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# RESTATING THE "RELIANCE INTEREST"

Robert E. Hudec†

## INTRODUCTION

No scholarly work during the period between the first and second Restatement of Contracts had more impact on the law of contracts than Fuller and Perdue's 1936 article *The Reliance Interest in Contract Damages*.<sup>1</sup> The article conceptualized contract remedies in terms of three "interests" that a promisee may be said to have: expectation, reliance, and restitution.<sup>2</sup> The main purpose of this interest matrix was to argue for acceptance of the reliance interest as a distinct basis of remedy. Fuller and Perdue documented the existing judicial practice of awarding reliance damages and other less-than-expectancy remedies in cases where the award of full expectancy damages is found to be inappropriate.

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<sup>1</sup> Fuller & Perdue, *The Reliance Interest in Contract Damages* (pts. 1 & 2), 46 YALE L.J. 52, 373 (1936).

<sup>2</sup> Fuller and Perdue defined the three interests as follows:

It is convenient to distinguish three principal purposes which may be pursued in awarding contract damages. These purposes, and the situations in which they become appropriate, may be stated briefly as follows:

*First*, the plaintiff has in reliance on the promise of the defendant conferred some value on the defendant. The defendant fails to perform his promise. The court may force the defendant to disgorge the value he received from the plaintiff. The object here may be termed the prevention of gain by the defaulting promisor at the expense of the promisee; more briefly, the prevention of unjust enrichment. The interest protected may be called the *restitution interest*. . . .

*Secondly*, the plaintiff has in reliance on the promise of the defendant changed his position. For example, the buyer under a contract for the sale of land has incurred expense in the investigation of the seller's title, or has neglected the opportunity to enter other contracts. We may award damages to the plaintiff for the purpose of undoing the harm which his reliance on the defendant's promise has caused him. Our object is to put him in as good a position as he was in before the promise was made. The interest protected in this case may be called the *reliance interest*.

*Thirdly*, without insisting on reliance by the promisee or enrichment of the promisor, we may seek to give the promisee the value of the expectancy which the promise created. We may in a suit for specific performance actually compel the defendant to render the promised performance to the plaintiff, or, in a suit for damages, we may make the defendant pay the money value of this performance. Here our object is to put the plaintiff in as good a position as he would have occupied had the defendant performed his promise. The interest protected in this case we may call the *expectation interest*.

*Id.* at 53-54.

They offered their interest analysis as a theoretical and policy justification for providing such remedies openly and explicitly. The interest analysis has since become standard fare in law school classrooms and in legal writing about contract remedies. Although explicit judicial recognition has been less widespread, the few decisions that have employed the analysis enjoy a "leading case" prominence that give it the feel of established doctrine.<sup>3</sup>

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<sup>3</sup> Consider, for instance, the treatment of *Sullivan v. O'Connor*, 363 Mass. 579, 296 N.E.2d 183 (1973) in R. DANZIG, *THE CAPABILITY PROBLEM IN CONTRACT LAW* 5-43 (1978). *Sullivan* contains perhaps the most extensive explicit application of the interest analysis, suggesting in dictum that the reliance measure would be the most appropriate remedy for breach of a doctor's promise guaranteeing results of treatment. Other decisions that have received similar attention include *L. Albert & Son v. Armstrong Rubber Co.*, 178 F.2d 182, 189 (2d Cir. 1949) (discussed in notes 61-66 and accompanying text *infra*); *Albre Marble & Tile Co. v. John Bowen Co.*, 338 Mass. 394, 399, 155 N.E.2d 437, 440 (1959) (discussed in note 33 *infra*); *Wheeler v. White*, 398 S.W.2d 93, 97 (Tex. 1965) (recovery of reliance damages for breach of promise to lend money).

Computer research turned up 25 majority opinions and 4 dissents in which the *Reliance Interest* article was cited. In addition to the opinions cited above, the following opinions indicate approval of some part of the article's substantive analysis: *Glasscock v. Wilson Constructors, Inc.*, 627 F.2d 1065, 1068 (10th Cir. 1980) (reliance damages recoverable in lieu of expectancy damages; without citation to article, court also applies "promissory estoppel" to enforce an oral promise within Statute of Frauds); *Hector Martinez & Co. v. Southern Pac. Transp. Co.*, 606 F.2d 106, 108 n.3 (5th Cir. 1979) (recites interest analysis; reliance damages recoverable where expectancy incalculable); *Coastal Steel Erectors, Inc. v. Algernon Blair, Inc.*, 479 F.2d 638, 640 n.1, 641 & n.7 (4th Cir. 1973) (restitution interest most compelling claim to recovery; contract price *not* a ceiling on restitution claim); *Kizas v. Webster*, 532 F. Supp. 1331, 1332 (D.D.C. 1982) (article cited in support of reliance damage measure of recovery where value of expectancy cannot be proved); *Pineman v. Oechslin*, 494 F. Supp. 525, 540 (D. Conn. 1980) (article cited for promissory estoppel; court also uses "reliance interest" terminology without citation, in finding that state pension plan creates contractual obligations); *In re Yeager Co.*, 227 F. Supp. 92, 96, 98 (N.D. Ohio 1963) (extensive dictum restating interest analysis; reliance damages recoverable in lieu of expectancy damages); *Johnson v. Healy*, 176 Conn. 97, 106, 405 A.2d 54, 59 (1978) (reliance damages recoverable where expectancy not accessible to proof); *Coleman v. Bossier City*, 305 So. 2d 444, 447 (La. 1974) (when contract fails for illegality, reliance damages not exceeding benefit received, recoverable under *culpa in contrahendo* rationale); *Center Garment Co. v. United Refr. Co.*, 369 Mass. 633, 639, 341 N.E.2d 669, 674 (1976) (reliance losses recoverable in lieu of lost profits); *Freund v. Washington Square Press*, 34 N.Y.2d 379, 383, 314 N.E.2d 419, 421, 357 N.Y.S.2d 857, 860 (1974) (defines three interests; finds plaintiff's damage claims would overcompensate all three); *West, Weir & Bartel, Inc. v. Mary Carter Paint Co.*, 25 A.D.2d 81, 88, 267 N.Y.S.2d 29, 36 (1966) (contract price is ceiling for reliance expenses); *Osborn v. Commanche Cattle Indus.*, 545 P.2d 827, 831-32 (Okla. Ct. App. 1975) (questionable holding that reliance damages available for breach of 30-day notice requirement for franchise termination, in addition to lost profits for 30 days).

Two dissents that incorporate a particularly important part of the article's analysis are found in: *Garcia v. Von Miesky*, 602 F.2d 51, 54 (2d Cir. 1979) (Oakes, J., dissenting) (surgeon's warranty of sterility justifies pregnant woman's recovery for out-of-pocket costs); *Coleman Eng'g Co. v. North Am. Aviation, Inc.*, 65 Cal. 2d 396, 420 & n.8, 420 P.2d 713, 719 & n.8, 55 Cal. Rptr. 1, 17 & n.8 (1966) (Traynor, J., dissenting) (reliance damages appropriate where contract fails due to indefiniteness).

The article is cited in one United States Supreme Court decision. In *Andrus v. Allard*, 444 U.S. 51, 66 (1979), Justice Brennan, in response to a claim that federal statutes prohibiting commerce in eagle feathers were an unconstitutional taking, cited *Fuller and Perdue* for

Quite naturally, Fuller and Perdue's analysis has influenced the Restatement (Second) of Contract's treatment of contract remedies. Its most significant impact is found in a number of black-letter rules authorizing the award of less-than-expectancy remedies, either as an alternative to recovery of the full expectancy or as a limited remedy where no liability for expectancy damages is recognized. The *Restatement Second* authorizes such remedies for certain promises that lack consideration (sections 86, 87, 89, 90), certain oral promises barred by the Statute of Frauds (section 139), and certain promises held enforceable despite a defense of mental incapacity (section 15). The *Restatement Second* also provides for less-than-expectancy remedies in some cases where promises have been excused under doctrines of mistake, frustration or impracticability (sections 158, 272). Finally, it provides that courts may award reliance damages when the value of the expectancy cannot be proved (section 349), and that courts may limit consequential damages when full compensation of the expectancy is deemed excessive (section 351(3)). In addition to these operative rules, the *Restatement Second's* "Remedies" Chapter opens with a separate section declaring the existence of the three interests and defining them (section 344).

Most of the operative rules authorizing partial recovery contain no reference to the interest analysis stated in section 344. Only two of the rules use the term reliance interest as an operative concept: section 349, which authorizes the award of reliance damages when the expectancy cannot be proved, and sections 158 and 272, which authorize relief in cases where contracts are discharged for reasons of mistake, impracticability or frustration. All the other rules give the courts authority to limit damages "as justice requires," either with no mention of reliance damages at all, or in one case, with reliance damages merely being mentioned as one possible measure of the recovery that justice may require.<sup>4</sup>

This Article examines that part of the *Restatement Second* which employs Fuller and Perdue's reliance interest concept directly. It deals primarily with section 344, which restates the interest matrix, and sections 158, 272 and 349, which use the concept as an operative term. Part I of this Article examines the theoretical significance of the *Restatement Second's* explicit recognition of the reliance interest. Part II examines the scope of the special damage remedy in section 349 for "damages based on [the promisee's] reliance interest."

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the proposition that "the interest in anticipated gains has traditionally been viewed as less compelling than other property-related interests." For an opinion incorporating the same analysis of the expectation interest, see *Perma Research & Dev. v. Singer Co.*, 542 F.2d 111, 127 (2d Cir. 1976) (VanGraafeiland, J., dissenting) (expectancy damages excessive for tenuous type of "contract" at issue).

<sup>4</sup> Sometimes the power to limit damages is stated explicitly, as in §§ 90 & 139; in other cases, it is made applicable by making the underlying promise binding only to a limited extent, as in §§ 86, 87 & 88.

