S272113

IN THE SUPREME COURT OF CALIFORNIA

MICHAEL R. RATTAGAN,
Plaintiff and Appellant,

v.

UBER TECHNOLOGIES, INC.,
Defendant and Respondent.

ON CERTIFICATION FROM THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT
CASE NO. 20-16796

APPLICATION FOR LEAVE TO FILE AMICUS BRIEF; AMICUS CURIAE BRIEF OF THE CHAMBER OF COMMERCE OF THE UNITED STATES OF AMERICA IN SUPPORT OF RESPONDENT

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APPLICATION FOR LEAVE TO FILE AMICUS BRIEF

Under California Rules of Court, rule 8.520(f)(1), the Chamber of Commerce of the United States of America requests permission to file the attached *amicus curiae* brief in support of defendant and respondent Uber Technologies, Inc.[1]

The Chamber is the world's largest business federation. It represents approximately 300,000 direct members and indirectly represents the interests of over 3 million companies and professional organizations of every size, in every industry sector, and from every region of the country. An important function of the Chamber is to represent the interests of its members in matters before Congress, the Executive Branch, and the courts. To that end, the Chamber regularly files *amicus curiae* briefs in cases, like this one, that raise issues of concern to the Nation's business community.

The Chamber has many members based in California and even more members who conduct substantial business in California. As a result, the Chamber has a significant interest in the sound and equitable development of California contract and tort law. The Chamber has appeared as *amicus curiae* many times before this Court and the California Courts of Appeal.

The economic loss rule prevents a party to a contract from recovering tort damages when it suffers only economic loss. This

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[1] No party or counsel for a party authored this proposed brief in whole or in part, and no person or entity other than amici, their members, or their counsel made any monetary contribution intended to fund the preparation or submission of this proposed brief. (See Cal. Rules of Court, rule 8.520(f)(4).)

rule is important to the Chamber's members because it helps prevent the so-called "tortification" of contract law. When negotiating contracts, businesses depend upon the predictability of contract law and its limitations on damages. Allowing plaintiffs to transform contract disputes into tort actions alters the terms of the bargain and dramatically increases the risk to contracting parties.

The Chamber is uniquely situated to assist the Court in understanding the negative impact that blurring the line between contracts and torts will have on the business community. The Chamber thus offers this *amicus* brief to explain why this Court should decline to create an exception to the economic loss rule for fraudulent concealment claims. Such an exception would swallow the rule, because plaintiffs will attempt to convert contract disputes into tort claims merely by pointing to omissions that they believe are material. This will undermine the important distinction between contract law and tort law, sowing uncertainty in the marketplace.

January 30, 2023

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AMICUS CURIAE BRIEF

INTRODUCTION

This case concerns the boundary between contract and tort law. Marking that boundary, the longstanding economic loss rule facilitates commercial transactions by keeping them efficient and predictable. Businesses depend upon the predictability of contracts, in which the parties allocate risks in advance and damages are normally limited to making the contracting parties whole. Contract law allows parties in privity to minimize their exposure to uncertainty and risk by agreeing to limitations on liability and opting out of certain remedies altogether. Unlike tort law, moreover, contract law is not based on fault but instead prizes the optimal use of resources and allocation of risk. This means that parties in privity are not penalized with punitive damages for breaching their contracts, which permits them instead to find the most efficient ways to allocate their resources.

For these reasons, under the economic loss rule, courts generally prohibit plaintiffs from recovering in tort for contract breaches that cause only economic losses. This rule is subject to very narrow exceptions. And courts must be careful not to permit the exceptions to swallow the rule. If the line between contracts and torts becomes too blurred—if predictable contract disputes routinely morph into unpredictable tort actions with windfall recoveries—the results will be a chilling of commercial activity and a gradual erosion of the legal norms underpinning contract law.

This Court should thus reject a new exception to the economic loss rule for fraudulent concealment claims. The tort of fraudulent concealment attaches liability to *omissions*—the failure to make certain statements. Because there is no limit to the things a person or entity does *not* say, endorsing a fraudulent concealment exception to the economic loss rule would threaten businesses with unlimited potential liability for every undisclosed idea, statement, or viewpoint that, in hindsight, a plaintiff alleges was material to a transaction.

