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COMMENT

Remedies—"Extra-Contractual" Remedies for Breach of Contract in North Carolina

I. INTRODUCTION

Historically, a number of problems, both conceptual and technical, have made it difficult for the civil litigant to secure punitive damages in North Carolina courts.¹ No litigant has faced more formidable obstacles than the party suing on a breach of contract theory, seeking both compensatory damages for the breach itself and punitive damages for the wrongful manner in which defendant breached.² Two recent decisions of the North Carolina Supreme Court, when read together (the first for its result, the second for its analysis), seem to increase greatly such a plaintiff's chances of reaching the jury with a punitive damage claim. The second decision seems to warn that the bad faith breach of an insurance contract may result in liability for an assortment of other special damages as well.

In *Oestreicher v. American National Stores, Inc.*,³ a divided court ruled that plaintiff's award need not be limited to compensatory damages dictated by the terms of the parties' agreement when the breach "smack[s] of tort because of the fraud and deceit involved."⁴ Language in the opinion, however, might have permitted a trial judge to grant summary judgment against a punitive damages claim unless he found the fraudulent conduct to be coupled with an "element of aggravation"⁵ that rendered the conduct "outrageous" and "asocial" as a

1. See, e.g., *Van Leuven v. Akers Motor Lines, Inc.*, 261 N.C. 539, 135 S.E.2d 640 (1964); *Lutz Indus., Inc. v. Dixie Home Stores*, 242 N.C. 332, 88 S.E.2d 333 (1955); *Baker v. Winslow*, 184 N.C. 1, 113 S.E. 570 (1922); *Holmes v. Carolina Cent. R.R.*, 94 N.C. 318 (1886); 3 J. STRONG, NORTH CAROLINA INDEX, *Damages* § 11, at 181 (2d ed. 1967). See generally 5 A. CORBIN, CONTRACTS § 1077 (1964 & Supp. 1971).

2. See, e.g., *Hardy v. Toler*, 288 N.C. 303, 218 S.E.2d 342 (1975); *King v. Insurance Co. of N. Am.*, 273 N.C. 396, 159 S.E.2d 891 (1968); *Davis v. North Carolina State Highway Comm'n*, 271 N.C. 405, 156 S.E.2d 685 (1967); *Nunn v. Smith*, 270 N.C. 374, 154 S.E.2d 497 (1967); *Swinton v. Savoy Realty Co.*, 236 N.C. 723, 73 S.E.2d 785 (1953); see Note, *Recovery of Punitive Damages for Fraud and Deceit*, 31 N.C.L. REV. 473 (1953).

3. 290 N.C. 118, 225 S.E.2d 797 (1976).

4. *Id.* at 136, 225 S.E.2d at 809.

5. *Id.* at 134, 225 S.E.2d at 807 (quoting *Swinton v. Savoy Realty Co.*, 236 N.C. 723, 725, 73 S.E.2d 785, 787 (1953)).

matter of law.⁶ *Newton v. Standard Fire Insurance Co.*⁷ clarified the *Oestreicher* holding, dispensing with the "aggravation" requirement in cases where the trial judge determines actionable fraud.⁸ The more recent case went further and suggested that a fraudulent breach of contract may not be the only breach for which "extra-contractual" damages can be awarded.⁹ The majority opinion in *Newton* seemed to say that the bad faith refusal of an insurer to pay a valid claim might itself give rise to a cause of action in tort.¹⁰ The question of what remedial consequences would flow from such a characterization was not clearly answered.

Oestreicher involved a commercial lease agreement, seemingly arm's length, between two business entities,¹¹ whereby defendant leased from plaintiff¹² a store building in which defendant conducted a retail furniture business.¹³ The lease provided that defendant was to pay a minimum rent plus five percent of its net sales income above a stated amount.¹⁴ In 1974, thirteen years after the signing of the initial agreement, *Oestreicher* sued, alleging that for a period of nine years American National Stores, Inc. had misrepresented its net sales so that *Oestreicher* had been deprived of \$11,233.20 due under the lease.¹⁵ The complaint stated a cause of action for breach of contract—with the fraudulent reporting of sales as the breach itself—and a separate cause of action reiterating the fraudulent conduct and asking for punitive damages in the amount of \$100,000.¹⁶

The superior court granted summary judgment for defendant on the second cause of action;¹⁷ the North Carolina Court of Appeals dis-

6. *Id.*

7. 291 N.C. 105, 229 S.E.2d 297 (1976).

8. *Id.* at 113-14, 229 S.E.2d at 302.

9. *Id.* at 115-16, 229 S.E.2d at 303.

10. *Id.* at 116, 229 S.E.2d at 303.

11. 290 N.C. at 120, 225 S.E.2d at 799; Complaint at 2-5, 27 N.C. App. 330, 219 S.E.2d 303 (1975). *Oestreicher-Winner* was a family-owned retail clothing business at the time the lease was made. The lease included an agreement by lessee not to compete with the *Oestreicher-Winner* line of business. 290 N.C. at 140, 225 S.E.2d at 810.

12. Plaintiff was Mrs. Bert *Oestreicher*, suing in her capacity as trustee for two other members of the family. 290 N.C. at 118, 225 S.E.2d at 797.

13. American National Stores, Inc. became a successor lessee in 1970. Earlier, American National had done business as Johnston's L & S Furniture Co. in whose name the original lease was signed. In 1970 the lease was renewed for a five-year period. *Id.* at 120, 225 S.E.2d at 799-800.

14. *Id.*

15. *Id.* at 132-33, 225 S.E.2d at 806-07.

16. *Id.* at 131-32, 225 S.E.2d at 806; Complaint at 2-5, 27 N.C. App. 330, 219 S.E.2d 303 (1975).

17. 290 N.C. at 121, 225 S.E.2d at 800.

missed Oestreicher's appeal as improperly interlocutory because the judgment was final as to only one of two claims.¹⁸ On discretionary review, the North Carolina Supreme Court ruled that the breach of contract cause and the punitive damages claim had been improperly severed.¹⁹ Reviewing exceptions to the general rules against punitive damages awards for breach of contract or for fraud, the court by a four-to-three vote ordered the question of punitive damages returned to the jury. The grant of summary judgment, the majority wrote, had overlooked the fact that although this was a "type of contract case," there were "substantial tort overtones emanating from the fraud and deceit."²⁰

No fraud was alleged in *Newton*. Plaintiff owned a retail business for which he had purchased theft insurance coverage from defendant. Plaintiff filed a claim for \$5,000 under the policy for losses suffered in a burglary of his premises. Defendant refused payment.²¹ In his complaint, plaintiff alleged: (1) that defendant had refused "to properly settle" the claim;²² (2) that the future of his business was threatened by his inability to collect his due benefits; (3) that although he had communicated to defendant this "desperate need,"²³ the insurer had continued in his refusal to comply with the terms of the insurance con-

18. 27 N.C. App. 330, 330, 219 S.E.2d 303, 304 (1975).

19. The court of appeals had held that because the judgment contained no determination from the trial judge that "there is no just reason for delay" in hearing the appeal, it was not final and appealable under their reading of N.C.R. Crv. P. 54(b). *Id.* On discretionary review, the supreme court decided to hear the interlocutory appeal because its outcome "affects a substantial right." 290 N.C. at 124, 130, 225 S.E.2d at 802, 805. The procedural stance is significant in its relation to the substance of the decision. The supreme court refused to allow the punitive damages or "tort" cause of action to be severed from the breach of contract cause of action. The "substantial right" of the plaintiff to have both causes heard before the same judge and jury is the reason that the supreme court gave for hearing the interlocutory appeal. The court said, regarding this first error on appeal, "The causes of action that the plaintiff alleges are related to each other. He seeks punitive damages in the second cause because of the alleged misconduct of defendant in the first cause of action." *Id.* at 130, 225 S.E.2d at 805. This holding is an indication that North Carolina has relaxed to some extent its requirement of a showing of an "independent tort" by the plaintiff seeking punitive damages for breach of contract. If the breach claim and the punitive damages claim are merged, the jury has been given more freedom to consider the culpability of the breach itself, as a breach of contract and not as a tort. See text accompanying notes 98 & 105 *infra*.

20. 290 N.C. at 136, 225 S.E.2d at 809.

21. 291 N.C. at 109, 229 S.E.2d at 300. Plaintiff also filed a claim for losses caused by a fire that occurred on the premises shortly after the burglary. In his brief before the court of appeals, *Newton* alleged that the insurance company had not paid this fire loss claim in a timely manner. Plaintiff Appellant's Brief at 2, 27 N.C. App. 168, 218 S.E.2d 232 (1975).

22. 291 N.C. at 110, 229 S.E.2d at 300.

23. *Id.*

tract; and (4) that defendant's conduct was "heedless, wanton and oppressive."²⁴ Plaintiff sought \$5,500 in compensatory damages and \$50,000 in punitive damages for the oppression involved in the breach.²⁵

The trial court struck the claim for punitive damages from the complaint on the stated ground that North Carolina law did not permit punitive damages for a breach of contract claim.²⁶ As in *Oestreicher*, the court of appeals held that the decision of the trial court was not appealable, because the dismissal of the punitive damages claim did not represent a final judgment.²⁷ Implicit in this decision was the finding that such a dismissal did not "affect a 'substantial right.'"²⁸ Again, the supreme court reversed, ruling that the party complaining of a breach of contract did have a "substantial right" to have the punitive damages issue heard by the same court that considered the breach.²⁹

Before the supreme court, plaintiff urged that defendant's oppressive conduct amounted to a tort for which punitive damages could be awarded.³⁰ The majority agreed that defendant would have been liable for punitive damages if its dealings with plaintiff had been fraudulent.³¹ The majority added that punitive damages might also have been in order if the insurer had refused to investigate plaintiff's claim *or* if the insurer, after investigation, had determined the claim to be valid but still refused to pay *and* if either refusal had been made with the intention of causing further damage to plaintiff.³² Finding none of these circumstances, the court affirmed the dismissal. On the way to denying the particular plaintiff's punitive damages, however, Justice Exum's opinion for the court answered a number of questions left open by *Oestreicher* and seemed to expand the remedial possibilities for breach of contract, at least when the breach is of an insurance contract.