## I

## RECOGNITION OF THE RELIANCE INTEREST

A. *The Message and its Overtones*

Fuller and Perdue's interest matrix appears in section 344. It reads:

## PURPOSES OF REMEDIES

Judicial remedies under the rules in this Restatement serve to protect one or more of the following interests of a promisee:

(a) his "expectation interest," which is his interest in having the benefit of his bargain by being put in as good a position as he would have been in had the contract been performed,

(b) his "reliance interest," which is his interest in being reimbursed for loss caused by reliance on the contract by being put in as good a position as he would have been in had the contract not been made, or

(c) his "restitution interest," which is his interest in having restored to him any benefit that he has conferred on the other party.<sup>5</sup>

Section 344 is a most curious black-letter proposition. It states no rule. The title suggests that section 344 may be a statement of purpose that will govern the answers to later operational issues, but such a role never materializes.<sup>6</sup> Nor do the definitions of the three interests play a significant role in the subsequent operative rules that define how the three remedies are to be measured. The expectation and restitution definitions are overtaken by more specific measuring standards stated in the subsequent operating rules.<sup>7</sup> The reliance definition does play a limited role later on, but hardly one that justifies a separate definitional section.<sup>8</sup> The absence of a functional purpose suggests that section 344 is meant simply to declare the separate existence of the three interests.

The purpose of the section 344 declaration must be sought in the origins of the interest matrix. Fuller and Perdue's use of the matrix was intended primarily to call attention to reliance losses as a particularly compelling object of remedial justice, and to argue that questions of liability for such losses ought to be considered separately from the liability rules for other kinds of loss caused by promise-breaking. Their assertion

<sup>5</sup> RESTATEMENT (SECOND) OF CONTRACTS § 344 (1979).

<sup>6</sup> The black-letter rule of § 344 makes only the more limited statement that contract remedies "serve to protect" these three interests. The idea of a governing purpose is further submerged in Comment a to § 344, where the reader is warned: "The interests described in this Section are not inflexible limits on relief and in situations in which a court grants such relief as justice requires, the relief may not correspond precisely to any of these interests. See §§ 15, 87, 89, 90, 139, 158 and 272." *Id.*, Comment a (1979).

<sup>7</sup> Although the terms "expectation interest" and "restitution interest" are both used in the black-letter rules defining their respective measures of recovery, both terms are effectively supplanted by more precise "as measured by" definitions. *See id.* §§ 347 & 371.

<sup>8</sup> For discussion of the reliance interest as a measuring standard in § 349, see notes 34-70 and accompanying text *infra*.

that a separate "reliance interest" exists was not meant to dictate any particular legal consequences. Rather, it was in part descriptive of certain already recognized remedies for reliance losses, such as promissory estoppel, and in part an open-ended invitation to consider all other matters involving reliance losses as distinct questions of policy that need not be controlled by the answers given for contract damages generally.

The substantive message of the reliance interest concept has often been clouded by theoretical concerns about the character and foundation of the separate rules of liability being advocated. The Fuller and Perdue article itself had to engage somewhat reluctantly in a certain amount of such conceptual argumentation to defend its position. The first *Restatement* had contained an elaborate analysis and justification of reliance damages, arguing that they involved no new principle of contract damages, but were merely an application of the conventional remedy of expectation damages without the element of profit.<sup>9</sup> Fuller and Perdue labeled the explanation "tendentious."<sup>10</sup> They were arguing that limits on the award of expectancy damages should not necessarily encumber the decision to grant reliance damages.<sup>11</sup> For example, they thought that courts should be able to award reliance damages for breach of an oral promise barred by the Statute of Frauds, without running afoul of the contention that such damages were a form of "contract damages," and thus a form of "contract enforcement" contrary to the policy of the Statute.<sup>12</sup> The "tendentious" insistence that reliance damages were merely a subspecies of expectation damages obviously made arguing against such conceptual limitations more difficult.

The remedy of restitution had not been limited by such thinking, for it was possible to argue that restitution involved a different kind of wrong (unjust enrichment) and was thus a separate cause of action distinct from contract damages. Fuller and Perdue disliked such a justification, frequently deriding the conceptualism involved in classifying remedies as the "same" or "separate."<sup>13</sup> They preferred to rest their argument on the more down-to-earth analysis of the varying degrees of ethical urgency involved in the package of harms usually covered by the expectation interest. Nonetheless, as their "tendentious" comment shows, Fuller and Perdue were prepared to insulate their argument against such "same-separate" objections by carving out some degree of "separateness" for reliance damages as well.

The identification of a separate reliance interest, parallel to and of equal rank with interests of expectancy and restitution served to ad-

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<sup>9</sup> RESTATEMENT OF CONTRACTS § 333, Comment a (1932).

<sup>10</sup> Fuller & Perdue, *supra* note 1, at 90.

<sup>11</sup> *Id.* at 89-90, 95, 401-06, 418-20.

<sup>12</sup> *Id.* at 386-94.

<sup>13</sup> *See, e.g., id.* at 387-88.

vance this idea of separateness. Although it was primarily an analytical tool to explain the policy Fuller and Perdue were advocating, their interest matrix also implied that reliance is just as separate from contract damages as is restitution. Fuller and Perdue were not above showing how the interest matrix could be used in this manner if necessary. Consider, for example, their argument that reimbursement of reliance under an oral contract within the Statute of Frauds should not be considered offensive to the Statute's policy against "enforcement" of such oral contracts:

There is, then, no distinction which requires a court to deny reimbursement for reliance, and, at the same time, permits it to grant restitution on a contract made unenforceable by the statute. A court which broadened its intervention to include a protection of the reliance interest might justify its stand on the ground that the admitted differences between the restitution and reliance interests are insufficient to warrant a difference in legal treatment, and might properly view the reimbursement of reliance, not as involving legal sanction for the unenforceable agreement, but as having the same *raison d'être* as restitution—that of remedying injustices left when the statute denies enforcement to the oral contract.<sup>14</sup>

Comments such as this reinforce a tendency to view reliance as involving a type of wrong wholly separate from promise-breaking, in the way that unjust enrichment is separate. Such a view, of course, leads to the classic losing-contract question: Whether reliance damages, like restitution, may exceed the amount that would have been recovered if the promised performance had been rendered (the so-called expectancy ceiling). Fuller and Perdue considered the question and rejected this line of reasoning. Their analysis implicitly treated reliance damages as a form of liability that, like ordinary contract damages, rested on the promisor's failure to render the promised performance. It followed that reliance damages should not exceed the loss caused by the promisor's failure to perform; thus compensation for reliance should not knowingly exceed the expectancy ceiling.<sup>15</sup> Although this position obviously contradicts the "separate wrong" idea, it has never completely laid that idea to rest. Reliance damages continue to be viewed as somehow separate, and the problem of the expectancy ceiling continues to be discussed in the literature.<sup>16</sup>

In sum, Fuller and Perdue's interest matrix is both an invitation to open-ended policy analysis and an elusive suggestion of distinctive theo-

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<sup>14</sup> *Id.* at 389.

<sup>15</sup> *Id.* at 79. Fuller and Perdue acknowledged that courts might be justified in exceeding the expectancy ceiling if some justification for a deterrent sanction were present, *id.* at 77, but by classifying the excess as a deterrent they were reaffirming that it could not be compensatory.

<sup>16</sup> *See, e.g.*, J. FRIEDMAN, CONTRACT REMEDIES IN A NUTSHELL § 3.3 (1981).

retical properties that are never defined. Obviously, section 344 is meant to affirm Fuller and Perdue's general policy analysis. What other uses, if any, does the *Restatement Second* make of these various ideas?

### B. *Correcting the First Restatement*

One of the obvious functions section 344 serves is to settle Fuller and Perdue's dispute with the first *Restatement* over the status of reliance damages vis-a-vis the remedy of expectancy damages. The "tendentious" Comment affirming the common foundations of reliance and expectation has been deleted altogether. It has been replaced by section 344's assertion that the two remedies flow from two separate interests, as well as by a new Comment on reliance damages which stresses that distinction.<sup>17</sup> The restatement of the interest matrix thus clears away the constraining theoretical structure erected by the first *Restatement*.

The content of this separate reliance interest has not been developed very much by the *Restatement Second's* own rules of reliance-based liability. The rules providing remedies for promises without consideration and promises barred by the Statute of Frauds do not mention the section 344 analysis.<sup>18</sup> They were drafted and adopted before section 344 existed. A remark by the Reporter indicates that the use of the interest terminology was considered at this time but was rejected, probably because of reluctance to use the terms in advance of their formal definition.<sup>19</sup>

The term "reliance interest" is used in only two of the *Restatement Second's* operative rules—the rule of section 349, and the pair of identical rules stated in sections 158 and 272. In each case, the use of the term adds something of interest.

### C. *Section 349: The Entitlement Overtones*

Section 349 authorizes reliance damages as an alternative to expectancy damages. The rule is designed primarily for situations in which

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<sup>17</sup> The Comment seems almost perversely intent on making clear that reliance damages may well exceed the expectancy where defendant cannot prove the loss of a losing contract:

Under the rule stated in this Section, the injured party may, if he chooses, ignore the element of profit and recover as damages his expenditures in reliance. He may choose to do this if he cannot prove his profit with reasonable certainty. He may also choose to do this in the case of a losing contract, one under which he would have had a loss rather than a profit. In that case, however, it is open to the party in breach to prove the amount of the loss, to the extent that he can do so with reasonable certainty under the standard stated in § 352, and have it subtracted from the injured party's damages.

RESTATEMENT (SECOND) OF CONTRACTS § 349, Comment a (1979).

<sup>18</sup> *Id.* §§ 87, 89, 90 & 139.

<sup>19</sup> Professor Farnsworth, when discussing the initial draft of § 158 (then § 300) said that ". . . I have undergone heavy fire whenever I have used the terms reliance interest and expectation interest. These terms may well be used in a later Chapter of the Restatement but they are not on the books now." 52 ALI PROCEEDINGS 403 (1975).

the plaintiff cannot prove, or chooses not to prove, the value of his expectancy. It provides:

DAMAGES BASED ON RELIANCE INTEREST

As an alternative to the measure of damages stated in § 347, the injured party has a right to damages based on his reliance interest, including expenditures made in preparation for performance or in performance, less any loss that the party in breach can prove with reasonable certainty the injured party would have suffered had the contract been performed.