This Court's cases do not support such an extension. In *Robinson Helicopter Co., Inc. v. Dana Corp.* (2004) 34 Cal.4th 979, 991, 993 (*Robinson Helicopter*), this Court created a "narrow" exception to the economic loss rule for *affirmative* fraudulent misrepresentations that are "separate from" the breach of contract and accompanied by risk of "personal damages independent of the plaintiff's economic loss." But the Court's reasoning does not support extending that exception to fraudulent *concealment*.

Unlike fraudulent concealment claims, which may rest on an unlimited scope of alleged omissions, affirmative fraud is inherently limited to actual misstatements made by a defendant to a plaintiff. A plaintiff alleging affirmative fraud can (and must) specifically identify the speaker and the statement. Litigants can then focus their dispute on whether the statement was true or false, whether the defendant intended to deceive, and whether the plaintiff actually and justifiably relied on the statement. Allowing tort remedies in that context does little

damage to the purpose of the economic loss rule: maintaining uniformity and predictability in commercial transactions. Businesses know and can control the affirmative statements they make, and they can anticipate potential liability and damages based on their own affirmative conduct.

By contrast, an exception to the economic loss rule for concealment-based claims would effectively eviscerate that fundamental rule and, with it, the critical separation of contract and tort law. Inviting gamesmanship, such an exception would inject chaos into commercial transactions. Plaintiffs who have suffered only economic loss would inevitably allege tagalong concealment claims in countless breach-of-contract cases. Placing businesses at risk of tort liability for every undisclosed viewpoint will inject substantial uncertainty and unpredictability into the contractual relationships on which commerce depends. By reducing the predictability of litigation damages, a fraudulent concealment exception to the economic loss rule would create disorder in the marketplace; harm businesses' goodwill and reputation; flood the courts with drawn out, fact-intensive cases; decrease the likelihood of case settlement; and disrupt other areas of California law.

Such major erosion of the bedrock economic loss rule would cause a watershed reordering of contract and tort law. As this Court has recognized, any significant restriction on the economic loss rule should be made—if at all—by the Legislature, which can better consider the competing interests and significant market disruption.

LEGAL ARGUMENT

I. The economic loss rule maintains predictability and fairness by keeping tort law and contract law separate.

Contract law and tort law have fundamentally different objectives. "Contract law exists to enforce legally binding agreements between parties." (*Applied Equipment Corp. v. Litton Saudi Arabia Ltd.* (1994) 7 Cal.4th 503, 514 (*Applied Equipment*); see also *Tameny v. Atlantic Richfield Co.* (1980) 27 Cal.3d 167, 176 (*Tameny*) [explaining that contract actions " 'are created to protect the interest in having promises performed' " and that the duties of conduct that give rise to them are based " 'upon the will or intention of the parties' "].) Contract damages thus provide a remedy for a contracting party's disappointed expectations caused by a breach (see Goodman et al., *A Guide to Understanding the Economic Loss Doctrine* (2019) 67 Drake L.Rev. 1, 28) and are designed to put the aggrieved party in "as good a position as if the other party had fully performed," but no better (Cal. U. Com. Code, § 1305, subd. (a)).

Contract damages must be foreseeable—that is, they must be "likely to result" from the breach "in the ordinary course of things." (Civ. Code, § 3300.) In other words, contract damages "must reasonably be supposed to have been within the contemplation of the parties when making the contract as the probable result of a breach." (*Christensen v. Slawter* (1959) 173 Cal.App.2d 325, 334.) Justice Holmes said it best: "The only universal consequence of a legally binding promise is, that the law makes the promisor pay the damages if the promised event

does not come to pass." (Holmes, Jr., *The Common Law* (1881) p. 301.)

These principles properly promote "efficient breaches," which occur when a party to a contract chooses to breach the contract and pay the resulting contract damages, because breaching the contract is more efficient than performance. (See *Huynh v. Vu* (2003) 111 Cal.App.4th 1183, 1198–1199 (*Huynh*).) Contract law "commends" even bad-faith breaches, because they promote economic efficiency if the "pecuniary gains" of the bad-faith breach exceed the liability for it. (Landsdorf, *California's Detortification of Contract Law: Is the* Seaman*'s Tort Dead?* (1992) 26 Loyola L.A. L.Rev. 213, 218; see *Freeman & Mills, Inc. v. Belcher Oil Co.* (1995) 11 Cal.4th 85, 106 (*Freeman*) (dis. & conc. opn. of Mosk, J.) [explaining that an intentional breach of contract is "viewed as a morally neutral act"].) Punitive damages are thus generally unavailable for breach of contract. (*Applied Equipment*, *supra*, 7 Cal.4th at p. 514; accord, *Barnes v. Gorman* (2002) 536 U.S. 181, 187 [122 S.Ct. 2097, L.Ed.2d 230]; Rest.2d Contracts, § 355.)