Chief Justice Sharp dissented emphatically in *Oestreicher* and, while concurring in their result, decried the thinking of the *Newton* majority. In the first case, she insisted: (1) that *Oestreicher's* only rights were those under the contract so that any recovery beyond the

24. *Id.*

25. *Id.*

26. Record at 6, 27 N.C. App. 168, 218 S.E.2d 232 (1975).

27. 27 N.C. App. 168, 169-70, 218 S.E.2d 231, 232 (1975).

28. 291 N.C. at 109, 229 S.E.2d at 300.

29. *Id.*

30. Plaintiff Appellant's Brief at 3, 27 N.C. App. 168, 218 S.E.2d 232 (1975).

31. 291 N.C. at 114, 229 S.E.2d at 302.

32. *Id.* at 115-16, 229 S.E.2d at 303.

obligations bargained for would unjustly enrich plaintiff;³³ (2) that if *Oestreicher* had a cause of action in tort for fraud, plaintiff had failed to plead it with sufficient particularity to distinguish it from the breach of contract claim;³⁴ and (3) that even a showing of actionable fraud would not merit jury consideration of punitive damages unless actual malice, oppression, willful wrong, insult or the like were shown.³⁵ According to the Chief Justice, the *Newton* majority's careful retracing of the steps taken in *Oestreicher* served only to "further confuse an area of the law which is rapidly becoming confusion worse confounded."³⁶

II. BACKGROUND

The conflict between the two majority opinions and those of Chief Justice Sharp contained the outlines of the doctrinal difficulty encountered by almost all courts that have considered the question of punitive damages for a cause of action that is based on contract theory but that alleges fraud, or other intentionally wrongful conduct, as well.³⁷

33. 290 N.C. at 146, 225 S.E.2d at 814 (Sharp, C.J., dissenting in part and concurring in part).

34. *Id.* at 148, 225 S.E.2d at 815. Chief Justice Sharp sought to distinguish the deceptive conduct of the defendant from "a factual situation in which it is alleged that a party was induced to enter into a contract by reason of a false and fraudulent representation." *Id.* at 147, 225 S.E.2d at 815. Arguably, a distinction can be made between false representations which induce the making of a contract ("fraud in the inducement") and false representations made in the course of performance of the contractual duties themselves ("fraud in the performance"). As long as the contract remains partially executory, however, and one party continues to perform in reliance upon the other's misrepresentation of facts, this inducement/performance distinction blurs considerably. In *Oestreicher*, for example, plaintiff relied to her detriment upon the false representations of defendant. She continued to perform in reliance upon the misrepresented fact that defendant was accurately reporting its income. In this sense, plaintiff was "induced to enter" into continuing performance by defendant's fraud.

The distinction is perhaps understood better as a graduated scale—with "tort" at one end and "contract" at the other—than as a simple dichotomy. Fraud in the inducement of a contractual agreement is distinct in time from the breach of duties under that agreement, so such fraud can be more easily regarded as the breach of a generalized duty. That is, as a tort. 37 C.J.S. *Fraud* § 64 (1943). The more misrepresentations become entangled with the failure to perform contractual obligations, the greater the difficulty in viewing the fraudulent conduct apart from the contract. Often, as in *Oestreicher*, the fraudulent conduct will be the breach. See text accompanying note 85 *infra*.

To the extent that the inducement/performance distinction can be made, this comment is limited to a consideration of fraud in the performance of contractual duties. Anything that can be said regarding an award of punitive damages for fraud in the performance will apply *a fortiori* to fraud in the inducement.

35. 290 N.C. at 148, 225 S.E.2d at 815.

36. 291 N.C. at 116, 299 S.E.2d at 304 (Sharp, C.J., concurring in result).

37. See 25 C.J.S. *Damages* § 120 (1966); Annot., 165 A.L.R. 614 (1946) (examines fraudulent breach of contract in terms of tort); Annot., 84 A.L.R. 1345 (1933)

The majority in *Oestreicher* justified the possibility of punitive damages on the basis of "substantial tort overtones"³⁸ in the pleaded facts; the Chief Justice tailored her argument rejecting punitive damages to a frame of contract theory. In past North Carolina decisions, a court's determination of whether a complaint sounded in tort or in contract has been critical to the question of punitive damages.³⁹ The purpose of punitive or exemplary damages is to punish intentionally wrongful conduct and thus, by example, to discourage the culpable state of mind behind the conduct.⁴⁰ Under this rationale, negligent behavior never warrants punitive damages unless somehow "wanton." Even intentional wrongdoing sometimes must be shown to have been aggravated before a court will allow them.⁴¹

The idea of awarding punitive damages in any civil action has jarred some judicial sensibilities.⁴² The plaintiff who receives punitive

(considers problem from perspective of contract theory); Note, *Damages—Punitive Damages for Breach of Contract*, 11 N.C.L. REV. 160 (1933). The complexity of the question is well illustrated by a string of South Carolina cases cited at 25 C.J.S., *supra*, at § 120, at 1129 nn.92-95. South Carolina seems to have moved further than most jurisdictions in the direction of allowing an award of punitive damages in the breach-cum-fraud situation. The South Carolina developments were given extensive treatment in Note, *Punitive Damages for Breach of Contract in South Carolina*, 10 S.C.L.Q. 444 (1958). The Indiana Supreme Court also has explored the question in some depth. See Note, *The Expanding Availability of Punitive Damages in Contract Actions*, 8 IND. L. REV. 668 (1975) [hereinafter cited as *Punitive Damages*].

38. 290 N.C. at 136, 225 S.E.2d at 809.

39. Discussion in J. STRONG, *supra* note 1 provides an illustration of the importance of classification. The sections of that work dealing with damages for breach of contract make no mention whatever of punitive damages. 3 J. STRONG, *supra* note 1, *Contracts* §§ 28.2-29.3 (3d ed. 1976). The punitive damages section, on the other hand, discusses *Swinton v. Savoy Realty Co.*, 236 N.C. 723, 73 S.E.2d 785 (1953), which is classified as an action based on the intentional tort of fraud, and *Lutz Indus. v. Dixie Home Stores*, 242 N.C. 332, 88 S.E.2d 333 (1955), which is placed in the "negligence" category, again a tort. The index fails to note that in both of these actions contractual relations existed between the parties. See 3 J. STRONG, *supra* note 1, *Damages* § 11.

40. See CAL. CIV. CODE § 3294 (West 1970); Note, *Exemplary Damages in the Law of Torts*, 70 HARV. L. REV. 517, 519 (1957); *Punitive Damages*, *supra* note 37, at 669. It is the punishment aspect of punitive or exemplary damages that results in their being called "smart money" in an occasional older case. See, e.g., *Cotton v. Fisheries Prod. Co.*, 181 N.C. 151, 152, 106 S.E. 487, 488 (1921).

Professor Clarence Morris distinguishes between the "reparative" and "admonitory" aspects of all tort damages. He points out that any damages award, except one given under a "strict liability" or "liability without fault" theory, is intended to admonish what may even be only a negligent "wrongdoer" as well as to restore the plaintiff's economic security. Morris, *Punitive Damages in Tort Cases*, 44 HARV. L. REV. 1173, 1174 (1931).

41. See D. DOBBS, HANDBOOK ON THE LAW OF REMEDIES § 3.9, at 205-06 (1973); *Punitive Damages*, *supra* note 37, at 669.

42. "[A] monstrous heresy. . . . [A]n unhealthy excrescence, deforming the symmetry of the body of the law." *Fay v. Parker*, 53 N.H. 342, 382 (1873). "The submission of the issue of punitive damages furnishes an opportunity for the exercise

damages from the jury has been made more than whole; he has made a "profit" on his injury beyond recovery for his losses, even beyond compensation for such remote losses as pain and suffering and mental anguish, although at the outer edges of recovery these distinctions blur. The defendant, in the meantime, has been punished, and punishment, in theory, is reserved for the criminal law. A party defending his conduct against the imposition of punitive damages in a civil action is denied a number of the procedural safeguards guaranteed to the criminal defendant.⁴³

The pleader in tort theory, however, has at least complained of a "wrong," a violation of a duty imposed by law rather than by a private agreement, so that a stronger rationale can be advanced for punishing the tortfeasor beyond the extent of the actual damage he has caused than for similarly punishing the contract breacher.⁴⁴ Conceptually, the tortfeasor has imposed a wrong upon a stranger; the parties to a contract have bargained for and balanced their several duties.⁴⁵ To extract payment from defendant on behalf of plaintiff beyond the duty undertaken by defendant is to "rewrite the contract for the parties," which the courts profess themselves unable to do.

of passion and prejudice upon the part of a jury, resulting in an unjust award" *Saberton v. Greenwald*, 146 Ohio St. 414, 442, 66 N.E.2d 224, 236 (1946) (Hart, J., dissenting).

43. In a criminal trial, a defendant cannot be made to testify against himself; the standard by which his guilt or innocence is determined is "guilt beyond a reasonable doubt"; the jury does not assess the penalty; the prohibition against "double jeopardy" insures that there will not be double punishment. In a civil trial for punitive damages, the defendant must testify when called to the stand by the plaintiff; the standard is "preponderance of the evidence"; the amount of the punitive damages is set by the jury subject to some control by the court; there is the possibility that the defendant, if his conduct has also violated criminal law, will be punished twice for the same conduct. *Saberton v. Greenwald*, 146 Ohio St. 414, 432, 66 N.E.2d 224, 232 (1946) (Hart, J., dissenting). Justice Hart also points out that any fines levied for conduct deemed a transgression of the public interest—i.e., a crime—are given over to the public, while civil punitive damages "enrich" only the plaintiff. *Id.* See also *Punitive Damages*, *supra* note 37. But see *Morris*, *supra* note 40, at 1182-83.

