scope of this project.

A more charitable interpretation of the Holmesian thesis, at least from the standpoint of corrective justice, is that it shows that while parties do undertake moral obligations by contracting, the obligations they undertake are not necessarily exactly as stated in the contract. Rather, the content of the promise is a covenant to either perform or pay damages. According to this view, the promisor does have an obligation under the contract in the thickly normative sense, but he fulfills that obligation either by performing or by breaching and paying expectation damages.

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123. "[T]he duty to keep a contract at common law means a prediction that you must pay damages if you do not keep it,—and nothing else." Oliver Wendell Holmes, *The Path of the Law*, 10 HARV. L. REV. 457, 462 (1897).

124. In fact, in some types of contracts, like futures contracts, breach is *expected*. Again, I am grateful to Professor Robert Rasmussen for this point.

125. Holmes, *supra* note 123, at 459.

Even this more limited Holmesian thesis is quite controversial.<sup>126</sup> It is not at all clear that parties who promise to perform really intend just to perform or to pay damages. And if they do have some sort of Holmesian promise in mind, it is even less clear exactly what that promise would be. Does a promise to perform mean that the promisor may for any reason choose to pay damages instead of performing? Or does a promise to perform mean he must do so unless a labor strike or a natural disaster occurs, or unless business goes bad, etc., in which case paying expectation damages would suffice? The latter kind of promise would more accurately capture the typical promisor's state of mind. But even in that case it would be necessary to determine which factors were included in the "unless" clause—a difficult, if not impossible, task.<sup>127</sup>

These difficulties aside, the Holmesian thesis certainly has had an impact on American contract law. If nothing else, sophisticated promisees should by now be on notice that in general promisors can breach freely and willfully as long as they pay expectation damages. Since promisees are now on notice, promises can fairly be interpreted as weaker, Holmesian obligations to either perform or pay damages. Therefore, a breach of contract will not usually warrant punitive damages because the payment of expectation damages will fulfill the normative requirements of the contractual obligation.

In some situations, however, it would be inappropriate to attribute the Holmesian promise to the promisor. Unsophisticated parties, for example, may be unaware of the way courts have accepted the Holmesian thesis. To some parties, performance itself will be important, perhaps for fear that damage remedies will be insufficient. Sophisticated parties typically will contract around this difficulty with liquidated damage clauses, but unsophisticated parties may not know to do that, especially when they do not have legal counsel present at the time of contracting. Instead, they may seek and rely on assurances from the promisor that it will indeed perform. When it is clear to a

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126. See, e.g., Craswell, *supra* note 18, at 512-13.

127. On the other hand, an appeal to such "unless" clauses might allow a corrective-justice account of contract law to address worries about the performance of inefficient contracts. Economic theorists argue against punitive damages in contract law on the ground that they would discourage efficient breaches and encourage parties to perform even when performance is wasteful. See, e.g., RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 131 (5th ed., Aspen Law & Bus. 1998) (1973). Efficiency arguments have won over much of the current legal scholarship as an explanation for why punitive damages are not awarded in contract cases. See, e.g., *RESTATEMENT (SECOND) OF CONTRACTS* introductory cmt. to ch. 16 at 100 (1981); FARNSWORTH, *supra* note 92, § 12.3. While a direct appeal to efficiency would be out of place in a corrective-justice account of contract law, to the degree that the content of a promisor's promise is something like a promise to perform unless performance would be wasteful, corrective-justice theory will not necessarily encourage wasteful performance.

promisor at the time of contracting that a promisee, whom the promisor knows to be unsophisticated, really desires performance and is likely to be greatly disappointed with expectation damages, it would be unjust for that promisor later to claim to have made only a Holmesian promise.