Tort law, by contrast, "is designed to vindicate social policy." (*Applied Equipment*, *supra*, 7 Cal.4th at p. 514; see *Tameny*, *supra*, 27 Cal.3d at p. 176 [explaining that tort actions " 'are created to protect the interest in freedom from various kinds of harm' " and that the duties of conduct that give rise to them " 'are imposed by law.' "].) Unlike contract law, tort law is based on fault. Reflecting that difference, tort remedies seek both to compensate the victim and, in appropriate cases, punish

the wrongdoer. (See *East River S.S. Corp. v. Transamerica Delaval, Inc.* (1986) 476 U.S. 858, 871 [106 S.Ct. 2295, 90 L.Ed.2d 865] (*East River*); Rest.2d Torts, § 901 & com. a, p. 451). Tort law therefore allows for the recovery of punitive damages when the defendant is sufficiently culpable. Punitive damages "by definition are not intended to compensate the injured party, but rather to punish . . . and to deter."[2] (*City of Newport v. Fact Concerts, Inc.* (1981) 453 U.S. 247, 266–267 [101 S.Ct. 2748, 69 L.Ed.2d 616]; see Rest.2d Torts, § 901 com. c, p. 452 ["the law of torts, which was once scarcely separable from the criminal law, has within it elements of punishment or deterrence"].)

The economic loss rule provides an important " 'line of demarcation between tort theory and contract theory.' " (*Aas v. Superior Court* (2000) 24 Cal.4th 627, 640 (*Aas*), superseded by statute on another ground as stated in *Rosen v. State Farm General Ins. Co.* (2003) 30 Cal.4th 1070, 1079–1080.) It maintains the separation of contract and tort law by barring tort remedies when a plaintiff has suffered no injury to himself or his property but has suffered only economic loss caused by a breach of contract. (See *East River*, *supra*, 476 U.S. at pp. 866–870; *Robinson Helicopter*, *supra*, 34 Cal.4th at pp. 984, 988.) A plaintiff can still maintain a claim against the party with whom he or she chose to enter into a contract but may not obtain the enhanced remedies available to a tort victim.

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[2] Tort law also allows for the recovery of "expanded consequential damages" and "compensation for emotional distress." (Dorff, *Attaching Tort Claims to Contract Actions*: *An Economic Analysis of Contort* (1997) 28 Seton Hall L.Rev. 390, 390.)

The economic loss rule "can trace its ultimate origins to the Uniform Commercial Code," which sought to create "a single, uniform body of law to govern commercial transactions throughout the United States." (Sylvester, *Economic Loss*: *Commercial Contract Law Lives* (2000) 27 Wm. Mitchell L.Rev. 417, 419 (hereinafter Sylvester).) From the beginning, the "principal policy basis" for the economic loss rule was therefore "maintaining a uniform and predictable body of commercial law." (*Id.* at p. 420.)

Whereas tort actions can subject business owners to indefinite damages, contract damages have a "built-in limitation on liability." (*East River*, *supra*, 476 U.S. at p. 874.) Contract law even allows parties in privity to minimize their exposure to risk by expressly limiting their liability and opting out of certain remedies. (See *Daugherty v. American Honda Motor Co., Inc.* (2006) 144 Cal.App.4th 824, 830 ["A seller may limit its liability for defective goods by disclaiming or modifying a warranty"]; see also *East River*, 476 U.S. at p. 873 [noting that a seller "can restrict its liability, within limits, by disclaiming warranties or limiting remedies. [Citations.] In exchange, the purchaser pays less"].) By excluding "tort remedies from broad categories of commercial disputes," the economic loss rule helps "commercial traders . . . determine in advance the legal rules applicable to a particular transaction." (Sylvester, *supra*, 27 Wm. Mitchell L.Rev. at p. 421.) This protects the freedom of contracting parties to allocate economic risks through contract, and it encourages each party to assess the risk of economic loss and then assume,

allocate, or insure against that risk. By ensuring that parties to commercial contracts cannot recover more damages than would be available under the agreed-upon remedies in the parties' contracts, the economic loss rule facilitates efficient commercial transactions.