44. There can be no doubt that the general purpose underlying the law of damages, whether they are given for a breach of contract or for a tort, is to promote security and to prevent disorder. . . . Breaches of contract, however, do not in general cause as much resentment or other mental and physical discomfort as do the wrongs called torts and crimes. . . . It has been found sufficient to give pecuniary compensation to the injured party with no necessity for satisfying his feelings and allaying community resentment by fines or physical punishment.

A. CORBIN, *supra* note 1, § 1077.

45. The measure of damages for breach of contract is the amount which will compensate the injured party for the loss which fulfillment of the promise could have prevented or the breach of it entailed, so that the parties may be placed as nearly as may be in the same monetary condition that they would have occupied had the contract not been breached.

3 J. STRONG, *supra* note 1, *Contracts* § 29.2, at 442 (3d ed. 1976).

The most loudly voiced criticism of awarding punitive damages in a civil action has been directed at the "passion and prejudice . . . [of the] jury."⁴⁶ Not only punitive damages but special damages in general are less accessible to the pleader in contract than to the plaintiff who is blessed with a tort cause of action. The disparity results from uncoordinated notions of "foreseeability."⁴⁷ The defendant to a tort claim is generally held to have "foreseen" much farther than the party who has spelled out his foresight in a contract.⁴⁸ A jury is allowed to look only as far as the parties have "foreseen." Beyond that, the jury's views are "conjectural." The parties to a contract have undertaken to measure their expectations of each other, so that the awarding of damages when breach of contract has been found can proceed against some objective (non-"conjectural") standard. In a tort action it is more difficult to measure "foreseeability" and, therefore, to limit the jury's freedom to set *whatever* damages are deemed appropriate—general, special or even punitive. Punitive damages are never bargained for, never foreseen. To allow the jury to consider and allocate risks which the parties themselves, despite the opportunity to do so, have not allocated is to permit the jury to speculate and conjecture. The further the jury proceeds beyond the easily quantifiable (*i.e.*, damages that "compensate" according to the terms agreed upon beforehand by the parties) the more it approaches the realm of "passion and prejudice."⁴⁹ This is the theory.

46. *Saberton v. Greenwald*, 146 Ohio St. 414, 442, 66 N.E.2d 224, 236 (1946) (Hart, J., dissenting). See also *Morris*, *supra* note 40, at 1178; Note, *supra* note 40, at 530; *Punitive Damages*, *supra* note 37, at 670.

47. *D. DOBBS*, *supra* note 41, § 12.3, at 812.

48. *Id.* at 804; see *Koufos v. Czarnikow, Ltd. (The Heron II)*, [1969] 1 A.C. 350. See generally *Hadley v. Baxendale*, 156 Eng. Rep. 145 (Ex. 1854). Any general discussion of *Hadley* is beyond the scope of this comment. It may be useful, however, to consider the treatment of *Hadley* by Lord Reid in *Koufos*, "The modern rule in tort is quite different [from the rule in contract] and it imposes a much wider liability. . . . I have no doubt that today a tortfeasor would be held liable for a type of damage as unlikely as was the stoppage of *Hadley's Mill* for lack of a crank shaft. . . . But it does not at all follow that *Hadley v. Baxendale* would today be differently decided." [1969] 1 A.C. at 385-86 (footnote omitted).

49. A 1930 *North Carolina Law Review* article examined the reason for this reluctance to permit the jury to second guess the bargaining parties:

a belief that since the vast majority of breaches of contract are due to inability or to erroneous belief as to the scope of the obligation, it is of doubtful wisdom to add to the risks imposed on entering into a contract, this liability to an acrimonious contest over whether a breach was malicious or fraudulent, and the danger of a large and undefined recovery of punitive damages.

McCormick, *Some Phases of the Doctrine of Exemplary Damages*, 8 N.C.L. REV. 129. 140 (1930).

If the principle of punitive damages is the curbing of a culpable mind, it is difficult to understand why such damages should be any less available for an intentionally wrongful breach of contract than for a tort.⁵⁰ Possibly the vocabulary—"foreseeability," "contemplation of the parties," "contract," "tort"—obscures a more real concern: the ability to monitor jury discretion.⁵¹ By classifying an action as one *ex contractu*, a court is able to justify foreclosing punitive damages. In any case, the courts have evolved a rubric: "Punitive damages are not awarded for breach of contract."⁵²

When the actions of the breaching party reach a certain level of reprehensibility, however, courts have characterized the behavior as "a tort" or "tortious" and, in that way, have saved the plaintiff's punitive damages from summary judgment.⁵³ In those cases, the court has placed to one side the contract theory implications in the pleading and culled from the facts pleaded "some intentional wrong, insult, abuse, or gross negligence which amounts to an independent tort."⁵⁴ That is, if the breaching behavior evidenced a "bad" enough state of mind, the pleading could achieve enough momentum to escape the pull of contract theory. On the other hand, findings even of a "malicious or oppressive breach of contract" have been insufficient to support an award of punitive damages when the court declined to characterize the defendant's conduct as an "independent tort."⁵⁵

The criterion that emerged from these cases, the factor that rendered conduct culpable enough to achieve "independence" from the

50. See D. DOBBS, *supra* note 41, § 3.9, at 207.

51. See generally *id.* § 12.3, at 814.

52. *Ostreicher v. American Nat'l Stores, Inc.*, 290 N.C. 119, 133, 225 S.E.2d 797, 807 (1976); *King v. Insurance Co. of N. Am.*, 273 N.C. 396, 398, 159 S.E.2d 891, 893 (1968); see 25 C.J.S. *Damages* § 120 (1966); Annot., 84 A.L.R. 1345 (1933). This flat prohibition was subject to exceptions for breaches of contracts to marry and for breaches by some public conveyances and utilities. The latter breach is commonly characterized as a breach of a tort duty to the public. At least one authority has said that a breach of a contract to marry is also more of a tort than a "pure" breach of contract. D. DOBBS, *supra* note 41, § 12.4, at 818; see note 129 *infra*.

53. *Binder v. General Motors Acceptance Corp.*, 222 N.C. 512, 23 S.E.2d 894 (1943); *Woody v. First Nat'l Bank*, 194 N.C. 549, 140 S.E. 150 (1927); *Carmichael v. Southern Bell Tel. & Tel. Co.*, 157 N.C. 21, 72 S.E. 619 (1911); *Ammons v. Railroad*, 140 N.C. 196, 52 S.E. 731 (1905); *Richardson v. Wilmington & W.R.R.*, 126 N.C. 100, 35 S.E. 235 (1900); 25 C.J.S. *Damages* § 120, at 1128-29 nn.86.5-90 (1966). But see *Williams v. Carolina & N.W.R.R.*, 144 N.C. 498, 57 S.E. 216 (1907).

54. *Oestreicher v. American Nat'l Stores, Inc.*, 290 N.C. 118, 135, 225 S.E.2d 797, 808 (1976) (quoting 25 C.J.S. *Damages* § 120, at 1129 (1966)).

55. *Newton v. Standard Fire Ins. Co.*, 291 N.C. 105, 111, 229 S.E.2d 297, 301 (1976); see *Swinton v. Savoy Realty Co.*, 236 N.C. 723, 734, 73 S.E.2d 785, 789 (1953); 25 C.J.S. *Damages* § 120 (1966).

contract action and thereby warrant admonition, was "an element of aggravation accompanying the tortious conduct which causes the injury."⁵⁶ Conduct tortious in nature but lacking aggravating circumstances would be found to be "dependent" upon and absorbed back into the breach of contract allegation.⁵⁷ Although often vague and general in their discussion, courts seemed to agree that aggravation would be found "when the wrong is done willfully and maliciously or under circumstances of rudeness or oppression, or in a manner which evinces a reckless and wanton disregard for the plaintiff's rights."⁵⁸ At the heart of the "aggravation" lay the defendant's intent to do wrong or, more frequently, his "spite,"⁵⁹ "ill-will,"⁶⁰ "malice,"⁶¹ or, sometimes, "recklessness."⁶²

Yet the party gained nothing by virtue of his contract rights: the "element of aggravation"—in North Carolina and elsewhere—was the same standard applied for punitive damages in *any* tort case. It seemed redundant to say that punitive damages could be awarded for breach of contract accompanied by a tort that was aggravated by malice, when the aggravated tortious conduct alone would qualify for punishment. Indeed, the tort pleader was more likely to be handicapped by his contract rights and would have to waive them if he had decided that the prospect of punitive damages made it worth his while to proceed in tort.

The breach + tort + aggravation analysis can be found in North Carolina decisions as early as 1891. In *Purcell v. Richmond & Danville Railroad Co.*,⁶³ a plaintiff ticket holder left standing beside

56. *Swinton v. Savoy Realty Co.*, 236 N.C. 723, 725, 73 S.E.2d 785, 787 (1953); cf. *Baker v. Winslow*, 184 N.C. 1, 5, 113 S.E. 570, 573 (1922) ("aggravation" language in case involving punitive damages but no contract). See also *Carmichael v. Southern Bell Tel. & Tel. Co.*, 157 N.C. 21, 26, 72 S.E. 619, 621 (1911) ("some features of aggravation"); *Ammons v. Railroad*, 140 N.C. 196, 197, 52 S.E. 731, 732 (1905) ("circumstances of aggravation"); *Holmes v. Carolina Cent. R.R.*, 94 N.C. 318, 323 (1886) ("causes of aggravation").

57. *Elmore v. Atlantic Coast Line R.R.*, 191 N.C. 182, 131 S.E. 633 (1926).

58. *Carmichael v. Southern Bell Tel. & Tel. Co.*, 157 N.C. 21, 26, 72 S.E. 619, 621 (1911).