Consider, for example, the *Peevyhouse* case.<sup>128</sup> In that case, the Peevyhouses leased sixty acres of their 120-acre farm to the defendant coal company for five years so that the coal company could conduct strip-mining on it.<sup>129</sup> The lease provided that at the conclusion of the mining operations, the coal company would fill in all the pits and smooth the surface.<sup>130</sup> The defendant did nothing to repair the land, and expert testimony at trial estimated that while the cost of such repairs would be around \$29,000, the increase in the value of the land due to the repairs would be no more than \$300.<sup>131</sup> Although the jury awarded a verdict of \$5,000 to the Peevyhouses,<sup>132</sup> the Oklahoma Supreme Court, in a four-to-three decision, reduced the verdict to \$300 on the ground that \$5,000 was more than the value of the land had the remedial work been done.<sup>133</sup> A dissent, however, pointed out that all the costs and benefits in the defendant's performance could have been foreseen at the time of contracting, and that by the defendant's own admission, the Peevyhouses had insisted on the remedial provision and had indicated that without it they would not have signed the lease.<sup>134</sup>

If any contract case cries out for punitive damages, the *Peevyhouse* case does. It is difficult to look at the facts of this case without concluding that the coal company simply breached because they could and because they had reason to believe that they would only pay \$300 by breaching even though they had assured the Peevyhouses they would actually perform the work. What seems particularly troublesome about the case is that the coal company was able to use the Peevyhouses' ability to contract against them. If the coal company had merely taken the coal without a contract, then they would have been subject to actions for trespass and conversion and would have been forced to pay for the entire value of the coal, pay for

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128. *Peevyhouse v. Garland Coal & Mining Co.*, 382 P.2d 109 (Okla. 1962); see also Maute, *Peevyhouse v. Garland Coal & Mining Co. Revisited: The Ballad of Willie and Lucille*, 89 NW. U. L. REV. 1341 (1995).

129. *Peevyhouse*, 382 P.2d at 111, 117.

130. *Id.* at 111, 114.

131. *Id.* at 111.

132. *Id.*

133. *Id.* at 114.

134. *Id.* at 115.

damage to the land, *and* be subjected to punitive damages, at least if a jury was inclined to award them. It was only because the Peevyhouses freely entered into the contract that the coal company was able to take the coal without trespassing. Its willful breach took advantage of the Peevyhouses, and it did so by means of the Peevyhouses' own agency and ability to contract. It is hard to imagine a better example of a violation of Kant's categorical imperative, whereby we are forbidden to use people as means to an end and are always to treat them only as ends in themselves. The coal company not only used the Peevyhouses as means to an end, but they also used the Peevyhouses' free will and autonomy, the very things that, according to Kant, make us human.

It is important to distinguish between cases like *Peevyhouse* and those in which the breaching party never intended to perform under the contract. When a party signs a contract with no intent to perform and does not perform, the breaching party is guilty of fraud, and such cases are usually considered torts. With the Peevyhouses, however, the malfeasance was not a knowing misrepresentation, but rather a willful refusal to do what one sincerely promised to do. This refusal is a specifically contractual harm because the only reason the Peevyhouses were vulnerable to the coal company was because both sides agreed to the contract. What troubles us about cases like *Peevyhouse* is that while it cannot be shown that the coal company knew at the time of contracting that it would not repair the land, it appears that circumstances at the time of breach were exactly as they might have expected, or even hoped, at the time of contracting. Without punitive damages, cases like *Peevyhouse* create a formula by which sophisticated parties can take advantage of unsophisticated parties by means of strategic breaches in certain kinds of contracts. This sort of behavior offends our sense of justice, and a corrective-justice account of contracting would seek to redress such wrongs even beyond the normal standard of expectation damages.

At this point it might be objected that the real problem with *Peevyhouse* is not that expectation damages were insufficient, but rather that the court applied the wrong measure of expectation damages. Indeed, *Peevyhouse* is a casebook chestnut example of the difference between measuring expectancy by the diminution of market value versus the measuring it by the cost of completion.<sup>135</sup> Measuring expectancy by the cost of completion is not unheard of in contract law: a famous example is *Groves v. John Wunder Co.*, another casebook standard.<sup>136</sup> In that case, the court awarded \$60,000 to cover the cost

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135. See, e.g., JOHN P. DAWSON ET AL., *CONTRACTS: CASES AND COMMENTS* 19 (7th ed. 1998).