Section 349's treatment of the losing-contract problem reveals a surprising dimension to the definition of "reliance interest" in section 344. Section 349 restates the Fuller and Perdue position: reliance damages should not knowingly exceed the amount that would have been recovered if the promise had been performed. This expectancy ceiling was not, however, made part of the section 344 definition. Section 344 defines the reliance interest as the promisee's interest in "being put in as good a position as he would have been in had the contract not been made."<sup>20</sup> Read literally, this *status quo ante* definition includes all reliance on the contract, even reliance that exceeds the value of the expectancy. Good authority exists for such a literal reading. The same *status quo ante* formula was used to state the theory of restitution in the first *Restatement*,<sup>21</sup> and courts commonly cited that formula to justify recovery in restitution exceeding the expectation interest.<sup>22</sup> Section 349 confirms this interpretation, characterizing the exclusion of reliance losses in excess of the expectancy ceiling as a *deduction* from the sum referred to as "damages based on his reliance interest."<sup>23</sup>

This definition of the reliance interest tends to amplify the confusing overtones that the interest matrix has always generated. Fuller and Perdue's definition of the reliance interest employs the same *status quo ante* standard.<sup>24</sup> Their definition was no doubt addressed to the ordinary contract situation in which this standard poses no problem, and was not intended to govern the losing-contract problem dealt with later in the Article. Although the *Restatement Second* may have intended the same divided treatment,<sup>25</sup> the formality and finality of a black-letter

<sup>20</sup> RESTATEMENT (SECOND) OF CONTRACTS § 344 (1979).

<sup>21</sup> RESTATEMENT OF CONTRACTS § 347, Comment b (1932). The *status quo ante* standard also appears in the *Restatement Second*, in Comment a to § 384, but its prominence is diluted by a greater emphasis on the "benefit" concept. See Perillo, *Restitution in the Second Restatement of Contracts*, 81 COLUM. L. REV. 37, 38-43 (1981).

<sup>22</sup> *E.g.*, *Acme Process Equip. Co. v. United States*, 347 F.2d 509, 530 (Ct. Cl. 1965), *rev'd on other grounds*, 385 U.S. 138 (1966).

<sup>23</sup> Because § 349 provides a deduction, it is impossible to read the expectancy ceiling into any part of § 344. Otherwise, it might have been plausible to argue that the phrase "loss caused by reliance on the contract" implied such a ceiling.

<sup>24</sup> See Fuller & Perdue, *supra* note 1, at 54; note 2 *supra*.

<sup>25</sup> The Illustrations in the Comments to § 344 deal with profitable contracts. Losing

definition makes it more difficult to maintain the same sense of reservation. The black-letter form adds a sense of finality and general validity to the idea that all promisees have some kind of prima facie equitable claim (interest) to compensation for all reliance expenditures, without regard to any expectancy ceiling.

Stated as a general proposition, the assertion of an entitlement to above-expectancy reliance losses seems improper. The reliance interest concept embraces many different entitlement claims, too varied to be reduced to any general definition as to the expectancy ceiling.

The entitlement claim most commonly recognized is the claim based on a promisor's duty to perform his promise. Recognition of that duty is a way of expressing a value judgment that the promisor should be responsible for losses caused by the failure to perform his promise. The expectancy ceiling is an essential part of this particular value judgment, for it states the critical causation element—the measure of the loss caused by the failure to perform. The value judgment gives no basis for any claim of entitlement going beyond that ceiling.

If the legal system never attached any other kinds of responsibility to the act of promise-making, there would never be any entitlement to reliance losses beyond the expectancy ceiling. The law can, however, attach more than one kind of responsibility to the act of promise-making. It can, as does the rule of section 349, attach responsibility for all reliance losses where breach precludes recovery and the expectancy is immeasurable. It could go much further. For example, the law could attach a kind of common-venture responsibility, pursuant to which both parties must share reliance losses caused by unforeseen disasters such as those found in the typical mistake and impossibility cases. These other forms of liability would not necessarily be bound by the expectancy ceiling. The measure of liability for each of them would be governed by the particular concept of duty or responsibility involved.

In this rather complex situation, no general definition of reliance-based liability is possible. The question, rather, is whether a concept as open-ended as the reliance interest should have been defined in black letter at all. Any definition broad enough to make room for the more extended types of reliance claims, as does the Section 344 definition, is bound to give misleading conceptual signals about the core area of reliance liability based on breach of the performance duty. The argument for some black-letter recognition was strong, if only to clear away the constraints of prior *Restatement* theory. Perhaps a more prudent course would have been to make the black-letter recognition more general, and to refrain from using the concept in operative rules.

The *Restatement Second*'s use of the term "reliance interest" as a measuring standard for reliance damages creates some minor technical problems as well. The broad definition of the term requires that some further attention be given to the issue of the expectancy ceiling each time that term is used in an operative rule. No problem exists in section 349, for the necessary limitation is stated correctly in the rule itself. The rule stated in sections 158 and 272, however, provides that a court may "grant relief on such terms as justice requires including protection of the parties' reliance interest." Read literally, that rule authorizes compensation measured by the *status quo ante* position. This may or may not be appropriate, depending on the case. Actually, the problem can be solved if one reads the reference to the "reliance interest" as subordinate to the "as justice requires" standard, thereby allowing the term "justice" to determine the proper measure of "reliance interest" compensation. This is a bit clumsy, but it is the type of correction needed to control the breadth of the reliance interest definition.

#### D. *Sections 158 and 272: A New Cause of Action?*

Sections 158 and 272 deal with cases in which a promise is excused for reasons of mistake, frustration, or impracticability. In identical text, they provide:

- (1) In any case governed by the rules stated in this Chapter, either party may have a claim for relief including restitution under the rules stated in §§ 240 and [376 or 377].
- (2) In any case governed by the rules stated in this Chapter, if those rules together with the rules stated in Chapter 16 will not avoid injustice, the court may grant relief on such terms as justice requires including protection of the parties' reliance interests.<sup>26</sup>

The exact scope of the reliance loss remedy stated in these sections, and in their accompanying Comments and Illustrations, was obscured by drafting changes made in the final days.<sup>27</sup> An argument might even

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<sup>26</sup> The only difference between the two sections appears in the sections cited at the end of subsection (1). Section 158(1) refers to the section governing restitution in mistake cases (§ 376), and § 272(1) refers to the section governing restitution in cases involving frustration and impracticability (§ 377).

<sup>27</sup> Section 272 was originally introduced as § 292 in Tentative Draft No. 9 in 1974; section 158 was originally § 300 in Tentative Draft No. 10 in 1975. Consideration of both sections was deferred until consideration of Chapter 16 on Remedies. 52 ALI PROCEEDINGS 435 (1975); 51 ALI PROCEEDINGS 385 (1974). In 1979, a revised black-letter text of the two sections was submitted together with Chapter 16, in Tentative Draft No. 14, and was adopted with little discussion. 56 ALI PROCEEDINGS 301-02 (1979).

The obvious starting point for analysis is the express reference to the reliance interest in subsection (2). Despite the very broad wording, some question could be raised whether this text is intended to authorize money compensation. Unlike the final draft, the original draft of these sections did not contain any reference to the reliance interest. It spoke of relief in the form of "supplying a term [in order] to avoid injustice." RESTATEMENT (SECOND) OF CONTRACTS § 300(2), Comment a (Tent. Draft No. 10 1975); RESTATEMENT (SECOND) OF CON-

be made that these sections do not, in fact, authorize the award of

TRACTS § 292(1), Comment c (Tent. Draft No. 9 1974). In explaining this original remedial power, both Comment c and the Illustrations dealt only with the sort of equitable reformation in which a court modifies the original bargain by adding new terms in order to salvage the deal. Although the present text now speaks of "relief on such terms as justice requires including protection of the parties' reliance interests," the original Comment c and Illustrations have not been changed; they continue to explain this new language in terms of equitable reformation. RESTATEMENT (SECOND) OF CONTRACTS § 158, Comment c, Illustrations 1-3 (1979); *id.* § 272, Comment c, Illustrations 1-5 (Illustration 6 primarily involves restitution). Equitable reformation could, of course, be classified as protection of the reliance interest; reliance is usually the reason for doing so.

The Comments to §§ 158 and 272 do contain references to the award of money compensation for reliance loss, but most of these references point to subsection (1). The original draft of these sections was quite clear on this; subsection (1) provided for "relief including restitution under the rules stated in [§ 240] and prospective Chapter 16." *See* RESTATEMENT (SECOND) OF CONTRACTS § 272(1) (Tent. Draft No. 9, 1974). At this time, it was anticipated that Chapter 16 would provide for some type of reliance-loss recovery in this situation. *See* 52 ALI PROCEEDINGS 435 (1975); 51 ALI PROCEEDINGS 385 (1974). The original Comment to subsection (1) (then, as now, Comment b) said so. For example, Comment b to § 272 (then 292) said: "In a proper case recovery may go beyond mere restitution and include elements of reliance by the claimant even though they have not benefited the other party. *See* prospective Chapter 16." RESTATEMENT (SECOND) OF CONTRACTS § 292, Comment b (Tent Draft No. 9, 1974). *See also id.* § 300, Comment b (Tent. Draft No. 10, 1975). Moreover, a few Illustrations in the substantive sections of the mistake and impracticability chapters mentioned the possibility of reliance-loss liability, and these Illustrations cited subsection (1) of §§ 158 and 272. *See* RESTATEMENT (SECOND) OF CONTRACTS § 153 (then § 295), Comment d, Illustration 8 (1979); *id.* § 262 (then § 282), Comment a, Illustration 3; *id.* § 265 (then § 285), Comment a, Illustration 2.

When §§ 158 and 272 were revised in 1979, the tidy structure of this provision for reliance-loss compensation under subsection (1) collapsed. The reliance-interest remedy was added to subsection (2), as already noted. As a practical matter, this seems to have been the way of supplying the missing link, and a practical construction might well stop here. To understand what to make of the other pieces, however, it is necessary to examine what happened to subsection 1. First, Chapter 16 turned out to contain no "rule" expressly providing for compensation of reliance losses in the mistake-impracticability situation. Instead, it contained only two sections stating a separate rule for restitution in such cases, *see id.* §§ 376 & 377, one of which expressly states that reliance losses cannot be taken into account in restitution awards. *Id.* § 377, Comment b. Thus, the black letter of subsection (1) was amended by deleting the provisional reference to Chapter 16, and by adding in its place a specific reference to the appropriate restitution section (376 or 377). This change left the black letter, as it now stands, authorizing only two specific types of relief: restitution, and the § 240 remedy of a pro-rated price for divisible performance.