59. Note, *Exemplary Damages in the Law of Torts*, 70 HARV. L. REV. 517, 517 (1957).

60. *Id.*; see *Saberton v. Greenwald*, 146 Ohio St. 414, 424, 66 N.E.2d 224, 229 (1946) ("insult"); C. McCORMICK, *LAW OF DAMAGES*, § 79, at 280 (1935) ("evil").

61. *Carmichael v. Southern Bell Tel. & Tel. Co.*, 157 N.C. 17, 21, 72 S.E. 619, 622 (1911); *Ammons v. Railroad*, 140 N.C. 196, 200, 52 S.E. 731, 733 (1905) (Hoke, J., concurring).

62. *Binder v. General Motors Acceptance Corp.*, 222 N.C. 512, 516, 23 S.E.2d 894, 896 (1943).

63. 108 N.C. 414, 12 S.E. 954 (1891).

the tracks when defendant railroad failed to stop at his station was told by the North Carolina Supreme Court that he had a cause of action in tort for breach of a public duty, even though the tortious conduct also constituted a breach of contract. Further, it was held that if defendant's conduct were shown to be "willful or . . . such gross negligence as to indicate a wanton disregard for the rights of the plaintiff,"⁶⁴ the railroad would be liable for punitive damages. If the harm to plaintiff resulted from simple negligence, the court said, plaintiff's recovery would be limited to the fifteen cents he had paid for the ticket and the twenty-five cents paid for other transportation—basic contract remedies.⁶⁵ The same analysis produced similar results in a number of other early common carrier and public utility cases.⁶⁶ In a 1943 case, the supreme court decided that a plaintiff had suffered a trespass when the company that had sold him an automobile under an installment contract breached that contract by repossessing the car "wrongfully" and in such a manner "that the plaintiff was humiliated in a public place."⁶⁷ Despite the contractual context, an award of punitive damages was upheld.

In contrast, the court has overturned a jury assessment of punitive damages against a defendant railroad whose conductor had required plaintiff passenger to leave the first class car for which he had purchased a ticket and ride in inferior accommodations.⁶⁸ The court noted the "aggravation" standard⁶⁹ and, finding "no evidence either of rudeness or unnecessary force,"⁷⁰ limited plaintiff's recovery to compensatory damages, presumably determined under the terms of the contract for passage.⁷¹ In a 1926 case not involving the special tort duty imposed on public conveyances, a plaintiff suing his former employer on a tort theory for "false, wilful and malicious"⁷² charges made against

64. *Id.* at 418, 12 S.E. at 955.

65. *Id.*

66. *See, e.g.,* Carmichael v. Southern Bell Tel. & Tel. Co., 157 N.C. 21, 72 S.E. 619 (1911) (telephone company); Ammons v. Railroad, 140 N.C. 196, 52 S.E. 731 (1905) (railroad); Hutchinson v. Railroad, 140 N.C. 123, 52 S.E. 263 (1905) (railroad). The North Carolina Supreme Court has implied a special tort duty owed by a bank to its customers. Woody v. First Nat'l Bank, 194 N.C. 549, 140 S.E. 150 (1927).

67. Binder v. General Motors Acceptance Corp., 222 N.C. 512, 515, 23 S.E.2d 894, 896 (1943).

68. Holmes v. Carolina Cent. R.R., 94 N.C. 318 (1886).

69. *Id.* at 323.

70. *Id.* at 324.

71. *Id.*

72. Elmore v. Atlantic Coast Line R.R., 191 N.C. 182, 183, 131 S.E. 633, 634 (1926).

him at the time of his allegedly improper discharge from employment was told by the North Carolina Supreme Court that his only rights were those under his employment contract with defendant.⁷³ The court refused to designate the alleged slander as the "independent tort" that would revive plaintiff's chance for punitive damages, although the court did recognize that possibility.⁷⁴ The implication in these cases was that the conduct of the breaching party might have been tortious but was not tortious enough to be "independent" of the contract claim.

III. FRAUD

In North Carolina, as elsewhere, a breach together with *unaggravated* tortious conduct had no cumulative effect.⁷⁵ The assessment of punitive damages in the contract cases proceeded under the same tort + aggravation = punitive damages equation that would have been determinative if the tortious conduct had been alleged alone without mention of a breach of contract. In a number of North Carolina decisions, "fraud" has been listed among the possible "elements of aggravation."⁷⁶ But since fraudulent conduct is, or can be, a tort itself, these cases suggest that fraudulent conduct would have to be coupled with a further "element of aggravation" to support a claim for punitive damages. This analysis, however, assumes that the intent to deceive that is an essential element of the fraud cause of action is not itself "aggravating." The aspect of intentional wrongdoing that punitive damages are meant to deter seems implicit in fraudulent or deceitful conduct. In this way fraud differs from other torts.⁷⁷

Nevertheless, the 1953 North Carolina Supreme Court decision, *Swinton v. Savoy Realty Co.*,⁷⁸ erased a jury grant of punitive damages for what was conceded to be "actionable fraud" when the court ruled that "there must be an element of aggravation accompanying the

73. *Id.* at 188, 131 S.E. at 636.

74. *Id.* at 186, 131 S.E. at 635.

75. *Swinton v. Savoy Realty Co.*, 236 N.C. 723, 73 S.E.2d 785 (1953); 25 C.J.S. *Damages* § 120, at 1128 (1966); Note, *supra* note 2; cf. *King v. Insurance Co. of N. Am.*, 273 N.C. 396, 159 S.E.2d 891 (1968) (Plaintiff alleged fraud. The supreme court affirmed grant of motion to strike tort claims and limited plaintiff to remedies under the contract.). See note 148 *infra*.

76. *Harris v. Queen City Coach Co.*, 220 N.C. 67, 69, 16 S.E.2d 464, 466 (1941); *Robinson v. McAlhaney*, 214 N.C. 180, 184, 198 S.E. 647, 650 (1938); *Tripp v. American Tobacco Co.*, 193 N.C. 614, 616, 137 S.E. 871, 872 (1927); *Holmes v. Carolina Cent. R.R.*, 94 N.C. 318, 323 (1886); Note, *supra* note 2, at 474.

77. Note, *supra* note 2, at 475.

78. 236 N.C. 723, 73 S.E.2d 785 (1953).

tortious conduct which causes the injury . . . Here fraud is not an accompanying element of an independent tort but the particular tort alleged.”⁷⁹ *Swinton* involved a fraudulent sale of land. The plaintiffs, “aged Negroes without education,”⁸⁰ had paid \$2,000 for a piece of land that the seller had represented to be of certain dimensions. After paying on the contract for three years and finally receiving a deed, plaintiffs learned that the property deeded them by the realty was one-tenth the size of the plot described to them at the time they contracted to purchase.⁸¹ The court ignored the possibility that defendant’s proven intent to deceive the buyers in a situation of widely unbalanced bargaining power might have evidenced the exact mental state for which punitive damages were designed. Fraud was a tort, the court reasoned and punitive damages were awarded for the commission of a tort only when that tort was aggravated.⁸² It made no apparent difference that the seller’s conduct in violating a tort duty against fraud had also violated plaintiffs’ contract rights. The net result of *Swinton* was that three elements must be presented in the complaint of fraudulent breach if the question of punitive damages is to go to the jury: breach + fraud (as the accompanying tort) + aggravation.

Although the *Swinton* court gave only perfunctory attention to contract theory, at least one later decision has cited the case for the familiar proposition that “punitive damages are not given for breach of contract.”⁸³ Several other North Carolina Supreme Court opinions have found in *Swinton* a new rubric: “[O]rdinarily punitive damages are not recoverable in an action for fraud.”⁸⁴ The overlap of the two meanings ascribed to *Swinton* points to the doctrinal kinship between the action for breach of contract and that for fraud,⁸⁵ a link that the North Carolina courts seemed to ignore prior to *Oestreicher*. The misrepresentation by defendant in *Swinton* was “tortious conduct” but it was also the breach of contract itself. The final remedy, after punitive

79. *Id.* at 725, 73 S.E.2d at 786.

80. *Id.*

81. *Id.* at 724, 73 S.E.2d at 786.

82. *Id.* at 726-27, 73 S.E.2d at 787-88.

83. *King v. Insurance Co. of N. Am.*, 273 N.C. 396, 398, 159 S.E.2d 891, 893 (1968).

84. *Hardy v. Toler*, 288 N.C. 303, 306, 218 S.E.2d 342, 344 (1975); *Davis v. North Carolina State Highway Comm’n*, 271 N.C. 405, 409, 156 S.E.2d 685, 688 (1967) (Sharp, J.); 3 J. STRONG, *supra* note 1, *Damages* § 11, at 181.

85. It is worth noting here that the action for breach of contract has its origins in tort theory in the action for fraud or deceit. “[T]respas on the case in assumpsit was made available by asserting that a breach of promise was similar to a deceit.” 2 A. CORBIN, *supra* note 1, § 429, at 472.

damages had been stricken, was contractual—the difference between the market value of the land that was promised and the market value of the land actually conveyed. The opinion noted that plaintiffs had “been made whole” within the terms of the sales contract.⁸⁶

In *Swinton* two very similar prohibitions converged; underlying that convergence was the thought that the victim of a misrepresentation (like the victim of a broken contractual promise) should have restored to him any amount he has lost by his reliance on the representation (as by reliance on the promise), but that he should not be “enriched” by any damages beyond those “foreseen” in the representation. Nor should a jury be given free rein to speculate on the amount of damages when it has at hand an objective standard: the value defendant’s representation would have had had he spoken truthfully.⁸⁷ While *Swinton* was a step removed from the language of the contract/tort forms of action analysis, the doctrinal underpinnings of that analysis remained. The court now distinguished “simple” and “aggravated” fraud as summarily as it had assigned certain claims to contract theory and others to tort. The effect was the same. Just as tortious conduct found by the court to be “dependent” was absorbed back into the contract breach allegation, the “simpler” a fraud became the more it resembled only the breach of a contractual promise.