136. 286 N.W. 235 (Minn. 1939); see, e.g., DAWSON, *supra* note 135, at 11-18.

of completion even though the property would have only been worth \$12,160 more after performance.<sup>137</sup> The *Groves* court cited the fact that the breach was deliberate and willful as a justification for what arguably was a windfall to the promisee.<sup>138</sup> Most courts have not followed *Groves*, and now the general rule is that promisees can only sue for the cost of completion if such cost is not "greatly out of proportion" to the diminution in market value.<sup>139</sup> One might argue that cases like *Peevyhouse* should be an exception to this rule, thereby making expectation damages sufficient and punitive damages unnecessary. But this objection is misplaced because the general rule for measuring expectation damages by the diminution of market value if the cost of completion is unreasonably high is the best measure of expectation damages. In most cases it seems entirely fair and reasonable not to give the plaintiff the windfall that a disproportionate cost of completion would provide, especially when "in none of the cases denying recovery for cost to remedy the defect had the claimant actually incurred that cost."<sup>140</sup> In a few cases, including *Peevyhouse*, expectation damages as measured by the diminution in market value will not be a satisfactory remedy, but not because the expected value is worth more. Indeed, while the restoration of the land might have had a higher subjective value to the *Peevyhouses*, its market value was the same. The difference was that they suffered a normative loss beyond the \$300 awarded by the Oklahoma Supreme Court. They were exploited in a way captured neither by the diminution in the value of their land, nor by the mere declaration by the court that the coal company had breached.

Another way of seeing this point is to recognize that sometimes the cost of completion will be much higher than what will be warranted by the normative loss. While the *Peevyhouses* were certainly wronged, a \$29,000 damage award (in 1963 dollars) would almost certainly have overshot the mark. The jury in the trial apparently agreed since it awarded the *Peevyhouses* \$5,000, an amount well over the \$300 loss in market value but well below the \$29,000 cost of completion. Although overturned on appeal,<sup>141</sup> the

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137. *Groves*, 286 N.W. at 236.

138. *Id.* at 238. Importantly, under my view the *Groves* case would not only not warrant the cost of completion, but it also would not warrant punitive damages. Although the breach may have been willful, not all willful breaches warrant punitive damages. *Groves* involved a contract between two parties that were both corporations in roughly the same business, which therefore presumably had relatively equal bargaining power and sophistication. *Id.* at 236.

139. See FARNSWORTH, *supra* note 92, § 12.13.

140. *Id.*

141. *Peevyhouse*, 382 P.2d at 114.

\$5,000 award seems just. It compensates the Peevyhouses for the way the coal company took advantage of them, without making unrealistic claims about the value of performance.

One might still object, however, that awarding damages for normative loss in this way would still be awarding expectation damages, but instead of measuring the expectancy by cost of completion or diminution of market value, we would be measuring it by the subjective value of the performance to the nonbreaching party. For example, while the Peevyhouses made clear that they wanted performance, a \$5,000 award on top of what they received for the coal itself might accurately capture their subjective value of the damage the mining inflicted on their family farm. Thus, such an award is not punitive, but rather awards expectation damages by another measure.

This is an objection I am prepared to embrace in part. Expectation damages, unlike reliance damages, do compensate for normative loss, as explained above.<sup>142</sup> The amount of normative loss is dictated by the circumstances and by the norms of contracting. When a promisee places a particularly high value on performance, she will suffer a correspondingly high normative loss through breach. But expectation damages should always be measured by the nonbreaching party's subjective value of performance. Fairness requires that damages be measured by an objective standard, such as the market value or a liquidated damages amount stipulated in the contract itself. A promisee is usually not entitled to claim damages for an amount above what the market dictates. But in some situations, such as when an unsophisticated promisee makes a heightened subjective value clear at the time of contracting, and a sophisticated promisor nonetheless breaches opportunistically, the promisee should be entitled to claim a higher value for the failed performance. In these rare cases, we may still call the higher damage award punitive because the exploitative wrongdoing of the breaching party justifies using a different measure for expectation damages. The problem is not a problem with the normal expectation damages remedy, but rather with the injustice of settling for that remedy in such egregious cases.