II. A fraudulent concealment exception would swallow the economic loss rule and seriously disrupt commerce.

A fraudulent concealment exception would eviscerate the economic loss rule because the tort of concealment attaches liability to *omissions*—statements that were *not* made or facts that were *not* disclosed. (See CACI No. 1901 [Concealment].) The actus reus elements of fraudulent concealment are (1) failure to disclose certain facts, (2) disclosing some facts but not others, or (3) preventing the plaintiff from discovering certain facts. (*Ibid.*) Because there is no limit to the scope of statements that are *not* made, there is no limit to the potential fraudulent concealment claims that enterprising plaintiffs can attach to breach-of-contract claims.

Indeed, judges and commentators have recognized that such plaintiffs can plead concealment-based tort claims in "virtually every breach of contract action."[3] (Arledge, *Is the California Supreme Court Confusing the Boundaries of the Economic Loss Rule?* (May 2005) Orange County Law. 22, 26.) As

[3] Petitioner is therefore wrong when he claims that there is "no basis for distinguishing between fraudulent misrepresentations and fraudulent concealment when it comes to the [economic loss rule]." (RBOM 38.)

Justice Werdegar warned in her *Robinson Helicopter* dissent, "every litigator can be expected to attach such a piggyback [concealment] claim to each breach of contract claim." (*Robinson Helicopter*, *supra*, 34 Cal.4th at p. 1001, dis. opn. of Werdegar, J.).) Allowing a fraudulent concealment exception to reinject tort remedies into contract disputes would thus cause tort remedies to "simply engulf" contract law. (See *Huron Tool and Engineering Co. v. Precision Consulting Services, Inc.* (Mich.Ct.App. 1995) 532 N.W.2d 541, 544.)

As a result, neither this Court's jurisprudence nor sound public policy supports an exception to the economic loss rule for fraudulent concealment. *Robinson Helicopter* created a "narrow" exception to the economic loss rule when a defendant (1) makes an "affirmative" fraudulent misrepresentation that is (2) "separate from" the breach and (3) accompanied by risk of "personal damages independent of the plaintiff's economic loss."[4] (*Robinson Helicopter*, *supra*, 34 Cal.4th at pp. 991, 993.) But businesses know and can control the affirmative statements they make, and they can reasonably anticipate potential liability and damages based on their own affirmative conduct. Allowing tort

[4] The Court should ignore petitioner's invitation to essentially overrule *Robinson Helicopter* to the extent that it held that the alleged fraud must be accompanied by a risk of personal damages independent of the economic loss. (See OBOM 45–50; RBOM 39.) As discussed above, the purpose of tort law has always been to compensate plaintiffs who have suffered injury to themselves (including, to some extent, their minds) or their property. The Court was therefore correct to require—at minimum—a *risk* of personal harm before allowing recovery in tort.

remedies in that limited context does not significantly undermine the economic loss rule's goal of fostering uniformity and predictability in commercial transactions. By contrast, a new exception for fraudulent concealment would make such predictability impossible because the scope of arguably material omissions is unlimited. *Robinson Helicopter* thus does not support such a limitless exception.

As this Court has acknowledged, preserving traditional limits on contract damages "encourage[s] contractual relations and commercial activity by enabling parties to estimate in advance the financial risks of their enterprise." (*Applied Equipment, supra*, 7 Cal.4th at pp. 514–518.) This "predictability about the cost of contractual relationships plays an important role in our commercial system," because it encourages businesses to regulate their interactions through contracts. (*Foley v. Interactive Data Corp.* (1988) 47 Cal.3d 654, 683; see *East River*, *supra*, 476 U.S. at pp. 872–873 [observing that contract law "is well suited to commercial controversies . . . because the parties may set the terms of their own agreements"].)

A fraudulent concealment exception to the economic loss rule would thus disrupt commerce in several harmful ways.