Comment b and the Illustrations citing subsection (1), however, remained unchanged. Comment b retains the statement that relief may extend beyond restitution to reliance claims, and the Illustrations still cite subsection (1) as authority for the award of money compensation for reliance. *Id.* §§ 158 & 272. As authority for the statement about reliance losses, Comment b to § 158 cites Illustration 8 to § 153, a rather appealing but remote example based on unilateral mistake. In Comment b to § 272, the same statement is supported by a puzzling citation to § 377, which, if anything, points to the opposite conclusion.

The final act in the reliance-loss scenario was an amendment to the Reporter's Notes for §§ 158 and 272, made at some time after the 1974-75 tentative drafts. The addition to the Note for § 158 is not much in point. It cites three cases that involve money damage awards in mistake cases, but none involve reliance damages. The addition to the § 272 note, however, cites four impracticability cases which do support the proposition that reliance losses may be compensated. Arguably, the discussion in *Albre Marble & Tile Co. v. John Bowen Co.*, 338 Mass. 394, 155 N.E.2d 437 (1959), is also authority for recognizing a long list of bogus restitu-

money compensation for reliance losses.<sup>28</sup> The intention to authorize such compensation is reasonably clear, however, and a literal reading of subsection (2) certainly gives that authority. Consequently, the following discussion proceeds on the assumption that compensation of reliance losses is authorized.

The rule of sections 158 and 272 involves an interesting extension of the reliance interest into areas outside the normal limits of promissory obligation. Professor Perillo has called these two sections "a new cause of action . . . for reliance,"<sup>29</sup> pointing out that they arise in situations in which the duty of performance has been discharged and in which liability cannot, therefore, be based on the breach of that duty. These sections appear to say that reliance-inducing behavior may create liability for losses other than those caused by a promisor's wrongful failure to perform. Such distinctive forms of reliance liability would be concrete examples of the independent liability that the *Restatement Second* meant to authorize when it recognized reliance as a separate and distinct interest.<sup>30</sup>

In what sense is the remedy of sections 158 and 272 different from contract liability and the more familiar forms of reliance liability (*e.g.*, sections 90 and 139)? The distinction does not lie in the nature of the conduct that gives rise to liability. Sections 158 and 272 apply to parties who have made contracts, or other promises that are binding due to reliance.<sup>31</sup> The conduct that gives rise to sections 158 and 272 liability is thus the same promise-making that triggers contract and other reliance liability.

The difference is that sections 158 and 272 have recognized additional obligations arising from the same conduct. Both contract liability and the more familiar reliance liability of sections 90 and 139 protect the promisee by imposing an obligation upon the promisor to perform. Breach of the duty of performance is the "wrong," and the harm to be compensated is the loss caused by that wrong. Sections 158 and 272 go beyond this and make promisors liable for some reliance losses that have not been caused by wrongful nonperformance, including some that oc-

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tion cases as added authority. These cases are cited in explanation of Comment c to § 272, which means that they are meant as authority for subsection (2)!

The simplest answer to this puzzling structure is to disregard the various problems with Comments and Illustrations, on the ground that they were drafted at an earlier date, and then to read the black letter of subsection (2)—the only text actually adopted by the Institute—as it is written. Subsection (2) states clearly that courts may grant remedies to protect the reliance interest if justice requires. The wording of subsection (2) requires one to accept the somewhat anomalous proposition that its reliance interest remedy is not within "the rules stated in Chapter 16"; the explanation, perhaps, is that § 344 is not a "rule."

<sup>28</sup> See the second paragraph of note 28 *supra*.

<sup>29</sup> Perillo, *supra* note 21, at 40.

<sup>30</sup> See notes 9-16 and accompanying text *supra*.

<sup>31</sup> See RESTATEMENT (SECOND) OF CONTRACTS § 158, Comment c (1979).

cur because the promisee is unable to perform.<sup>32</sup> It is difficult to be precise about the basis and the exact dimensions of this added liability. The justification is usually stated in terms of overall equities, and several different and even contradictory theories of justification may be involved.

The most distinctive theory of liability in this area would be a loss-sharing theory which asserts that the parties to a contract are participants in a common venture, and so should bear common responsibility for losses caused by unforeseen disasters for which neither party is to blame. If one thinks about the basis of such a theory, it is evident that the *conduct* being relied upon to justify liability (for at least fifty percent, anyway), is no more than the ordinary promise-making behavior that began the contract venture. The liability does not depend on any further duty to do or not do anything. It is simply an insurance-type responsibility for disaster losses, resting on the reliance-inducing promise alone.

It may be some time before such a pure theory is stated in decisions. The typical result in the reliance-restitution cases in this area is that some or all of one party's reliance losses are shifted to the other. That is, at least, the formal outcome. Where the stated outcome is an unequal distribution of the loss (and especially where that is really the outcome), the result obviously cannot be justified on a pure loss-sharing theory. To justify a decision imposing an unequal distribution of the loss, some other factor must be relied upon, either a different view of the responsibility assumed by promise-making or some other conduct or omission by the defendant that can be recognized as creating a superior responsibility for the loss.

One justification for such unequal distribution could be a different value judgment about the responsibility that arises from the promise-making behavior itself. That is, one might argue that the party whose performance is being excused should be liable for the other's reliance. This implies another form of absolute liability. Unlike the loss-sharing version, however, it entails the conclusion that each party assumes total responsibility for the other's reliance losses if its own performance is excused.

Other justifications may be based on particular aspects of the promise-making behavior—for example, where loss imposition is justified because the defendant initiated the project, or had superior knowl-

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<sup>32</sup> Subsection 2 of §§ 158 and 272 authorizes courts to grant relief in order to protect "the parties' reliance interest." The use of the plural possessive extends the protection to either party's reliance interest, including the party whose performance duty is being excused because of mistake or impracticability/frustration. Three of the four cases cited by the Reporter's Note in support of subsection (2) of § 272 involve recovery by the party whose duty has been excused. *See* note 33 *infra*.

edge of the risk. The liability here has a fault-oriented character, and its logic resembles the justification for conventional misrepresentation liability. Still other justifications may be found in conduct occurring after the contract is made. These justifications would also involve fault-oriented judgments, as where the defendant's conduct has somehow contributed to the disaster, or the defendant has failed to make use of superior ability to prevent or insure against it. Justifications of this kind suggest that promise-making also creates a lesser duty not to endanger the other party's reliance investment, a theory whose logic resembles ordinary tort liability.

The various theories suggested by sections 158 and 272 illustrate two important facets of a conceptual structure that treats the reliance interest as a separate basis of liability. First, these theories demonstrate that the independent analysis of reliance claims can identify bases of liability that are more than just the extension of a contract-type duty of performance. It is evident that other, quite distinctive duties may also flow from reliance-inducing behavior.

Second, the recognition of these other types of liability shows that there is not necessarily a single measure of reliance liability. The measure of recovery will necessarily depend on the discrete value judgments underlying the particular concept of liability at issue. For example, a loss-sharing theory necessarily implies liability limited to fifty percent of combined reliance losses. Moreover, that theory may or may not mean an expectancy ceiling on the amount of reliance losses to be shared. The recognition of an insurance-type responsibility for disaster losses could well include the judgment that both parties ought to share at least one kind of over-expectancy expense as well—the extra expense that a party incurs in a good-faith effort to overcome the excusing difficulties that both parties failed to foresee. Likewise, a theory of liability based on the conclusion that the defendant has somehow warranted or misrepresented the feasibility of the plaintiff's performance could also lead to liability for more-than-expectancy losses, but in this case the justification would be that the defendant's particular conduct (the representation of feasibility) was an important cause of the plaintiff's excess expenditures.

The *Restatement Second* does little to develop the theory or dimensions of the remedy stated in sections 158 and 272. The Comments give a sense of broad equitable power to do what is fair, suggesting that it is impossible to generalize in view of the infinite variety of equitable considerations that may arise in this area. The Illustrations and case citations relevant to the reliance remedy present a mixture of apparent theories, many of which appear to rely only slightly on extended ideas of

loss sharing.<sup>33</sup> The reliance interest concept opens the door to a wide-ranging analysis, but the articulation of the particular theories of sections 158 and 272 awaits further judicial development.

## II

### THE RELIANCE MEASURE OF DAMAGES

Section 349 of the *Restatement Second* establishes a special remedy for "damages based on [the promisee's] reliance interest." It allows the plaintiff to recover such reliance losses without having to prove the value of the expectancy.

In contrast to the terms "expectation interest" and "restitution interest," both of which embody an extensive case law furnishing detailed rules of application,<sup>34</sup> neither the term "reliance interest" nor the more common expressions "reliance loss" or "reliance damages" are very well developed. This section examines the guidance furnished by the *Restatement Second* on a few of the central issues in defining the concept of reliance damages under section 349.

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<sup>33</sup> The one pertinent illustration cited in the Comment to § 158 is a mistaken bid case, in which the party guilty of the unilateral mistake is made to pay the reliance expenses of the other party as a condition of being excused from his contract duty. RESTATEMENT (SECOND) OF CONTRACTS § 153, Illustration 8 (1979). It takes very little loss-sharing to explain the result.

A shade less blatant, but still fairly obvious, is the degree of fault involved in three of the four cases cited in the Reporter's Note to § 272. In *Hol-Gar Mfg. Corp. v. United States*, 360 F.2d 634, 638 (Ct. Cl. 1966) and *Maxwell Dynamometer Co. v. United States*, 386 F.2d 855, 872 (Ct. Cl. 1967), liability rested on the conclusion that, by providing specifications that called for performance that was not feasible, the United States was warranting or representing to the other party that the performance was feasible. *Northern Corp. v. Chugach Elec. Ass'n*, 518 P.2d 76, 82-85 (Alaska), *modified on rehearing*, 523 P.2d 1243, 1245-46 (1974), *aff'd*, 562 P.2d 1053 (1977), relied on *Hol-Gar* and *Maxwell* in holding that a public utility undertakes similar responsibility for reliance losses when, with superior knowledge, it uses its contract rights to insist upon further efforts to perform after it should have become aware of the impossibility of performance. Liability in *Chugach* was limited to the additional reliance expenditures caused by the utility's insistence on performance. In all three of these cases, incidentally, recovery was *in favor of* the party who was seeking to be excused from performance. *Albre Marble & Tile Co. v. John Bowen Co.*, 338 Mass. 394, 155 N.E.2d 437 (1959) also mentions fault as a prominent factor—the fault being the general contractor's erroneous bidding procedure which led to the general contract being declared illegal. Nevertheless, the court also discussed more general ideas of loss-sharing, and gave the appearance that the fault issue was only one of many equities that were involved.