I have been arguing for the somewhat startling conclusion that a corrective-justice account of contract law would, properly conceived, sometimes call for punitive damages. As surprising as this conclusion may be, I have tried to show how slight its departure is from our common-law tradition. I have done so by arguing that although American contract law has strict liability and a *per se* rule against punitive damages for breach of contract, its normal measure of

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142. *See supra* Part III.



expectation damages is actually based on the idea of normative loss. Moreover, the punitive damages for which I argue would not be available in all cases, or even in all cases of willful breach, but rather only when a certain kind of normative harm is done. Still, while my appeal to Kantian norms to distinguish breaches that warrant punitive damages from normal willful ones does not run counter to Weinrib's views, others might object that my appeal is too far removed from our common-law traditions. In the next part, I shall answer this objection by examining the history of the tort of the bad-faith breach of contract. While the tort of bad-faith breach is now mostly out of favor in judicial decisions (unfortunately, in my view), its brief rise suggests that my arguments are not completely out of touch with the common law. A cause of action for bad-faith breach of contract is still recognized in insurance cases. The rationale behind recognizing the cause of action in those cases coheres with my arguments for punitive damages and justifies extending their application beyond the context of insurance.

## V. BAD-FAITH BREACH CASES

Although it is currently well established that contract law does not provide punitive damages,<sup>143</sup> most states now recognize the tort of bad-faith breach of contract in insurance cases and often award punitive damages in those cases.<sup>144</sup> In fact, for a short time, California extended the reach of the bad-faith breach of contract beyond insurance cases.<sup>145</sup> Only Montana followed California's lead,<sup>146</sup> and both states have since restricted the bad-faith breach of contract tort to insurance cases.<sup>147</sup> I now turn briefly to examining the reasoning behind those cases.

The bad-faith tort arose in the 1950s as a cause of action against insurance companies that refused to accept reasonable

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143. "Punitive damages are not recoverable for a breach of contract unless the conduct constituting the breach is also a tort for which punitive damages are recoverable." RESTATEMENT, *supra* note 127, § 355; "[P]enal damages may [not] be had except as specifically provided in this Act or by other rule of law." U.C.C. § 1-106(1) (1991); "Furthermore, a court will not ordinarily award damages that are described as 'punitive,' intended to punish the party in breach, or sometimes as 'exemplary,' intended to make an example of that party." FARNSWORTH, *supra* note 92, § 12.8. *But see* Randy L. Sassaman, Note, *Punitive Damages in Contract Actions—Are the Exceptions Swallowing the Rule?*, 20 WASHBURN L.J. 86 (1980) (arguing that courts are finding more and more ways to circumvent the rule against punitive damages in contract actions).

144. FARNSWORTH, *supra* note 92, § 12.8.

145. *Id.*

146. *Id.*

147. *Id.*

settlement offers in cases where a third party was suing an insured.<sup>148</sup> The tort is based on the covenant of good faith and fair dealing implicit in all contracts.<sup>149</sup> In the 1970s, the California Supreme Court extended the tort to first-party cases in which the insurer unreasonably denied liability to the insured.<sup>150</sup> While most states followed California and began to recognize such a tort in insurance cases, in 1984 the California Supreme Court went even further, suggesting in *Seaman's Direct Buying Service v. Standard Oil Company of California* that the bad-faith tort might be extended to noninsurance contexts so long as a similar "special relationship" was present.<sup>151</sup> Although the language in *Seaman's* was dicta, and the *Seaman's* court did not specify which relationships besides insurer/insured would be appropriately special, the California Court of Appeals soon applied it to the employment and banking contexts.<sup>152</sup> The bad-faith breach tort reached its apex in Montana with a few cases that allowed such causes of action even absent a special relationship.<sup>153</sup> In the 1990s, however, when no other states had joined California and Montana in recognizing the bad-faith tort outside the context of insurance, both states once again restricted the tort to insurance cases.<sup>154</sup>

Although no states currently recognize the bad-faith breach of contract tort outside of the insurance context, most continue to recognize it for insurance cases.<sup>155</sup> It is worth examining, then, what it is about the insurance cases that justifies exemplary damages for breach of contract. *Seaman's* provides a good starting point.