“Simple fraud,” then, was almost a synonym for “breach of contract” as a catch phrase for courts to employ in withdrawing a plea for punitive damages beyond the reach of the jury. The problem was to distinguish between fraud that evidenced a culpable mind and for which punitive damages should be permitted and conduct that was so close to a mere broken promise that compensation was remedy enough.⁸⁸ What was the promisor’s intent at the time he made his promise? Did the promisor mean what he said when he said it? If he intended not to honor his promise, what resulting harm did he intend, or recklessly ignore? Given these shadings of intent, the distinction between “aggravated” and “simple” fraud seems realistic and useful only as a device with which the trial judge could remove in-

86. 236 N.C. at 726, 73 S.E.2d at 788.

87. See Note, *supra* note 2, at 477.

88. Certainly, it is a different thing to breach a promise than to commit fraud. A promise predicts future conduct. Fraud is a misrepresentation relating to some past or present fact. In a given contract, however, promises and representations often blend inextricably. A promise made with no intention of its future performance could be regarded as the misrepresentation of a presently existing fact. See *Reed v. Cooke*, 331 Mo. 507, 514-15, 55 S.W.2d 275, 278 (1932). The intention of the party at the time he made the promise would be a question for the jury.

volved questions from the jury. In *Swinton*, the real question was not the culpability of the defendant. Everyone—two juries, the trial judge and the North Carolina Supreme Court—agreed that the real estate salesman was guilty of reprehensible conduct.⁸⁹ Rather, it was the extent to which juries should be permitted to look behind the breach and directly at the breaching behavior. The *Swinton* court did not even wish to entertain the possibility.

Oestreicher and *Newton* can be measured by their respective treatments of *Swinton*. In *Oestreicher*, although plaintiff's punitive damages claim was restored, a result inconsistent with the result in *Swinton*, the majority was deferential toward the earlier case. In *Newton*, where no issue of fraud was before the court, the majority opinion "overruled" *Swinton*.

The question in *Oestreicher* was whether the continuing falsification of income figures upon which a term of the contract was based was such a breach as could safely be assessed by a jury for possible damages beyond payment of the unreported funds. That is, whether defendant's fraudulent conduct alone demonstrated sufficient "bad motive" or would require a showing of additional aggravation. Characterizing *Oestreicher's* plea as one seeking "damages for fraud arising from a contract arrangement,"⁹⁰ the majority considered the rules against punitive damages *both* for breach of contract *and* for fraud.

The first segment of the majority's analysis attempted to reconcile punitive damages with contract theory. The majority struggled to find in *Swinton* the rule that punitive damages may be considered when a contract breach is "'attended by some intentional wrong, insult, abuse, or gross negligence which amounts to an independent tort.'" ⁹¹ Perhaps to shore up what had only been dictum in *Swinton*, the majority turned to an Ohio decision that the *Swinton* court had considered in setting out its standards for punitive damages. In *Saberton v. Greenwald*,⁹² the Ohio Supreme Court had found in a breach of contract pleading a viable tort claim based on the fraudulent sale of a watch. A lower court had limited plaintiff buyer's remedy to the cost of the watch. Following the "independent tort" doctrine, the Ohio Supreme Court had held this limitation erroneous and had remanded for a jury's

89. 236 N.C. at 727, 73 S.E.2d at 788.

90. 290 N.C. at 133, 225 S.E.2d at 807.

91. *Id.* at 135, 225 S.E.2d at 808 (quoting 25 C.J.S. *Damages* § 120, at 1128-29 (1966)).

92. 146 Ohio St. 414, 66 N.E.2d 224 (1946).

consideration of punitive damages.⁹³ The *Oestreicher* majority made note of the theory under which the Ohio court had preserved plaintiff's punitive damages and then read *Swinton* to "adopt . . . [this] general philosophy . . . by the . . . language: . . . 'fraudulent representations alleged . . . accompanied by . . . outrageous conduct.'"⁹⁴ That is, *Oestreicher* determined that in *Swinton* North Carolina had adopted the breach + "independent tort" test.

In the second segment of analysis, the court considered whether the falsification of records by American National Stores constituted such a tort. The question then was whether the court would require further aggravation or hold, contrary to *Swinton*, that "simple" (but, by definition, intentional) fraud was itself "aggravation" enough to gain "independence" of the contract claim for the purpose of punitive damages. Was the mental state of the "simple" fraudfeasor a fit subject for the jury's consideration?

The court set up its answer by asserting: "In cases involving fraud, our Court has consistently used language such as the following: 'Punitive damages are never awarded, except in cases where there is an element either of fraud, malice, . . . or other causes of aggravation in the act or omission causing the injury.'"⁹⁵ This statement by the court is inaccurate when examined against the history of the cases. North Carolina courts had used such language in cases involving other torts, but had never spoken this way in a case where fraud was the tort alleged.⁹⁶ Indeed, if this proposition were applied to *Swinton*, that decision could be read to hold that punitive damages might flow from a finding of breach + fraud (qua tort) + fraud (qua aggravation), a *reductio ad absurdum* of the *Swinton* analysis. Far from being a "consistent" application of an old rule, the statement in *Oestreicher* was a considerable departure from history, or at least from *Swinton*, which was the only case in which the question of fraud as the "accompanying tort" had been considered. The majority did not overrule or even distinguish *Swinton*, but here in *Oestreicher* was the clear suggestion that the *Swinton* formulation in requiring an "element of aggravation" when fraud was the tort had required one element too many. However wrongly it had read its own precedent, the supreme court seemed to give notice that henceforth punitive damages would be possible even in a

93. *Id.* at 431, 66 N.E.2d at 231.

94. 290 N.C. at 135, 225 S.E.2d at 808.

95. *Id.* at 136, 225 S.E.2d at 808.

96. See Note, *supra* note 2, at 475.

suit for breach of contract when "an element of fraud" was found. Not "aggravated fraud," but, simply, "fraud." The language of the majority opinion seemed to offer a new formulation: breach + fraud (*Oestreicher*), rather than breach + fraud + aggravation (*Swinton*).⁹⁷

But if this was the new rule, it was not clearly implemented by the *Oestreicher* court. The majority seemed to lean in both directions on the question of punitive damages. It cannot be said with certainty that *Oestreicher* even required a distinct cause of action in tort. The majority spoke of punitive damages for "breach of contract actions that smack of tort because of the fraud and deceit involved" and "this type of contract case with substantial tort overtones emanating from the fraud and deceit."⁹⁸ No two trial judges are likely to agree on the point at which a breaching party's conduct begins to "smack of tort." On the other hand, it is difficult to know what to make of the statement by the *Oestreicher* majority that "[i]t seems to us that the overall allegations bring the plaintiff within the rationale of *Swinton v. Savoy Realty Co.*"⁹⁹ There is a nagging reference early in the opinion to the distinction made in *Swinton* "between aggravated and simple fraud, with punitive damages allowable in the one case and refused in the other."¹⁰⁰ The two cases seem irreconcilable—if the swindle of the aged illiterates in *Swinton* is not "aggravated," how can an "element of aggravation" be found in the facts of *Oestreicher*?

Oestreicher increased the likelihood that a contracting party who is a victim of fraud will reach the jury with a claim for punitive damages. The weakness of the case is that it failed to clear North Carolina law of the slogans and cluttered tests of the earlier cases. The court was either careless or purposely vague in its treatment of earlier law, particularly the *Swinton* decision. The uselessness of the catch phrases, introduced in *Swinton* and reinforced by *Oestreicher*, is illustrated by the fact that neither the majority nor the dissent in *Oestreicher* sought to distinguish *Swinton*. Rather, both used language from the case in support of their opposing positions. Indeed, a less than

97. Evidence that the court intended to eliminate the "aggravation" requirement may be found in the court's reliance upon a student note. See 290 N.C. at 136, 225 S.E.2d at 809 (citing Note, *supra* note 2). That note had criticized the additional requirement and had made policy arguments for the possibility of punitive damages in the instance of fraudulent breach. The note is the only authority cited for the last step in reaching the *Oestreicher* holding.

98. *Id.* at 136, 225 S.E.2d at 809.

99. *Id.* at 136, 225 S.E.2d at 808.

100. *Id.* at 133-34, 225 S.E.2d at 807 (quoting *Swinton*, 236 N.C. at 726, 73 S.E.2d at 787).

scrupulous reading of *Oestreicher* could justify the imposition of any test from "breach of contract that smacks of tort" through breach + fraud + aggravation. The majority opinion, rather than broadening the area within which the trial judge had to permit a jury to determine particular damages in a civil action, merely expanded the area within which a judge *could*, if he wished, send the question to a jury.

Newton reaffirmed the rule that punitive damages could be allowed for an independent tort that accompanies a breach of contract.¹⁰¹ The requirement that the tortious conduct be somehow aggravated was reiterated.¹⁰² The opinion of Justice Exum, however, narrowed drastically the discretion of the trial judge when that accompanying tort is fraud:

The aggravated conduct which supports an award for punitive damages when an identifiable tort is alleged may be established by allegations of behavior extrinsic to the tort itself, as in slander cases. . . . Or it may be established by allegations sufficient to allege a tort where that tort, *by its very nature*, encompasses any of the elements of aggravation. Such a tort is fraud, since fraud is, itself, one of the elements of aggravation which will permit punitive damages to be awarded. . . .

. . . .

. . . Insofar as *Swinton v. Realty Co.* requires some kind of aggravated conduct in addition to actionable fraud or makes any distinction between "simple" and "aggravated" fraud, permitting punitive damages only for the latter, that case is overruled, as are all cases so holding.¹⁰³

Justice Exum blamed the result in *Swinton* upon "a misapprehension concerning our traditional public policy which supports the doctrine of punitive damages."¹⁰⁴ The rationale for cancelling punitive damages in *Swinton*—and one of the arguments in Chief Justice Sharp's dissent in *Oestreicher*—was that once the plaintiff had been made whole within the terms of the contract, there remained no justification for punitive damages. Justice Exum emphasized that in North Carolina the policy behind punitive damages was not "to compensate the plaintiff for non-quantifiable compensatory damages"¹⁰⁵ but to punish the defendant and deter others by example. The punishment of "simple" fraud as an intentional wrongdoing was certainly within this policy.