First, it would destroy commercial predictability by raising the stakes in contract disputes and creating an ever-present threat of uncertain tort liability. In every breach case, such an exception would allow plaintiffs to subvert their contract terms by seeking to recover in tort what they could not recover under the terms to which they initially agreed. Punitive damages—

available only in tort cases—are in particular much more difficult to predict than compensatory expectation damages because punitive damages depend on the factfinder's perception of the defendant's culpability.

Against this uncertain legal backdrop allowing concealment-based tort claims for every breach, merchants would be unsure how to bargain over warranties and potential contract remedies. As Justice Werdegar recognized, forcing contracting parties "to bargain in the shadow of potential tort liability" "cannot be a good thing." (*Robinson Helicopter*, *supra*, 34 Cal.4th at p. 997 (dis. opn. of Werdegar, J.).) The unpredictable risk of tort liability would "discourage valuable commercial and economic activity and thus create an undesirable barrier to the efficient reallocation of resources." (Sebert, Jr., *Punitive and Nonpecuniary Damages in Actions Based Upon Contract*: *Toward Achieving the Objective of Full Compensation* (1986) 33 UCLA L.Rev. 1565, 1566.)

Second, allowing potential tort liability whenever a contracting party asserts fraudulent concealment may chill open, creative, and constructive communications within businesses. Good businesses experiment with new ideas, adopting some and rejecting others. This makes businesses particularly vulnerable to unsubstantiated allegations of fraud, based on alleged "concealment" of internal communications aimed at improving goods and services.

Even frivolous fraud allegations are costly to defend and can irreparably harm a business's reputation and good will. Such

reputational damage will persist and may even expand while a business fights to disprove fraud allegations—which can take years. And that reputational harm may be impossible to repair even after a business prevails by successfully disproving the allegations. As a result, if businesses face potentially unlimited tort liability (on top of contract damages) for the failure to disclose every piece of information they ever possessed—every email and stated opinion of every employee, consultant, or consumer—then they may respond to this uncertainty by squelching research, internal debate, and information sharing.

Third, a fraudulent concealment exception to the economic loss rule would also likely increase the up-front costs of entering into contracts, particularly in the context of disclosures. For example, under California law, there is no general duty to disclose information during arm's length negotiations preceding the formation of a contract. (See, e.g., Directions for Use to CACI 1901 [explaining the circumstances under which a duty to disclose can arise].) But allowing fraudulent concealment claims for breach will potentially impose on contracting parties a duty of disclosing during negotiations a variety of trade secrets or business strategies, sensitive financial information, internal speculation and debate, as well as the parties' confidential view of the contract's potential risks and rewards. Besides adding costs for attorneys' and accountants' fees, these disclosure requirements can chill contract negotiations and will likely have a disproportionate impact on startups and small businesses struggling to attract clients or customers.

The resulting fear of unpredictable liability for inadequate disclosure could significantly unsettle numerous areas of California law that depend on the economic loss rule, including construction defect cases (e.g., *State Ready Mix, Inc. v. Moffatt & Nichol* (2015) 232 Cal.App.4th 1227, 1232); loan/mortgage modification cases (e.g., *Sheen v. Wells Fargo Bank, N.A.* (2022) 12 Cal.5th 905, 915–916, 922–948); cases involving fraudulent financial transactions (e.g., *Kurtz-Ahlers, LLC v. Bank of America, N.A.* (2020) 48 Cal.App.5th 952, 959–962); and data-privacy cases (e.g., *Moore v. Centrelake Medical Group, Inc.* (2022) 83 Cal.App.5th 515, 535).

For example, if the economic loss rule no longer applies to fraudulent concealment claims, subcontractors would have to overdisclose all conditions about their construction plans, materials, and job sites that a counterparty could later claim carried a latent risk of failure. In hindsight, contracting parties whose expectations are disappointed could always claim that they would not have entered into or performed under the terms of a contract if they had been told that a different design or material was available. This sort of claim will waste time and money, raising prices.

Overdisclosure could actually *harm* counterparties. It may overwhelm counterparties and cause them to ignore material facts buried amid unnecessary information disclosed simply to minimize the risk of tort liability. The perverse disclosure incentives could thus lead to a general decrease in collaboration

and comprehensive project knowledge, which in turn could reduce construction quality and even public safety.