The *Seaman's* court made an important distinction between two kinds of bad-faith breaches. The first category is comprised of breaching parties who, without any legal justification, deny the very existence of the contract, thereby seeking to avoid *any* contract damages at all.<sup>156</sup> While the nonbreaching party may be reasonably expected to anticipate the possibility of a breach, she is still entitled to expect damages for that breach.<sup>157</sup> This latter expectation is vindicated in most insurance cases in which punitive damages are

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148. *Id.*

149. See RESTATEMENT, *supra* note 127, § 205; FARNSWORTH, *supra* note 92, § 7.17.

150. FARNSWORTH, *supra* note 92, § 7.17.

151. 686 P.2d 1158, 1166 (1984).

152. FARNSWORTH, *supra* note 92, § 12.8.

153. See *id.*

154. See *id.*

155. See *id.*

156. *Seaman's*, 686 P.2d at 1174.

157. *Id.*

awarded. Courts deal harshly with insurance companies that deny coverage without a good-faith justification in the mere hope that the insured will not have the will or the resources to take the insurance company to court.<sup>158</sup>

This first category covers most, if not all, cases in which courts have awarded punitive damages for bad-faith breaches even outside the insurance context. For example, in *Seaman's*, the dispute turned on whether the defendant's denial that the contract met the requirements of the statute of frauds was in good faith.<sup>159</sup> Similarly, in *Wallis v. Superior Court*, an often-cited employer/employee pension case discussed in more detail below, the court awarded punitive damages after the defendant told the plaintiff that the pension monies it had promised to pay him in exchange for his early retirement were "gratuitous payments" that were "not based on a legal obligation."<sup>160</sup> In *Commercial Cotton Co. v. United California Bank*, which represents "the high-water mark in the history of the bad-faith tort in California,"<sup>161</sup> the court awarded punitive damages against a bank that had refused to credit a customer's account, citing as its only defense a statute of limitations that its counsel knew, and later admitted it had known, to be inapplicable.<sup>162</sup> Even the Montana case of *Nicholson v. United Pacific Insurance Co.*,<sup>163</sup> in which the Montana Supreme Court extended the breach of the bad-faith tort still further, involved a bad-faith denial of liability on the part of the breaching party.<sup>164</sup> In *Nicholson*, the defendant had contracted with Nicholson for Nicholson to do construction work.<sup>165</sup> During the course of Nicholson's performance, the defendant began making unreasonable demands of Nicholson, accused him of material breach for not meeting those demands, and then claimed that it was not liable to Nicholson because of his breach.<sup>166</sup>

Although the cases in which courts have awarded punitive damages for the breach of the covenant of good faith have been instances in which the breaching party denied all liability whatsoever, the *Seaman's* court identified a second category of breaches that might

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158. FARNSWORTH, *supra* note 92, § 12.8.

159. *Id.* at 1167.

160. 207 Cal. Rptr. 123, 125 (1984).

161. Kerry L. Macintosh, *Gilmore Spoke Too Soon: Contract Rises from the Ashes of the Bad Faith Tort*, 27 LOY. L.A. L. REV. 483, 496 (1994).

162. 209 Cal. Rptr. 551, 553 (1985).

163. 710 P.2d 1342 (Mont. 1985).

164. *Id.* at 1348.

165. *Id.* at 1344.

166. *Id.*

warrant the award of punitive damages for bad faith.<sup>167</sup> In this second category, the breaching party is willing to pay expectation damages, but the damages do not seem to do justice:

This could happen, for example, if at the time of contracting, the parties expressly indicate their understanding that a breach would be impermissible. Or, it could happen if it were clear from the inception of the contract that contract damages would be unavailable or would be inadequate compensation for a breach.<sup>168</sup>

The *Peeveyhouse* case falls into this second category.<sup>169</sup> Although research reveals no cases in which the courts have found a bad-faith breach when the breaching party admits liability and is prepared to pay expectation damages, the reasons that justify awarding punitive damages for the first kind of bad-faith breach may also justify awarding them in cases in the second category.