101. 291 N.C. at 111, 229 S.E.2d at 301.

102. *Id.* at 112, 229 S.E.2d at 301.

103. *Id.* at 112-13, 229 S.E.2d at 301-02.

104. *Id.* at 113, 229 S.E.2d at 302.

105. *Id.*

Although it did so in *dictum*, the *Newton* majority established clearly that a trial judge can no longer dismiss a claim for punitive damages if the plaintiff has alleged the elements of breach + fraud. The decision was a definite move toward allowing juries to consider directly the blameworthiness of a breach of contract itself, as a *breach* and without prior filtering through a mesh of legal standards.

IV. "EXTRA-CONTRACTUAL" DAMAGES

The language of North Carolina cases confirms that the expressed purpose of punitive damages has been to burden defendant with costs that exceed plaintiff's losses, thus, by public example, deterring further such conduct. Yet, there are practical considerations that seem to cut against Justice Exum's disavowal in *Newton* of any policy of compensation in the awarding of punitive damages. The defendant's "bad mind" might cause an unpleasant mental state that the plaintiff would not have experienced if the defendant's harmful conduct had been merely careless. Mental distress on the part of the plaintiff might be seen as the other side of the defendant's "intentional wrongdoing" or "malice," so that punishing the defendant for his mental state might, at the same time, compensate the plaintiff for his.¹⁰⁶ It would be difficult to say that such damages were "punitive" if "punitive" must mean utterly non-compensatory.

In another sense, plaintiff in *Oestreicher*, if the jury now decides to award punitive damages, will have been compensated for having to bring a lawsuit to recover what was always due her under the contract and what defendant has intentionally and wrongfully withheld. Defendant will have been made to pay plaintiff for the extra effort to which plaintiff has been put. The "punitive" damages sanctioned in *Oestreicher* were not based upon the purely punitive, exemplary, non-compensatory policies stated by Justice Exum in *Newton*. By its use of the term "punitive damages," the *Oestreicher* majority seemed to suggest damages that were compensatory but that, at the same time, were not damages of the sort usually awarded for the non-performance of contractual obligations. The dual aspect of the "punitive" damages approved in *Oestreicher*—punitive and compensatory—reflected three common-sense equities noted by the majority: (1) there is little deter-

106. See D. DOBBS, *supra* note 41, § 3.9, at 205. Professor Dobbs notes that some courts have regarded such damages as compensation for "dignitary invasions." *Id.*

rent against fraud in the contractual arrangement if all that the perpetrator stands to lose is that which he had promised under the contract in the first place; (2) compensating plaintiff by reference to the terms of the contract will not make him entirely whole; and (3) any award will be lessened by the expenses of litigation.¹⁰⁷

Punitive damages, in the sense intended by Justice Exum in *Newton*, constitute only one of several classes of special damages generally denied the plaintiff who asserts rights that are his only by virtue of a contract.¹⁰⁸ The meaning of "compensation" may vary depending upon whether a plaintiff is suing in contract or in tort. The policy of compensation in a contract action is, in general terms, to provide the complaining party with those benefits that would have been his had the other party performed.¹⁰⁹ In the case of an insurance contract such as the one in *Newton*, performance amounts to payment of the amount of the policy. *Newton* complained, however, that he had to borrow money as a result of his inability to collect the \$5,500 due him under the policy and that interest payments on the borrowed money represented losses that he would not have sustained but for defendant's refusal to make timely payment. In addition, an insured, like *Newton*, may be forced to surrender mortgaged property or incur the expenses of defending against suits brought by creditors, losses that flow from the breach of the insurance contract but for which the face value of the policy is inadequate compensation. It has been held generally that "in the absence of special circumstances in the contemplation of the parties at the time of the making of the contract," damages for the failure or delay of an insurer to pay are limited to the amount due under the policy, with interest.¹¹⁰ Recovery of such consequential damages requires a showing that the possibility of such damages was "foreseen" by both insurer and insured.¹¹¹ For many of the same reasons, the

107. 290 N.C. at 136, 225 S.E.2d at 809.

108. D. DOBBS, *supra* note 41, § 12.3, at 804, 812; J. MCCARTHY, PUNITIVE DAMAGES IN BAD FAITH CASES § 2.2, at 12 (1976). The discussion that follows depends heavily on McCarthy's analysis of the California bad faith action. McCarthy's book is cited by both the majority and dissent in *Oestreicher*, 290 N.C. at 137, 147, 225 S.E.2d at 809, 815, and by the majority in *Newton*, 291 N.C. 105, 111, 229 S.E.2d 297, 301.

109. J. MCCARTHY, *supra* note 108, § 2.25, at 79; RESTATEMENT OF CONTRACTS § 329, Comment a (1932).

110. Annot., 47 A.L.R.3d 314, 326 (1973); *accord*, J. MCCARTHY, *supra* note 108, § 2.2, at 13.

111. RESTATEMENT OF CONTRACTS § 330 (1932); *see* 3 J. STRONG, *supra* note 1, *Contracts* § 29.3; Annot., 47 A.L.R.3d 314, 326-31 (1973); *cf.* D. DOBBS, *supra* note 41, § 12.3 (recognizing but criticizing the framing of the rule in terms of foreseeability).

insured has little hope of recovering damages for mental distress brought on by the breakdown of his insurance coverage.¹¹² In most cases, regardless of the cause of action, the prevailing party cannot recover attorney's fees.¹¹³ It is too speculative to say what such special damages might have been and safer for the jury to stay within the limits of the contract where presumably the plaintiff, if he was able, bargained any such otherwise "unforeseeable" risks onto the defendant.¹¹⁴ In contrast, "compensation" of the tort victim is the restoration of the plaintiff to a position as near as possible to that which he occupied before the wrong occurred.¹¹⁵ A successful contract plaintiff is to be placed where he might have been; a successful tort plaintiff is to be placed where he was. The jury is not to be trusted to search for damages in the vague realms of "might have been," but is to be held close to the terms of the contract. Again, this is the theory. The practical effect of this dichotomy is that the pleader in tort stands a better chance of having his consequential economic losses made good, his mental well-being repaired, and perhaps even his attorney's fees remitted.¹¹⁶

V. BAD FAITH

In *Oestreicher*, it was decided that a defendant might be liable for damages beyond the amount due under the terms of the contract upon a showing of defendant's intent to deceive and induce reliance upon his deceit. *Oestreicher* alleged that defendant had lied to her and that it was this lie that breached the contract. She asserted that the lie, in addition to being a breach, was a tort. In assessing damages, this "tortious breach" can be contrasted to an entirely innocent breach—a misunderstanding of the scope of the obligation or genuine inability to perform. In the latter, there is no "culpable mind" at work. What damages, however, should be visited upon the defendant who has not

112. J. MCCARTHY, *supra* note 108, § 2.2, at 14; see 5 A. CORBIN, *supra* note 1, § 1076; D. DOBBS, *supra* note 41, § 12.4, at 819; RESTATEMENT OF CONTRACTS § 341 (1932).

113. D. DOBBS, *supra* note 41, § 3.8, at 194; J. MCCARTHY, *supra* note 108, § 2.28, at 81.

114. *Koufos v. Czarnikow, Ltd. (The Heron II)*, [1969] 1 A.C. 350, 385.

115. J. MCCARTHY, *supra* note 108, § 2.25, at 79; RESTATEMENT OF TORTS § 901, Comment a (1939).

116. Attorney's fees are sometimes awarded under the guise of "punitive damages" so that the plaintiff who is permitted to assert a tort claim is a step ahead toward these damages as well as the other special damages. D. DOBBS, *supra* note 41, § 3.8, at 197.

induced plaintiff's reliance with a promise that he never intended to perform (*i.e.*, a lie), but whose failure or refusal to perform is based nonetheless upon his own interest rather than upon honest mistake or inability? The state of mind in such a middle ground breach has sometimes been designated bad faith.¹¹⁷

A number of jurisdictions have recognized that a bad faith breach of an insurance contract may be an appropriate occasion for "extra-contractual" remedies. The damages that legislatures and courts have extended to plaintiffs in this situation seem to be found in a gray policy zone somewhere between compensation of a plaintiff whose suffering has been particularly burdensome and punishment of an unusually blameworthy defendant. Georgia, for example, provides by statute that an insurer who breaches in bad faith his obligation to the insured is liable for plaintiff's attorney's fees as well as for a "penalty" of up to twenty-five percent of the insurer's contractual liability.¹¹⁸ An Indiana court has imposed punitive damages for "oppressive conduct" in a case where the insurer refused payment under policy provisions found by the jury to be "so clear that the insurers could not dispute the amount of liability in good faith."¹¹⁹ At least a portion of the "punitive damages" awarded in that case may have been intended by the court as compensation for financial losses to plaintiff's business that came as a consequence of defendant's refusal to pay.¹²⁰ Plaintiffs suing a breaching insurer in California have recovered "for all detriment proximately resulting" from his conduct,¹²¹ including economic

117. *Bundy v. Commercial Credit Co.*, 202 N.C. 604, 607, 163 S.E. 676, 677 (1932).

118. GA. CODE ANN. § 56-1206 (1971) ("Term 'bad faith,' as used in Code § 56-1206 means any frivolous and unfounded refusal in law or in fact to comply with demand of policy holder to pay according to terms of policy." *Royal Ins. Co. v. Cohen*, 105 Ga. App. 746, 747, 125 S.E.2d 709, 711 (1962)); *cf.* MONT. REV. CODES ANN. §§ 40-2617, -4011, -4034 (1961) (Statute provides for fine or imprisonment for delay in payment of insurance proceeds upon written proof of loss. Punitive damages have been awarded under this statute where the insurer's failure to pay promptly was found to be oppressive, malicious or fraudulent. *State ex rel. Larson v. District Court*, 149 Mont. 131, 423 P.2d 598 (1967)).

