

IMPLIED WARRANTY, PRODUCTS LIABILITY, AND THE BOUNDARY BETWEEN CONTRACT AND TORT

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An unusual type of products liability case raises the issue of whether an injured consumer can recover for breach of an implied warranty of merchantability under the Uniform Commercial Code when the product that causes the injury is not defective under the tort rules governing products liability. Only a small number of cases fit this pattern, because in the overwhelming majority of cases a product that is unmerchantable—that is, not fit for the ordinary purposes for which it is used—will also be “in a defective condition unreasonably dangerous,” to use the widely followed language of section 402A of the *Restatement (Second) of Torts*. Nevertheless, this type of case illuminates the nature of liability in implied warranty and in products liability, the relationship between the two, the broader relationship between contract law and tort law, the wisdom of portions of the proposed *Restatement (Third) of Torts: Products Liability*¹ and of the proposed revision of Article 2 of the Uniform Commercial Code, and the current politics of the legal process.

I. LIABILITY IN IMPLIED WARRANTY AND IN PRODUCTS LIABILITY

Although the law of products liability is hardly uniform across the country, a fair generalization is that strict liability in tort has triumphed over breach of implied warranty in contract as the preferred cause of action in products liability cases.² In some cases, however, the strict liability action fails because the product is not unreasonably dangerous under the applicable tort rule. The victims in these cases may still seek a contract-based remedy when the tort remedy fails, basing their actions on breach of an implied warranty of merchantability. Courts and scholars have divided on whether the implied warranty action should be available to the victim. One camp asserts

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1. See *RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY* (Tentative Draft No. 2, Mar. 13, 1995).

2. See Marshall S. Shapo, *In Search of the Law of Products Liability: The ALI Restatement Project*, 48 *VAND. L. REV.* 631, 647-49 (1995).

that the warranty action has a residual role when the tort action is unavailable. This position (“residual liability”) is taken by the New York Court of Appeals in *Denny v. Ford Motor Co.*³ and by the Drafting Committee of the Revised Article 2 of the Code.⁴ The other camp argues that the strict liability tort action has developed to such a degree that it is now exclusive of the warranty action. This view (“exclusive liability”) is proposed by Judge Simons, dissenting in *Denny*, and the drafters of the proposed *Restatement (Third) of Torts: Products Liability*.⁵

The approach taken in *Denny v. Ford Motor Co.*⁶ illustrates the residual liability position. Nancy Denny was severely injured when the Ford Bronco II that she was driving rolled over as she slammed on her brakes to avoid a deer. Denny’s evidence at trial demonstrated that “sport utility vehicles in general, and the Bronco II in particular,” are more prone to rollover accidents than ordinary passenger cars.⁷ Ford responded that the features that increased the risk of rollover, such as a narrow track width and high center of gravity, were necessary to the vehicle’s off-road capabilities. The jury found that the Bronco was not “defective” such that Ford was not liable on Denny’s strict products liability claim, but the jury did find that Ford was liable for breach of an implied warranty.⁸

On appeal, the U.S. Court of Appeals for the Second Circuit certified three questions to the New York Court of Appeals:

(1) whether the strict products liability claim and the breach of implied warranty claim are identical; (2) whether, if the claims are different, the strict products liability claim is broader than the implied warranty claim and encompasses the latter; and (3) whether, if the claims are different and a strict liability claim may fail while an implied warranty claim succeeds, the jury’s finding of no product defect is reconcilable

3. 662 N.E.2d 730 (N.Y. 1995).

4. Draft, Uniform Commercial Code Article 2—Sales (199_) § 2-319 n.3 (Nat’l Conference of Comm’rs on Unif. State Laws, July 12-19, 1996) [hereinafter July 1996 Annual Meeting Draft, Art. 2], available at <<http://www.law.upenn.edu/library/ulc/ulc.htm>> (visited on Jan. 10, 1997); see also *infra* note 31.

5. *Denny*, 662 N.E.2d at 739 (Simons, J., dissenting); RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 2(b) (Tentative Draft No. 2, Mar. 13, 1995); see also *Larsen v. Pacemaker Sys., Inc.*, 837 P.2d 1273 (Haw. 1992) (allowing recovery for breach of warranty of merchantability but not for strict liability).

6. *Denny*, 662 N.E.2d at 730-33.

7. *Id.* at 732.

8. *Id.* at 732-33.

with its finding of a breach of warranty.⁹

Ford argued that the strict liability and warranty claims were identical, and therefore, the jury's verdict was internally inconsistent. As products liability law has developed, Ford asserted, the tort action has supplanted the contract-based action for breach of implied warranty.¹⁰

Favoring a residual role for implied warranty, the New York Court of Appeals held that the products liability and warranty actions are not the same.¹¹ To hold otherwise would "overlook[] the continued existence of a separate *statutory* predicate for the breach of warranty theory and the subtle but important distinction between [products liability and breach of warranty] theories that arises from their different historical and doctrinal root."¹² The warranty claim can survive even if the strict liability claim fails, so the jury's finding that the Bronco was not defective but was unmerchantable could be upheld. The establishment of a tort remedy for personal injuries caused by defective products diminished the need to use the breach of implied warranty theory, but the tort action did not completely subsume the warranty action.¹³ Warranty actions originate in contract law, with its emphasis on disappointed expectations, while strict liability originates in tort law, which is concerned with "social policy and risk allocation by means other than those dictated by the marketplace."¹⁴ The difference is reflected in the different concepts of defect in each action: in strict liability, a negligence-oriented balancing test asks whether the risks created by the product outweigh its utility, and in warranty, the test asks whether the product is "fit for the ordinary purposes for which such goods are used."¹⁵ The difference is preserved by the continued existence of a statutory remedy in the Uniform Commercial Code that, in the absence of specific legislative revision,¹⁶ requires that the courts continue to allow breach of warranty claims.