One way to explore whether such reasons actually justify awarding punitive damages in cases in the second category is to examine what the California courts thought was important about the insurer/insured relationship when they were extending the tort to other relationships. In *Wallis v. Superior Court*, an employer/employee pension case, the court identified five characteristics that together would be sufficient to constitute a special relationship that might give rise to a bad-faith breach claim:

(1) The contract must be such that the parties are in inherently unequal bargaining positions; (2) the motivation for entering the contract must be a nonprofit motivation, i.e., to secure peace of mind, security, future protection; (3) ordinary contract damages are not adequate, because (a) they do not require the party in the superior position to account for its actions, and (b) they do not make the inferior party "whole"; (4) one party is especially vulnerable because of the type of harm it may suffer and of necessity places trust in the other party to perform; and (5) the other party is aware of this vulnerability.<sup>170</sup>

These five factors were repeated often in future cases involving bad-faith breach claims.<sup>171</sup> How well do they cohere with the understanding of contract law as a form of corrective justice under discussion here?

These five factors cohere with my view of corrective justice in contract law in three ways. First, the factors help to specify the content of the norms of private law, in particular the requirements of fairness. The concern for whether or not the parties occupy an unequal bargaining position, as well as the concern for the vulnerability of the nonbreaching party, is not new to contract law, as shown in the short

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167. *Seaman's Direct Buying Serv. v. Standard Oil Co.*, 686 P.2d 1158, 1174 (Cal. 1984).

168. *Id.*

169. See *supra* note 134 and accompanying text.

170. 207 Cal. Rptr. 123, 125-26 (1984).

171. Macintosh, *supra* note 161, at 495.

discussion of unconscionability in Part III. While American courts value freedom of contract and are reluctant to write terms into contracts or interfere because of inadequate consideration, they may intervene when the parties are of very unequal sophistication or bargaining positions, when a contract of adhesion is involved, or when there is a fiduciary relationship. On the other hand, when parties bargain at arms' length and both parties are capable of fending for themselves, courts are much less likely to intervene. Arguably, this disparate treatment satisfies basic notions of fairness.

For the same reasons, courts should treat willful breaches differently in some cases. Those who are not particularly vulnerable, who are in relatively equal bargaining positions, and who are contracting to make a profit can be better expected to anticipate what Holmes thought was obvious, i.e., that parties actually agree to perform *or* to pay damages. When their contracting partner breaches and pays only expectation damages, we do not sense the same normative loss that is so frustrating to our sense of fairness in the *Peevyhouse* case. The first, second, and fourth factors, then, are consonant with well-settled norms of contract law.

Second, the *Wallis* court's third characteristic helps to emphasize that awarding punitive damages to these plaintiffs would really be a form of corrective and not distributive (or retributive) justice. Earlier, we saw how, contrary to Fuller and Purdue, Weinrib and Benson treated expectation damages as truly compensatory and therefore corrective rather than distributive.<sup>172</sup> I have also argued that, given Weinrib's distinction between normative and factual loss, exemplary damages may be compensatory as well.<sup>173</sup> Characteristics (3)(a) and (3)(b) are reminiscent of Weinrib's distinction between normative and factual loss and lend themselves to the argument that exemplary damages in contract law can be compensatory. Characteristic (3)(b), which states that normal expectation damages would not make the plaintiff "whole," helps to ensure that the exemplary damages are not a form of distributive justice, but rather are still compensatory and corrective. These "punitive" damages are not essentially concerned with public policy and the manipulation of human behavior, but rather with the compensation of private parties for certain egregious wrongs done to them by other private parties. They are awarded only when the normal measure of damages is not sufficiently compensatory—or, to hijack language from Weinrib, when normative losses exceed factual losses such that normal damages will

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172. See *supra* Part III.

173. See *supra* Parts II & IV.

not properly compensate. Furthermore, characteristic (3)(a) reminds us that corrective justice is relational. The amount of compensation is determined not just by the (factual) loss suffered by the nonbreaching party, but also by the amount of normative gain by the breaching party (and the corresponding normative loss by the nonbreaching party).

Third and finally, characteristics (4) and (5) ensure that awarding punitive damages based on a bad-faith breach of contract really is at heart a *contractual* cause of action, and the norms that justify punitive damages are related to the Kantian norms already cited. I realize that here I am perhaps on thin ice. All of the cases that award punitive damages for breach of contract do so because they recognize a *tort* of bad-faith breach of contract. I suspect that this hesitancy is largely because of inertia: judges are in general conservative, and it may seem much less radical to recognize a new tort than to challenge a principle as entrenched as the rule that contract law does not allow for punitive damages. Even if this is true, the reasoning behind rules is more important than the labels themselves. And the reasoning in this case sounds in contract.