Finally, the two most pertinent Illustrations cited in Comment b to section 272 do not contain any conspicuous issues of fault on either side; they are straightforward cases of supervening frustration or impossibility. While both Illustrations could be taken to suggest a loss-sharing approach, both involve liability imposed on the party whose duty is being discharged. RESTATEMENT (SECOND) OF CONTRACTS § 262, Illustration 3 (1979); *id.* § 265, Illustration 2.

The Illustrations to §§ 158 and 272 themselves do not deal with the issue of compensation for reliance losses. For a general explanation of what Illustrations are cited where and why, see note 27 *supra*.

<sup>34</sup> See RESTATEMENT (SECOND) OF CONTRACTS §§ 347, 348 & 371 (1979). Apart from these master definitions, the measures are refined and elaborated throughout the Comments and Illustrations of Topics 2 and 4 of Chapter 16.

### A. *Out-of-Pocket Expenses vs. Foregone Opportunities*

Fuller and Perdue's definition of the reliance interest included not only direct out-of-pocket expenditures in reliance on a promise, but also opportunities, such as alternative contracts, that are foregone in reliance on the promise at issue.<sup>35</sup> Fuller and Perdue defined the interest broadly, reserving for later consideration questions about the particular legal effects that various kinds of reliance ought to have. Although they confessed doubts whether the loss of the foregone opportunities should be compensated in situations where enforcement of the full expectation was precluded, they did not offer a firm conclusion.<sup>36</sup> The rule of section 349 raises this issue squarely.

Courts will look with disfavor on the broader claims of reliance loss under section 349. The section states a separate and easier standard of proof for damages. The more favored treatment is based on the perception that the type of loss in question has a particularly compelling character. The discrete ethical appeal of reliance losses is the perception that the plaintiff has been made "worse off" than before. Out-of-pocket expenditures fit within this notion quite comfortably, because they involve a clear diminution of existing assets. Foregone opportunities appear less clear, because it is more difficult to regard opportunities for gain as present assets.

Arguably, courts could make a distinction simply based on certainty. That is, if a party to a contract can prove the loss of a foregone opportunity and its value with the requisite certainty, then courts should treat the opportunity like a present asset, and the foregoing of that opportunity like a worse-off reliance loss.<sup>37</sup> More complex perceptions of gain and loss, however, will probably come into play. For example, there is likely to be a distinction between opportunities that involve entrepreneurial gain and those that involve wages. Opportunities that involve wages (the foregoing of an existing or clearly available job) will make an attractive claim, for working time is usually perceived as a present asset, and its value is typically measured by opportunity cost. Opportunities that involve entrepreneurial gain, on the other hand, have a stubborn tendency to look like gain wherever they come up. It will be difficult for a court to award out-of-pocket reliance on the con-

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<sup>35</sup> See note 2 *supra*.

<sup>36</sup> Fuller & Perdue, *supra* note 1, at 417-18.

<sup>37</sup> Even if the certainty test does not *validate* claims for foregone opportunity, it should play an important role in the opposite direction—that is, in *excluding* such claims. The typical opportunity foregone when making a contract is the opportunity to contract with someone else for the same performance. If a party cannot prove the value of the contracted-for performance (the only case that we need to worry about), it is highly unlikely that he will be able to prove the value of the alternative contract foregone. The only case of foregone opportunity likely to surmount the certainty barrier is the case of the promisee who gives up an existing, or at least relatively certain, business opportunity in order to take advantage of a more speculative, uncertain, or intangible opportunity offered by the promisor.

tract *and* lost profit on a foregone alternative venture, without feeling that such a recovery leaves the plaintiff "better off."<sup>38</sup>

Section 344's definition of reliance interest appears to say very little on this point. The definition has two parts: the promisee is to be reimbursed for (1) "loss caused by reliance on the contract" by (2) "being put in as good a position as he would have been in had the contract not been made."<sup>39</sup> The first part of the definition could include almost any form of detrimental reliance. The key question is whether "loss" includes a foregone opportunity. Similarly, the second part of the definition turns on the word "position"—implying asset position, but leaving open the ultimate question of what things constitute assets.

The black letter of section 349 merely incorporates the section 344 term "reliance interest." Comment a to section 349 uses the word "expenditure" as synonymous with "reliance loss." For example, the Comment says, "[u]nder the rule stated in this Section, the injured party may . . . recover as damages his expenditures in reliance." Expenditure is considerably less pliable than loss or position, but it also ultimately turns on one's concept of assets. Thus, the word is probably broad enough to encompass claims for foregone wages, especially if the loss were rephrased as working time invested in the contract. It would be difficult, however, to make the word "expenditure" fit a foregone business opportunity.

The Illustrations of reliance damages in section 344 and 349 all involve the expenditure of money. The only Illustration that treats a foregone opportunity as a damage issue is Illustration 10 to section 90, which restates *Hoffman v. Red Owl Stores, Inc.*<sup>40</sup> The issue in that case was the compensability of prospective grocery store income that had been foregone when the plaintiff sold his grocery store in reliance on the defendant's promise to award him a Red Owl franchise. Technically, the issue in both the section 90 Illustration and the case itself was not whether such foregone income was a reliance loss, but rather whether justice required compensation of that item in a promissory estoppel action.<sup>41</sup> Both the court and the Illustration answered in the negative. Notwithstanding the different issue involved, both explanations imply a characterization of the foregone income as something outside the category of reliance loss. The court stated that "[j]ustice does not require that the damages . . . should exceed any actual loss sustained. . . ."<sup>42</sup>

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<sup>38</sup> "[I]t is in the field of gains prevented that the reliance and expectation interests tend to lose their separate identities." Fuller & Perdue, *supra* note 1, at 417 (footnote omitted). Fuller and Perdue acknowledge that most persons perceive wages differently, even though they could see no logical distinction. *Id.* at 418.

<sup>39</sup> RESTATEMENT (SECOND) OF CONTRACTS § 344(b) (1979).

<sup>40</sup> 26 Wis. 2d 683, 133 N.W.2d 267 (1965).

<sup>41</sup> *Id.* at 701, 133 N.W.2d at 276.

<sup>42</sup> *Id.* at 702, 133 N.W.2d at 277.

Illustration 10 states that “[s]ince the proposed agreement was never made, . . . [the plaintiff] is not entitled to lost profits from the sale of the grocery or to his expectancy interest in the proposed franchise. . . .”<sup>43</sup>

On the whole, the *Restatement Second* appears to lean toward limiting the concept of reliance losses under section 349 to something like out-of-pocket expenditures, in apparent agreement with the “better-off/worse-off” distinction suggested earlier. Still, the black-letter definitions themselves leave considerable room for interpretation, and that is not necessarily undesirable. The border line is vague, and case-by-case resolution appropriate.

### B. *Overhead and Pre-Contract Expenses*

Not all out-of-pocket losses are reliance losses. The Comment to section 349 states that reliance losses do not include fixed overhead expenses charged to the contract. The reason for this exclusion is that the concept of reliance requires a traceable causal connection between the making of the expenditure and the contract; the contract promise must induce the expenditure. Because fixed expenses are by definition incurred whether or nor the particular contract is undertaken, the causal link between the expense and the contract does not exist. The theory that excludes fixed expenses actually excludes any expenses or obligations to incur future expenses made before the parties entered into the contract, whether the expenses are deemed fixed or variable with regard to the overall transaction to which they relate.

Because the issue is causation, a certain flexibility as to the time line can be anticipated. Flexibility is most likely to appear when pre-contract expenses make a particularly appealing claim, as in the case where, although the value of the expectancy cannot be proved, the circumstances suggest that the plaintiff would have recovered all pre-contract expenses had the contract been performed. In such a case courts may adopt various time-bending constructions to justify awarding the pre-contract expenses as reliance damages. The most familiar example is *Security Stove & Manufacturing Co. v. American Railway Express Co.*,<sup>44</sup> in

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<sup>43</sup> RESTATEMENT (SECOND) OF CONTRACTS § 90, Illustration 10 (1979). The implication of Illustration 10, that things might be different if the parties had concluded the franchise contract, could give one second thoughts about its message concerning reliance losses. Clearly, concluding the franchise contract would have given the plaintiff a claim for ordinary expectancy damages—the lost profits of the franchise agreement. Is the Illustration also saying, however, that in the absence of provable franchise profits, the plaintiff could claim lost grocery-store profits as a § 349 reliance loss? If so, the Illustration points in a direction contrary to the out-of-pocket concept that I am suggesting.

Although this possibility must be recognized, my reason for not so interpreting the Illustration is its characterization of the foregone grocery profits as “lost profits,” and the seemingly parallel treatment that it gives to these lost profits and the actual expectancy profits of the franchise.

<sup>44</sup> 227 Mo. App. 175, 184, 51 S.W.2d 572, 577 (1932).

which the court held that a common carrier's duty to accept shipments from the public made it possible for the plaintiff to rely on the shipment contract before it was actually concluded. Pre-contract negotiations may possibly generate a similar reliance link to pre-contract expenses.<sup>45</sup>

The distinction between reliance expenditures and other out-of-pocket expenses complicates the losing-contract calculation under the rule of section 349. In cases where the claim for reliance expenses includes only some of the total out-of-pocket expenses, it will not be enough for the defendant to show that the total return from performance would have fallen short of total costs.<sup>46</sup> The fact that revenues would not have covered the plaintiff's fixed and pre-contract expenditures will be immaterial. If the return would have covered only the reliance costs, then the plaintiff is not being made better off if he now recovers damages for them.