The facts in *Denny* show how the two theories of liability can diverge. The jury found that the Bronco II was not defective; the features that made it prone to roll over were necessary to its performance as an off-road vehicle

9. *Id.* at 733.

10. *Id.*

11. *Id.* at 734.

12. *Id.* at 733.

13. *Id.* at 734.

14. *Id.* at 736.

15. U.C.C. § 2-314(2)(c) (1995).

16. The court cited statutes in a number of other jurisdictions that specifically preempted residual implied warranty claims. *Denny*, 662 N.E.2d at 736-37.

and the risk of rollover did not outweigh its utility for off-road use.¹⁷ However, the “ordinary purpose” for which the Bronco was used was everyday driving on paved roads. Because the Bronco was prone to rollover accidents under ordinary conditions, it was not fit for its ordinary purpose, thus breaching the implied warranty of merchantability.¹⁸

The drafting committee for Revised Article 2 of the Uniform Commercial Code—but not, so far, the National Conference of Commissioners on Uniform State Laws—concur with the result reached by the Court of Appeals.¹⁹ In the draft of Revised Article 2 prepared for the July 1996 meeting of the Conference, the Reporter, Professor Richard Speidel, and the drafting committee, proposed to clarify implied warranty’s residual role.²⁰ The drafters rejected making tort liability the exclusive remedy for product injuries because of the lack of uniformity in products liability law among the states, including states that make implied warranty the primary means of imposing liability.²¹ Their solution was stated in proposed section 2-319(b): “This [article] applies to a claim for injury to person or property resulting from any breach of warranty to the extent that the goods are not defective under other applicable law.”²²

Proposed section 2-319(b) would codify the result in *Denny*. The drafters suggested that “the relevant factors defining merchantability in section 2-413(b) are broader than those defining defect in tort.”²³ Accordingly, a victim who has a strict tort liability claim may not also assert a breach of implied warranty claim, but a victim who is injured by a product that is not, in tort terms, defective, may still argue that the product is unmerchantable.²⁴

17. *Id.* at 732-33

18. *Id.* at 732-33, 738.

19. The *Denny* problem is one of many consumer protection issues that are being debated during the redrafting of the Code. See generally Jean Braucher, *Politics and Principle in the Drafting of UCC Consumer Protection Provisions*, 29 UCC L.J. 68 (1996).

20. July 1996 Annual Meeting Draft, Art. 2, *supra* note 4, § 2-319.

21. *Id.* § 2-319 n.3.

22. *Id.* § 2-319(b). Other parts of section 2-319 limit the definitions of “person” and “property” for purposes of the section and state rules for the application of the distinctive features of warranty law to personal injury and property damage cases. See *id.* § 2-319(a).

23. *Id.* § 2-319 n.3. The proposed revision makes a slight change in the relevant section 2-314 standard: “be fit for the ordinary purposes for which [such] goods of that description are used.” *Id.* § 2-314(b)(3) (currently U.C.C. § 2-314(2)(c) (1995)).

24. At the July 1996 meeting of the National Conference of Commissioners on Uniform State Laws, this proposed section was withdrawn by the drafting committee for reconsideration because of opposition to it from several quarters. Interview with Professor Amelia H. Boss, Member of Drafting Committee, NCCUSL (July 25, 1996).

Arguing that a strict liability action excludes a warranty claim, Judge Simons dissented in *Denny*. He argued that the risk/utility test of products liability was broader than the expectation-based standard of warranty law, and thus should exclude the application of that standard in a personal injury action. Products liability arose from the interaction of contract and tort law but now stands independently:

The law imposing liability without fault against those making and marketing consumer products evolved in stages, progressing from negligence to implied warranty and eventually to the adoption in New York of a new cause of action known as strict products liability. . . .

. . . .

This new cause of action was not separate from implied warranty but an amalgam which had been constructed by the courts to establish a cause of action for liability without fault by merging warranty concepts (to avoid fault analysis) with negligence concepts (to avoid privity). The new cause of action recognized products liability as a discrete area of tort law, which borrows from both negligence and warranty, and attempts to avoid the confusion spawned by trying to categorize the various claims and remedies under prior law. It imposes strict liability as a matter of social policy predicated on the idea that defendants ought "to pay for the costs attributable to damaging events caused by defects of a kind that made the product more dangerous than it would otherwise be"²⁵

Moreover, the reference to consumer expectations inherent in implied warranty has been generally rejected in products liability law. Consumer expectations are part of the sales law, in which a seller agrees to indemnify a buyer if the goods do not measure up to the bargain. In the realm of personal injury and strict products liability, however, the concern for product safety dictates a balancing of a product's risks and benefits under the risk/utility test.

The drafters of the proposed *Restatement (Third) of Torts: Products Liability* take an even more extreme view than Judge Simons. Section 2(b) of the proposed *Restatement* substantially narrows the test for design defect:

a product is defective in design when the foreseeable risks of harm

25. *Denny v. Ford Motor Co.*, 662 N.E.2d 730, 740-41 (Simons, J., dissenting) (citations omitted).

posed by the product could have been reduced or avoided by the adoption of a reasonable alternative design by the seller or other distributor, or a predecessor in the commercial chain of distribution, and the omission of the alternative design renders the product not reasonably safe²⁶

Although section 2 of the proposed *Restatement* and the process by which it has been drafted and considered have been enormously controversial, the American Law Institute gave tentative approval to the section at its 1995 Annual Meeting.²⁷

The standard in section 2 is a version of the risk/utility test that is equivalent to negligence liability.²⁸ It requires that the plaintiff prove that a reasonable alternative design that would have prevented the injury was available to the manufacturer at the time the product was made. It explicitly rejects the consumer expectations test that some courts have used as an alternative to risk/utility analysis. Instead, it consigns consumer expectations—and, implicitly, the broader concept of product representation—to one element of a list of “[a] broad range of factors [that] may legitimately be considered in determining whether an alternative design is reasonable and whether its omission renders a product not reasonably safe.”²⁹ Accordingly, section 2 diminishes the effect of the representational concepts of manufacturer liability in products liability actions.