Fourth, a fraudulent concealment exception would deter "efficient" breaches of contract. An efficient breach "occurs when the gain to the breaching party exceeds the loss to the party suffering the breach, allowing the movement of resources to their more optimal use." (*Freeman*, *supra*, 11 Cal.4th at p. 106 (dis. & conc. opn. of Mosk, J.).) California courts have recognized that efficient breach is among the " 'most enlightening insights of law and economics.' " (*Huynh*, *supra*, 111 Cal.App.4th at p. 1198, quoting McChesney, *Tortious Interference with Contract Versus "Efficient" Breach*: *Theory and Empirical Evidence* (1999) 28 J. Legal Stud. 131, 132.) Efficient breaches are encouraged, because if it is "worth more to the promisor to breach rather than to perform a contract," then it is "more efficient for the law to allow the promisor to breach the contract and to pay the promisee damages." (*Id.* at p. 1199.)

But as Justice Werdegar warned in her *Robinson Helicopter* dissent, if allegations of fraudulent concealment are exempted from the economic loss rule, "every breach case can be expected to focus on when a party learned it was in breach and why it failed to disclose that fact to the other side." (*Robinson Helicopter*, *supra*, 34 Cal.4th at p. 1001, dis. opn. of Werdegar, J.).) And if a party can attach a concealment-based tort claim to any intentional-breach claim, then the principle of efficient breach will be a nullity in California. Exposing breaching parties to potential tort damages, including punitive damages, upsets

market efficiency by increasing the cost of breach. That cost harms the rest of society, which no longer benefits from the most efficient allocation of resources.

Taken together, the consequences of creating an exception to the economic loss rule for fraudulent concealment claims will discourage businesses from entering into contracts and making economically efficient decisions, thereby chilling vital commercial activities. (See *Freeman*, *supra*, 11 Cal.4th at p. 109 (dis. & conc. opn. of Mosk, J.) [cautioning that "courts should be careful" when applying tort remedies to contract disputes because doing so will "discourage commerce"].) This would undermine the very purpose of contract law in general and the economic loss rule in particular: to *facilitate* market transactions. (See Thoma, *Having Your Cake and Eating It Too*: *Post-Contract-Formation Fraud* (2014) 66 Baylor L.Rev. 782, 804.)

Indeed, such an exception would be most harmful for small businesses, which are essential to California's economy and "the engine of job growth in this country." (See U.S. Chamber Inst. for Legal Reform, *Tort Liability Costs for Small Business* (July 2010) p. 1 <https://tinyurl.com/5n7y6zsv> [as of Jan. 23, 2023].) Even unmeritorious lawsuits create leverage requiring small businesses to pay at least nuisance value settlements rather than engage in costly litigation. And "litigation causes not just financial loss, but also substantial emotional hardship, and often changes the tone of the business." (Klemm Analysis Group for Small Bus. Admin. Off. of Advocacy, *Impact of Litigation on Small Business* (Oct. 2005) p. ii <https://bit.ly/2h58h8x> [as of

Jan. 23, 2023].) Without the economic loss rule's protection against all-too-easily alleged concealment claims, the unlimited potential tort liability that would hover over every commercial contract would be catastrophic. Businesses would inevitably pass along that increased and more uncertain risk to consumers and employees in the form of higher prices and lower wages.

III. A fraudulent concealment exception would encourage and prolong litigation, increasing costs for litigants and the entire judicial system.

The costs of California's burdensome tort system already exceed $60 billion—nearly $4,600 per household (fifth highest in the nation) and 2 percent of the state's entire GDP. (See U.S. Chamber Inst. for Legal Reform, *Tort Costs in America*: *An Empirical Analysis of Costs and Compensation of the U.S. Tort System* (Nov. 2022) p. 17, 20 <https://tinyurl.com/TortCostsInAmerica> [as of Jan. 26, 2023].) A fraudulent concealment exception to the economic loss rule will exacerbate these costs.

First, when contract disputes have the potential to result in windfall tort damages, plaintiffs will be encouraged to take the chance of litigating their claims and will therefore be less likely to settle. (See Gergen, *A Cautionary Tale About Contractual Good Faith in Texas* (1994) 72 Tex. L.Rev. 1235, 1236; Pennington, *Punitive Damages for Breach of Contract: A Core Sample from the Decisions of the Last Ten Years* (1989) 42 Ark. L.Rev. 31, 101 (hereafter Pennington).)