If the breach results in a saving, whether from salvage of pre-contract expenses, reassignment of fixed expenses to another contract made possible by the breach, or saving of variable costs not yet expended, this saving will have to be deducted from the projected return. That reduced figure must then be the basis of the comparison with the reliance claim. For example, if the projected return is just enough to cover 100% of the reliance expenses, and if the breach has enabled plaintiff to salvage some pre-contract expense, a court should not award all of the reliance expenses. Full recovery of reliance expenses would, when added to the saving, put plaintiff in a better position than performance would have.

How often these losing-contract problems will appear is an open question. Section 349 is designed for cases in which neither side can prove the expectancy. Many plaintiffs, however, may be tempted to seek section 349 reliance damages in cases where they clearly have a losing contract in the hope that the breaching party will not be able to prove so. A section 349 claim might become a common companion to a restitution claim in such circumstances, particularly if courts accept the *Restatement Second's* invitation to tighten the concept of benefit in restitution actions.<sup>47</sup>

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<sup>45</sup> The situation that I have in mind is not the promise-induced pre-contract reliance of *Hoffman v. Red Owl Stores, Inc.*, 26 Wis. 2d 683, 133 N.W.2d 267 (1965), but *Hoffman*-like reliance that takes place during the negotiation of a contract that is actually concluded, based simply on the plaintiff's (correct) judgment that the deal is going to go through.

<sup>46</sup> The text of § 349 could be read the other way, because it speaks of deducting "any loss . . . the injured party would have suffered had the contract been performed." The references in all four Illustrations to proving the "profit or loss [plaintiff] would have made" give the same impression that "loss" means the final overall result. RESTATEMENT (SECOND) OF CONTRACTS § 349, Illustrations 1-4 (1979). For the reasons stated in the text, that interpretation makes no sense if, as I assume, the object here is to apply the expectancy ceiling.

<sup>47</sup> Whether intentionally or not, the reliance damages and restitution provisions of the *Restatement Second*, read together, produce a subtle design for law reform that could produce

### C. *Essential and Incidental Reliance*

The Comment to section 349 makes clear that its special rule for reliance damages applies both to "essential" and "incidental" reliance expenditures. The essential/incidental distinction is Fuller and Perdue's.<sup>48</sup> As generally understood, the two categories cover the field; reliance that is not essential is incidental. The Comment tells us, therefore, that the section 349 rule for recovery of reliance losses applies to all reliance losses.

The Comment confirms an important change made by the black letter of section 349. The first *Restatement* rule authorizing recovery of reliance damages (section 333) limited recovery to "expenditure[s] reasonably made in performance of the contract or in preparation therefor."<sup>49</sup> This limitation excluded from recovery reliance expenditures invested in collateral transactions, the type of reliance expenditure that Fuller and Perdue labeled incidental. Fuller and Perdue criticized the limitation as being contrary to the overwhelming weight of the case law, even in 1932.<sup>50</sup> The section 349 black letter of the *Restatement Second* signals somewhat obliquely the elimination of the prepara-

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considerable business for § 349 if it works. The design unfolds like this: Over the years, courts have expanded the concept of "benefit" in restitution law in order to compensate pure reliance losses that, for one reason or another, fell outside the area in which contract remedies operate. One of the unfortunate by-products of this development has been a tendency to compensate reliance losses in excess of the expectancy ceiling, because under restitution doctrine the remedy for unjust enrichment is not limited by the contract expectancy. The *Restatement Second* relieves this pressure on the restitution remedy by granting or expanding reliance remedies in several needed areas, especially § 349 and §§ 139, 158, and 272. It also introduces some tightening into the benefit concept of restitution law, albeit at the same time also recognizing broader concepts of benefit that are by now too well established to ignore. See Perillo, *supra* note 21, at 38-43. The result is a potentially narrower restitution standard that will permit and encourage courts to redirect reliance claims into the new reliance remedies. To the extent this happens, reliance-loss claims based on losing contracts will be dealt with under the rules of § 349.

<sup>48</sup> Fuller & Perdue, *supra* note 1, at 78.

<sup>49</sup> Section 333 of the first *Restatement* provided:

WHEN DAMAGES MAY BE MEASURED BY  
EXPENDITURES IN PART PERFORMANCE

The amount of the plaintiff's expenditure, reasonably made in performance of the contract or in necessary preparation therefor, is included in compensatory damages, with the following limitations:

- (a) Such expenditures are not recoverable in excess of the full contract price promised by the defendant.
- (b) Expenditures in preparation are not recoverable unless they can fairly be regarded as part of the cost of performance in estimating profit and loss.
- (c) Instalments [sic] of the contract price already received and the value of materials on hand that would have been consumed in completion must be deducted.
- (d) If full performance would have resulted in a net loss to the plaintiff, the amount of this loss must be deducted, the burden of proof being on the defendant.

RESTATEMENT OF CONTRACTS § 333 (1932).

<sup>50</sup> Fuller & Perdue, *supra* note 1, at 90-92. On the related issue of whether the "contract

tion/performance limitation, authorizing recovery of "damages based on [the promisee's] reliance interest, *including* expenditures made in preparation for performance or in performance."<sup>51</sup>

The essential/incidental terminology raises many ghosts. Fuller and Perdue invented the distinction to make an important point about the expectancy ceiling for reliance damages. Unfortunately, their explanation of the distinction was one of the least clearly expressed ideas in their article, and not everyone agrees on its exact meaning.<sup>52</sup> This lack of clarity seems to be at the root of some rather puzzling statements in the *Restatement Second's* discussion of the expectancy ceiling on reliance damages.

The difficulty with the essential/incidental distinction arises primarily because two distinctions, rather than one, lurk in this terminology. One is the distinction between reliance that is required to satisfy a contract duty, and reliance that is not. Examples of the former, which might be called obligatory reliance,<sup>53</sup> would be: (1) expenditures by a contractor in preparation to perform, and in performance of, the services called for by the contract; (2) expenditures by a seller of goods to purchase or manufacture the goods required by the contract; and (3) expenditures by a franchisee to rent a store, hire salesmen, and promote sales of the franchised product, under a franchise contract that requires the franchisee to do so. Examples of the latter, which might be called nonobligatory reliance, would be: (1) expenditures by a purchaser of a retail store for a stock of goods he intends to sell in the store; (2) expenditures by a buyer of industrial machines for other equipment and furnishings needed to make profitable use of the purchased machines; and (3) expenditures by a lessee of a theater to prepare a series of theater performances, under a theater lease that provides for a fixed rental and contains no obligation to perform anything.

The second distinction lurking in the essential/incidental terminology relates to the issue of whether reliance expenditures would have been recovered had the breaching party performed. Reliance expenditures are an investment made in expectation of some transfer of value in return in value. In order to determine whether reliance expenditures would have been recovered, it is necessary to identify the value-producing transaction that would have covered the expenditures. Two types of

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price" should be a ceiling on recovery of § 349 damages, see notes 58-59 and accompanying text *infra*.

<sup>51</sup> RESTATEMENT (SECOND) OF CONTRACTS § 349 (1979) (emphasis added).

<sup>52</sup> See, e.g., the text accompanying note 65 *infra*, disagreeing with Judge Hand's application of the distinction in *L. Albert & Son v. Armstrong Rubber Co.*, 178 F.2d 182 (2d Cir. 1949).

<sup>53</sup> The term "obligatory" is not a perfect one, for it might be read to suggest a distinction between performance and preparing to perform. I mean to include both. The idea is reliance that is devoted to the satisfaction of a contract duty.

value-producing transactions may be distinguished. One is the value received by obtaining the promised performance itself, such as the price received by a seller of goods. The other is value received from consequential transactions that would have been undertaken on the basis of the promised performance—for example, where the contract involves the purchase of business premises, the revenues that would have been received from the business being located there.<sup>54</sup>

In the case where reliance expenditures look solely to the value of the return performance, it is clear that such expenditures would only have been recovered up to the value of the return performance. In such cases, the “contract price” (i.e., the value of the return performance) is a ceiling upon reliance damages. Where, however, a party invests the reliance expenditures in other, consequential transactions, the ceiling on recovery is the expected return from those consequential transactions. That is, in order to determine whether the reliance expenditures would have been recovered, it is necessary to determine the amount of value these consequential transactions would have produced.

This second distinction may be termed the distinction between direct reliance and consequential reliance. Some illustrations are helpful. Consider the three examples of obligatory reliance given earlier. The first two examples—the contractor investing in the performance of his promised service, and the seller of goods investing in his promised goods—are instances of direct reliance. They are expenditures invested solely in the value of the return performance; to the extent that they exceed the value of the return performance, they would not have been recovered by performance.

The third example, involving preparation expenses by a franchisee, is an instance of consequential reliance. The return performance by the franchisor is merely the granting of the franchise rights. The franchisee’s expenditures may be a contractual obligation, necessary to earn the legal right to the franchisor’s return performance, but the expenses are actually an investment in a transaction that is consequential to

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<sup>54</sup> Fuller and Perdue make the point that the income to be derived from consequential transactions can be described as being part of the value of the contracted-for property; for example, the capitalized income that a machine can earn can be said to be the machine’s “value,” as much as its market price. See Fuller & Perdue, *supra* note 1, at 75-76. I find the point, and the concepts of “objective” and “subjective” value that they developed in order to deal with it, needlessly confusing. If a piece of property has consequential value and the loss of that property prevents the realization of that consequential value, what one wants to know is how much it would have earned, and what it would have cost to do so. Nothing is gained by adding a step that requires us to recalculate this data so that we may speak of it as the property’s value.

The objective-subjective terminology also confuses communication about another issue where one would normally use the term subjective, namely, the case where the consequential transaction is of personal (subjective) rather than economic value. For example, a sportsman flies to a remote Alaskan lake to go fishing, but the common carrier fails to deliver his fishing equipment!

granting the franchise, namely the expected revenues from the sale of the franchised product to the public. It is the revenue from sales, not the abstract value of the franchise right, that would have covered these reliance expenditures. In this case it would not be proper to use the contract price (the fair market value of the franchise right) as a ceiling on the amount of expenditures that could be recovered as reliance damages.