The proposed *Restatement* makes the standard for liability for a defectively designed product under section 2 exclusive of all other liability rules. Whether the action is brought in strict liability, negligence, or implied warranty of merchantability, the “reasonable alternative design” standard of section 2 controls.³⁰ Section 2 effectively eliminates breach of implied warranty as a residual cause of action in personal injury cases. The belief

26. RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 2(b) (Tentative Draft No. 2, Mar. 13, 1995).

27. *Continuation of Discussion of Restatement of the Law Third, Torts: Products Liability*, 72 A.L.I. PROC. 201, 230 (1995). For discussion of the proposed *Restatement*, see *A Symposium on the ALI's Proposed Restatement (Third) of Torts: Products Liability*, 61 TENN. L. REV. 1043 (1994); and Symposium, *The Revision of Section 402A of the Restatement (Second) of Torts: Occasion for Reform of Product Liability Law?*, 10 TOURO L. REV. 1 (1993).

28. RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 2 cmts. a, c (Tentative Draft No. 2, 1995).

29. *Id.* § 2 cmt. e.

30. *Id.* § 2 cmt. m & rptr.'s note. Professor Gray describes this as “a proposition of breathtaking audacity.” Oscar S. Gray, *The Draft ALI Product Liability Proposals: Progress or Anachronism?*, 61 TENN. L. REV. 1105, 1111 (1994) (discussing comment j).

underlying exclusive liability is that "it is monstrous for the law to be talking out of both sides of its mouth," by permitting representational liability under warranty while prohibiting it on the same facts in products liability as ALI Director Geoffrey Hazard commented.³¹ However, because the ALI has not considered revised Article 2, section 2-319 and Professor Speidel's response to Hazard—"We are not talking out of both sides of the mouth if you have a vibrant theory of contract that protects expectations, as opposed to a tort theory that focuses on other factors"³²—are still open for consideration.

II. THE BROADER RELATIONSHIP BETWEEN CONTRACT LAW AND TORT LAW

One of the most interesting things about the scholarly and judicial attempts to deal with the relationship between implied warranty theory and products liability is the recognition that the appropriate solution depends on more than a strong doctrinal or policy argument about the particular issue. Everyone who deals with the problem understands that it implicates the broader relationship between contract law and tort law. By focusing on that broader issue, I will suggest why different people reach different conclusions on the narrower issue, how the narrower issue ought to be resolved, and what is at stake in the controversy.

The proponents of the different positions start from a shared vision of the doctrinal structure of contract and tort law. Contract and tort are different in their objectives and their subject matter. Contract law is concerned with relations that are created primarily by affirmative promissory acts that plan for the future conduct of the contracting parties. Tort law, on the other hand, seeks to remedy wrongful violations of established interests that are not created by agreement, particularly interests that concern the physical integrity of person or property. Accordingly, as the *Denny* majority stated, "contract law . . . directs its attention to the purchaser's disappointed expectations; . . . tort law . . . traditionally has concerned itself with social policy and risk allocation by means other than those dictated by the marketplace."³³ Contract law focuses on reasonable expectations and reasonable reliance raised by a promise (on the plaintiff's side) and on the social value of honoring one's

31. *Report on the Uniform Commercial Code, Revised Article 2*, 72 A.L.I. PROC. 419, 430 (1995) [hereinafter *U.C.C. Report*].

32. *Id.*

33. *Denny v. Ford Motor Co.*, 662 N.E.2d 730, 736 (N.Y. 1995).

obligations (on the defendant's side). Conversely, tort law is concerned with compensating for harm (on the plaintiff's side) caused by the wrongful act of another (on the defendant's side). Contract protects the plaintiff's expectation and reliance interests to promote initiative and to provide security in commercial activity. Tort is concerned with accident avoidance and efficient and appropriate allocation of risk.

This doctrinal structure is so familiar that it hardly needs explanation. Simply stating its basic elements evokes the structure that lawyers internalize from their first semester in law school and implement in virtually every contract and tort case. At the same time, it has become widely recognized that the doctrinal structure is limited or deficient in certain respects.³⁴ Neither the criteria that we use to separate contract cases from tort cases nor the policies and values implemented in each area are as starkly different as the initial description suggests. *Denny* illustrates the underlying problem. Nancy Denny arguably was injured in two respects: by Ford's disappointment of her expectations about the performance of her Bronco, and by Ford's creation of an unreasonable risk of harm to her. Thus, the facts that trigger both contract and tort inquiry are present, and the policies of both contract and tort law are at least potentially involved. Simply put, contract and tort overlap, and cases such as *Denny* lie in the area covered by both.

Consider how the different positions on the availability of implied warranty actions in personal injury cases deal with the overlap of contract and tort. Both the advocates of residual liability and the advocates of exclusive liability recognize the overlap and sharpen the differences between the two subjects, but they do so in very different ways.

Advocates of residual liability embrace the overlap when they allow the application of either contract law or tort law to a case. The policies of tort law—notably deterrence, compensation, fairness, and loss-spreading—permit the application of strict liability, but they do not bar the application of the policies of contract law, particularly the protection of legitimate expectations, in an appropriate case.