119. *Vernon Fire & Cas. Ins. Co. v. Sharp*, — Ind. App. —, 316 N.E.2d 381, 384 (1974). An Ohio court has held that an insurer must act in good faith to protect the interests of its insured. *Kirk v. Safeco Ins. Co.*, 28 Ohio Misc. 44, 273 N.E.2d 919 (Franklin County C.P. 1970). Punitive damages were awarded when the court found defendant insurer's refusal to pay to be such "a breach of contract amounting to a wilful, wanton and malicious tort." *Id.* at —, 273 N.E.2d at 921.

120. — Ind. App. —, —, 316 N.E.2d 381, 384 (1974).

121. *Fletcher v. Western Nat'l Life Ins. Co.*, 10 Cal. App. 3d 376, 401-02, 89 Cal. Rptr. 78, 93-94 (1970).

loss,¹²² emotional distress¹²³ and attorney's fees,¹²⁴ as well as punitive damages.¹²⁵

Legislatures and courts have rested these results on the nature of the insurance contract.¹²⁶ It has been noted that bargaining power between insurer and insured is vastly out of balance:¹²⁷ often, the would-be insured has been handed a ream of "fine print" documentation on a take-it-or-leave-it basis. To the extent that he has bargained at all, however, the policyholder has bargained for the exact financial security and peace of mind that the insurer's breach will deny him.¹²⁸ Loss of this peace of mind is clearly within the contemplation of both parties at the time the insurance policy is signed.

The rule denying damages for emotional distress brought on by a breach has been excepted to when defendant has breached an agreement that had "personal rather than pecuniary purposes in view."¹²⁹ In California, at least, the insurance contract has been classified as such a "personal contract."¹³⁰ In his agreement with the insurance company, the insured has sought no commercial advantage. Further, the very purpose of insurance coverage is to provide for unpredictable risks, that is, those economic losses that might have resulted if plaintiff had not secured insurance. It could be argued that the losses that have now resulted as a consequence of the insurer's refusal to pay are the very losses that were contemplated by the contracting parties.

122. See *Silberg v. California Life Ins. Co.*, 11 Cal. 3d 452, 521 P.2d 1103, 113 Cal. Rptr. 711 (1974) (loss of business); *Gruenberg v. Aetna Ins. Co.*, 9 Cal. 3d 566, 510 P.2d 1032, 108 Cal. Rptr. 480 (1973) (loss of earnings from business; costs of defense of lawsuits brought by creditors); *Fletcher v. Western Nat'l Life Ins. Co.*, 10 Cal. App. 3d 376, 89 Cal. Rptr. 78 (1970) (loss of investment property).

123. See cases cited note 122 *supra*.

124. See *Mustachio v. Ohio Farmers Ins. Co.*, 44 Cal. App. 3d 358, 118 Cal. Rptr. 581 (1975). See also *McDowell v. Union Mut. Life Ins. Co.*, 404 F. Supp. 136 (C.D. Cal. 1975).

125. See *Silberg v. California Life Ins. Co.*, 11 Cal. 3d 452, 521 P.2d 1103, 113 Cal. Rptr. 711 (1974) (dictum); *Fletcher v. Western Nat'l Life Ins. Co.*, 10 Cal. App. 3d 376, 89 Cal. Rptr. 78 (1970). See also CAL. CIV. CODE § 3294 (West 1970).

126. J. MCCARTHY, *supra* note 108, § 1.1, at 2-3, § 2.1, at 8-9.

127. *Id.* § 2.20, at 62.

128. *Crisci v. Security Ins. Co.*, 66 Cal. 2d 425, 434, 426 P.2d 173, 179, 58 Cal. Rptr. 13, 19 (1967). See also D. DOBBS, *supra* note 41, § 12.4, at 820 n.22.

129. D. DOBBS, *supra* note 41, § 12.4, at 819; see, e.g., *Chelini v. Nieri*, 32 Cal. 2d 480, 196 P.2d 915 (1948) (contract to bury a family member); *Mitchell v. Shreveport Laundries, Inc.*, 61 So. 2d 539 (La. App. 1952) (contract to launder wedding garments in time for the ceremony); 11 C.J.S. *Breach of Marriage Promise* § 40(b), at 809 n.65 (1938 & Cum. Supp. 1976).

130. *Crisci v. Security Ins. Co.*, 66 Cal. 2d 425, 426 P.2d 173, 58 Cal. Rptr. 13 (1967); J. MCCARTHY, *supra* note 108, § 2.4, at 18.

The California Supreme Court has avoided the difficulties of this "contemplation" question by its willingness to imply a "covenant of good faith and fair dealing"¹³¹ between the insurance company and the policy holder—a covenant that the insurer "will do nothing to deprive the insured of the benefits of the policy."¹³² Through a line of decisions of that court since 1958, that personal covenant has been generalized into a duty—wholly apart from the obligations under the contract—of good faith treatment of the insured's interests. In *Gruenberg v. Aetna Insurance Co.*,¹³³ the court described this duty:

It is the obligation, deemed to be imposed by the law, under which the insurer must act fairly and in good faith in discharging its contractual responsibilities. Where in so doing, it fails to deal fairly and in good faith with its insured by refusing, without proper cause, to compensate its insured for a loss covered by the policy, such conduct may give rise to a cause of action in tort for breach of an implied covenant of good faith and fair dealing.¹³⁴

Furthermore, good faith on the part of the insurer required that any ambiguity in the policy be resolved in favor of the insured.¹³⁵ In California, then, bad faith on the part of an insurer gives rise to a claim for relief sounding in tort capable of bringing in damages—economic loss, mental distress, attorney's fees and punitive damages—normally beyond the reach of a plaintiff whose contract rights have been violated.

The *Newton* majority acknowledged the special nature of insurance contracts:

[B]ecause of the great disparity of financial resources which generally exists between insurer and insured and the fact that insur-

131. *Crisci v. Security Ins. Co.*, 66 Cal. 2d 425, 430, 426 P.2d 173, 176, 58 Cal. Rptr. 13, 16 (1967). The same or similar language is used by the California Supreme Court in *Silberg v. California Life Ins. Co.*, 11 Cal. 3d 452, 460, 521 P.2d 1103, 1110, 113 Cal. Rptr. 711, 716 (1974); *Gruenberg v. Aetna Ins. Co.*, 9 Cal. 3d 566, 573, 510 P.2d 1032, 1036-37, 108 Cal. Rptr. 480, 484-85 (1973); *Fletcher v. Western Nat'l Life Ins. Co.*, 10 Cal. App. 3d 376, 401, 89 Cal. Rptr. 78, 93 (1970).

132. *Fletcher v. Western Nat'l Life Ins. Co.*, 10 Cal. App. 3d 376, 401, 89 Cal. Rptr. 78, 93 (1970). The covenant has been described elsewhere as "an implied covenant of good faith and fair dealing . . . that neither party will do anything which will injure the rights of the other to receive the benefits of the agreement." *Gruenberg v. Aetna Ins. Co.*, 9 Cal. 3d 566, 573, 510 P.2d 1032, 1036, 108 Cal. Rptr. 480, 484 (1973) (quoting *Comunale v. Traders & Gen. Ins. Co.*, 50 Cal. 2d 654, 658, 328 P.2d 198, 200 (1958)).

133. 9 Cal. 3d 566, 510 P.2d 1032, 108 Cal. Rptr. 480 (1973).

134. *Id.* at 573, 510 P.2d at 1037, 108 Cal. Rptr. at 485. The case also described the conduct that breached the tort duty as an "unreasonable withholding" of insurance proceeds. *Id.* In another case, the tort duty was held to be breached by an "unwarranted refusal to pay." *Crisci v. Security Ins. Co.*, 66 Cal. 2d 425, 430, 426 P.2d 173, 176, 58 Cal. Rptr. 13, 16 (1967).

135. J. MCCARTHY, *supra* note 108, § 2.20, at 66.

ance companies, like common carriers and utilities, are regulated and clearly affected with a public interest, we recognize the wisdom of a rule which would deter refusals on the part of insurers to pay valid claims when the refusals are both unjustified and in bad faith.¹³⁶

In his complaint, Newton had alleged "the failure and refusal of defendant to properly settle and pay plaintiff" the insurance proceeds "to which he was entitled." He further alleged that the insurer's awareness of plaintiff's "desperate need" for the insurance proceeds without which he could no longer "effectively carry on his business" made defendant's refusal to perform "heedless, wanton and oppressive."¹³⁷ In his appellate brief, Newton had cited to the supreme court the California cases that had established the implied-in-law duty of good faith. Newton urged that the insurance company's "unjustified failure to pay"¹³⁸ amounted to "oppressive conduct constituting a tort."¹³⁹ Such conduct should give rise to liability for punitive damages, the appellant argued. Beyond that, he asked that the North Carolina Supreme Court declare "a rule . . . permitting recovery of all proximately caused detriment in a single cause of action."¹⁴⁰

The issue directly before the court was whether punitive damages could be awarded for the insurer's bad faith. Implicit in that inquiry was the question of the validity of bad faith as a tort cause of action. The two questions were not co-extensive. A denial of punitive damages did not have to be a denial of Newton's ability to claim in tort. Short of punitive damages, a bad faith claim had the potential for generating "extra-contractual" recovery of economic losses, damages for mental distress and attorney's fees. The court need not have limited itself to the stark choice between punitive damages at one end of the spectrum and the contractual remedy at the other. The complaint alleged financing arrangements with creditors under which interest

136. 291 N.C. at 116, 229 S.E.2d at 303. It is worth noting here that the North Carolina Supreme Court has imposed a tort duty upon one party to a contract in the case of a banker who has wrongfully refused to pay on a depositor's check. The possibility of punitive damages was acknowledged. *Woody v. First Nat'l Bank*, 194 N.C. 549, 552, 140 S.E. 150, 152 (1927). The same policies applied by Justice Exum in *Newton* to insurers, public utilities and conveyancers were noted with regard to banks in *Woody*. *Id.* at 555, 140 S.E. at 154. The analogy between banks and insurers seems to be a sound one.