We have already seen how contract law has a special concern for unconscionable contracts. Vulnerability is often a factor in such considerations. For example, courts will not enforce modifications to a contract when a first party agrees to them under duress caused by the second party, especially where it appears that the second party has exploited that vulnerability.<sup>174</sup> But the insurance context suggests a further kind of vulnerability. Insurance companies are very often in an overwhelmingly superior bargaining position to those they insure, not only at the time of contracting, but especially at the time that a claim is filed. In addition to the normal advantages that insurance companies often enjoy due to their size and sophistication, they can also be in a superior position because once an accident has occurred, it is too late for an insured person to bargain for different coverage.<sup>175</sup> Purchasing insurance creates a level of dependence and vulnerability not present in typical contract cases.

What is not mentioned in the typical bad-faith breach tort case is how parties can be made more vulnerable by the act of contracting even outside the insurance context. Weinrib has stated that while both tort and contract are private law, they are distinct in that the rights and duties in contract law are undertaken voluntarily, while those in

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174. FARNSWORTH, *supra* note 92, §§ 4.21-22.

175. *Id.* at 503.

tort generally are not.<sup>176</sup> I have suggested that one of the bases for the kind of normative loss that could justify an award of exemplary damages is a violation of Kant's categorical imperative that we treat people only as ends and never as means. According to Kant, the capacity of the will to choose freely is what makes us human and is the source of normativity. When a promisor by contracting places someone in a particularly vulnerable position and then knowingly and willfully takes advantage of that vulnerability, he not only treats that person as an object by failing to respect her moral status as an agent with free will, but he also uses that very status as a means to an end. It is one thing to willfully breach a contract and pay damages when the other party should reasonably expect the possibility and be prepared to deal with it. But when the promisee makes clear at the time of contracting that damages would never do, when she only enters into the contract when reassured of actual performance by the promisor, and when it is also clear that the promisee makes herself particularly vulnerable by entering into the contract, it is incumbent on the promisor to actually perform if at all possible. The failure to do so might warrant punitive damages in some cases as a means of compensating the promisee for the normative loss she incurs by being exploited.

Thus, while punitive damages for bad-faith breaches are now only awarded in insurance cases, and while they have never been awarded in the second kind of cases that the *Seaman's* court imagined, the justification for awarding such damages in the insurance context supports their extension to other cases. That justification coheres well with the norms of contract law and with the goals of corrective justice.

## VI. CONCLUSION

It has been nearly thirty years since Grant Gilmore and P.S. Atiyah could confidently claim that contract was dead, subsumed by tort. Since that time it has become evident that contract law is not dead or even dying. But its status as private law is indeed in doubt—as is, ironically, tort law's status.<sup>177</sup> Before we give up on the laws of tort and contract, however, and completely surrender all of private law to economics and public policy, we would do well to try to make sense of private law on its own terms and to elucidate a coherent,

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176. See WEINRIB, *supra* note 2, at 136.

177. See, e.g., John C. P. Goldberg, *Unloved: Tort in the Modern Legal Academy*, 55 VAND. L. REV. 1501 (2002).

comprehensive private law of tort and contract. Corrective-justice theories may be the key to this enterprise.

Weinrib has gone a long way toward providing such a theory of tort law, and in so doing has at least laid the groundwork for a similar theory of contract. His theory may be the best corrective-justice theory now available; at the very least, any other theory will have to take his views into account. But his view comes at a price. We must be willing to accept a Kantian theory of morality, in particular of the morality of transactions. We shall also have to be able to make sense of his distinction between normative and factual losses—a controversial distinction that this Note has assumed, for the sake of argument, is intelligible. Finally, we shall have to do more than Weinrib himself admits: we must be prepared to award punitive damages in particularly egregious tort cases and even particularly egregious bad-faith breach of contract cases. To refuse to do so in tort cases is to return to Coleman's annulment thesis, or at least to stop well short of Weinrib's persuasive "fully relational" view. Refusing to do so in contract cases not only stops short of a fully relational view, it also undermines the reasoning that explains how expectation damages are compensatory and corrective rather than distributive.

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