There is nothing about contract law generally which says we shouldn't have personal injury liability.³⁵

34. See generally Jay M. Feinman, *The Jurisprudence of Classification*, 41 STAN. L. REV. 661 (1989).

35. Commissioner Marion W. Benfield, 1995 NAT'L CONF. COMM'RS ON UNIF. STATE LAWS PROC. 477.

[T]he beauty of [section] 402A and the 1990 text of the Uniform Commercial Code is that, if you had goods that caused damage to person or property, it might either be tort or warranty or both. There was no preemption. Plaintiffs had a choice to pick one or the other or both, and there was no attempt to dictate by warranty that it can't be tort or vice versa.³⁶

Advocates of exclusive liability also emphasize the differences between contract and tort, but to a different purpose. Although the two subjects overlap, each subject has a primary sphere of application within which its policies govern to the exclusion of the other. The essential facts of a case determine whether it falls within the primary sphere of application of contract law or tort law. If the case involves a bargain transaction between two parties, it is a matter for contract law. If it involves an accidental injury to person or property, it falls to tort law.

[I]t seems to me that the correct way to approach [the issue] is to say what should be the terms of liability for personal injury, the premise being that that's a different kind of injury than an economic or commercial injury.³⁷

There is another way of dealing with the overlap of contract and tort. Instead of thinking of these cases as instances of the broad categories of contract or tort, we might construct a narrower, separate area. This is, of course, what has been done over the past fifty years in the creation of products liability. As Judge Simons noted in *Denny*, the law of products liability is an "amalgam" of contract and tort concepts, in which elements are drawn from each area and transformed into something new and more appropriate for the particular kinds of cases at issue.³⁸ This is the theory behind the current *Restatement* project, that products liability merits treatment as the first, and for perhaps the foreseeable future, the only portion of tort law that requires a new restatement.

As a general matter, I believe that reconstructing traditional doctrinal structures is long overdue, especially in the area covered by the common-law trivium of contracts, torts, and property. This move is related to a relational

36. *U.C.C. Report*, *supra* note 31, at 426-27 (quoting Professor Richard E. Speidel).

37. *Id.* at 428 (quoting Director Geoffrey C. Hazard, Jr.). For the same position on a different doctrinal issue, see William Powers, Jr., *Border Wars*, 72 TEX. L. REV. 1209 (1994).

38. *Denny*, 662 N.E.2d at 741.

approach to legal analysis. In deciding any case, we ought to begin by focusing on the relationships in the factual setting that gives rise to the case, recognizing that the relationships often will be more complex than is acknowledged by the traditional categories. Focusing on those relationships often leads us to see the advantage of constructing new categories, such as "products liability" or "economic negligence."³⁹

Recasting the doctrinal structure can be a major improvement, but it does not necessarily solve the particular doctrinal problem. In creating a new area out of existing ones, we must take pains to ensure that the relevant elements of the underlying relationships, which may have been expressed in the previous categories, are not lost in the reconstruction. Also, constructing the categories is not simply a matter of projecting from the facts and relationships; there are choices to be made in the process, and the choices depend on one's values and orientation to the issues involved.

In the overlap between implied warranty and products liability, Judge Simons and the drafters of the proposed *Restatement* have appropriately focused on the category of "products liability" as relatively independent of its roots in contract and tort. Beyond that first step, however, I believe that they have gotten it very wrong. This is particularly true of the *Restatement* drafters, who link exclusive liability in tort with a new formulation of the rules of product liability that shift us from strict liability to negligence, and a narrow form of negligence at that. They have lost sight of some of the important roots of products liability, because they have followed their own values, values that are inconsistent with the bulk of the law and its spirit. In the discussion that follows, therefore, I focus on the problems with the proposed *Restatement* draft because they are more extreme than those in Judge Simons's dissent.

First, the advocates of exclusive liability who authored the proposed *Restatement* slight the representational concerns that have been an essential element of products liability. Under section 2(b), for example, "consumer expectations do not constitute an independent standard for judging the defectiveness of product designs."⁴⁰ Instead, they are only one of the factors that go to "the necessity for, or the adequacy of, a proposed alternative

39. See JAY M. FEINMAN, *ECONOMIC NEGLIGENCE: LIABILITY OF PROFESSIONALS AND BUSINESSES TO THIRD PARTIES FOR ECONOMIC LOSS* 177-208 (1995); Feinman, *supra* note 34, at 712-16.

40. *RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY* § 2 cmt. f (Tentative Draft No.2, Mar. 13, 1995).

design."⁴¹ The consumer expectations test for product defect has been controversial, mostly when it has served as an exclusive rather than a partial test for liability, but it still figures in the law in many states.⁴²

More broadly, the focus on risk/utility as the exclusive measure of unreasonable danger, and particularly the requirement of a reasonable alternative design,⁴³ pay insufficient attention to the representational basis of products liability. "[T]he portrayal of the product which is made, caused to be made or permitted by the seller"⁴⁴ is crucial to the evaluation of the product. A Bronco II is unreasonably dangerous not only because it is prone to rollover accidents in ordinary driving, but because it is prone to those accidents and it is represented by the manufacturer and its dealers and understood by the public to be suitable for ordinary driving, in which excessive rollovers are not to be expected.