137. 291 N.C. at 110-11, 229 S.E.2d at 300.

138. Plaintiff Appellant's Brief at 4, 27 N.C. App. 168, 218 S.E.2d 231 (1975) (quoting G. COUCH, *CYCLOPEDIA OF INSURANCE LAW*, § 58.9, at 13 (2d ed. 1966)).

139. *Id.* at 3.

140. *Id.* at 14 (quoting *Fletcher v. Western Nat'l Life Ins. Co.*, 10 Cal. App. 3d 376, 402, 89 Cal. Rptr. 78, 94 (1970)).

charges were mounting as long as Newton's insurance claim remained unpaid. These were damages recoverable under a tort theory. Denied punitive damages in the strict sense, Newton might also have sought damages for mental distress occasioned by the company's refusal to pay and the consequent economic burden. In *Oestreicher*, the majority had stated that one of the purposes of what it called "punitive" damages was to provide some recompense for the plaintiff who had incurred legal expenses in the course of vindicating a contract right with which the defendant had wrongfully interfered.¹⁴¹ The relationship of trust between the parties to an insurance contract and the nearly helpless position of the insured at the time when he most needs help provide even stronger arguments for the awarding of attorney's fees in the case of an insurer's interference with its policyholder's rightful recovery. The policies outlined in *Oestreicher* as well as the doctrinal clarity insisted upon in *Newton* would have been well met by the array of compensations available to the plaintiff who proves bad faith. Indeed, the majority in *Newton* clearly acknowledged these other "extra-contractual" remedies, although the idea was not fully developed. In exploring the concept of bad faith, Justice Exum went beyond the category of punitive damages and spoke more generally of "allowing tort damages in insurance cases."¹⁴² The first California case cited by the court is not a punitive damages case at all, but a case in which an insured was awarded damages for mental distress suffered as a result of her insurer's bad faith refusal to settle a claim.¹⁴³

In *Silberg v. California Life Insurance Co.*,¹⁴⁴ the California Supreme Court had noted the distinction between punitive and other "extra-contractual" damages:

It does not follow that because plaintiff is entitled to compensatory damages [for a bad faith claim] that he is also entitled to exemplary damages. In order to justify an award of exemplary damages, the defendant must be guilty of oppression, fraud or malice. He must act with the intent to vex, injure or annoy, or with a conscious disregard of the plaintiff's rights. While we have concluded that defendant violated its duty of good faith and fair dealing, this alone does not necessarily establish that defendant acted with the requisite intent to injure plaintiff.¹⁴⁵

141. 290 N.C. at 136, 225 S.E.2d at 806.

142. 291 N.C. at 115, 229 S.E.2d at 303 (emphasis added).

143. *Id.* (citing *Crisci v. Security Ins. Co.*, 66 Cal. 2d 425, 426 P.2d 173, 58 Cal. Rptr. 13 (1967)).

144. 11 Cal. 3d 452, 521 P.2d 1103, 113 Cal. Rptr. 711 (1974).

145. *Id.* at 462-63, 521 P.2d at 1110, 113 Cal. Rptr. at 718.

In effect, California had required the familiar "element of aggravation." The pleader who sought punitive damages for insurer's bad faith must allege: breach + independent tort (bad faith) + aggravation ("oppression, fraud or malice"). The *Newton* court could have decided the only issue before it by stating simply that it had failed to find the requisite aggravation. Conversely, the California court had made it clear that a showing of aggravation was not prerequisite to recovery of other special damages.¹⁴⁶ Even after disarming *Newton* of his punitive damages claim, the court remained in a position to equip him with a tort cause of action.

Newton was sent back to the trial court with only his contract rights intact. The court went further than was necessary to decide the punitive damages question and held that "the allegations in the complaint of oppressive behavior by defendant in breaching the contract are insufficient to plead any recognizable tort."¹⁴⁷ At the same time, however, Justice Exum held out hope that a cause of action in tort for bad faith would be upheld if the necessary elements were before the court.¹⁴⁸

Justice Exum looked to the California rulings for their definition of bad faith. The California plaintiff need show only that defendant insurer lacked a reasonable justification for his refusal to pay. In *Silberg*, for example, the insurer defended on the ground that it had reasonably withheld payments while awaiting the outcome of a workmen's compensation proceeding that could have compensated plaintiff fully. The California Supreme Court held that defendant should have paid the insured the full amount of the policy and attached a lien to any future workmen's compensation recovery. Defendant's stance in waiting two years to see if it would be required to perform was held to "deprive the insured of the benefits of the policy." Despite the possibility that by the strict terms of the insurance agreement defendant

146. *Gruenberg v. Aetna Ins. Co.*, 9 Cal. 3d 566, 510 P.2d 1032, 108 Cal. Rptr. 480 (1973).

147. 291 N.C. at 114, 229 S.E.2d at 302.

148. "We need not now decide whether a bad faith refusal to pay a justifiable claim by an insurer might give rise to punitive damages." *Id.* at 115, 229 S.E.2d at 303.

The question had been raised earlier in *King v. Insurance Co. of N. Am.*, 273 N.C. 396, 159 S.E.2d 891 (1968), where plaintiff insured sought punitive damages, alleging that defendant insurer had exercised bad faith in its refusal, first, to defend insured against a counterclaim and, second, to pay the counterclaim when insured lost at trial. The supreme court held that "there is no allegation of facts giving rise to a right of action for deceit or any other tort" and, therefore, limited plaintiff to his remedies under the contract. *Id.* at 398, 159 S.E.2d at 893. In *Newton*, Justice Exum distinguished *King* as a case in which the allegation of bad faith was unsupported by facts as a matter of law. 291 N.C. at 115, 229 S.E.2d at 303.

might never have been compelled to pay, his conduct was held to be unreasonable.¹⁴⁹

Newton alleged an "unjustified failure to pay."¹⁵⁰ The *Newton* majority responded: "Insurer's knowledge that plaintiff was in a precarious financial position in view of his loss does not in itself show bad faith on the part of the insurer in refusing to pay the claim, or for that matter, that the refusal was unjustified."¹⁵¹ If *Newton* did not mean to approve the California definition of bad faith, the North Carolina court made extensive use of the term without providing a definition of its own. The majority gave only one indication that it might have had in mind something other than the California definition:

Had plaintiff claimed that after due investigation by defendant it was determined that the claim was valid and defendant nevertheless refused to pay or that defendant refused to make any investigation at all, and that defendant's refusals were in bad faith with an intent to cause further damage to plaintiff, a different question would be presented.¹⁵²

But *which* question: the question of whether a bad faith claim had been stated, or whether punitive damages could be awarded in addition to other damages available for that claim? If *Newton* established that allegations of either (1) investigation + valid claim + refusal to pay, or (2) no investigation + refusal to pay are sufficient to state a valid bad faith claim, but that for *punitive damages* one needs the *additional* allegation of "intent to cause further damage to plaintiff," then the court was correct in upholding the denial of punitive damages. The majority, however, may have been inconsistent with its own guidelines in holding that "this case involves no tort."¹⁵³ In complaining of an "unjustified failure to pay" and "a refusal to properly settle,"¹⁵⁴ *Newton* was saying, at least implicitly, that Standard *had* investigated his claim—in the year since the burglary—*had* found it valid and *still* refused to make good the claim.

Admittedly, *Newton* had not alleged the insurer's intent to cause him further damage, but that "element of aggravation" is essential only to the punitive damages claim and not to the bad faith cause of action itself. The court does not suggest what damages might be available

149. 11 Cal. 3d at 457, 521 P.2d at 110, 113 Cal. Rptr. at 714.

150. See text accompanying note 138 *supra*.

151. 291 N.C. at 115, 229 S.E.2d at 303.

152. *Id.* at 115-16, 229 S.E.2d at 303.

153. *Id.* at 114, 229 S.E.2d at 302.

154. See text accompanying notes 137-38 *supra*.

to plaintiff if the insurer had breached "with a conscious disregard of the plaintiff's rights" without the insurer's specific intent to injure plaintiff, the more likely case between a large foreign insurance company and a relatively anonymous policyholder. How the insured would go about proving the company's actual intent to harm him remains a mystery, unless the insurer could be held to have intended the probable consequences of his refusal to comply with the contract.

VI. CONCLUSION

While questions remain unanswered, some relatively certain assessments of the two cases can be made. In *Oestreicher*, the North Carolina Supreme Court relaxed its "aggravation" standard for punitive damages recovery by a party complaining of a fraudulent breach of contract. At the same time it expressed a pragmatic concern for various expenses to plaintiff resulting from such a wrongful breach. The formula breach + fraud (as accompanying tort + inherent element of aggravation) = punitive damages is clearly accepted. In *Newton* the court suggested the possibility of an action for an insurer's breach of an implied tort duty of good faith dealing. Acceptance of this tort duty into North Carolina law would give a complaining policyholder an avenue to punitive damages if he can plead and prove breach + bad faith (as accompanying tort) + aggravation. Further, the ability to proceed under a theory of breach of a tort duty of good faith may enable recovery of special damages heretofore not available in North Carolina for breach of contract, even an insurance contract.

If a plaintiff in a North Carolina court can recover economic losses that were a consequence of an insurance company's unreasonable failure to honor its contractual obligations to him—damages for emotional distress resulting from this failure, and the attorney's fees expended in redressing it—whether these recoveries are characterized as "punitive" or as new forms of compensatory damages, the plaintiff has gained considerable ground. Perhaps even more significant is the fact that in these two holdings, the North Carolina court has rebalanced the relationship between trial judge and jury, restricting the judge's discretion to deny certain damage claims and granting the jury new freedom in the design of a remedy.

SEAN DEVEREUX