The "allure of punitive damages" is "a golden carrot that entices into court parties who might otherwise be inclined to resolve their differences." (*Oki America, Inc. v. Microtech Intern., Inc.* (9th Cir. 1989) 872 F.2d 312, 314 (conc. opn. of Kozinski, J.).) Because the "standards are vague and the stakes are high," punitive damages incentivize litigation as plaintiffs cling to hopes of a "pot of gold." (Pennington, *supra*, 42 Ark. L.Rev. at p. 101.) Indeed, "punitive damages in commercial relations lead to overcompensation of a few, and the resulting incentive to make every issue a lawsuit, at the expense of the efficiency of the system as a whole." (Deacon, *Punitive Damages in Business and Contract Litigation*: *Punishment or Profit?* (1989) 17 W. St.U. L.Rev. 1, 15.) Uncertainty about tort damages therefore "increase[s] the cost of litigation" because defendants will increase their litigation investments in proportion to the risk of "large, unpredictable punitive award[s]." (*Ibid.*) Likewise, plaintiffs will be more likely to pursue litigation even when they have weak claims, as they chase potential windfall damages awards. (See *ibid.*) The increased probability of litigation inevitably leads to expensive discovery and larger attorneys' fees.

Second, greater uncertainty regarding potential damages will also make it more difficult for parties to calculate a realistic settlement value of hybrid breach-of-contract/concealment claims. Benefit-of-the-bargain expectation damages are relatively easy to quantify, but as noted, tort damages—and especially punitive damages—are highly subjective and less predictable. Potential tort damages therefore plague settlement negotiations with

uncertainty and intractable disagreement about the value of tortified contract claims. Defendants in these disputes will be forced to litigate cases when their reasonable settlement offers are rejected, or to pay unduly inflated settlements for weak or even meritless claims just to avoid the increased litigation costs and, in many cases, the risk of an inordinate punitive-damages verdict.

Third, more unnecessary trials strain not only party resources but also judicial resources. Those burdens are more significant when tort claims are involved. "Because the economic loss doctrine determines whether a matter proceeds in court as a tort or contract action, that decision is a significant one." (Anzivino, *The Fraud in the Inducement Exception to the Economic Loss Doctrine* (2007) 90 Marq. L.Rev. 921, 923.) Tort cases are frequently more fact-intensive than contract cases. Intent, scienter, materiality, breach, and reliance are all questions of fact that must be determined at trial. (See *Marzec v. California Public Employees Retirement System* (2015) 236 Cal.App.4th 889, 915; *Beckwith v. Dahl* (2012) 205 Cal.App.4th 1039, 1061; *Buist v. C. Dudley De Velbiss Corp.* (1960) 182 Cal.App.2d 325, 332; *Elkind v. Woodward* (1957) 152 Cal.App.2d 170, 179.) Thus, allowing tort remedies in contract cases would impose an outsized burden on California courts. Further clogging court dockets with piggyback tort claims will divert courts away from more pressing matters.

IV. Fraudulent inducement is not at issue here, but the economic loss rule equally bars tort claims for inducement by concealment.

Petitioner discusses fraudulent inducement at length, but that issue is not before the Court in this case. That issue can and should be decided in the context of one of the other cases presented to this Court for review. (See *Dhital v. Nissan North America, Inc.* (2022) 84 Cal.App.5th 828, petn. for review pending, petn. filed Dec. 2, 2022, time for grant or denial of review extended to Mar. 3, 2023 [petition raising the question whether claims for fraudulent inducement by concealment are exempted from the economic loss rule]; *Kia Am., Inc. v. Superior Court (Spellman)*, review granted Apr. 20, 2022, S273170 [granting a petition for review, on a grant-and-hold basis, raising the question whether the economic loss rule bars tort claims alleging that a vehicle manufacturer failed to disclose facts relating to the same malfunction that is the subject of an express-warranty claim].)

Even so, the arguments above apply equally to concealment in the inducement and concealment in the performance of a contract. This Court has never recognized an inducement-by-concealment exception to the economic loss rule. That issue was not before the Court in *Robinson Helicopter*. And even if it had been, the "narrow" exception that *Robinson Helicopter* created for affirmative misrepresentation does not imply an exception for inducement by concealment, much less one divorced from the requirement that there be a risk of "personal damages

independent of the plaintiff's economic loss." (*Robinson Helicopter*, *supra*, 34 Cal.4th at p. 993.)