Second, the *Restatement* has abandoned the roots of product liability in protecting consumers from harm by imposing strict liability rather than negligence. As Professor Shapo noted, "[T]he Reporters have severed the black letter of products liability from its moorings, most centrally 30 years of judicial development under § 402A, and . . . perhaps they have even unmoored it from the general body of tort law and even from relevant contract law."⁴⁵

Since 1960, products liability has exploded, and the explosion has been based on what Professor Carl Bogus called "Cardozo's Paradigm," after the

41. *Id.*

42. See Howard Klemme, *Comments to the Reporters and Selected Members of the Consultative Group*, *Restatement of Torts (Third): Products Liability*, 61 TENN. L. REV. 1173 (1994); see also e.g., *Soule v. General Motors Corp.*, 882 P.2d 298 (Cal. 1994); *Camacho v. Honda Motor Corp.*, 741 P.2d 1240 (Colo. 1987).

43. RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 2 cmt. c (Tentative Draft No.2, Mar. 13, 1995).

44. Marshall S. Shapo, *A Representational Theory of Consumer Protection: Doctrine, Function and Legal Liability for Product Disappointment*, 60 VA. L. REV. 1109, 1370 (1974) (in statement of the thesis).

45. *Discussion of Restatement of the Law Third, Torts: Products Liability*, 72 A.L.I. PROC. 179, 182 (1995); see also Joseph W. Little, *The Place of Consumer Expectations in Product Strict Liability Actions for Defectively Designed Products*, 61 TENN. L. REV. 1189, 1194 (1994) ("Gone is the notion that where a product is determined by law to be unreasonably dangerous (or 'not reasonably safe') for users, consumers, and bystanders, a seller places such a product in the market *at the seller's peril*, notwithstanding the inability of plaintiffs to prove a better design or more effective warning."). See generally Jerry J. Phillips, *Achilles' Heel*, 61 TENN. L. REV. 1265 (1994); Frank J. Vandall, *The Restatement (Third) of Torts: Products Liability Section 2(b): The Reasonable Alternative Design Requirement*, 61 TENN. L. REV. 1407 (1994).

author of *Macpherson v. Buick Motor Co.*⁴⁶

The concern is not so much whether the product had a flaw, irregularity, or other shortcoming that caused it to perform differently than the purchaser expected as it is with the consequences of the product. The focus is wider. It is not restricted to the bipolar relationship between seller and purchaser. A product may be unreasonably dangerous because it places others—nonpurchasers and even nonusers—at risk. The analysis encompasses all of the social benefits and costs which result from the product. . . .

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Those who subscribe to Cardozo's Paradigm focus on societal rather than individual consequences. For them, products liability primarily serves as a deterrent to distributing unsafe products.⁴⁷

Limiting the test for defective products to risk/utility, particularly the narrow version of risk/utility in the proposed *Restatement*, rejects this history by substituting a restricted version of the negligence test that the courts have consistently rejected.⁴⁸ As Professor Shapo explains:

[A]nother idea supporting the development of Section 402A inheres in the supposition that the traditional negligence rules of proof create hurdles that are too high for many plaintiffs with meritorious cases. The [*Restatement*] Draft accepts this point concerning manufacturing defect cases. With its requirement that plaintiffs show a reasonable alternative design, it implicitly rejects it in design cases. . . .

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In general, the Draft at least implicitly raises the question of whether Section 402A is too generous in its commitment to consumer protection. It seems to imply that this is so, and that consumers are

46. Carl T. Bogus, *War on the Common Law: The Struggle at the Center of Products Liability*, 60 MO. L. REV. 1, 15 & n.54 (1995) (discussing the paradigm from *Macpherson v. Buick Motor Co.*, 111 N.E. 1050 (N.Y. 1916)).

47. *Id.* at 15-16 (footnotes omitted).

48. See RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY § 1 cmt. a (Tentative Draft No. 2, Mar. 13, 1995) ("Subsections (b) and (c) of § 2 rely on a reasonableness test traditionally used in determining whether an actor has been negligent.").

better able to take care of themselves than the Institute believed when it adopted Section 402A.⁴⁹

I conclude, therefore, that as a conceptual matter the most desirable path would be to reformulate the structure of legal doctrine to continue to focus on products liability. But the new structure must take adequate account of the traditional objectives of the area (prominently including protection against unsafe products) and of its basic principles (recognizing the significance of product representation). This solution would require rejecting the proposed *Restatement* draft. Although that war has not yet been lost, it is at best difficult to win the battle on the floor of the ALI at this stage of the game. Whether the courts will follow suit is another matter; in my judgment, the courts ought to reject the new *Restatement* if it is adopted as proposed. The next-best solution, I believe, would be either to adopt the proposed section 2-319 of the Uniform Commercial Code, which preserves the representation emphasis of products liability within contract rather than in a separate subject, or to reach the same result without a specific statutory mandate, as in *Denny v. Ford Motor Co.*

III. THE CONTRACT-TORT OVERLAP IN OTHER AREAS

Taken on its own terms, the *Denny* problem is relatively limited, arising in a small number of cases. Looked at more broadly, it illustrates approaches to the overlap of contract and tort. In recent years, the overlap problem has been addressed in a number of other areas as well, in ways that are related to the approaches to the *Denny* problem. I will mention three such areas: so-called "tort reform," product-related economic loss, and breach of contract as a tort.