Which of these two distinctions did Fuller and Perdue's essential/incidental distinction mean to signal? The functional purpose of the distinction points in one direction, while the words point in the other. Fuller and Perdue's purpose was to define when the contract price should and should not be a ceiling on reliance damages.<sup>55</sup> This should have led to the direct/consequential distinction, which looks at the value-producing transaction in which the reliance was invested. Fuller and Perdue's terminology, however, pointed toward the obligatory/nonobligatory distinction, as did their much-quoted explanation that essential reliance was "in a loose sense the 'price' of whatever benefits the contract may involve for the plaintiff."<sup>56</sup>

The *Restatement Second's* description of the essential/incidental distinction retains the ambiguity found in Fuller and Perdue. Comment a to section 349 states:

Often the reliance consists of preparation for performance or actual performance of the contract, and this is sometimes called "essential reliance." See, for example, Illustration 3. It may, however, also consist of preparation for collateral transactions that a party plans to carry out when the contract in question is performed, and this is sometimes called "incidental" reliance. See Illustration 4.

The reference to the Illustrations brings the ambiguity into focus. Illus-

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<sup>55</sup> *Id.* at 75-79.

<sup>56</sup> *Id.* at 78. Fuller and Perdue go on to name a category of acts which seems to be based on the idea of performing legal obligations. The conclusion that they *meant* obligatory reliance would not be a distortion of what they said.

The reliance damage provision of the first *Restatement* (§ 333) employed a concept of obligatory reliance in defining compensable reliance. See note 49 *supra*. Fuller and Perdue attacked this limitation, primarily because it excluded the many kinds of consequential reliance that courts were already compensating, most of which were instances of nonobligatory reliance, such as the planting of crops in the seed cases. Fuller & Perdue, *supra* note 1, at 90-92. It is at least possible that, when discussing the expectancy ceiling, the authors were led to define the direct/consequential distinction in terms of the somewhat different distinction that § 333 had employed to precipitate the debate over recoverability.

It is doubtful that the similarity between obligatory reliance and the restitution concept of "benefit" had any direct bearing on the matter. Benefit in restitution law is a favored classification, because of the ethical appeal of the fact that the defendant has bargained for the reliance involved, and thus can more readily be made responsible for paying for it. Essential reliance in Fuller and Perdue's distinction is a disfavored classification, for it subjects the reliance in question to a contract-price ceiling on recovery. The benefit concept may, of course, have influenced the § 333 definition, and in that way have introduced the idea of obligatory reliance into the field.

trations 3 and 4 themselves are correctly classified according to the definition suggested here; the former is clearly direct reliance (construction expenditures under a building contract), and the latter is clearly consequential reliance (expenditures by the purchaser of a retail store for the stock of goods he intends to sell in the store). But what of Illustrations 1 and 2? The "for example" in Comment a suggests that Illustrations 1 and 2 are two other examples of essential reliance. Yet in fact, both are difficult borderline cases where the ambiguities of the essential/incidental distinction can lead one astray. Illustration 1 is the example used in this Article to illustrate consequential reliance that also happens to be obligatory—the franchisee's promotion and start-up expenses. Illustration 2 involves a joint-venture theatre production, where formal classification as direct or consequential depends on just how the venture is set up, but where in either case the reliance expenses of preparing the production are an investment in sales of tickets to the public.<sup>57</sup> An understanding of the essential/incidental distinction which suggested that the contract price is the relevant ceiling for reliance damages in either of these two cases would very likely lead to an improper analysis.

Another passage in Comment a to section 349 also demonstrates the need for clarity here. It states:

If the injured party's expenditures exceed the contract price, it is clear that at least to the extent of the excess, there would have been a loss. For this reason, recovery for expenditures under the rule stated in this section may not exceed the full contract price.

If the Comment means to use the term "contract price" in its normally accepted sense—the value of the defendant's performance—the quoted passage would be a correct statement of the expectancy ceiling for direct reliance expenditures. It would not, however, be a correct statement of

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<sup>57</sup> A contracts with B to stage a series of performances in B's theater, each to have 50 per cent of the gross receipts. After A has spent \$20,000 in getting ready for the performances, B rents the theater to others and repudiates the contract, and A stages the performance at another theater. A's expenditures in preparation for performance of the contract with B are worth \$8,000 to him in connection with staging the performances at the other theater. If neither party proves with reasonable certainty what profit or loss A would have made if the contract had been performed, A can recover as damages the \$12,000 balance of his expenditures in preparation for performance.

RESTATEMENT (SECOND) OF CONTRACTS § 349, Illustration 2 (1979).

If we view this as a simple employment-type arrangement, B's promised performance (the contract price) is to pay 50% of the gross receipts, and this can be called direct reliance. If we consider this to be a demise of the theater to A, however, with A's rent being to pay 50% of the gross receipts to B (plus a good-faith obligation to put on some production), the reliance would be consequential, even though obligatory. In either case, the prospective revenues of the production constitute the ceiling on reliance expenditures. The latter case could be confusing if one began with the assumption that the contract price was a ceiling; the only performance promised by B would be the demise of the premises, and one could wind up thinking that the fair market value of the rental was relevant datum.

the expectancy ceiling for consequential reliance expenditures. The statement might, of course, have been intended to place a cap on damages for consequential reliance, possibly as a way of limiting potentially excessive recovery under the generous rule of section 349. A contract-price ceiling, however, would simply be too drastic for that purpose.<sup>58</sup> Moreover, it is hard to imagine such a purpose after Fuller and Perdue had so effectively attacked the contract-price limitation in the predecessor provision of to the first *Restatement*.<sup>59</sup> That meaning becomes even less plausible given that Illustrations 1 and 4 to section 349 involve consequential reliance, and point to the outcome of the appropriate consequential transactions as the appropriate ceiling.

According to Fuller and Perdue's analysis, the troublesome statement should say that the ceiling on reliance damages is the value of the expectation interest. The statement itself will probably be read that way when the need arises.

#### D. *Limiting Damages for Consequential Reliance*

If the only ceiling on reliance damages under section 349 is the expectancy ceiling,<sup>60</sup> then large awards for consequential reliance expenditures will be relatively easy to prove. The rule stated in section 349 does not distinguish between different types of reliance. The test for recoverability is the same for all: proof of the reliance expense, subject to the defendant's opportunity to prove that the expenses would not have been recovered upon performance. If the defendant cannot prove the value of the expectancy, the plaintiff can recover all consequential reliance expenditures.

Although actual reliance expenditures clearly present a more compelling case for relief than lost profits, claims for consequential reliance expenditures can raise many of the same concerns about remoteness and disproportion that lead courts to look for ways of limiting consequential damages generally. For claims made under section 349, these concerns are likely to be intensified because of the rather limited proof required.

The best illustration of this potential problem is found in a case which serves as one of the leading authorities for section 349 itself, *L. Albert & Sons v. Armstrong Rubber Co.*<sup>61</sup> The case involved the sale of four

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<sup>58</sup> Any recovery for consequential reliance losses would be ruled out in cases where the plaintiff demands both return of the price and compensation for expenditures made in attempting to use the defective product. A contract price ceiling would also, *inter alia*, overrule the recovery in Fuller's favorite case, *Security Stove & Mfg. Co. v. American Ry. Express Co.*, 227 Mo. App. 175, 51 S.W.2d 572 (1932), where the court awarded reliance damages of \$801.50 on a contract of carriage costing \$192.12 for freight and express charges.

<sup>59</sup> Fuller & Perdue, *supra* note 1, at 95. See generally *id.* at 89-95. The first *Restatement* provision was § 333. See note 49 *supra*.

<sup>60</sup> See notes 58-59 and accompanying text *supra*.

<sup>61</sup> 178 F.2d 182 (2d Cir. 1949).

rubber reconditioning machines which the buyer intended to use to produce reclaimed rubber. The sale price was approximately \$25,000. In reliance on the contract, the buyer made unsalvageable expenditures of approximately \$118,000 for other equipment in its rubber reclaim department, \$28,000 for rubber scrap, and \$3,000 for laying a special foundation to support the four machines. The buyer asserted that late delivery of the machines caused the collapse of the entire reclaim department, and claimed all these reliance expenses as damages.

The federal district court ruled that the buyer failed to prove its damages. Specifically, the court found that the buyer had not proved that the delay in delivery of the machines caused the collapse of the reclaim department. Delayed delivery, the court concluded, was only one of several possible causes.

The court of appeals agreed with the district court's conclusion as to causation. It agreed that this conclusion barred the claims of \$118,000 for the reclaim department and \$28,000 for the scrap rubber, saying that "[s]uch a possibility is not sufficient proof of causation to impose liability on the plaintiffs for the cost of all machinery and supplies for the reclaim department."<sup>62</sup> This part of the decision is often not mentioned, but it is the key to approaching the other holding in the case.

The court of appeals proceeded to hold that the claim for the \$3,000 foundation was different. It classified this item as an expense "necessary to prepare for performance,"<sup>63</sup> implying that the other two items were something different. As to this one item, the court invoked the rule now stated in section 349: the plaintiff was entitled to the reliance expense (the \$3,000), unless the defendant could prove that the expense would not have been recovered through the prospective earnings of the four machines. In effect, the court changed the burden of proof on causation for this one item.

The court's separate analysis of the \$3,000 foundation expenditure cannot be explained in economic terms. All three of the buyer's investments were investments in the reclaim department. All three expenditures would have been covered solely by the income from refining operations. If the department never ran, the plaintiff would not have recovered any of these expenditures. Analytically, the trial court was correct in treating all three items alike; all three rise or fall on the same causation question.

The appellate court's reasons for distinguishing the \$3,000 are simply wrong. Its statement that laying the foundations was "necessary to prepare for performance" was apparently the basis of this distinction,

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<sup>62</sup> *Id.* at 189.

<sup>63</sup> *Id.*

because it subsequently quoted the same language as it appears in section 333 of the first *Restatement*, the rule authorizing the award of reliance damages.<sup>64</sup> The court also labeled the foundation expense as "essential reliance" under Fuller and Perdue's dichotomy.<sup>65</sup> Apparently the court's idea was that the foundation expense was direct and/or obligatory reliance, and thus different in kind from the consequential, non-obligatory expenditures for the reclaim department and the rubber scrap. No such distinction was possible. The foundation expenditure certainly was not direct reliance, for as the court itself conceded, it could have been covered only by income from the refining operation. Nor was it obligatory reliance required by the contract, because the buyer's only contractual obligation was to pay the price.