The practical concerns discussed above weigh against creating an inducement-by-concealment exception. As discussed, such an exception would pressure parties to contracts and warranties to disclose during negotiations all potentially negative information and even the parties' confidential view of the contract's potential risks and rewards—every consumer complaint or government agency inquiry, test or research result, expert or lay opinion. Without such disclosure, parties would risk facing a concealment-based inducement claim whenever their counterparties might claim in hindsight that they would not have agreed to a contract or warranty had they known about some undisclosed fact. Businesses routinely must make decisions about tradeoffs when adopting designs and processes, taking into account affordability and convenience for consumers. No merchant or service provider does or could volunteer every piece of knowledge that might later be the subject of a claim based on alleged concealment in the inducement.

V. The California Legislature, rather than this Court, is best positioned to consider any new exceptions to the economic loss rule.

This Court should reaffirm that the economic loss rule is a foundational doctrine subject only to the existing and narrow exceptions that are at least arguably consistent with the doctrine's underlying rationale. Affirmative misrepresentations are one such exception, but concealment-based claims are not. As

discussed above, a concealment-based exception would have far-reaching and disruptive consequences across California law and virtually every industry. Only the Legislature is properly equipped to create such an exception—as this Court has recognized in a similar context before.

In *Aas*, *supra*, 24 Cal.4th at page 632, this Court was invited to create an exception to the economic loss rule for construction defects that cause only economic loss. The Court declined to do so based on "settled law limiting the recovery of economic losses in tort actions." (*Ibid.*) The Court noted that the issue implicated "many considerations of social policy" that were "better left to the Legislature," which has "a wider range of options and superior access to information about the social costs and benefits of each." (*Id.* at p. 652.) The Court found no "sufficiently compelling reason to preempt the legislative process with a judicially created rule of tort liability." (*Id.* at p. 653.)

After the *Aas* opinion, the Legislature responded by enacting Senate Bill No. 800 (2001–2002 Reg. Sess.) § 3, the Right to Repair Act (see Civ. Code, §§ 895–945.5), which, among other things, creates a limited exception to the economic loss rule under which homeowners have "the right to sue . . . even in the absence of property damage or personal injury." (*McMillin Albany LLC v. Superior Court* (2018) 4 Cal.5th 241, 247.) As part of the Act, the Legislature also enacted further provisions (which the Court in *Aas* could not have done), such as "a prelitigation dispute resolution process that affords builders notice of alleged construction defects and the opportunity to cure such defects."

(*Ibid.*) The Act is the result of exactly the kind of *legislative* process that the Court in *Aas* recognized as essential for such a major legal change.

For the reasons discussed above, an exception for concealment-based fraud claims would completely upend the traditional economic loss rule—and contract and tort law with it. Such a substantial restriction on the economic loss rule should not be made lightly. And if made, it should be made through the legislative process, which can properly consider the attendant competing policy considerations. Unlike this Court, the Legislature can engage in public fact finding considering the effects of expanding tort remedies, including punitive damages, against contracting parties in a wide range of industries and involving a wide range of claims. The Legislature also has a wider set of tools than the judiciary to craft careful compromises in ways that can more delicately balance competing interests.

CONCLUSION

For these reasons, the Court should answer the certified question in the negative and reject a fraudulent concealment exception to the economic loss rule.

January 30, 2023

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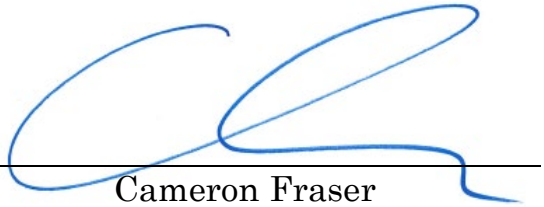
By: 
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Case No. S272113

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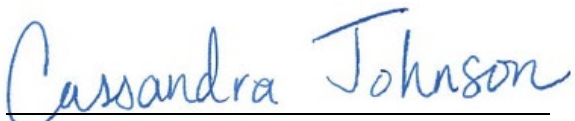

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STATE OF CALIFORNIA
Supreme Court of California

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