The first example, tort reform, has been one of the most controversial issues in private law during recent years, as advocates for business and insurance interests have pressed for numerous cutbacks in the tort liability system. For example, Peter Huber of the Manhattan Institute has written prolifically about the problems of tort law and the need for change.⁵⁰ The problem, according to Huber, is that scholars and judges have expanded tort law to encroach upon the sphere of private transactions properly governed by contract.⁵¹ The solution is to permit and encourage "neocontracts" by which

49. Shapo, *supra* note 2, at 689-90 (footnote omitted).

50. See, e.g., PETER W. HUBER, *LIABILITY: THE LEGAL REVOLUTION AND ITS CONSEQUENCES* (1988).

51. *Id.* at 5-8.

private agreements will replace tort liability.⁵²

Huber begins with the familiar distinction between tort and contract. “Tort law is the law of accidents and personal injury”⁵³ of which a car accident between strangers is the most common example. But injuries between strangers are relatively rare; “most unintended injuries occur in the context of commercial acquaintance.”⁵⁴ In commercial relationships in which the parties can bargain in advance, the law traditionally encouraged agreements that dealt with potential risks. “Most accidents were handled under the broad heading of *contract*—the realm of human cooperation—and comparatively few relegated to the dismal annex of tort, the realm of unchosen relationship and collision.”⁵⁵ The allocation of cases reflected fundamental and desirable differences between the areas of law.

Contract, the mirror image of tort, is the law of cooperation Contract is the right that supports all others, most especially in a modern technological society with highly specialized production. It is through voluntary agreement that we control our own bodies . . . control our social universe . . . and control our spiritual destiny In a well-ordered world, the mutual benefits that are possible through cooperation would favor it unconditionally.

Tort law, however, sharpens every possible difference or suspicion Tort law magnifies conflict to the point where it swamps the benefits of cooperation.⁵⁶

The desirable distinction between contract and tort law was lost as the founders of modern liability law—“the likes of” Prosser, Wade, and Traynor—shifted attention to the problem of allocating and minimizing the costs of accidents and providing victims with compensation through tort law.⁵⁷ The result has been a transformation of the law that imposes both a massive tax on consumers through mandatory tort liability that cannot be bargained away through contract and a concomitant loss of individual freedom.

The solution to this social problem is to reinstate contract to its position as

52. *See id.* at 194-96.

53. *Id.* at 5.

54. *Id.*

55. *Id.*

56. *Id.* at 189.

57. *Id.* at 6-7.

the paramount private law subject. "The guiding principle must be to promote consent and agreement wherever possible—to prefer contract over tort whenever the choice may be presented—and to elevate [contractual] direct insurance over liability-driven compensation."⁵⁸ Parties could contract in advance for the level of care and compensation that they desired. An airline and its passengers, for example, could include in each ticket a binding insurance contract that would replace the passengers' actions against the airline in case of a crash.⁵⁹ "In the end, compensation clothed in the working garb of contract is far more beautiful than tort dressed up in China silks, cashmere shawls, and Golconda diamonds, because the attire of contract is affordable, earned, and paid for, not just seized from others by the compulsion of misguided law."⁶⁰

The second example of the overlap of contract and tort law is product-related economic loss. It is the reverse of the *Denny* situation, and is presented in cases in which a buyer of goods suffers purely economic loss but seeks a remedy in tort law, particularly products liability, rather than contract warranty law.⁶¹ The prevailing view in cases of this type bars the use of the tort action even when the contract action is unavailable. The leading cases in this area are *Seely v. White Motor Co.*⁶² and *East River Steamship Corp. v. Transamerica Delaval Inc.*⁶³

In *Seely*, the commercial purchaser of a truck discovered that the truck bounced violently. The dealer was unable to correct the problem, even with guidance from the manufacturer's representative. The court allowed the purchaser to recover from the manufacturer the portion of the purchase price he had paid as damages for breach of express warranty and lost profits as consequential damages.⁶⁴ This decision was an early step in surmounting the privity barrier for remote purchasers in actions against manufacturers, particularly because the court did not require proof of reliance on the warranty.⁶⁵ However, in the more widely cited portion of the opinion, the

58. *Id.* at 193.

59. *Id.* at 194.

60. *Id.* at 225-26.

61. See FEINMAN, *supra* note 39, at 495-554.

62. 403 P.2d 145 (Cal. 1965) (en banc).

63. 476 U.S. 858 (1986).

64. *Seely*, 403 P.2d at 147-48.

65. Indeed, the purchaser did not know that the warranty came from White rather than the dealer. *Id.* at 144-48.

court refused to allow a claim stated in strict liability.⁶⁶ The primary basis of the California court's rejection of strict liability was a distinction between the body of law governing personal injury claims and the law governing economic loss.

[T]he law of sales has been carefully articulated to govern the economic relations between suppliers and consumers of goods. The history of the doctrine of strict liability in tort indicates that it was designed, not to undermine the warranty provisions of the sales act or of the Uniform Commercial Code but, rather, to govern the distinct problem of physical injuries.⁶⁷

The manufacturer in *Seely* was liable because its express warranty determined the quality of the product that it was obligated to deliver. If it were strictly liable, however, it might be liable for losses due to uses of the truck that it could not anticipate. Only where the parties have agreed as to the buyer's economic expectations is a manufacturer liable for disappointing those expectations. The expectation of safety from physical injury caused by the product, on the other hand, is one that a consumer is entitled to have even in the absence of agreement. The court distinguished between personal injury, the calamitous consequences of which strict tort liability is designed to prevent, and economic loss, which is governed by the law of contract.⁶⁸

The United States Supreme Court adopted and extended the principles of *Seely* in *East River Steamship Corp. v. Transamerica Delaval Inc.*, an admiralty case.⁶⁹ In *East River*, the charterers of several ships (who were affiliated companies of the owners and other contracting parties) brought an action against Transamerica Delaval, which had defectively manufactured and installed the turbines in the ships.⁷⁰ Like the previous courts, the Supreme Court concluded that contract warranty law was the appropriate body of law to protect the buyer's economic expectations.⁷¹ Contrary to *Seely*, however, the Court also extended that principle to physical damage to the defective product.

Even when the harm to the product itself occurs through an abrupt,

66. *Id.* at 149-50.