The reason for the court's divided treatment seems obvious. The transaction took place near the end of World War II. The court noted that the market for reclaimed rubber was collapsing at the time that the department was about to commence operations.<sup>66</sup> Even if the machines had arrived on time, it was quite doubtful that the buyer would have commenced operations, or if it had, that it would have earned any money. In this situation, it seems that the court simply was not willing to give the plaintiff the benefit of the doubt when it came to substantial damage claims. True, the court did give the plaintiff the very small amount represented by the \$3,000 foundation expense, but in retrospect this looks like a token recognition of the legal wrong.

Consider how the rules of the *Restatement Second* would apply to the type of problem illustrated by *L. Albert & Sons*. If it is correct to say that no distinction exists between any of the three reliance claims, then the rule of section 349 must apply to all of them. This means that the defendant will be prima facie liable for all three reliance expenditures, unless it can prove that the plaintiff would not have recovered them upon performance. Cases will exist, of course, where the evidence of likely loss is strong enough to permit courts to find that the defendant has met its burden. On occasion, courts may even be able to compromise by finding that only a partial loss has been proved. In short, room exists within the rule of section 349 itself to eliminate the most troublesome cases.

For cases in which the evidence of causation and expectancy value is simply too uncertain to justify a finding for defendants, the *Restatement Second* offers other doctrinal methods of containment. Reliance damages are subject to all the rules stated for contract damages generally. Doctrines of certainty and foreseeability have traditionally been manipulated to control consequential damage claims deemed excessive.

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<sup>64</sup> *Id.* at 190.

<sup>65</sup> *Id.* at 191.

<sup>66</sup> *Id.* at 186.

The certainty requirement of section 352 will not be much help, given the limited proof that section 349 requires.<sup>67</sup> A strict application of the foreseeability test in section 351(1) and (2) might be used, but the *Restatement Second* provides a new rule asking courts to deal with such issues openly. Section 351(3) states:

A court may limit damages for foreseeable loss by excluding recovery for loss of profits, by allowing recovery only for loss incurred in reliance, or otherwise if it concludes that in the circumstances justice so requires in order to avoid disproportionate compensation.

The relationship between section 351(3) and reliance damages must be carefully analyzed. The rule's reference to reliance damages as a possibly suitable compromise does not, in terms, apply to reliance damages proved solely under section 349. The section is addressed to a situation in which a court wishes to *limit* damages. The only case in which an award of reliance damages can be viewed as a limitation is one in which the plaintiff has proved, or can prove, the full expectation measure of recovery—that reliance expenses plus anticipated profits would have been recovered had the contract been performed. The award of section 349 damages would never be called a limitation, because the proof given under section 349 never entitles the plaintiff to any more than reliance damages in the first place.

In addition, section 351(3) by no means creates a presumption in favor of reliance damages. It goes on to state that courts have a general power to limit consequential damages "if . . . justice so requires in order to avoid disproportionate compensation." The rationale stated for this general power refers to factors such as a relatively small contract price in relation to the size of the consequential-damage claim. It states that such factors can be evidence that the parties did not intend to make the defendant assume the risk of the much larger consequential transactions based on the contract.<sup>68</sup> If this rationale about nonassumption of risk is

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<sup>67</sup> RESTATEMENT (SECOND) OF CONTRACTS § 352, Comment a (1979).

<sup>68</sup> Comment f to § 351 provides:

*Other limitations on damages.* It is not always in the interest of justice to require the party in breach to pay damages for all of the foreseeable loss that he has caused. There are unusual instances in which it appears from the circumstances either that the parties assumed that one of them would not bear the risk of a particular loss or that, although there was no such assumption, it would be unjust to put the risk on that party. One such circumstance is an extreme disproportion between the loss and the price charged by the party whose liability for that loss is in question. The fact that the price is relatively small suggests that it was not intended to cover the risk of such liability. Another such circumstance is an informality of dealing, including the absence of a detailed written contract, which indicates that there was no careful attempt to allocate all of the risks. The fact that the parties did not attempt to delineate with precision all of the risks justifies a court in attempting to allocate them fairly. The limitations dealt with in this Section are more likely to be imposed in connection with contracts that do not arise in a commercial setting. Typical examples of limitations imposed on damages under this discre-

taken literally, it will apply to all liability for consequential losses—reliance expenditures as well as lost profits. Moreover, even if a court's objective is merely to reduce consequential liability to a more proportional amount, that will often be difficult to do without limiting reliance damages, because like any business transactions, the average consequential transaction figures to be about eighty percent expenses. In sum, despite its approving reference to reliance damages, section 351(3) states a rule that could limit consequential reliance damages, both generally and especially as applied to those proved solely under the rule of section 349.

The *Restatement Second* contains no direct recognition of the need to limit section 349 reliance damages in particular. Two curious statements in the commentary, however, indicate some underlying sensitivity to the problem. First, the Comment to section 349, mentioned in the previous section, states that the contract price is a ceiling on reliance damages under section 349.<sup>69</sup> Read literally, of course, the contract-price limit would obliterate claims for consequential reliance losses. Assuming that this was not meant, the existence of this puzzling statement may reflect an intuitive recognition of the difficulty with consequential reliance claims under the rule of section 349.

The idea of a contract price ceiling appears again in Comment d to section 90, which says that “[i]n the case of a promise to make a gift it would rarely be proper to award consequential damages which would place a greater burden on the promisor than performance would have imposed.”<sup>70</sup> Given that section 90 damages must be proved with all the certainty and foreseeability required for ordinary contract damages, this statement must be read as an illustration of how the “as justice requires” limitation might be applied to otherwise provable section 90 damages.

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tionary power involve the denial of recovery for loss of profits and the restriction of damages to loss incurred in reliance on the contract. Sometimes these limits are covertly imposed, by means of an especially demanding requirement of foreseeability or of certainty. The rule stated in this Section recognizes that what is done in such cases is the imposition of a limitation in the interests of justice.

RESTATEMENT (SECOND) OF CONTRACTS § 351, Comment f (1979).

<sup>69</sup> See notes 58-59 and accompanying text *supra*.

<sup>70</sup> RESTATEMENT (SECOND) OF CONTRACTS § 90, Comment d (1979).

The drafting history of the *Restatement Second* contains a third instance in which the contract price was offered as a ceiling on recovery for purposes that went beyond simple expectancy theory. The problem involved the anomalous situation in restitution law in which, in certain cases, a party who completes performance before breach can recover only the contract price, whereas the party who performs only partly may sue in restitution for the value of benefits conferred by the part performance, and in that case the contract price is not a ceiling. The 1979 tentative draft proposed to limit restitution recovery in such cases to the sum that would have been recoverable on full performance (i.e., the contract price). RESTATEMENT (SECOND) OF CONTRACTS § 387(2) (Tent. Draft. No. 14, 1979). The proposal was, in effect, withdrawn, see 56 ALI PROCEEDINGS 405-13 (1979), and the old rule left standing, see RESTATEMENT (SECOND) OF CONTRACTS § 373(2) (1979).

The suggestion seems to be that the gratuitous nature of the promise should be considered as a factor relevant to the justice of imposing extended liability for consequential damages. Although this section 90 Comment clearly does not pertain to section 349 reliance damages generally, it does indicate a recognition that large consequential-reliance claims are often less compelling than the more modest claims for direct reliance.

Distinctions between various types of reliance claims tend to be obscured by our preoccupation with the larger reliance-expectancy distinction, in which the point is usually to show that reliance claims are the more compelling. We need to be reminded that important differences in the degrees of ethical urgency exist within the category of reliance claims as well. These differences are quite likely to influence decisions, appearing in one form or another as a grudging attitude toward some consequential-reliance claims.

#### CONCLUSION

One can well understand the reasons for wishing to give formal recognition to the reliance interest in the *Restatement Second*. The substance of the new *Restatement* owes an enormous intellectual debt to the analysis underlying that concept. Far beyond its message about reliance, that analysis has served a generation of contracts scholars as a model of how to think about contract law generally. The *Restatement Second* without the reliance interest would have been the words without the music.

Moreover, some tangible gain obviously accrues from according formal approval to the ideas represented by the reliance interest concept. At a minimum, such approval helps to clear away the wooden conceptual structure of the first *Restatement* with which Fuller and Perdue had to contend. The ideas themselves deserve to be commended as the most useful starting point from which to seek understanding of the reliance-based law that is, and to think about less settled issues such as those opened by sections 158 and 272.

Because of its musical quality, however, the reliance interest concept does not translate easily into the more formal and precise medium of Restatement black letter. Fortunately, the concept is used only sparingly, so that the problems it creates are not significant. Still, the problems do illustrate the difficulties of giving more formal status to concepts so general and multi-functional.

Restating the reliance interest has probably hardened some of the less helpful conceptual overtones suggested by the expectation-reliance-restitution matrix. This Article's quarrel with the overbroad entitlement overtones of the reliance-interest definition is a small example. More generally, the meaning of the interest matrix is likely to continue to serve as a puzzling classroom problem for first-year law students, and

writers will continue to feel obliged to explain how it fits with the losing-contract problem. After all, it now says so in the *Restatement Second*.

Use of the reliance interest as an operative measuring standard involves more serious problems. As Fuller and Perdue defined it, the reliance interest concept was made broad and loose enough to serve as an analytical tool for a variety of problems. By making the reliance interest serve the specific function of defining section 349 reliance damages, the *Restatement Second* necessarily has begun to erect fences around that general definition. The possible exclusion of foregone opportunities is one example. The technical problems encountered by the difficulty of stating an expectancy or causation ceiling are another. This is an inevitable result when one uses a general concept to do black-letter work.

On the whole, the reliance-interest concept and its attendant Comments do not furnish any sort of systematic definition of reliance damages. This is hardly surprising, for the notion of reliance damages as an explicit remedy is relatively new, and contains many difficult issues of application that appear unlikely to be resolved without considerable experience. The *Restatement Second's* expansion of explicit reliance remedies will help bring more of these issues into the open. Meanwhile, it seems fair to conclude that in this area, as in others, the role of the reliance-interest concept in the *Restatement Second* is to invite development, not to restate it.