67. *Id.* at 149.

68. *Seely*, 403 P.2d at 151-52.

69. 476 U.S. 858 (1986).

70. *Id.* at 859-60.

71. *Id.* at 872-73.

accident-like event, the resulting loss due to repair costs, decreased value, and lost profits is essentially the failure of the purchaser to receive the benefit of its bargain—traditionally the core concern of contract law.⁷²

Only personal injury or damage to property other than the product itself would activate the tort principles of products liability law.

The third example, one of the issues on which the conflict between contract and tort law has been most contested, concerns when a breach of contract also constitutes a tort. The issue arises in cases of bad faith breach and negligent breach.

It is hornbook law that every contract includes an obligation of good faith performance. In many jurisdictions, breach of the good faith obligation has been argued as a basis for tort recovery beyond the damages permitted in contract. The California story is the best known. It began with a series of insurance cases, expanded for a time to employment cases, potentially included general commercial contracts, and then contracted severely in *Foley v. Interactive Data Corp.*,⁷³ a case that relied on the prevailing model of contract and tort law.

The early insurance cases in California rested on an insurance company's "failure to meet the duty to accept reasonable settlements" of claims against its insureds, "a duty included within the implied covenant of good faith and fair dealing."⁷⁴ Subsequently, the insurer's specific obligations were generalized into a duty to "act fairly and in good faith in discharging its contractual responsibilities."⁷⁵ A breach of that duty could result in "a cause of action in tort for breach of an implied covenant of good faith and fair dealing."⁷⁶ Decisions of the lower courts extended the availability of the tort cause of action from insurance cases to employment and banking cases, and dictum in the California Supreme Court's decision in *Seaman's Direct Buying Service, Inc. v. Standard Oil Co.*⁷⁷ suggested that tort liability might expand into general commercial contracts.

However, in *Foley* the California Supreme Court precluded the application of the bad faith tort to the employment area and effectively

72. *Id.* at 870.

73. 765 P.2d 373 (Cal. 1988) (en banc).

74. *Crisci v. Security Ins. Co.*, 426 P.2d 173, 177 (Cal. 1967) (en banc).

75. *Gruenberg v. Aetna Ins. Co.*, 510 P.2d 1032, 1037 (Cal. 1973) (en banc).

76. *Id.*

77. 686 P.2d 1158 (Cal. 1984) (en banc).

foreclosed its expansion to other areas as well.⁷⁸ At one level, the court's opinion was motivated by a model of tort and contract.⁷⁹ The opinion rested on a perception of the difference between tort and contract law and on the origins of the obligation of good faith in contract law. The court reasoned:

The distinction between tort and contract is well grounded in common law, and divergent objectives underlie the remedies created in the two areas. Whereas contract actions are created to enforce the intentions of the parties to the agreement, tort law is primarily designed to vindicate "social policy." The covenant of good faith and fair dealing was developed in the contract arena and is aimed at making effective the agreement's promises.⁸⁰

Because the obligation of good faith is a contract term, its scope in *any* particular case depends on the intentions of the parties and the reasonable expectations created by their contract, and contract damages, not tort damages, provide the appropriate remedy for such a breach.⁸¹

The insurance bad faith cases constituted an exception to this rule because of the unique characteristics of the insurance relationship. Through the insurance relationship, the insured seeks protection against calamity, not commercial advantage.⁸² The relationship is an inherently unequal one, in which the insured typically has no ability to bargain for terms and is at the insurer's mercy in case a claim is made. The insurance company provides a quasi-public service and has more responsibilities to its insureds than does an ordinary contracting enterprise.⁸³ In short, the distinctive features of the insurance relationship remove it from the model of contract; the harm that can be visited upon the subordinate insured by the dominant insurer is tortious by default.⁸⁴

78. *Foley*, 765 P.2d at 389-401.

79. *Id.* At another level, the decision was motivated by what one could reasonably describe as politics; the composition of the court had changed dramatically and several of its liberal justices were removed by the electorate and replaced with conservatives.

80. *Id.* at 389 (citation omitted).

81. *Id.* at 390 ("As a contract concept, breach of the duty led to imposition of contract damages determined by the nature of the breach and standard contract principles.").

82. *Id.*

83. *Id.* (citation omitted).

84. The denouement of the California story came recently in *Freeman & Mills, Inc. v. Belcher Oil Co.*, 900 P.2d 669 (Cal. 1995). The majority of the California Supreme Court overruled *Seaman's Direct* because of "uniform confusion and uncertainty regarding its scope and application, and widespread doubt about the necessity or desirability of its holding" without much discussion of the

In the bad faith cases, plaintiffs attempt to use the contractual obligation of good faith performance as the basis for a tort action. In cases of negligent breach of contract, plaintiffs even more ambitiously seek to transform the breach of any contractual obligation into a tort.

*Southwestern Bell Telephone Co. v. DeLanney*⁸⁵ is typical of a line of cases that illustrates the approaches to this problem. DeLanney was a business owner who advertised in the Yellow Pages directory published by Southwestern Bell.⁸⁶ Due to an error in its internal procedures, Bell negligently deleted DeLanney's advertisement from the 1980-81 directory.⁸⁷ Under the standard contract for directory advertising, Bell's liability to DeLanney was limited to a refund of the amount paid for the advertisement, so DeLanney sued in tort, alleging negligence.⁸⁸

The Texas authority and scholarly commentary relied on by the court delineated the distinctions between contract and tort actions. Where the defendant agreed to repair a water heater in the plaintiff's home and did so negligently, causing the heater to start a fire that destroyed the house and its contents, the action lay in tort because a common-law duty to act reasonably to avoid physical harm exists independent of the contract.⁸⁹ Negligently failing to publish a Yellow Pages advertisement is different, though.

If the defendant's conduct—such as negligently burning down a house—would give rise to liability independent of the fact that a contract exists between the parties, the plaintiff's claim may also sound in tort. Conversely, if the defendant's conduct—such as failing to publish an advertisement—would give rise to liability only because it breaches the parties' agreement, the plaintiff's claim ordinarily sounds only in contract.

In determining whether the plaintiff may recover on a tort theory, it is also instructive to examine the nature of the plaintiff's loss. When

contract-tort boundary. *Id.* at 679. Justice Mosk concurred in the result but dissented from the overruling of *Seaman's Direct* in an opinion that examined the boundary at length. *Id.* at 680-89 (Mosk, J., dissenting in part and concurring in part).

85. 809 S.W.2d 493 (Tex. 1991).

86. *Id.* at 493.

87. *Id.*

88. *Id.*

89. *Id.* at 494 (citing *Montgomery Ward & Co. v. Scharrenbeck*, 204 S.W.2d 508, 510 (Tex. 1947), and W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 92, at 655 (5th ed. 1984)).

the only loss or damage is to the subject matter of the contract, the plaintiff's action is ordinarily on the contract. . . .

The acts of a party may breach duties in tort or contract alone or simultaneously in both. The nature of the injury most often determines which duty or duties are breached. When the injury is only the economic loss to the subject of a contract itself the action sounds in contract alone.

Bell's duty to publish DeLanney's advertisement arose solely from the contract. DeLanney's damages, lost profits, were only for the economic loss caused by Bell's failure to perform. Although DeLanney pleaded his action as one in negligence, he clearly sought to recover the benefit of his bargain with Bell. We hold that Bell's failure to publish the advertisement was not a tort. . . . DeLanney's claim was solely in contract.⁹⁰

IV. CONCLUSION

We might draw a number of different conclusions from the combination of these other developments and the *Denny* problem.

We might view this struggle in a positive light. These are difficult, perhaps intractable, problems. The courts and scholars have done an admirable job of trying to resolve them. In the cases and the literature, we see an increasingly sensitive examination of the principles of contract and tort law, the relationship of those principles to the institutional strengths and limits of the legal system, and the ways in which the conflict of the two areas can best be reconciled consistent with those principles and institutional factors. Scholars and judges have concluded that each subject has its main sphere of influence, with a troublesome but limited gray area in between. Several of the solutions are symmetrical; because contract reigns where bargaining is possible and tort reigns where it is not, *East River* bars tort actions in commercial cases and the proposed *Restatement* bars contract actions in personal injury cases.⁹¹

Or we could take a negative view of the process. Despite all the examinations of the issue, we continually are thrown back on traditional

90. *Id.* at 494-95 (citations and footnotes omitted).

91. *See supra* notes 26-32, 69-73 and accompanying text.

views of the subjects and formulaic categorizations of the settings. Contract is about bargaining among free individuals; tort is about accidents to people who can't bargain. In every setting but the most extreme, bargaining is available, so the law ought to limit its intervention through tort law.

Or we could combine this examination of an "internal" perspective—a perspective that focuses only on the common-law process—with consideration of a set of "external" factors that might shed further light on what is going on in this area.⁹² To list only a few relevant factors outside the common-law process that ought to evoke the whole picture:

- Ronald Reagan was elected President in 1980 largely with the promise of lifting "government off the backs of the people." The two basic means of accomplishing this end were to cut taxes and decrease government regulation of the economy.
- The Republican Congress elected in 1994, under the leadership of Newt Gingrich, promised a "Common Sense Legal Reform Act" to do away with many tort remedies,⁹³ as part of its Contract with America that also would amend the Constitution to require a balanced budget to make further government expenditures less likely, and would reshape the regulatory process to make it more difficult for administrative agencies to prevent environmental harm, dangerous workplaces, and shoddy or harmful consumer products.
- The wealth and income gap between the richest and poorest segments of American society has widened.
- A Democratic President and a Republican Congress agree on the principle and the method to "end welfare as we know it."
- Legislative tort reform has decreased the ability of victims of careless manufacturers, physicians, accountants, securities brokers, and other tortfeasors to recover for their injuries.
- In both the academic and the popular literature, there is a new emphasis on "responsibilities" instead of "rights."⁹⁴

92. Cf. Phillips, *supra* note 45, at 1270-75 (possible "charitable" explanations for *Restatement Reporters'* rejection of strict liability will not withstand scrutiny).

93. The Congress passed, but the President vetoed the Common Sense Legal Reform Act. See H.R. 956, 104th Cong. (1996).

94. See generally MARY ANN GLENDON, *RIGHTS TALK: THE IMPOVERISHMENT OF POLITICAL*

- Legislation, judicial decisions, and referenda have limited affirmative action and other remedies for racial injustice.
- The idea has gained favor that there are “Simple Rules for a Complex World,”⁹⁵ rules that almost uniformly involve politically conservative policies.

Seen in this light, the relatively trivial problem of excluding liability for breach of implied warranty causing personal injury is part of a larger picture. What is going on in this area is part of the effort to limit the legal liability of businesses and other major societal actors; more broadly, the effort is to limit the responsibility that institutions and individuals in society owe to each other. The effort also aims to limit the ability of the courts to establish reasonable standards of behavior in the commercial as well as the social realms; more broadly, the effort seeks to limit the ability of the people through collective action by government to remedy social injustice.

DISCOURSE (1991).

95. RICHARD A. EPSTEIN, *SIMPLE RULES FOR A COMPLEX WORLD* (1995).